UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF PENNSYLVANIA

BARRY J. BELMONT, PHILADELPHIA FINANCIAL SERVICES, LLC, THOMAS J. KELLY, JR., FRANCES R. KELLY and GARY O. PEREZ, **Plaintiffs,** **v.** **MB INVESTMENT PARTNERS, INC., CENTRE MB HOLDINGS, CENTRE PARTNERS MANAGEMENT, LLC, ROBERT M. MACHINIST, MARK E. BLOOM, RONALD L. ALTMAN, LESTER POLLACK, WILLIAM M. TOMAI, GUILLAUME BEBEAR, P. BENJAMIN GROSSCUP, THOMAS N. BARR, CHRISTINE MUNN AND ROBERT A. BERNHARD,** **Defendants.**	**Civil Action No. 09-cv-04951**

MEMORANDUM OF LAW IN FURTHER SUPPORT OF DEFENDANTS CENTRE MB HOLDINGS LLC, CENTRE PARTNERS MANAGEMENT LLC, LESTER POLLACK, GUILLAUME BÉBÉAR AND WILLIAM TOMAI'S MOTION TO DISMISS THE AMENDED COMPLAINT

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Defendants Centre MB Holdings LLC ("Centre MB Holdings"), Centre Partners Management LLC ("Centre Management," with Centre MB Holdings, the "Centre Entities") Lester Pollack ("L. Pollack"), William M. Tomai ("Tomai"), Guillaume Bébéar ("Bébéar" and with L. Pollack and Tomai, collectively, the "Centre Directors"; the Centre Directors together with the Centre Entities, the "Centre Defendants") submit this memorandum of law in accordance with the Court's order dated March 17, 2010 in further support of their motion to dismiss the claims asserted against them in the Amended Complaint ("Am. Compl.") pursuant to Fed. R. Civ. P. 12(b)(6) (the "Motion").

PRELIMINARY STATEMENT

As discussed in the Centre Defendants' Motion, this case is about alleged wrongdoing by Defendant Mark Bloom ("Bloom") a former officer and director of Defendant MB Investment Partners, Inc. ("MB"). The Amended Complaint alleges two causes of action against the Centre Defendants: (i) that the Centre Defendants are subject to "control person liability" under Section 20(a) of the Securities Exchange Act of 1934 (the "Act"), given their alleged status as "control persons" over MB; and (ii) that the Centre Defendants are liable for negligent supervision under Pennsylvania common law. Plaintiffs fail to state a claim with respect to each of these causes of action.

First, in order to allege a cause of action under Section 20(a), there must be a primary violation of the Act. The Amended Complaint, however, fails to allege such a violation by MB. Moreover, the Amended Complaint does not allege that the Centre Defendants ***actually*** controlled MB with respect to the alleged fraudulent transactions, which it must in order to plead a cause of action under Section 20(a). Recognizing that the Amended Complaint is inadequately pled, Plaintiffs argue in their Opposition papers (the "Opposition Brief") that, the Amended

Complaint has sufficiently alleged a "reasonable inference" of control through the Centre Defendants' status as directors and shareholders, and in any event, control is a fact-dominated question that cannot be resolved without discovery. The cases cited by Plaintiffs to support the sufficiency of their "control" allegations are distinguishable. As discussed below, those cases all involve Section 20(a) claims against a senior officer or director of a company with direct responsibility or oversight over an allegedly false or misleading public filing, i.e., a situation in which the control person could have prevented the alleged fraud. The circumstances here are completely different, as they concern a surreptitious fraud carried out by Mark Bloom that involved his own private meetings with Plaintiffs, and his theft from the North Hills hedge fund in which Plaintiffs had invested funds but over which none of the Centre Defendants had any control. Moreover, and as demonstrated by the cases cited in the Centre Defendants memorandum of law in support of the Motion (the "Brief"), a Court may dismiss a cause of action under Section 20(a) as a matter of law where the allegations of control rest solely on the defendants' status as directors or shareholders, as is the case here. Accordingly, the cause of action for control person liability should be dismissed.

Finally, the Amended Complaint's cause of action for negligent supervision against the Centre Defendants is also insufficiently pled. In order to be liable for this tort, the wrongdoing must have been foreseeable, which Plaintiffs fail to allege. In their Opposition Brief, Plaintiffs respond by arguing that the Centre Defendants failed to supervise MB, and that, therefore, they cannot now argue that the fraud was not foreseeable. See Opp. at 42. It is irrelevant, however, whether the Centre Defendants were supervising MB because Bloom's alleged fraud in this case is predicated upon his activities in North Hills, an entity that Plaintiffs admit was under Bloom's

"almost complete control" (Am. Compl. ¶ 33). Accordingly, the cause of action for negligent supervision should be dismissed.

ARGUMENT

I. PLAINTIFFS HAVE FAILED TO STATE A CLAIM UNDER SECTION 20(A) OF THE EXCHANGE ACT

A. Plaintiffs Have Not Pled A Violation By MB Of Section 10(b) Of The Exchange Act Or Rule 10b-5

The Centre Defendants established in the Motion that the Complaint must plead a primary violation of the Act as a predicate to any viable Section 20(a) cause of action. See, e.g., In re Alpharma Inc. Sec. Litig., 372 F.3d 137, 153 (3d Cir. 2004) ("Plaintiffs must 'prove not only that one person controlled another person, but also that the 'controlled person' is liable under the Act. If no controlled person is liable, there can be no controlling person liability.'" (quoting Shapiro v. UJB Fin. Corp., 964 F.2d 272, 279 (3d Cir. 1992)). For the reasons detailed in the MB Brief (at 8-19) and the MB Reply Brief (at 3-7), Plaintiffs have not pled such a claim under the stringent pleading standards set forth in Tellabs, Inc. v. Makor Issues & Rights, Ltd., 551 U.S. 308 (2007). Plaintiffs argue that regardless of their allegations against MB, the Amended Complaint adequately pleads a primary violation by Defendants Altman and Bloom, and that such primary violation is sufficient to plead a secondary against the Centre Defendants. See Opp. at 39. However, the Section 20(a) claim against the Centre Defendants alleges that they are secondarily liable because of their control over MB, not because of any alleged control over Altman and Bloom. See Am. Compl. ¶¶ 93-101. Thus, a Section 20(a) claim can be pled against the Centre Defendants only to the extent that a primary violation can be pled against MB. Accordingly, the Section 20(a) claim against the Centre Defendants must be dismissed.

B. Plaintiffs Have Not Pled "Control" Over MB By The Centre Defendants

The Centre Defendants established in the Motion that, as a matter of law, allegations of control cannot be based solely on board membership or stock ownership. See In re Ravisent Techs., Inc. Sec. Litig., 2004 WL 1563024, at *15 (E.D. Pa. July 13, 2004) ("Status or stock ownership is not necessarily sufficient by itself to establish control person liability."); In re Digital Island Securities Litigation, 223 F. Supp. 2d 546, 561 (D. Del. 2002) ("[I]t is well settled that '[t]he mere fact that an individual is a director of a firm is not sufficient to show he is a control[ling] person of the firm."), aff'd, 357 F.3d 322 (3d Cir. 2004). Indeed, the control must be actual, not merely hypothetical: "'[i]n order to establish controlling person liability under [Section 20(a)], a defendant must possess 'actual control over the transactions in question.'" Antinoph v. Laverell Reynolds Sec. Inc., 1989 WL 102585 at *5 (E.D. Pa. Sep. 5, 1989), aff'd, 911 F.2d 719 (3d Cir. 1990) (TABLE); see also Ravisent, 2004 WL 1563024, at *15 ("To establish a defendant is a control person, a plaintiff must demonstrate that 'the defendant had actual power or influence over the allegedly controlled person'").

In their Opposition, Plaintiffs ignore this authority and argue instead that they "need only make allegations that support a reasonable inference that defendants had the potential to influence and direct the activities of the primary violator, such as alleging that the individual defendants had direct and supervisory involvement in the day-to-day operations of the company by virtue of their positions, ownership rights and contractual rights." Opp. at 38, citing In re Rent-Way Sec. Litig., 209 F. Supp.2d 493, 524 (W.D. Pa. 2002); In re U.S. Interactive, Inc. Class Action Sec. Litig., 2002 WL 1971252 (E.D. Pa. Aug. 23, 2002). This argument is wholly without merit and the cases Plaintiffs rely upon are easily distinguishable: unlike here, the underlying violations of the Act in those cases involved allegedly false public filings for which the control

persons (i.e., high ranking corporate officers) were clearly responsible by virtue of their positions at their respective companies.

For example, in Rent-Way, the Court denied a motion to dismiss Section 20(a) claims against officer defendants on the basis of a "reasonable inference that [all of the defendants . . .] had the potential to influence and direct the activities of the primary violator." Plaintiffs fail to point out, however, that the court's decision in Rent-Way was informed by the fact that "[e]ach of these defendants [was] alleged to have signed one or more statements filed with the SEC that were eventually restated, and to have the ability to control the contents of these various statements." Rent-Way, 209 F. Supp.2d at 524 (emphasis supplied). The Ravisent case, which the Centre Defendants cited in support of the "actual" control standard but which Plaintiffs argue supports ***their*** contention that control may be determined by corporate status alone, is similarly inapposite. See Opp. at 42. Although the court in Ravisent found that it was sufficient to allege that the defendants were CEO and CFO, respectively, in order to allege that they had "actual power" or "influence" over the Company, the primary violation for which the officers were held secondarily liable involved an allegedly false and misleading registration statement – a publicly filed document for which the CEO and CFO would typically bear responsibility.

These cases stand in stark contrast to the facts at issue here. In Rent-Way and Ravisent, the alleged fraud concerned misstatements in public filings for which the defendants had responsibility by virtue of their senior management positions. Here, however, the alleged fraud involves communications between Bloom and Altman on the one hand and Plaintiffs on the other, and Bloom's activities in connection with North Hills; there is no allegation that the Centre Directors had any responsibility for these matters simply by virtue of their positions as outside directors of MB.

U.S. Interactive, a case cited by Plaintiffs (see Opp. at 38), where the Court denied a motion to dismiss Section 20(a) claims against defendants, is especially instructive here. In finding that the complaint had adequately pled that the defendants controlled the company, the court noted that "[e]ach of the [individual defendants] was provided with or had unlimited access to copies of . . . internal reports, press releases, public filings and other statements alleged by plaintiffs to be misleading prior to and/or shortly after these statements were issued ***and had the ability to prevent the issuance of the statements or cause the statements to be corrected***." U.S. Interactive, 2002 WL 1971252, at *20 (emphasis supplied). The Complaint here does not allege that the Centre Directors could have prevented the alleged underlying violation of the Act, but rather, it alleges generally that they had "control" over MB.[1] Indeed, the real fraud in this case – the theft by Bloom of Plaintiffs' investments in North Hills – could only have been discovered (and prevented) by those in control of North Hills, and Plaintiffs admit that North Hills was under Bloom's "almost complete control." Am. Compl. ¶ 33.

The allegations of control asserted against the Centre Entities (i.e., Centre MB Holdings and Centre Partners) are equally deficient. As set forth in the Amended Complaint, Centre MB Holdings is the majority shareholder of MB, and Centre Partners is a majority shareholder of Centre MB Holdings. Id. ¶¶ 9, 10. The Amended Complaint contains no allegations concerning any actual control or influence exercised by the Centre Entities over MB, nor does it allege that they could have prevented the alleged fraud itself. Rather, Plaintiffs attempt to allege control by relying on the Centre Entities' status as majority shareholders of MB, which is insufficient since, as discussed above, control cannot be based on status alone.

[1] As discussed in the Centre Defendants' brief, the Form ADV filed by MB is immaterial for determining Section 20(a) control since it does not say (either expressly or by implication) whether Tomai and Pollack and Centre MB Holdings had any control over the specific alleged wrongdoing at issue here. See Br. at 11.

In their Opposition Brief, Plaintiffs also assert that the Centre Entities controlled the day-to-day operations of MB through a "written contractual operating agreement," but they never allege how the written agreement provided the Centre Entities with actual control over Bloom and Altman in connection with the alleged fraud. Furthermore, Plaintiffs' allegation that there was an "interlocking directorate" between MB and the Centre Entities through shared officers is irrelevant. What is relevant for the purposes of Section 20(a) is whether the Centre Entities had actual control over the alleged wrongdoing at MB. Arguing that there was an "interlocking directorate" does not speak to this issue at all and therefore cannot serve as a basis for alleging control.

In a last ditch effort to survive the Centre Defendants' motion to dismiss, Plaintiffs argue that discovery is necessary in order to determine whether the Centre Defendants are "control person(s)" because control, in their view, is a factual issue. Opp. at 37.[2] To the contrary, courts routinely dismiss Section 20(a) claims at the pleading stage where, as here, a plaintiff alleges nothing more than status as a director or shareholder. See, e.g., In re Alstom SA Sec. Litig., 406 F. Supp. 2d 433, 499 (S.D.N.Y. 2005) (dismissing control person claim against outside director and audit committee member where "the Complaint does not contain any facts from which [control] can reasonably be inferred . . . ."); In re Livent, Inc. Sec. Litig., 78 F. Supp. 2d 194, 221 (S.D.N.Y. 1999) (dismissing control person claims against outside directors who were alleged to have "power and influence . . . to cause Livent to engage in . . . illegal conduct . . . 'by virtue of

[2] In support, Plaintiffs cite In re Countrywide Fin. Corp. Sec. Litig., 588 F. Supp. 2d 1132 (C.D. Cal. 2008), a case in which Section 20(a) claims were alleged against the CEO, CFO and COO, respectively, of a company that was alleged to have made false public filings. Given that the underlying violations of the Act involved public filings, the Court held that the defendants were "plausible control persons who allegedly aided and abetted Countrywide's violations." Id. at 1201. For the reasons discussed above, Countrywide is equally inapposite because the defendants would have had responsibility for public filings by virtue of their positions at the company.

their executive position, their knowledge of and involvement in the Company's business, and/or stock ownership, and/or power and ability to make public statements on behalf of the Company'" because "[o]fficer or director status alone does not constitute control.").

In sum, the Amended Complaint fails to allege a Section 20(a) violation and the cause of action should be dismissed.

II. PLAINTIFFS HAVE FAILED TO STATE A CLAIM FOR NEGLIGENT SUPERVISION

As the Centre Defendants explained in the Motion, the law is clear that, in order to assert a cause of action for negligent supervision, the alleged wrongdoing must be reasonably foreseeable. Other than noting that Bloom led an extravagant lifestyle, the Amended Complaint does not allege that Bloom's fraud was foreseeable, and, therefore, this cause of action must fail. In response, Plaintiffs fall back on their allegation that the Centre Defendants failed to supervise MB, and argue that the Centre Defendants cannot "abrogate their anti-fraud duties, on the one hand, and then contend they didn't anticipate that a fraud would occur, on the other hand." Opp. at 42. This reasoning is specious. It is irrelevant whether the Centre Defendants were supervising MB because Bloom's alleged fraud is predicated upon his activities in North Hills. Furthermore, because the Amended Complaint admits that North Hills was under Bloom's "almost complete control" (Am. Compl. ¶ 33), no "anti-fraud" measures undertaken by the Centre Defendants at MB could have uncovered Bloom's fraud at North Hills. Accordingly, the fraud was not foreseeable, and this cause of action should be dismissed.[3]

[3] The Centre Defendants also incorporate by reference pages 8-9 of the MB Reply Brief, which address Plaintiffs' cause of action for negligent supervision.

CONCLUSION

For the foregoing reasons, and those set forth in the Brief, Plaintiffs' claims against the Centre Defendants should be dismissed with prejudice.

Dated: May 4, 2010

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CERTIFICATE OF SERVICE

I hereby certify that a copy of the foregoing Reply Memorandum in Support of the Motion to Dismiss of Defendants Centre MB Holdings LLC, Centre Partners Management, LLC, Lester Pollack, Guillaume Bébéar and William M. Tomai was served on this date via filing with the Court's ECF system (with the exception of Mark Bloom who has been served by U.S. Mail) and is available for viewing and downloading from the ECF System on this 4th day of May, 2010 by the following counsel:

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