

THE BON SECOURS
COMMUNITY INVESTMENT
FUND

Plaintiff

v.

NETWORK TECHNOLOGIES
GROUP, INC., *et al.*

Defendants

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IN THE

CIRCUIT COURT FOR

BALTIMORE CITY

24-C-03-001338

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MEMORANDUM OPINION

This case stems from an investment gone awry. In March of 2002, after conducting a due diligence investigation, The Bon Secours Community Investment Fund, L.P. (“Bon Secours”) invested \$1 million in Network Technologies Group, Inc. (“NTG”). Within three months of the investment, Bon Secours discovered that NTG’s officers had generated and distributed false financial documents such that what was shown as a net profit of \$82,338 was in fact a net loss of over \$1.8 million. After the fraud was discovered, NTG’s bank, Mercantile-Safe Deposit and Trust Company (“Mercantile”) terminated NTG’s credit line and demanded repayment of all outstanding loans. The result was that NTG’s assets were liquidated and Bon Secours and other investors lost all the money they had invested. In an attempt to recover its \$1 million investment, Bon Secours filed suit against NTG, NTG’s officers and Outside Directors, and NTG’s accountant Ellin & Tucker, Chartered (“E & T”).

PROCEDURAL BACKGROUND

Plaintiff Bon Secours filed its complaint against: NTG; NTG's CEO Michele A. Tobin ("Tobin"), NTG's CCO, founder, and Board member Victor J. Giordani, Jr. ("Giordani"), NTG's CFO Thomas S. Bray ("Bray"), and NTG's Controller Beverly Baker ("Baker"); NTG Outside Directors Nora Zietz ("Zietz"), Robert M. Stewart ("Stewart"), John Picciotto ("Picciotto"), and Gerhard Pilcher ("Pilcher"); and NTG's accountant E & T. Count I alleges Maryland Securities violations against all Defendants; Count II alleges intentional misrepresentation against NTG, Tobin, and Bray; Count III alleges negligence against all Defendants; Count IV alleges negligent misrepresentation against all Defendants; Count V alleges negligent retention and failure to supervise against NTG, Giordani, Zietz, Stewart, Picciotto, and Pilcher; and Count VI alleges civil conspiracy against NTG, Bray, and Baker.

Defendant E & T filed a cross-claim against Defendants Tobin, Bray, and Baker. Defendants Zietz, Stewart, and Picciotto filed a cross claim against Defendants Bray and Baker. Both Baker and Bray filed cross claims against Zietz, Stewart, Picciotto, Pilcher, Giordani, Jr., Tobin, Bray, and NTG.

Bon Secours filed a Motion for Order of Default against NTG, which was granted on August 13, 2003, and Bon Secours then filed a Motion for Summary Judgment as to damages against NTG. Defendant E & T filed a Motion for Summary Judgment.¹ The Outside Directors filed Motions for Summary Judgment against Bon Secours and against Baker and

¹Defendant E & T earlier filed a Motion to Dismiss Count I which was denied on July 11, 2003.

Bray on the cross claims. On March 30, 2004, the parties stipulated that all claims brought against Outside Directors Picciotto and Pilcher would be dismissed with prejudice. This opinion addresses the Outside Directors' and E & T's Motions for Summary Judgment as well as Bon Secours' Motion for Summary Judgment against NTG.

STATEMENT OF FACTS

Network Technologies Group, LLC ("NTG LLC"), the predecessor to NTG was formed in October 1997. Its primary business was providing telecommunication infrastructure and construction services. Tobin served as NTG's CEO until June of 2002. Bray served as NTG's CFO and Baker was NTG's Controller. By May of 2000, NTG's Board of Directors was composed of two members of NTG's management, Tobin, and Giordani (the COO) and four independent directors, Zietz, Stewart, Picciotto and Pilcher. Zietz was The Abell Venture Fund's ("Abell") representative and was responsible for overseeing Abell's investment in NTG.² Defendant Stewart, a professional investor and partner at Spring Capital, served as the Spring Capital representative who was responsible for administering Spring Capital's loan to NTG and was Spring Capital's nominee on NTG's Board.³

Need for Additional Capital and PPM

From 1999 through mid-2001 NTG experienced rapid growth. As a result of its quick growth and the nature of the business, which involved large contracts requiring up front

² In the Fall of 1998, Abell lent \$500,000.00 to NTG and in January, 1999, increased its commitment to NTG by investing \$1.5 million in the company in exchange for preferred stock. In March of 2002, Abell invested an additional \$750,000.00 in NTG.

³ In May, 2000, Spring Capital, a Baltimore-based subordinated debt fund, provided \$3.5 million in mezzanine financing to NTG. The Spring Capital debenture was secured by a second lien on NTG's assets, subordinate to Mercantile's first lien.

investments, NTG had an urgent need for additional capital. In April of 2001, NTG retained Ferris Baker Watts, Inc (“FBW”), a prominent investment banking firm, to assist the company in obtaining \$4 million in additional capital. In June, 2001, FBW circulated to potential investors a Confidential Private Placement Memorandum (“PPM”) soliciting potential investors for an offering of \$4 million of series C preferred stock in NTG. The PPM contained historic financial information and financial projections.

The terrorist attack on 9/11 had an immediate and pronounced effect on NTG’s business. Its insurance rates doubled; its customers began taking longer to pay invoices. One of its largest customers, Adesta, filed for bankruptcy in the Fall of 2001, leaving NTG with an unpaid receivable of approximately \$900,000.00. NTG released an Addendum to the PPM in early 2002.

Lack of Borrowing Availability Under the Mercantile Line of Credit

NTG’s primary lender was Mercantile, which extended an initial \$750,000.00 secured line of credit to NTG in December, 1998. By May, 2000, the Mercantile credit had expanded to include a \$2 million equipment line and a \$2.5 million revolving loan. By early 2002, NTG had exhausted its borrowing availability with Mercantile and its cash flow suffered. In January of 2002, NTG overdrew its bank account with Mercantile and by the end of February, an “overadvance” existed on the Mercantile line of credit, meaning that the amount outstanding on the line of credit exceeded the amount which NTG was allowed to borrow under its loan agreement. The overadvance was also an event of default under the Mercantile loan agreement. In addition, during January 2002, NTG Controller Baker wrote a series of bad checks which resulted in an overdraft of approximately \$800,000.

Bon Secours' Decision to Invest \$1 million in NTG

In August 14, 2001, Maritza Alvarez of Smith Whiley & Co. ("Smith Whiley"), a Connecticut-based investment management company that manages private investments for Bon Secours, contacted Stewart to inquire about potential investments in the Baltimore area. Stewart informed her that NTG was searching for new investors and referred her to FBW. On August 15, 2001, FBW sent Alvarez a copy of the PPM, along with copies of E & T audited financial statements for 1999 and 2000 and internally prepared financial statements through May, 2001.

Smith Whiley performed a due diligence investigation for Bon Secours and after it was completed, Alvarez and Smith Whiley's President Gwendolyn Iloani decided that NTG was a suitable investment for Bon Secours. Before making its investment, Bon Secours also obtained the results of due diligence compiled by several other funds that were considering an investment in NTG. Bon Secours retained a Connecticut law firm, Shipman & Goodwin, to represent it in the transaction and to perform additional due diligence. Bon Secours advised NTG in mid-January of 2002 that it was willing to move forward with its \$1 million investment and in March, 2002, made the investment. At the time of the Bon Secours investment, there were no investors for the other \$3 million NTG needed.

Discovery of the Fraud

In May 2002, Tobin advised NTG's Board that she had cancer and could no longer serve as CEO. The Board of Directors hired a turn around consultant, John Collard, to serve as interim CEO of the Company and on July 1, 2002, Collard assumed day-to-day management of NTG. He quickly learned that NTG's financial condition was not accurately

reflected in the company's financial statements. A subsequent investigation by Collard and E & T revealed that NTG's books had been fraudulently altered to overstate revenues and receivables and understate expenses.

The investigation showed that beginning in early December 2001, Tobin had instructed NTG's Controller Baker to stop entering payables into NTG's accounting system. As a result, approximately \$300,000.00 of expenses were improperly omitted from NTG's financial statements for the period that ended December 31, 2001. Additionally, in January 2002, Ms. Tobin created various invoices in NTG's accounting system and back-dated the invoices to various dates in December. Some of the invoices were for progress billings on legitimate contracts that NTG was not yet entitled to bill, but others were completely fictitious. These improper billings overstated revenues and receivables on NTG's financial statements for the period that ended December 31, 2001 by approximately \$1.9 million. Of the contract revenues shown on a Preliminary Statement of Operations of NTG as of December 31, 2001, of \$2,229,138, over \$1,900,000 – over 85% – was non-existent. What was shown to be a net profit for the year of \$82,338 should have been a net loss of over \$1,800,000.

After the fraud was revealed, Mercantile terminated NTG's credit line and demanded repayment of all of its loans. When Spring Capital, Abell, and Bon Secours refused to invest additional funds, the decision was made to close down the company. Soon after, NTG's assets were liquidated for the benefit of Mercantile. Spring Capital, Abell, and Bon Secours lost all of the money which they lent to or invested in NTG. Tobin, Bray, and Baker all have pled guilty to federal fraud charges relating to their efforts to cook the books of NTG.

BON SECOURS' SUMMARY JUDGMENT MOTION AGAINST NTG

Bon Secours filed a Motion for Summary Judgment against NTG requesting \$1,000,000 in direct and consequential damages, pre-judgment interest from March 4, 2002, post-judgment interest, attorneys' fees, and expenses. In support of its Motion, Bon Secours has submitted the Series C Convertible Stock Purchase Agreement entered into between Bon Secours and NTG, and an excerpt from the deposition of Iloani, who executed the Agreement on its behalf. Both exhibits, which show that Bon Secours purchased \$1,000,000 in stock from NTG, support its claim for direct and consequential damages. NTG has offered no rebuttal evidence. Thus, the Court shall grant Bon Secours's Motion for Summary Judgment against NTG.

DEFENDANTS' MOTIONS FOR SUMMARY JUDGMENT

THE SECURITIES ACT CLAIMS

Bon Secours alleges that E & T and Outside Directors Stewart and Zietz violated CORP. & ASSOC. ART § 11-703(a)(1)(ii) and (c)(1) of the Maryland Securities Act. As the Court of Appeals has stated repeatedly, "the cardinal rule of statutory interpretation is to ascertain and effectuate the intention of the legislature." *Handy v. State of Maryland*, 357 Md. 685, 704-05 (2000) (citations omitted). In order to determine legislative intent, a court should always begin with the language of the statute, and where the language is "plain and clear and expresses a meaning consistent with the statute's apparent purpose, no further analysis of legislative intent is ordinarily required." *Id.* at 704-05 (2000) (citations omitted). Thus the Court begins with the language of the statute.

Section 11-703(a)(1)(ii) provides that a seller of securities is civilly liable to the buyer under certain circumstances. More specifically it provides that a person is civilly liable to the person buying security from him if he:

offers or sells the security by means of any untrue statement of a material fact or any omission to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they are made, not misleading, the buyer not knowing of the untruth or omission, and if he does not sustain the burden of proof that he did not know, and in the exercise of reasonable care could not have known, of the untruth or omission.

Id. Section 11-101(k) defines “offer” and “offer to sell” as including “every attempt to offer to dispose of or solicitation of an offer to buy, a security or interest in a security for value.” And (n) defines “sale” or “sell” as including “every contract of sale of, contract to sell, or disposition of a security or interest in a security for value.”

“A seller is only liable to his or her buyer.” *Baker, Watts, & Co. v. Miles & Stockbridge*, 95 Md. App. 145, 182 (1993). Two things must be true in order to show that a person is a seller under the Act. “First, the person must pass title to the buyer or successfully *solicit* the purchase of securities.” *Id.* at 183 *citing Pinter v. Dahl*, 486 U.S. 622, (1988) (emphasis added). The Court noted that Black’s Law Dictionary defines “solicit” as

[t]o appeal for something; to apply to for obtaining something ... to ask for the purpose of receiving.... The term implies personal petition and importunity addressed to a particular individual to do some particular thing.

Id. at 183-84 *citing* Black's Law Dictionary (5th ed. 1983). The *Baker, Watts* Court noted with approval that the Supreme Court in *Pinter* had expressly rejected the “substantial factor” test or a test based on “participation in soliciting the purchase.” *Id.* at 184. The second

requirement is that the person must be “motivated at least in part by a desire to serve his own financial interests or those of the securities owner.” *Id.*

Clearly the seller of the stock was the corporation, NTG. Neither E & T, Stewart, or Zietz did or could have passed title to Bon Secours. Thus, to decide if these Defendants offered to sell the Court must (1) examine whether the Defendants solicited the purchase and, if they did, (2) whether they were motivated by a desire to serve their own financial interests or those of NTG.⁴

OUTSIDE DIRECTORS STEWART AND ZEITZ

_____A. *LIABILITY AS SELLERS*

In support of its argument that Stewart and Zietz are liable as sellers, Bon Secours points to evidence that they (1) directly participated in and were responsible for the issuance of representations made in the PPM; (2) Stewart originally brought NTG to Bon Secours’ attention; (3) Stewart informed Bon Secours that Abell was pleased with the performance of NTG and implied that Bon Secours was a good investment; and (4) Stewart and Zietz provided financial information to Smith Whiley. Bon Secours also points out that Tobin testified at her deposition that Stewart was responsible for talking with Smith Whiley; that she left the issue of establishing the valuation of the stock sold to Bon Secours to Stewart and Zietz and that Stewart and Zietz reviewed and evaluated the term sheets.

A.1. SOLICITATION

Assuming all of these facts to be true, none of them show that Stewart and Zeitz solicited Bon Secours. First, the fact that Stewart brought NTG to Bon Secours’ attention

⁴As directors, Stewart and Zeitz were required to act in the interest of NTG; thus a desire to serve the financial interests of NTG only proves that they were acting consistently with their role as directors.

and stated that Abell was pleased with the performance of NTG and thought that it was a good investment is not a solicitation. Second, as discussed below, the review of the term sheet, establishing the valuation of the stock, and preparation of the PPM and, unless they did so fraudulently, providing information to Smith Wiley for its due diligence does not amount to solicitation.

A.1.a. Predictions in the PPM

In *Baker, Watts*, the Court rejected the argument that the attorneys' preparation of the offering memorandum brought them within the definition set forth in *Pinter* and concluded that there was not a "single fact" demonstrating that the attorneys "solicited" the security. 95 Md. App. at 184. *See also In re Enron Corp. Securities Litigation*, 258 F. Supp. 2d 576, 644 (S.D. Texas 2003) (Plaintiff failed to allege facts to show that Outside Directors were liable as sellers); *In re Activision Securities Litigation*, 621 F. Supp. 415, 421 (N.D. Calif. 1985) (Outside Directors were not sellers although they "helped draft the Prospectus, participated in 'road show' presentations of information to securities brokers and investment analysts, analyzed the market and set the price for [the] shares, and negotiated the agreement with the underwriters."); *In re Cendant Corp Securities Litigation*, 190 F.R.D. 331, 339 (D. N.J. 1999) (Court rejected plaintiff's argument that Outside Director's were sellers because they "signed the Registration Statement, and the Joint Proxy Statement/Prospectus contained statements by them.").

Even if the information provided was incorrect, a securities claim may not be based on financial projections made in a private placement memorandum where such projections are accompanied by specific warnings regarding the subjective nature of the projections and

the risks of the investment. *Saltzberg v. TM Sterling/Austin Associates, Ltd.*, 45 F.3d 399, 400 (11th Cir. 1995).

The context in which a statement is made is important. When an offering document's projections are accompanied by meaningful cautionary statements and specific warnings of the risks involved, that language may be sufficient to render the alleged omissions or misrepresentations immaterial as a matter of law.

Id. See also *Gasner v. Board of Sup'rs of the County of Dinwiddie, Va.*, 103 F.3d 351, 359 (4th Cir. 1996) (“[C]autionary language in the Offering Statement renders immaterial as a matter of law the alleged misrepresentations and omissions relied upon by appellants.”).

Here, the PPM contained explicit warnings and disclaimers regarding the accuracy of the financial information and projections set forth in the PPM. For example, the PPM stated:

AN INVESTMENT IN SERIES C PREFERRED STOCK IS SPECULATIVE, INVOLVES A HIGH DEGREE OF RISK, AND SHOULD BE CONSIDERED ONLY BY SOPHISTICATED INVESTORS WHO CAN BEAR THE ECONOMIC RISKS OF THE INVESTMENT FOR AN INDEFINITE PERIOD AND CAN AFFORD TO SUSTAIN A COMPLETE LOSS OF THE INVESTMENT.

The PPM also warned that

Neither FBW nor *the Company* nor any of their respective affiliates, *directors*, employees or representatives *make any representations or warranty, express or implied, as to the accuracy or completeness of any of the information* contained in this Memorandum. Any other information (whether communicated in written or oral form) transmitted or made available to prospective investors and each of such persons expressly disclaims any and all liability relating to or resulting from the issue of this Memorandum or such other information by a prospective investor or any of their affiliates or representatives. *NTG has not independently verified the*

information contained herein. Only those particular representations and warranties, if any, which may be made by the Company to an investor in a definitive written agreement, when, as and if executed, and subject and restrictions as may be specified therein, will have any legal effect.

(Emphasis added.) In addition, the PPM contained a specific warning with respect to the future financial projections set forth in the PPM:

The *financial projections* in this Memorandum represent the *subjective views* of the management of the Company and management's current estimates of future performance based on various assumptions which management believed are reasonable, but which may or may not prove to be correct. There can be *no assurance that management's opinions are valid* or that management's projections will be realized. Industry experts may disagree with these assumptions and with management's view of the market and the prospects for the Company.

(Emphasis added). Bon Secours knew it was undertaking a substantial risk and cannot rely on financial projections which failed to come to fruition.

Bon Secours contends that the statements of the directors amounted to misrepresentations concerning underlying financial conditions that may impact future performance, which are clearly actionable under Maryland law. *See Weisman v. Connors*, 312 Md. 428, 454-459 (1988). The evidence does not support this claim. As discussed throughout this Opinion, there is no evidence that Zeitz and Stewart were aware of or in any way participated in the fraud or that they had any meaningful information that Bon Secours did not have.

Furthermore, as a sophisticated investor, Bon Secours would not have been justified in relying upon the projections in the PPM. As the Court recognized in *Banca Cremi v. Alex*

Brown, 955 F. Supp. 499, 515 (D. Md. 1997), sophisticated investors are “powerful enough to demand and get the information they need before committing their money.” In fact, Bon Secours, by its own admission, *did not* rely upon the forward looking statements and projections contained in the PPM and the Addendum. Instead, it relied upon Smith Whiley’s due diligence investigation which consisted of performing an independent analysis. Smith Whiley’s President explicitly stated: “We never use their [NTG] numbers for anything.” When asked about the disclaimers in the PPM, she acknowledged, “the riskiness of [the] investment” and the disclaimer “address[ed] the financial projections” in the event “the company doesn’t grow as they’ve projected to grow.” The due diligence investigation included a “sensitivity analysis for that.”⁵

_____ *A.1.b. Misleading Information*

Plaintiff states that its “core charge” is not “for [the directors’] affirmative communications” but for the “failure to correct material representations that proved to be untrue and their concealment of material facts from Bon Secours.” Plaintiff’s use of the phrase “*proved to be untrue*” is based on a look backwards, at how things actually panned out, instead of an examination of the information that was available to the parties at the time of the investment.

As an example, one of Plaintiff’s claim of wrongdoing concerns NTG’s relationship with Mercantile. The crux of this claim is that the directors failed to notify Bon Secours, in January\February\March 2002 that it was being “shoved” away from Mercantile. However,

⁵Of course the due diligence did not count on fraud but there is no evidence that the Outside Directors knew about the fraud.

Bon Secours had its own discussions with Mercantile. The discussions included verifying the status of NTG's loans with Mercantile and obtaining copies of all of the relevant Mercantile loan documents, along with copies of the borrowing base certificates which NTG submitted to Mercantile showing the current availability on the line of credit. According to the people it spoke to at Mercantile "everything seemed fine."

As a result of its review of these materials, and its discussions with Mercantile and NTG management, Bon Secours knew that NTG was in default because of an overadvance on its line of credit. Further, Bon Secours was aware that NTG's inability to borrow against bonded jobs or older receivables under its line of credit with Mercantile was tightening the company's cash flow. When asked why the closing occurred when it did, the lawyer for Smith Whiley was brutally honest in stating that Bon Secours knew that NTG needed the money because of its severe cash flow problem:

Q: Was there any reason why the closing had to occur in March of 2002 as opposed to some later time?

R: I don't mean to be flip, but I think the simple answer was the company needed the money.

Mercantile did not terminate NTG's line of credit and demand repayment of all the loans until the fraud was discovered in July 2002 and there is nothing to indicate that Mercantile planned to do so absent the discovery of the fraud, or if it did that Zeitz and Stewart knew of those plans.

Bon Secours argues that from September 2001 to March 2002 the company suffered "one 'calamity' after another" as if the company was "cursed." According to Bon Secours, Stewart and Zeitz knew or should have known of "the impact and effect of those calamities,"

but “failed and omitted to disclose the existence and enormity of those calamities to Bon Secours.” Bon Secours then describes those calamities, but with the exception of what it calls the “Nationwide Trenching Claim,” Bon Secours knew about the “calamities.”

With respect to the Nationwide Trenching Claim (described in greater detail at 24-26), Bon Secours argues that Stewart and Zietz had a duty to correct the statement in the PPM that NTG “is not aware that it is a party to any litigation,” because in fact NTG was sued by Nationwide Trenching for more than \$880,000 in January 2002. Tobin, NTG’s CEO, was clearly aware of the suit at the time of the investment but Bon Secours does not point to any *facts* to show that Zeitz and Stewart knew about it. Instead, Bon Secours asks the Court to *assume* they knew.

Given the closeness of Stewart’s and Zietz’s monitoring of NTG’s affairs, it is highly unlikely that Tobin did not inform them of the existence and seriousness of the Nationwide Trenching claim.

Interestingly after Tobin’s deposition was taken, Bon Secours did not direct the Court’s attention to anything Tobin said to substantiate this supposition. Thus, there are no facts upon which a jury could find that they knew about the suit the day of the Bon Secours closing.

In sum, there is no way to predict what would have happened to Bon Secours’ investment in NTG had there not been fraud, it is also clear that the collapse of NTG at the time it occurred was the direct result of fraud and there is no evidence that Stewart and Zeitz knew about or should have known about the fraud at the time of Bon Secours investment. Bon Secours alleges that the Outside Directors had access to the fraudulent financial statements at an earlier date, and therefore, should have detected the fraud. Yet, there is no evidence to support the allegation.

Bon Secours argues:

***Given Stewart's and Zeitz's financial sophistication and their insider knowledge concerning the significant impact of NTG's cash crunch on its ability to conduct business by utilizing subcontractors and suppliers not being paid, it is extremely difficult to understand how they were unable to detect that over 85% of the contract revenues reported to the board for December 2001 were bogus. At the very least, these facts create an inference that Stewart and Zeitz, through their negligence and gross lack of care, enabled Tobin, Bray and Baker to pursue the financial fraud to which they have admitted guilt.

The problem with this argument is that it does not recognize the law that permits directors to rely upon information provided to them by the corporation's officers. *See* discussion of CORP. & ASSOC. ART § 2-405(1)(b) below at pages 18-19. Furthermore, the evidence shows that Bon Secours had as much, if not more information than the Outside Directors about the financial state of NTG, and yet it was unable to detect the fraud.

_____A.2. FINANCIAL INTEREST

Bon Secours also failed to present facts showing that Stewart and Zietz were motivated in part by their own financial interests. There is no evidence that either of them had any personal ownership interest in NTG or that they received any commission or other special remuneration in connection with the sale. In fact they were not compensated by NTG for their service on NTG's Board.

Bon Secours contends that Zietz was motivated by her own financial interests because of her ties to Abell. Zietz was also a director of Abell and Bon Scours alleges that Zeitz acted to protect Abell's investment and thus to protect her own interest. Similarly, Bon Secours contends that Stewart benefitted from Bon Secours' investment proceeds because of his ties to Spring Capital. As proof of Stewart's financial interest, Bon Secours points out

that on the day of the Bon Secours closing, Tobin instructed Mercantile to transfer \$34,708.33 in interest payments to Spring Capital.

Zeitz and Stewart were representatives of Abell and Spring Capital respectively. Thus in order to find that Zeitz and Stewart had a personal financial interest in the investment, Bon Secours would have to show that Abell and Spring Capital would have benefitted from the investment and that Zeitz and Stewart would have then reaped a financial reward. Even assuming that the evidence supports a finding that Abell and Spring Capital benefitted from or would have benefitted from the Bon Secours investment, there is not a scintilla of evidence that Stewart and Zeitz received or expected to receive any personal benefits as a result of the investment.

_____ *B. LIABILITY AS AIDERS AND ABETTORS*

Bon Secours also argues that the Outside Directors are directly liable pursuant to § 11-703(c)(1), as “director[s] of the persons liable . . . [and as an] agent who materially aid[ed]” in defrauding Bon Secours. Section 11-703(c)(1) provides:

Every ... *director of the person liable*, [is] ... also liable jointly and severally with and to the same extent as the person liable, unless able to sustain the burden of proof *that he did not know, and in exercise of reasonable care could not have known*, of the existence of the facts by reason of which the liability is alleged to exist.

(Emphasis added). The Directors argue that they are not liable under this section because all the evidence shows that they “did not know, and in exercise of reasonable care could not have known, of the existence of the facts by reason of which the liability is alleged to exist.”

Id.

In determining whether a director knew or in exercise of reasonable care could have known the facts that form the basis of liability the Court begins with CORP. & ASSOC. ART § 2-405.1(b), which limits the liability of directors who rely on information provided by the corporation's officers, employees, attorneys, accountants, and other professionals.⁶ That section provides that a director may:

rely on any information, opinion, report, or statement, including any financial statement and other financial data, prepared or presented by:

- (i) Any officers or employees of the corporation whom the director reasonably believes to be reliable and competent in the matters presented;
- (ii) A lawyer, certified public accountant, or other person, as to a matter which the director reasonably believes to be within the person's professional or expert competence;

Subsection 2-405.1(c) provides that if a director reasonably relies on such information in compliance with subsection (b), the director has immunity from any liability pursuant to *CTS. & JUD. PROC.* § 5-417. This immunity from liability applies in suits by third parties alleging violations by the director. James. J. Hanks, *Maryland Corporation Law* § 6.9 (2001 Supp.). A director may not rely on the information if “he has any knowledge concerning the matter in question which would cause such reliance to be unwarranted.” § 2-405.1(b)(2).

⁶Pointing out that NTG was incorporated in Delaware, the Outside Directors cite both Maryland and Delaware law on the duty of the directors. While, the law of the state of incorporation applies to a director's duty in a shareholder derivative suit, *Tabas v. Mullane*, 608 F.Supp. 759, 764 (D.N.J.1985), “a tort action [is] governed by the substantive law of the state where the wrong occurred.” *Philip Morris Incorp. v. Angeletti*, 358 Md. 689, 746 (2000). Thus Maryland law applies.

Based on the facts presented before the Court, there is no evidence upon which a jury could conclude that the Outside Directors are liable as aiders or abettors because of their position as directors or because they acted as agents who materially aided the sale.

ELLIN & TUCKER

Bon Secours argues that E & T is liable as a seller and an aider and abettor because it “directly involved itself in NTG’s money-raising activities, and knew of and participated in the fraud perpetrated on Bon Secours.” In its argument, Bon Secours does not distinguish between which facts it is relying upon to support its allegation that E & T is liable as a seller, and which facts support its allegation that E & T is liable as an aider or abettor. Thus it is necessary to go through the facts upon which it relies to determine if they form the basis of liability for E & T under either provision of the Act.

A. *E & T’S INVOLVEMENT WITH NTG AND ITS FINANCING ACTIVITIES*

Bon Secours points out that E & T in 1999 was engaged to help NTG develop a business plan in order to secure financing and that when Spring Capital invested in NTG in 2000, E & T provided Spring Capital with a draft copy of the 1999 year-end statement for the express purpose of facilitating Spring Capital’s investment in NTG. Whatever role E & T played in 1999 in developing a business plan and in 2000 in the Spring Capital investment has no bearing on whether E & T was an aider or abettor for Bon Secours’s investment which was initiated in late 2001 and actually occurred in March 2002.

Bon Secours also alleges that Todd Feuerman served simultaneously as NTG’s Chief Financial Officer and as lead audit partner for E & T. NTG’s Board minutes on January 20, 2000 support this allegation:

The firm of Bengur Bryan & Company is in process of requesting funds from various lenders. Projection is to receive proposals on funds for \$3.5 million by late February and settle in march... *Todd Feuerman will represent NTG as CFO.*

(Emphasis added). Although Feuerman has denied that he ever served as CFO, both Giordani, NTG's COO and Director, and Picciotto, an Outside Director, offered testimony consistent with those minutes. Thus, there is evidence from which a jury could find that Feuerman acted as NTG's CFO at some time during 2000.

However, there is *no evidence* that he acted as CFO during the time that Bon Secours made its investment in 2002. During that period, all of the evidence shows that the CFO was Bray. Thus the fact that Feuerman previously served as CFO cannot form the basis of E & T's liability as seller because there is no evidence that Feuerman was in this role at the time of the Bon Secours investment. Nor can it form the basis of any liability as aider and abettor because Bon Secours had the minutes describing Feuerman's role as CFO and lead auditor.

Bon Secours alleges that E & T is liable because it was "simultaneously providing NTG with audit services and services aimed at obtaining financing for NTG," and in support of that allegation points out that on January 23, 2002, during the time that Bon Secours was considering the investment, Feuerman e-mailed Tobin, "[p]lease let me know if there is anything I can do to assist in the new equity round." Bon Secours also notes that NTG's relationship with Mercantile was problematic in January 2002, and Feuerman began "contacting banks to see who in the industry... would be interested" in providing financing to NTG. There is evidence that Feuerman made many efforts between January and April 2002 to that end but there is no evidence that he participated in any way in the solicitation of Bon Secours.

Bon Secours contends that E & T is liable because it knew that its financial statements would be used for NTG to attract outside investors. Indeed, there are references made by E & T representatives during the audits that the statements would be used for “outside potential investors.” E & T counters that the engagement letters between E & T and NTG required NTG to obtain E & T’s permission to use the audited financial statements and there is no evidence that E & T gave permission to NTG to use them for the Bon Secours investment. However, while there is no evidence that NTG ever obtained such permission, there is evidence from which a jury could find that E & T implicitly gave permission because it was aware that NTG was actively seeking new investors who were conducting a due diligence investigation that could not be done without those statements. However absent a showing of fraud (which is addressed below), knowledge that its earlier audits would be used to attract potential investors is not enough to establish E & T’s liability as a seller or aider and abettor.

Bon Secours argues that E & T is liable because it knew that Bon Secours wanted a draft audit statement for FY 2001. On February 18th 2002 Tobin sent Feuerman an e-mail concerning “completion of due diligence” where she requested “a draft audit document” saying that “[w]e’ll just come to a stand still with the investors if some sort of draft is not provided.” Feuerman replies “I am sure we can pull a draft together quickly but we still need some ‘critical’ information even to prepare a draft.” Attached to this e-mail was an email that Tobin had received from a Bon Secours representative stating “if you already have ... a draft of FY 2001 financial statements (prepared by your accountant),” please provide us a copy. No draft existed at that time, and despite the evidence that Tobin was “demanding” one, none was prepared before Bon Secours made its investment. Thus E &

T's knowledge that Bon Secours wanted a draft audit that did not exist cannot form the basis for E & T's liability.

Bon Secours also alleges that E & T failed to disclose the "going concern" issue with NTG as evidenced by the fact that E & T issued an draft audit in May, 2002, that made no reference to the going concern issue. This draft was prepared *two months* after Bon Secours' investment and thus had no bearing on Bon Secours' decision to invest in NTG. Even Bon Secours' expert acknowledges, E & T was not free to disclose information to Bon Secours from its on-going audit at the time of Bon Secours' investment. In partial recognition of the absence of a duty to it, Bon Secours argues that E & T had a duty to tell the NTG Board about the going concern issues. Assuming that E & T breached its duty to the Board, that breach does not make it liable to Bon Secours.

B. E & T'S KNOWLEDGE AND ALLEGED PARTICIPATION

E & T denies that it even had knowledge of the Bon Secours investment but although Feuerman testified that E & T had no knowledge of Bon Secours' investment, Bon Secours points to evidence upon which a jury could find that it did. Bon Secours first relies upon the e-mail discussed above where Tobin requested a draft audit. As E & T points out, that audit was clearly requested in connection with potential investments by other firms. It states:

Todd,

Is there any way we can come up with a draft audit document. I understand there are some things outstanding We'll just come to a stand still with the investors if some sort of draft is not provided.

The other funds:

Sustainable Job Fund and Kenilworth Holdings have requested a draft. New Sr. Banks have requested draft

(Emphasis added). However because the inquiry about a draft from Bon Secours was attached, a jury could infer that Feuerman was aware of the Bon Secours investment. In addition, there is evidence that Feuerman reviewed draft term sheets that referred to potential investors, including Bon Secours. Also, there is an email from Tobin to Feuerman dated February 11th stating that she is “pushing Smith Whiley for a close on 2/28,” a March 1st e-mail from Feuerman stating that “I trust the company’s closing went fine today—great job!,” and a March 7th e-mail stating: “Tom-congrats on closing.”⁷ These emails suggest Feuerman knew that the closing was originally scheduled for March 1st and was then changed to March 4th.

Of course, simple knowledge of the fact that Bon Secours was making the investment is not sufficient to show that E & T was a seller or aider and abettor. Bon Secours relies on the fact that Feuerman represented NTG as its CFO and accountant, and participated in offering NTG securities and soliciting offers to Spring Capital. For the reasons discussed above, neither of those facts show that E & T was a seller or aider and abetter. Bon Secours also argues that E & T’s actions in contacting lenders on NTG’s behalf and reviewing the term sheets of Bon Secours and other potential investments, are *tantamount* to actively assisting in offering securities for sale and soliciting offers to buy.

E & T’s contacting banks as potential lenders and even its solicitation of other investors (of which there is no evidence) does not make it a seller or aider or abetter in the Bon Secours investment. Thus the only question is whether E & T’s review of the term sheets, unknown to Bon Secours, is “*tantamount* to actively assisting in offering securities

⁷The original closing date was March 1st and was later changed to March 4th.

for sale and soliciting offers to buy,” thereby establishing primary and/or secondary liability under the Act. As a matter of law it is not.

C. E & T'S KNOWLEDGE OF AND PARTICIPATION IN THE FRAUD

Bon Secours claims that E & T participated in and had knowledge of the fraud as evidenced by E& T's knowledge of (1) the Nationwide Trenching claim; and (2) the failure to record all accounts payables.

_____1. Nationwide Trenching Claim

Bon Secours alleges that E & T worked with NTG management to not disclose an \$880,000 claim Nationwide Trenching had against NTG. Nationwide Trenching had done trenching work on behalf of NTG for another company, Adesta, and as stated earlier Adesta went into bankruptcy. Tobin disputed the amount of the Nationwide Trenching claim and according to her she first spoke to Feuerman about the claim in April 2002, which is at least a month after Bon Secours' investment. NTG's Controller Baker testified that she overheard a discussion between Feuerman and Tobin on the Nationwide Trenching claim as early as January 2000, but Tobin had no recollection of any such conversation. Baker's testimony about the conversation appears to be inadmissible hearsay, but for purposes of this motion the Court need not determine if it is because there is other evidence from which a jury could find that E & T knew about the Nationwide Trenching suit in January 2002.

Although Tobin testified that she does not recall discussing the Nationwide Trenching lawsuit with anyone other than the lawyer working on the Adesta bankruptcy, NTG's CFO Bray testified that he and Tobin told Feuerman about the Nationwide Trenching lawsuit in January 2002. Furthermore Greg Hinkleman, who was the COO for

Nationwide Trenching has stated in an affidavit that in late 2001 he received a letter from E & T asking him to confirm that NTG owed Nationwide Trenching approximately \$500 and then called E & T and spoke to someone who identified herself as “Aileen”⁸ and told her that NTG in fact owed Nationwide Trenching over \$2 million and that Nationwide Trenching was in the process of suing NTG for \$880,000. He states that he sent a copy of the complaint to E & T but he cannot recall if he sent a draft complaint before the suit was filed or a copy of the complaint that had been filed. Nationwide Trenching filed suit on January 24, 2002 and lawyers entered an appearance for NTG on March 15, 2002.

Bon Secours argues that E & T had a duty to tell it about the Nationwide Trenching suit as a result of an e-mail Tobin sent to Feuerman asking him to “fax Smith Whiley’s attorney copies of letters from attorneys to Ellin & Tucker for each audit.” E & T faxed to Smith Whiley’s attorney a letter dated February 6, 2002 stating that there are no claims against NTG “of any kind, ...*associated with this litigation* [the Adesta bankruptcy].” (emphasis added). On February 26, 2002, that same lawyer was retained by NTG to represent it in the suit brought by Nationwide Trenching. That lawyer has signed an affidavit that the February 6th letter was accurate and was written in response to an inquiry from E & T in connection with the audit they were doing. That attorney also states that at the time the letter was written she was unaware of any other litigation involving NTG.

Assuming that E & T knew about the Nationwide Trenching claim, E & T was not obligated to verify the accuracy of the letter before faxing it; nor is there any evidence that it purported to do so. When Smith Whiley’s attorney received the letter, he was in a position to verify its

⁸Aileen Eskildsen was one of the E & T auditors working on the NTG audit.

contents and ask any follow up questions, which would have been properly directed to the author of the letter, not E & T. By faxing it, E & T made no representation other than that it had received the letter. As to the claim that E & T failed to include the Nationwide Trenching claim in accounts payables, the preliminary year-end statement, that allegedly wrongfully excluded the Nationwide Trenching claim did not come out until two months after Bon Secours' investment. Thus it could not form the basis for liability to Bon Secours for its March investment.

2. Failure to Record Account Payables

As early as January 2002 Feuerman noted in his audit field handwritten notes that "there seems to be a lot of A/P [account payables] not recorded \$400k." Eskildsen, another E & T auditor, testified in January she got accounts payable from NTG that were inconsistent with the general ledger entries and pointed out the inconsistencies to NTG's CFO Baker. When Eskildsen attempted to obtain the original inaccurate report, Baker advised Eskildsen that she had thrown it away. During this same time period, Eskildsen also reviewed documents provided by NTG accounts receivable manager, Bonnie Towner, which showed that January 2002 deposits had been backdated to December 2001. Towner was unable to provide a satisfactory explanation and after speaking with Feuerman, E & T proposed an adjustment which was never signed off on by NTG.

E & T's expert, Barsky testified that E & T could not ethically disclose the information obtained in its audit process to non-clients. Bon Secours' expert Demchick testified that an accountant could not have revealed any information about the incomplete 2001 audit without the consent of NTG. NTG's other expert, Epstein acknowledged that direct communication with Bon Secours would have created a conflict. Thus, because E

& T was in the process of conducting its audit, it is clear that E & T could not have disclosed the information it was uncovering.

Bon Secours claims that E & T was under an obligation in January 2002 to discuss the Nationwide Trenching claim and the account payable problem with NTG's Board of Directors prior to the time of Bon Secours's investment, but even if E & T had such a duty and failed to fulfill it, there is nothing to show that failure to notify the NTG Board turned E & T into "sellers" or "aiders and abettors" under the Securities Act. *See Central Bank of Denver v. First Interstate Bank of Denver*, 511 U.S. 164, 174 (1994) ("When an allegation of fraud is based upon nondisclosure, there can be no fraud absent a duty to speak.").⁹

_____*D. NO EVIDENCE OF AIDING OR ABETTING*

_____Not only is there no evidence from which a jury could find that E & T solicited Bon Secours to purchase the securities, there is no evidence from which a jury could find that E & T was a control person or an agent who materially aided the sale. Subsection (c)(1) provides:

(c)(1) Every person who **directly or indirectly controls** a person liable under subsection (a) of this section, every partner, officer, or director of the person liable, every person occupying a similar status or performing similar functions, every employee of the person liable who materially aids in the conduct giving rise to the liability, and **every** broker-dealer or **agent who materially aids in such conduct** are also liable jointly and severally with and to the same extent as the person liable, unless able to sustain the burden of proof that he did not know, and in exercise of reasonable care could not have known, of the

⁹The Court also notes that its attention has not been directed to the testimony of any expert who said that E & T should have discovered *the fraud* earlier than it did.

While the parties dispute the admissibility of certain opinions of Bon Secours expert Epstein, assuming that all of the opinions listed in his report are admitted, there is no opinion with respect to the discovery of the fraud.

existence of the facts by reason of which the liability is alleged to exist.

(Emphasis added.) As the Court noted in *Baker, Watts*, the “ability to persuade and give counsel is not the same thing as ‘control.’” 95 Md. App. at 176. “*Control* almost always means the practical ability to *direct* the actions,” of those selling the securities. *Id.* (emphasis in original). “Controlling person is one who has power to direct the management and policies of the person held liable.” *Id.* (citation omitted). In order to be considered a control person, an individual must actively participate in the overall management and operation of the controlled entity.” *Id.* (Citation omitted). *At best* the evidence is sufficient to show that E & T was in a position to give counsel to NTG concerning the sale to Bon Secours. It was not in a position to direct NTG officers or directors. Nor is there evidence that E & T “materially” aided the sale. As the *Baker, Watts* Court recognized:

To hold an individual to be an *agent* who has participated or aided in *making sales* of securities, the Court must find that the individual was so entangled in the actual sale of the security *that his activities were at least a substantial factor in the purchaser's decision to buy the security* and that his activities were either authorized by or ratified by the issuer.

95 Md. App. at 169 *citing In re N. Am. Acceptance Corp. Sec. Cases*, 513 F.Supp. 608 , 623 (N.D.Ga.1981) (emphasis in original and added). As the Court stated in *Prince v. Brydion*, 764 P.2d 1370, 1371 (Or. 1988), whether participation in a sale is “material,” “depends on the importance of one’s personal contribution to the transaction.”

There is simply no evidence upon which a jury could find that the activities of E & T were a “*substantial factor*” in Bon Secours’ decision to invest in NTG. Bon Secours argues that E & T failed to give timely information to NTG’s Board of Directors and “to

disclose complete and accurate information in response to Bon Secours' due diligence attorney letter request." As stated previously, any failure of E & T to fulfill its duty to the Board of Directors of NTG did not create liability to Bon Secours. Also as discussed above, there is no evidence that E & T participated in the due diligence investigation conducted by Bon Secours. There is no evidence that Bon Secours knew that E & T reviewed the term sheets, and certainly no evidence that Bon Secours relied upon that review. Nor could a jury conclude based on the evidence before the Court that E & T's fax of the letter to Smith Whiley's attorneys was a "substantial factor" in the decision. And because E & T *did not* issue a draft preliminary audit before Bon Secours invested, whatever it did, or failed to do in its preliminary audit was not a factor at all in Bon Secours' investment decision.

NEGLIGENCE CLAIMS

Both the Outside Directors and E & T argue that the negligence claims should be dismissed because they did not owe Bon Secours a duty of care,¹⁰ and if they did, they did not breach it, and if they did Bon Secours' contributory negligence operates a bar to recovery. The Outside Directors also argue that Bon Secours lacks standing to assert the negligence claims because they are derivative.

OUTSIDE DIRECTORS

In order to show that the Outside Directors were negligent, Bon Secours must establish that the Outside Directors owed Bon Secours a "duty of care." *Cooper v. Berkshire Life Ins. Co.*, 148 Md. App. 41, 57 (2002). Directors of a corporation do not owe a duty to

¹⁰Perhaps because there is no evidence to support it, Bon Secours has not pressed its claim that the directors negligently supervised Tobin, Bray and Baker.

third-parties dealing with the corporation simply because of their status as directors. One commentator noted:

A director or officer must participate in the tort in order to be liable therefor. The liability arises from one's conduct, not one's status as director or officer.

1 William E. Knepper & Dan A. Bailey, *Liability of Corporate Officers and Directors* § 6.07 at 6-15 (7th ed. 2003); *See also Lobato v. Pay Less Drug Stores, Inc.*, 261 F.2d 406, 408-09 (10th Cir. 1958) (holding that merely being an officer or agent of a corporation does not impose personal liability for acts of corporation); *Insurance Co. of N. Am. v. Miller*, 362 Md. 361, (2001). *See also Jordan v. Earthgrains Companies, Inc.*, 576 S.E.2d 336, 340 (N.C. Ct. App. 2003) (negligent misrepresentation claim against the president and CEO of corporation was dismissed because he owed no duty to individual employees). Therefore, in order to show that the Directors owed it a duty of care, Bon Secours must rely on something more than their status as directors.

A duty of care to avoid causing an economic loss to another requires “an intimate nexus between the parties,” which is satisfied by “contractual privity or its equivalent.” *Jacques v. First National Bank*, 307 Md. 527, 538 (1986). *See also Noble v. Bruce*, 349 Md. 730 (1998) (“In general, if the risk created by negligent conduct is merely one of economic loss, no tort duty will be found absent a showing of privity or its equivalent.”); *Huntington Mortgage Co. v. Mortgage Power Fin. Servs., Inc.*, 90 F. Supp.2d 670, 67 (D. Md. 200) (“Maryland law requires that contractual privity, [or its equivalent], exist between the parties for a claim for negligent misrepresentation to lie.”). There is no evidence of a contractual relationship between the Outside Directors and Bon Secours. As discussed above, the

Outside Directors were clearly not “sellers” and Bon Secours did not have an “intimate” relationship with any of the Outside Directors that rises to the level of contractual privity.

Because the Outside Directors did not owe Bon Secours a duty of care, all of the negligent claims against them fail.¹¹

ELLIN & TUCKER

In addressing the negligence claims against E & T, both parties cite *Walpert, Smullian & Blumental v. Katz*, 361 Md. 645 (2000). There the Court held that an accountant may be liable to a third party where three factors are present:

(1) the accountants must have been aware that the financial reports were to be used for a particular purpose or purposes; (2) in the furtherance of which a known party or parties was intended to rely; and (3) *there must have been some conduct on the part of the accountants linking to that party or parties, which evinces the accountants' understanding of that party or parties' reliance.*

Id. at 674 citing *Credit Alliance Corp. v. Arthur Andersen & Co.*, 483 N.E.2d 110, 118 (1985) (emphasis added).

Elaborating on the third factor, the Court stated that “the required linking conduct,” must be conduct “of the accountant” which “evinces the accountant’s knowledge of the plaintiff’s reliance.” *Walpert*, 361 Md. at 692. The evidence must show that the accountant understood “that party's reliance.” *Id.* at 693. “All that is required is that the trier of fact could find that the evidence suffices to appraise the [accountant] of ... the purpose for which its work product is to be used, who is intended at the time of the engagement to use it for that

¹¹If the Outside Directors were negligent, the harm that resulted was harm to NTG and therefore the claim is derivative and cannot be brought by Bon Secours for its benefit. See *Danielewicz v. Arnold*, 137 Md. App. 601, 616-19 (2001)

purpose and some connection with that party that is the equivalent of privity, such as knowledge of that party's reliance.” *Id.* There is no requirement that the accountant directly communicate with the third party or “otherwise act in some manner specifically calculated to induce reliance on the report.” *Id.* (Citation omitted.)

In *Walpert* there was evidence of all three factors. There was evidence that the accounting firm “was aware that the financial report was going to be used for a particular purpose, i.e., to help [the plaintiff] decide whether to make the \$425, 000 loan...” Further, the accounting firm knew that the plaintiff “was going to rely on [its] financial report, because [the plaintiff] informed [the accountant’s representative] of this fact at a face-to-face meeting.” *Id.* at 694. Finally, “there was sufficient [evidence of] conduct on the part of [the accounting firm], through [its representative], to meet the 'linking conduct,' [The representative] met with [the plaintiff] to discuss [the company’s] financial condition in order for [the plaintiff] to determine whether to 'lend money to [the company].’ Moreover, [the representative] gave a copy of the 1989 audit *directly* to [the plaintiff].” *Id.* (emphasis added in original).

Here there is no evidence of any “linking conduct,” which is the third factor --- “some conduct on the part of the accountants linking to that party...which evinces the accountants’ understanding of that party[’s] reliance.” Initially the Court notes that the PPM and the Addendum warned that the accountant had not reviewed the financial information.

The Company’s independent accountants, Ellin & Tucker, Chartered, have not examined or reviewed the historical information or projections presented herein and accordingly assume no responsibility for them.

There is no evidence that despite this warning, there was any type of relationship between

Bon Secours and E & T. As discussed above, except for E & T faxing a letter it had not authored, there was no communication directly between them.¹² There were no other e-mails, and no phone calls or face to face contacts. The first direct communication occurred at the June 26, 2002 Board meeting, three months after the investment was made.

Although direct communication is not required, there must be “*some* connection with that party that is the equivalent of privity.” (emphasis added.) In *Security Pacific Bus. Credit, Inc. v. Peat Marwick Main & Co.*, 79 N.Y.2d 695, 586 N.Y.S.2d 87, 597 N.E.2d 1080 (1992), the plaintiff relied on a “telephone call from its vice-president to the defendant's audit partner during, and with respect to, the applicable audit and the audit work papers the client supplied the plaintiff.” *Walpert*, 361 Md. at 691. The Court held that was not sufficient to establish a relationship.

The fact that E & T was aware of the date of closing is not evidence of a relationship between Bon Secours and E & T. Nor is a connection between the parties established by the fact that E & T had knowledge that Bon Secours had requested a copy of the draft audit of 2001 *if one existed* (especially since no draft existed). As stated earlier, E & T did not participate at all in Bon Secours' due diligence investigation and had no way of knowing what information Bon Secours did or did not have. The only contact, the fax sent to Smith Whiley's attorneys, is significantly less communication than the phone call in *Security Pacific Bus. Credit*.

¹²This contrast sharply with the March 22, 2000 where Feuerman provided NTG with a draft copy of the 1999 year-end statement for the express purpose of facilitating Spring Capital's investment.

CONTRIBUTORY NEGLIGENCE

Finally, if the Outside Directors and E & T were negligent, Bon Secours' negligence claims are barred by contributory negligence.¹³ "Contributory negligence [is] a complete bar to recovery." *Prudential Securities Inc. v. E-Net, Inc.*, 140 Md. App. 194, 226 (2001) Contributory negligence is an absolute bar "no matter how slight the [plaintiff's] fault may be." *E.F. Hutton Mortg. Co. v. Pappas*, 690 F. Supp. 1465, 1475-76 (D. Md. 1988). In *E. F. Hutton*, the plaintiff, who had purchased high risk mortgage loans, sued its accountant for failing to discover the seller's fraud. In rejecting the claim the court stated:

Hutton...knew these were high risk loans made to desperate borrowers by a lender of last resort. Before accepting these loans in its portfolio, Hutton had every opportunity to review all the loan papers and decide whether or not each loan should be purchased.

669 F. Supp. at 1476. In *Banca Cremi v. Alex Brown*, 955 F. Supp. 499, 515 (D. Md. 1997), the Court noted the "sophistication" of the plaintiff in finding that contributory negligence barred a negligence claim by an investor against its security broker for a failed investment. A plaintiff "who voluntarily consents, either expressly or impliedly, to exposure to a known risk cannot later sue for damages from exposure to that risk." *Prudential Sec., Inc. v. E-Ney, inc.*, 140 Md. App. at 226 (internal quotations and citations omitted).

As a sophisticated investor making a high risk investment, Bon Secours had every opportunity to review all the information and make an independent judgment. Further, Bon Secours had as much, if not more information than the Outside Directors about the financial state of NTG, but did not detect the fraud or any other financial problem that caused it to

¹³The facts showing that Bon Secours was contributorily negligent also show that as a sophisticated investor, Bon Secours had all the information that these defendants had and thus was not misled by *these* Defendants. See discussion at pages 12-13 above.

decide not to invest. The information that Bon Secours had before it has been discussed throughout this opinion and is only summarized here.

Smith Whiley prepared for Bon Secours an “Investment Review” that was an in-depth analysis of NTG’s financial statements, management, and business plan. Smith Whiley “stress-tested” the numbers and developed its own independent financial projections for the company. Smith Whiley noted various risks associated with a potential investment in NTG such as its limited history of operations and the fact that it was highly leveraged and would need additional capital to implement its business plan. Smith Whiley knew that NTG was highly susceptible to a slow down in the telecommunications industry and only a handful of customers accounted for most of its business. Prior to the investment, Smith Whiley had minutes from NTG Board meetings. Its attorneys had minutes from 2000 Board meetings. Smith Whiley was aware that other fund investors were concerned about NTG’s financial condition.

All of the financial information that Smith Whiley received in connection with its due diligence was received directly from NTG or from its investment banker, FBW. Smith Whiley was aware that: NTG did not have an audit for the first year it was in business, 1998; NTG’s last audited financial statement was for December 31, 2000; audited statement of 1999 showed that NTG had operated at a loss; and audited statement for 2000 showed NTG had high debt and not enough equity. Smith Whiley received interim financial statements monthly from NTG and business projections prepared by NTG. Smith Whiley knew that NTG had experienced tremendous growth each year and NTG was seeking to raise at least 4 million in order to meet its contract obligations.

Bon Secours conducted additional due diligence that included obtaining all financial materials provided to NTG's Board, including internally prepared financial statements for year end 2001, and revised budgets and financial projections, customer lists, contract lists, a breakdown of revenue by contract, and accounts receivable. Bon Secours also obtained and relied upon due diligence compiled by several other funds who were considering an investment in NTG. Its attorneys performed additional due diligence and reviewed the legal documents for all previous loans and investments, minutes from all of NTG's Board of Directors meetings, NTG's major contracts and subcontractor agreements, and the audit responses that E & T had received from NTG's law firms.

Despite the fact that NTG's \$4 million offering was only partially purchased, Bon Secours moved forward with its \$1 million investment on the hope of getting a return of 25% per annum. In other words, they gambled and lost.

CONCLUSION

For all the reasons stated above, this Court will enter an order: (1) granting the Motions for Summary Judgments filed by Defendants Zietz and Stewart against Plaintiff Bon Secours and Cross Claimants Baker and Bray, (2) granting the Motion for Summary Judgment filed by E & T and (3) granting Bon Secours' Motion for Summary Judgment against NTG.

Dated: May 17, 2004

JUDGE EVELYN OMEGA CANNON