

IN THE COURT OF COMMON PLEAS OF LYCOMING COUNTY, PENNSYLVANIA

PAUL SEMO, RICHARD HINKLE,	:	NO. 03-00,299
JEAN RECLA, Individually and on	:	
behalf of others similarly situated,	:	
Plaintiffs	:	
	:	
vs.	:	
	:	CIVIL ACTION - LAW
JOHN BAUSCH, WALNUT STREET	:	
SECURITIES, INC., INTERSECURITIES,	:	
INC., COMMONWEALTH EQUITY	:	
SERVICES, INC.,	:	
Defendants	:	Motions for Summary Judgment

OPINION AND ORDER

Before the Court are the motions for summary judgment filed by Defendant Walnut Street Securities, Inc. (Walnut Street) and Commonwealth Equity Services, Inc. (Commonwealth Equity) on July 20, 2005, and August 3, 2005, respectively, as well as Plaintiff’s Motion to Strike those motions, filed August 17, 2005. Argument on all motions was held September 7, 2005.

This action arises from the purchase by Plaintiffs of promissory notes issued by the Premium Finance Trust and the Premium Finance Trust II, from Defendant Bausch who, at various times, was an authorized agent of the corporate defendants. In their complaint, Plaintiffs seek recovery from defendants on the basis of negligence, breach of statutory duty and breach of fiduciary duty, both directly and vicariously based on the agency relationship between Bausch and the corporations. In their motions for summary judgment, Walnut Street and Commonwealth Equity argue (1) the claim for negligence fails as a matter of law because a broker-dealer owes no duty of care to a purchaser where there is no relationship between the broker-dealer and the purchaser, (2) the claim for breach of fiduciary duty fails as a matter of law because no fiduciary duty arises without a fiduciary relationship, (3) the claim for breach of statutory duty fails as a matter of law because the statute gives a private cause of action to only a seller or buyer and that here there was no seller-buyer relationship, and (4) the claims based on vicarious liability fail as a matter of law because the corporations cannot be liable for Bausch’s actions unless Plaintiffs can show that they fell within the scope of his authority or

that the corporations ratified those actions. Defendants point to the deposition testimony of Plaintiffs which indicates Plaintiffs held no accounts with Defendants, never consulted Defendants, never communicated with Defendants, and in fact had never heard of Defendants until the instant lawsuit was initiated. In dealing with Bausch, Plaintiffs did not rely on his association with Defendants, as they had no knowledge of such. Defendants also point to evidence that no commissions on the sale of the notes were received by them. Plaintiffs do not dispute the lack of a relationship between Plaintiffs and the corporate defendants, or that Defendants received no financial benefits from the transactions, but argue that the corporate defendants are liable based on the concept of “an undisclosed principal”.

Initially, with respect to Plaintiffs’ Motion to Strike, Plaintiffs argue that the motions for summary judgment are premature inasmuch as discovery has yet to be completed. Plaintiffs argue that expert reports remain to be provided. The Court fails to see how any expert report, which would address the issue of the standard of care to be exercised by a corporation in supervising its agent, could affect the issues presented herein. The dispositive facts come from the Plaintiffs’ depositions, as well as documentation, which have already been provided in discovery. Plaintiffs’ Motion to Strike is therefore without merit.

With respect to the claim of negligent supervision, the Court agrees with Defendants that Plaintiff cannot establish the requisite duty when the facts indicate there was no relationship between Plaintiffs and the corporations. The Superior Court has held that a broker-dealer’s duty of supervision does not extend to customers of an agent whose accounts were not placed with the broker-dealer. Cover v. Cushing Capital Corporation, 497 A.2d 249 (Pa. Super. 1985), and while there is authority to suggest that “customer status may not be needed” to establish vicarious liability for the acts of an agent, Morgan v. Staats, 1988 U.S. Dist. LEXIS 1580, (W.D. Pa. Jan. 22, 1988), that same authority refused to extend liability to a broker-dealer where the evidence indicated the plaintiff did not rely on the broker-dealer in making his investment, explaining that “under Pennsylvania respondeat superior case law, it is clear that justifiable reliance is required. Off-book customers of the agent are required to show such reliance on the broker-dealer.”

With respect to the claim of breach of fiduciary duty, the same facts prevent a finding that the corporations owed a fiduciary duty to Plaintiffs. Where there is no contractual

relationship, and no confidential relationship, there can be no fiduciary duty. Kohn v. Optik, Inc., 1993 U.S. Dist. LEXIS 7298 (C.D. Cal. April 2, 1993).

With respect to the claim of breach of statutory duty, the Pennsylvania Securities Act provides for a cause of action for only a buyer or seller, and since the corporations here are not sellers of the notes in question, this claim also fails. 70 Pa.C.S. Section 1-501.

With respect to the claims based on vicarious liability, as noted above, such claims are based on the agency relationship between Bausch and the corporate defendants. Defendants argue they cannot be held liable where there is no evidence that Bausch had authority (either explicit or implicit) to act on their behalf in selling the notes in question. Plaintiffs contend no such evidence is necessary, and that liability can be imposed under Section 261 of the Restatement (Second) of Agency. That Section provides:

A principal who puts a servant or other agent in a position which enables the agent, while apparently acting within his authority, to commit a fraud upon third persons is subject to liability to such third persons for the fraud.

Plaintiffs emphasize the Comment to that section, which provides:

The principal is subject to liability under the rule stated in this Section although he is entirely innocent, has received no benefit from the transaction, and, as stated in Section 262, although the agent acted solely for his own purposes. Liability is based upon the fact that the agent's position facilitates the consummation of the fraud, in that from the point of view of the third person the transaction seems regular on its face and the agent appears to be acting in the ordinary course of the business confided to him.

Restatement (Second) of Agency, Section 261, Comment a. What Plaintiffs fail to recognize, however, is that this section requires apparent authority, and such can arise only where the principal is known to the buyer and the buyer relies on the principal's involvement or reputation. See American Society of Mechanical Engineers, Inc. v. Hydrolevel Corp., 456 U.S. 556 (1982) (liability under Section 261 is based upon the fact that the agent's position facilitated the consummation of the fraud and that the agent's statements appeared to a third person to have the full weight of the principal's reputation behind them); Dark v. United States, 641 F.2d 805 (C.A. 9th Cir.) (where an agent secretly intends to act for a purpose of his own and not on his principal's behalf, he can still bind the principal by his acts where one relies on facts which indicate apparent authority: as far as the third party bettors were concerned, the bets

were taken on behalf of the employer). Since in the instant case there is no dispute Plaintiffs did not purchase the notes in question based on any apparent authority provided by the corporate defendants to Bausch, inasmuch as they had no idea the corporate defendants had any involvement with Bausch, Plaintiffs claims based on vicarious liability necessarily fail.

Accordingly, no issues of material fact remaining, and it appearing Walnut Street and Commonwealth Equity are entitled to judgment as a matter of law, entry of summary judgment in their favor is appropriate.

ORDER

AND NOW, this 15th day of September 2005, for the foregoing reasons, the motions for summary judgment filed by Walnut Street Securities, Inc. and Commonwealth Equity Services, Inc. are hereby granted, and judgment is hereby entered in favor of Walnut Street Securities, Inc. and against Paul Semo, and in favor of Commonwealth Equity Services, Inc. and against Jean Recla.

BY THE COURT,

Dudley N. Anderson, Judge

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