

## Silvergate Must Face Investor Suit Over FTX Ties, Judge Says

By **Katryna Perera**

Law360 (March 21, 2024, 11:13 PM EDT) -- The now-defunct Silvergate Bank and its CEO must face a proposed class action brought by customers of bankrupt cryptocurrency exchange FTX, a California federal judge ruled Wednesday, finding that Silvergate owed a duty to FTX customers and that its conduct harmed them.

U.S. District Judge Ruth Bermudez Montenegro issued an **order** on Wednesday denying a **dismissal motion** filed by the defunct bank in June in which it argued that the customers' negligence proposed class claim can't go forward because Silvergate "did not owe plaintiffs — customers of FTX, not [Silvergate] — any duty of care."

The FTX Trading Ltd. customer group bringing claims against Silvergate alleges the bank knowingly facilitated FTX's "dissipation" of extraordinary sums of money in the lead-up to the exchange's November 2022 collapse, which rocked the fintech sector and led federal prosecutors to level fraud, money laundering and campaign finance charges against FTX founder Sam Bankman-Fried the following month.

The FTX customers' complaint accuses the bank of failing to "account for its actions and inactions" regarding its relationship with FTX. It notes that the run on deposits that led to Silvergate's failure was precipitated by FTX's own collapse.

Judge Montenegro disagreed with Silvergate's assertion that it did not owe a duty of care to the FTX customers, noting that FTX customers were the intended beneficiaries of the Silvergate Exchange Network, a "virtually instantaneous" payment network for digital currency industry participants.

Based on the framework of this network and its instantaneous nature, it was foreseeable that "allowing FTX customer funds to be deposited into non-FTX accounts would lead to fraud and harm the owners of those funds," the judge said.

Their injury was certain, the judge said, and the customers have adequately alleged that Silvergate benefited from FTX's fraud.

"Silvergate had a strong incentive to continue accepting FTX and Alameda customer deposits and executing transfers because Silvergate's business centered around the adoption of the FTX exchange platform and app," the judge said. "Silvergate also earned income from transaction fees and interest on money deposited in FTX accounts."

According to the order, Silvergate argued in its dismissal motion that its alleged conduct was not a "substantial factor" in causing the customers' injury since their inability to withdraw their deposited funds was a direct cause of fraudulent actions by FTX and Bankman-Fried. Additionally, the bank argued that had it not processed the FTX transfers, the exchange would have simply found another bank.

However, Judge Montenegro disagreed and said the suggestion that FTX would have found another bank "is highly speculative."

Silvergate also moved for dismissal of the customers' aiding and abetting claims, saying they fail because there is no evidence that Silvergate had any "actual knowledge" of FTX's wrongdoings, and FTX and Bankman-Fried did not owe any fiduciary duties to their customers as a matter of law.

Again, the judge disagreed, saying the customers adequately and directly alleged that Silvergate knew about FTX's fraudulent scheme and that FTX owed a fiduciary duty to its customers.

"Plaintiffs allege defendants discovered through their compliance and due diligence programs that FTX and Alameda never retained an outside auditor, never generated audited financial statements, did not observe corporate formalities, accepted several billion dollars from FTX customers which was deposited in trading accounts in the name of or associated with Alameda, and more. Therefore, the court finds that plaintiffs have adequately pled 'actual knowledge,'" the order said.

Judge Montenegro added that the allegations "sufficiently plead several theories under which a fiduciary relationship existed between plaintiffs and FTX — one based on contract, one based on FTX's representations that they would act for the benefit of its customers, and one based on the confidential relationship between FTX and its customers."

Representatives for the parties did not immediately respond to requests for comment on Thursday.

The customers are represented by Daniel C. Girard, Adam E. Polk and Tom Watts of Girard Sharp LLP, Jack Fitzgerald, Paul K. Joseph, Melanie Persinger, Trevor M. Flynn and Caroline S. Emhardt of Fitzgerald Joseph LLP, Timothy G. Blood, Thomas J. O'Reardon and James M. Davis of Blood Hurst & O'Reardon LLP, Michael J. Reiser, Matthew Reiser and Isabella Martinez of Reiser Law PC, Jason Kellogg, Victoria J. Wilson and Marcelo Diaz-Cortes of Levine Kellogg Lehman Schneider & Grossman LLP and Jason S. Hartley and Jason M. Lindner of Hartley LLP.

The defendants are represented by Polly Towill, John M. Landry and Madalyn A. Macarr of Sheppard Mullin Richter & Hampton LLP.

The case is *Bhatia et al. v. Silvergate Bank et al.*, case number 3:23-cv-01406, in the U.S. District Court for the Southern District of California.

--Editing by Brian Baresch.

All Content © 2003-2024, Portfolio Media, Inc.