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## Securities Sales Not Subject To Fraud Act: NJ Court

By **Christie Smythe**

Law360, New York (June 05, 2009) -- The New Jersey Supreme Court has ruled that a broker accused of failing to properly transfer funds for the purchase of securities and the firm that employed him — First Union Brokerage Services Inc., now part of Wells Fargo & Co. — can't be held liable under the state's Consumer Fraud Act.

The state high court on Wednesday affirmed a lower court's decision that the plaintiff, Margaret L. Lee, can't pursue claims under the state law, which allows for the recovery of treble damages and court costs.

In coming to that conclusion, the court evaluated whether securities were included in the CFA's definition of "merchandise" and whether there was a distinction between the purchase of a security and the purchase of the service to buy the security.

"We hold that the sale of securities is not covered under the CFA and that recognition of a separate 'service' to purchase securities would thwart the CFA's design to keep the sale of securities beyond the CFA's application," the state Supreme Court said.

The dispute stems from an incident in 2000, when Lee received \$12,000 from a personal injury settlement and sought to invest about \$2,000 of the funds in purchasing shares of mutual fund, Evergreen Omega, according to the opinion.

Lee opened a brokerage account with First Union and gave securities broker Gregory Mack the \$2,000 to effectuate the purchase, the opinion said.

However, Mack did not deposit the funds into a brokerage account as requested, leaving Lee with insufficient funds to make the transaction, according to the high court. First Union's banking unit applied about \$500 from Lee's checking account, then liquidated

about \$1,500 of the mutual fund's units, which had been allocated to the account.

Lee claims that after contacting Mack, she discovered that he had stolen the money and offered to pay her \$1,500 if she would agree not to tell his supervisor about the action, the opinion said. Lee, however, maintains that she would not accept less than \$2,000 and initiated the lawsuit against Mack and First Union.

In 2006, Lee filed her suit, which was dismissed by the trial court in part because of a two-year statute of limitations in the New Jersey Uniform Securities Law, the opinion said.

The trial court also found that Lee failed to state a claim under the CFA because "the CFA is inapplicable to the sale of securities," the high court said.

On appeal, however, the New Jersey Superior Court's Appellate Division reversed the trial court's dismissal of both counts, concluding that the trial court had inappropriately applied the two-year statute of limitations when Lee's complaint should have been subject to a six-year statute of limitations, according to the ruling.

On the CFA count, the appeals court found that while the sale of securities may not be covered by the statute, the unlawful act at issue was actually the misappropriation of funds, which could be construed to be covered under the "services" section of the law, the opinion said.

However, the state Supreme Court, which agreed to hear the case only to address the CFA issue, found that the legislative intent for the act was for it not to include securities under the definition of merchandise.

"Similarly, we conclude that the present matter should not be contorted to achieve coverage under the CFA by calling Mack's conduct a fraudulent 'service' in order to draw it within the CFA's reach," the Supreme Court said. "Doing so thwarts the legislative design that the Act not intrude in the area of securities sales."

Thomas B. Lewis, an attorney with Stark & Stark who represents First Union, said that the court "had a proper, well-reasoned opinion in not applying the New Jersey Consumer Fraud Act to the sale of securities."

Doing so could be harmful to banks and brokerage houses, as the ramifications of applying the statute to such sales could be "mind-

boggling” because of the treble damages and court costs provisions, Lewis said.

Henry Gurshman, an attorney representing the plaintiff, said he was disappointed with the ruling and noted that earlier case law had expanded the scope of the Consumer Fraud act.

The defendants are represented by Stark & Stark.

The plaintiff is represented by Henry Gurshman.

The case is Margaret L. Lee v. First Union National Bank et al., case number A-58-08, in the Supreme Court of New Jersey.

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