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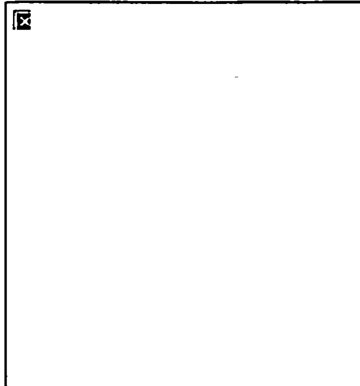
Investor can't recover against fund manager

By: David E. Frank September 6, 2010



A Superior Court judge has ruled that a CEO whose company pension plan lost nearly $1.5 million during the stock market collapse of 2000 could not recover against a hedge fund manager under the Massachusetts Uniform Securities Act.

The Harvard University- educated CEO, who had run a high-tech company for more than 25 years, argued that the defendant hedge fund manager's material misrepresentations caused him to suffer major monetary losses.

But a Superior Court jury and later Judge Margaret R. Hinkle, who heads the Business Litigation Session in Boston, disagreed, finding that the CEO was a sophisticated investor who knew the risks associated with hedge funds.

"The inescapable conclusion ... is that the Plan remained invested in the Fund not because of [the defendants'] promises or assurances, but because it hoped that the downturn in the stock market would resolve itself and provide the Plan with future positive returns," Hinkle wrote. "I therefore conclude that none of the [defendants'] alleged post-investment misrepresentations constitute a violation of G.L.c. 93A, §11."

The 16-page decision is Marram, trustee v. Kobrick Offshore Fund, Ltd., et al., Lawyers Weekly No. 12-209-10. The full text of the ruling can be ordered by clicking here.

Key footnote

Jeffrey S. Robbins, who represented the defendants, said the 10-year-old case was tried after the Supreme Judicial Court in 2004 reversed then-BLS Judge Allan van Gestel's allowance of a motion to dismiss.

The Boston litigator from Mintz, Levin, Cohn, Ferris, Glovsky & Popeo said the SJC's Marram decision, which was authored by Chief Justice Margaret H. Marshall, became one of the most frequently cited cases in the Massachusetts securities field.

"Lawyers and judges have cited it for everything from how materials that are attached or implicit in pleadings can be considered for [motions to dismiss] to the fact that reliance is not an element of a state Securities Act claim to the fact that an integration clause will not bar a plaintiff from alleging there were oral misrepresentations which caused him to invest," he said.

Robbins added that the recent results in Marram should send a message to plaintiffs that it is one thing to survive a motion to dismiss, but quite another to establish a misrepresentation at trial.

"This is a case, which, now that it's over, illustrates the divide between the theoretical and the actual," he said. "The SJC decision emphasized the theoretical possibility that a plaintiff could allege he had been orally assured something that was totally different than what was in writing, but the actual evidence showed that nothing of the sort ever occurred."

The plaintiff, he said, chose to ride out the stock market collapse and sued only when that decision resulted in a huge financial loss.

"My client is somebody whose life had been spent in the securities industry with a great deal of success, who had never been sued before and who was required to expend 10 years, and all that goes with it, defending his

reputation against what turned out to be a meritless claim," he said. "But one thing that comes out of this is that when someone sues after knowingly seeking a risky investment which ultimately doesn't pan out, they are going to be exposed in front of a jury and the court."

Philip Y. Brown of Boston's Adler, Pollock & Sheehan, who represented the plaintiff, said the case ultimately came down to how the judge and jury viewed what had transpired during a meeting between the parties in 1999.

"Both people came away with different versions of what they thought had been said," Brown noted. "Our client acted based on what he was told and felt he had been assured that the fund was not heavily involved in high-tech stocks and would not be in the future."

Michael A. Collora of Dwyer & Collora in Boston, who was not involved in the case, said the SJC's 2004 Marram ruling clarified long-standing questions about investment fraud complaints.

As long as a misstatement is alleged in a complaint, sellers still have a heavy burden to show they did not mislead a buyer or make material misstatements, Collora said.

The jury's verdict and Hinkle's findings, he said, do not change that principle.

"[Marram] made bringing plaintiffs' cases in Massachusetts much more favorable than it had been in the past," he said. "So while the jury's decision and Judge Hinkle's 93A ruling is significant, plaintiffs are still going to be more likely to win a motion to dismiss or a motion for summary judgment because of it."

Meeting of the minds

In 1999, plaintiff Edward Marram discussed a possible investment in an offshore fund with defendant Frederick Kobrick of Kobrick Capital Management. Marram, chairman and CEO of GEO-Centers, Inc., oversaw his company employee pension plan.

During that meeting, Marram said, Kobrick told him the fund was non-volatile and diversified. He allegedly also said it was a suitable investment for the pension plan.

In 2000, Marram invested $2 million of the pension plan in the fund.

A short time later, the market decline hit and the pension plan's investment drastically declined. According to Marram's testimony, Kobrick continued to express confidence that the fund's outlook was good. But the fund continued to lose value and, by November 2000, the pension plan's investment was worth only $751,910.

When the CEO directed the fund to liquidate the account in December 2000, Kobrick told Marram he was confident the fund would do better and promised to provide him with a list of other companies held by the fund, Marram testified.

As a result, Marram said, he rescinded his liquidation order. But he told the court the fund continued to decline, and Kobrick never followed up on his promises. By the time Marram liquidated his holdings in April 2001, he had lost more than $1.4 million.

The CEO then sued the hedge fund for a variety of infractions, including false statements, negligent misrepresentation and violation of Chapter 93A.

In 2002, van Gestel dismissed the complaint. On appeal, the SJC vacated the dismissal and remanded the case to the BLS.

A jury in November returned defense verdicts on the securities claims. Hinkle then conducted a two-day bench trial on the 93A issue.

Buyer beware

In entering judgment for the defendant, Hinkle said she agreed with the jury that the hedge fund manager had not made any misrepresentations. The judge said the fund's offering memorandum explained its speculative nature and risks, and Marram was an extremely sophisticated investor who read and understood the memorandum.

To the extent that the CEO offered testimony that misrepresentations were made, Hinkle said, such claims lacked credibility. For example, he testified he did not know and was not informed he was investing in a hedge fund.

"That testimony is discredited by Marram's contemporaneous notes from the meeting referring to 'hedge fund,' and [a fellow executive's] acknowledgment that Kobrick told the two of them that the Offshore Fund was a hedge fund," she said.

While Hinkle said the lawsuit was weak, she ruled that the plaintiff's conduct did not warrant an award of attorneys' fees and costs under G.L.c. 231, §6F.

"In drawing that conclusion, I note that the SJC reversed Judge van Gestel's dismissal of plaintiff's complaint, and both Judge van Gestel and Judge Gants later denied defendants' summary judgment motions," she said. "Although insufficient to prevail, plaintiff's claims were not wholly insubstantial, frivolous and not advanced in good faith."

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