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UNITED STATES DISTRICT COURT

NORTHERN DISTRICT OF CALIFORNIA

SAN FRANCISCO DIVISION

EMILY FAIRBAIRN and MALCOLM FAIRBAIRN,

Plaintiffs,

v.

FIDELITY INVESTMENTS CHARITABLE GIFT FUND,

Defendant.

Case No. 3:18-cv-04881-JSC

PLAINTIFFS' FURTHER OPPOSITION TO DEFENDANT'S MOTION *IN LIMINE* NO. 5 REGARDING RESTORATION OF DAF LOSSES

Hon. Jacqueline Scott Corley

INTRODUCTION

At the motion to dismiss stage, Fidelity argued that the question on Plaintiffs' negligence claim for loss-restoration was whether Plaintiffs have "a sufficient special interest" to "enforce a charitable trust." MTD Order, ECF No. 39 at 9 (citation omitted); MTD, ECF No. 21 at 20 (claiming only Attorney General may sue to "prevent breaches of trust" (citation omitted)). Given Fidelity's argument and this Court's ruling that Plaintiffs have standing, Plaintiffs have since litigated their negligence claim for restoration of DAF losses primarily under the breach of trust rubric, consistent with case law permitting "an action against trustees based on negligence." *Lynch v. John M. Redfield Found.*, 9 Cal. App. 3d 293, 302 (1970). Viewed through that lens, it is clear that Plaintiffs may seek the remedy of surcharge to require Fidelity to restore losses to Plaintiffs' DAF.

Because of space constraints and Plaintiffs' understanding of the Court's request at the final pretrial conference, this brief will focus on surcharge. But even if the Court rejects the surcharge remedy, it will ultimately need to consider the full range of remedies sought by the Fairbairns. Plaintiffs seek legal, equitable, and declaratory relief on *all* claims to redress *both* their tax injury and the injury to their substantial interest in directing DAF assets to charities they support. Fidelity does not dispute that Plaintiffs may seek tax damages. But the Fairbairns also permissibly seek equitable relief to remedy the DAF losses that Fidelity caused. The Court must consider, at minimum: specific performance; appropriate relief on plaintiffs' equitable claim for promissory estoppel; and injunctive or declaratory relief requiring Fidelity to grant Plaintiffs advisory privileges over assets equivalent to the losses it caused (using either its substantial revenues generated by account fees or its assets not designated for other donors). *See, e.g.*, Stokes Dec. Ex. C ¶¶ 57, 59; Stokes Dec. ¶ 6, Ex. E.[1]

These complex, claim-specific issues warrant full briefing on a full record—and once it is clear

[1] These remedies help illustrate Plaintiffs' point that they need not hold legal title to obtain relief. Fidelity cannot possibly be arguing, for example, that it could not enter into a contract about how it would dispose of its own property. And as Plaintiffs intend to explain at the appropriate time, the equitable remedies they seek are flexible enough to "adjust the remedy in order to do right and justice" and "protect all of the equities of the parties" by requiring Fidelity to restore DAF losses (or otherwise grant Plaintiffs advisory rights over sufficient funds) and thereby put Plaintiffs where they would be absent Fidelity's misconduct. *Hutton v. Gliksberg*, 128 Cal. App. 3d 240, 249 (1982); *see also, e.g.*, *Signal Hill Aviation Co. v. Stroppe*, 96 Cal. App. 3d 627, 640 (1979) (approving "the exercise of judicial discretion in promissory estoppel cases to fashion relief to do justice"); *Heckmann v. Ahmanson*, 168 Cal. App. 3d 119, 125, 136-37 (1985) (affirming injunction restricting use of defendant's assets to certain purposes to prevent frustration of final judgment).

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on which of Plaintiffs' six claims Fidelity is liable. It would be remarkable to decide the full panoply of Plaintiffs' remedies, after two years of hard-fought litigation, based on truncated *in limine* briefing that doesn't address all requested remedies. Plaintiffs thus ask the Court to reserve decision on all remedies issues beyond surcharge. This will permit full vetting of the remaining issues at no efficiency cost: Plaintiffs' experts must testify for the tax losses, which requires evaluating Fidelity's botched trading anyway. The Court should wait until the remedies phase to make a final decision on remedies.

ARGUMENT

Surcharge is the quintessential remedy for mismanagement of charitable assets, whether involving negligent investment decisions, intentional misappropriation, or asset diversion. It is monetary, make-whole *equitable* relief that will obligate Fidelity to restore losses to Plaintiffs' charitable account. Fidelity may use its insurance policy to pay for this remedy (Stokes Dec. Ex. D), but it may also draw from the revenue generated by account fees (*id.* Ex. C ¶¶ 57, 59) or its $40 million in assets not designated for other donors (Stokes Dec. ¶ 6, Ex. E). At the final pretrial conference, Fidelity raised four arguments for why Plaintiffs could not obtain surcharge. Each of them is wrong.

First, Fidelity argued that a negligence claim cannot be analyzed as breach of trust. FPTC Tr., Stokes Dec. Ex. A at 32. But Fidelity itself has *always* argued that the negligence claim should be precisely so construed—as a breach of trust claim. In its motion to dismiss, Fidelity claimed that only the Attorney General can "prevent breaches of trust," specifically arguing that "[t]he Fairbairns' complaint about Fidelity Charitable's supposed 'botched trading' is the paradigmatic example of this type of mismanagement claim"—*i.e.*, a breach of trust claim. ECF No. 21 at 20, 21 (citation omitted); *id.* at 14 (arguing that the Attorney General "has exclusive standing to enforce *breach of trust claims* against Massachusetts charities") (emphasis added); MTD Reply, ECF No. 32 at 9 n.4 ("Plaintiffs also ignore a key California case that dismissed donors' claims because *enforcement of a charitable trust* is 'a prerogative left solely to the Attorney General.'") (emphasis added) (citation omitted).

In response to Fidelity's argument that they were asserting a breach of trust claim, Plaintiffs explained that their negligence claim was based on two distinct, independent theories. Plaintiffs first argued they could assert a direct, personal negligence claim against Fidelity. But they also argued that "even if the Fairbairns' negligence claim is viewed as an attempt to enforce a charitable trust,"

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Plaintiffs had standing under the trust-enforcement cases that Fidelity invoked. MTD Opp., ECF No. 29 at 29. Indeed, California courts do not hesitate to style breach of trust claims based on imprudent investment as claims for "negligence." *Lynch*, 9 Cal. App. 3d at 301-02 ("increase in value of the corpus is no excuse for negligence in failing to invest trust funds"; "good faith is no defense in an action against trustees based on negligence"; "liability of trustees for negligence is joint and several").

In its motion to dismiss order, the Court held that Plaintiffs had special interest standing to sue for negligently mismanaging their donation, based on cases holding that the Attorney General's power to enforce a charitable trust and redress breaches of trust is not exclusive. MTD Order, ECF 39 at 9-12. Given Fidelity's argument and the Court's holding, Plaintiffs have litigated the negligence claim primarily under the breach of trust rubric ever since the motion to dismiss.[2]

Plaintiffs' negligence claim is thus appropriately viewed as a claim for breach of trust, and it would be improper and unfair to hold otherwise at this stage. California law makes clear that a breach of trust claim can be labeled "negligence." And, if necessary, there would be no prejudice to Fidelity if Plaintiffs were permitted to add a breach of trust cause of action to their Complaint—it would contain identical allegations. This is especially true given that complaints properly plead facts, not legal theories, and the preference for adjudication on the merits rather than legal labels. *E.g.*, *Johnson v. Shelby*, 574 U.S. 10, 11-12 (2014) (summarily reversing dismissal for improper claim labeling).[3]

Second, Fidelity's assertion that Plaintiffs can only sue for violation of a specific provision of the trust declaration is wrong. *See* FPTC Tr. 32, 41. Innumerable cases hold that an appropriate plaintiff (as the Fairbairns undisputedly are here) may sue a charity to restore losses caused by

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[2] As noted (*supra* 1 & n.1), Plaintiffs could independently obtain the functional equivalent of loss restoration on a "direct" negligence claim through declaratory and injunctive relief requiring Fidelity to grant Plaintiffs advisory rights over assets equivalent to the losses caused by its botched liquidation. This issue, like the other remedies issues flagged above, warrants separate briefing at Phase II.

[3] Fidelity misleadingly attached Plaintiffs' proposed jury instructions to its motion *in limine* without including the meet-and-confer correspondence showing that Plaintiffs sought equitable relief on their negligence claim. Based on the fact that Plaintiffs sought restoration of DAF losses for all claims, brought their negligence claim in both a personal and representative capacity, the functional similarity between legal damages and surcharge, and the cases describing trust losses as "damages" (*e.g.*, *The Woodward Sch. for Girls. v. City of Quincy*, 469 Mass. 151, 170 (2014)), Plaintiffs planned to argue that the jury could address the DAF losses question—and that at minimum, an advisory ruling was appropriate, given that Plaintiffs' tax damages were undoubtedly for the jury to decide. But Plaintiffs also made explicit to Fidelity that they sought "equitable relief in the form of an order from the Court directing Fidelity to restore the lost value to the donor-advised fund." Stokes Dec. Ex. B at 4.

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negligent investment decisions. These include special-interest standing suits, Attorney General suits, and beneficiary suits; the rule is the same in all of them. *E.g.*, *In re Francis Edward McGillick Found.*, 537 Pa. 194, 202 (1994) (special-interest standing case involving, *inter alia*, whether "the rate of return on the assets of the foundation was inadequate or that the trustees should be surcharged because of any loss of income suffered by the trust as a result of improper or imprudent investments made by the trustees"); *Lynch*, 9 Cal. App. 3d at 298 (Attorney General negligence suit against charity based on rule that "[i]n investing, reinvesting, purchasing, acquiring, exchanging, selling and managing property for the benefit of another, a trustee shall exercise the judgment and care, under the circumstances then prevailing, which men of prudence, discretion and intelligence exercise in the management of their own affairs"); *Mandel v. Cemetery Bd., Dep't of Prof. & Vocational Standards*, 185 Cal. App. 2d 583, 587 (1960) (in suit over mismanagement of assets by charity, holding "trustees [are] under the mandate of the 'prudent investors' rule in regard to all of their financial transactions").[4]

Third, California law allows surcharge to be awarded without the Attorney General. *See, e.g.*, Cal. Gov. Code § 12591 (state jurisdictional statute requiring Attorney General to be party only in suits "to modify or terminate any trust of property for charitable purposes"). In any event, California

[4] *See also, e.g.*, *The Woodward Sch. for Girls*, 469 Mass. at 166 ("Quincy engaged in several shortcomings in its management of the Adams Fund's investment portfolio that indicate that it failed to perform as a prudent investor would under the circumstances."); *In re Estate of Janes*, 90 N.Y.2d 41, 55 (1997) (applying "prudent investor" rule and imposing "surcharge" liability where charitable trust held concentrated position of Kodak stock that decreased in value from $135 when it was placed in the trust to $47 when the stock was sold several years later); *id.* ("In imposing liability upon a fiduciary on the basis of the capital lost, the court should determine the value of the stock on the date it should have been sold, and subtract from that figure the proceeds from the sale of the stock . . . ."); *In re Rosenfeld Found. Tr.*, No. 1664IV2002, 2006 WL 3040020, at *13 (Pa. Com. Pl. July 31, 2006) ("[T]he test of a fiduciary's liability on the sale or retention of securities is common prudence, common skill and common caution; that failure so to exercise such prudence, skill and caution will not be excused because of a testator's exemption concerning the fiduciary's discretionary sale or retention." (citation and emphasis omitted)); *In re Billmyer*, 37 N.Y.S.3d 330, 332-33 (2016) (Attorney General and charitable beneficiary suit to surcharge trustee for negligently selling assets for less than they were worth); *Stern v. Lucy Webb Hayes Nat'l Training Sch.*, 381 F. Supp. 1003, 1007 (D.D.C. 1974) (individuals with special interest standing could sue a charitable hospital for breaching its duty of "care and loyalty in the management of [its] funds"); *Stern*, 367 F. Supp. 536, 540 (D.D.C. 1973) (holding in same case that plaintiffs could pursue remedies including "an award of damages to be paid into the Hospital's funds"); *In re Estate of Kenney*, 117 N.Y.S.3d 800, at *3 (N.Y. Sur. 2019) (Attorney General suit to surcharge trustee of charitable trust for, *inter alia*, negligent management of trust assets); *Hardman v. Feinstein*, 195 Cal. App. 3d 157, 159-62 (1987) (individuals with standing may sue for "mismanagement of the trust" or to "protect the assets of the trust"); *Exec. Bd. of the Mo. Baptist Convention v. Mo. Baptist Found.*, 497 S.W.3d 785, 797, 798 (Mo. Ct. App. 2016) (persons with special interest may "sue to allege that a charitable corporation . . . is being mismanaged").

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law does not govern joinder or dismissal—federal Rule 19 does. *E.g., Provident Tradesmens Bank & Tr. Co. v. Patterson*, 390 U.S. 102, 125 n.22 (1968). Fidelity did not assert either affirmative defense in its answer, and it has not moved for joinder or dismissal—nor could it successfully do so. At minimum, Fidelity cannot backdoor a Rule 19 motion via truncated briefing on an *in limine* motion, particularly since the standards for such a motion are not satisfied, much less factually established.

Fourth, Plaintiffs were not required to name members of Fidelity Charitable's Board of Trustees as defendants. It is an elemental trust principle that "[t]he 'trustee'"—and thus the appropriate defendant in a breach of trust case—"is the person who holds trust property." Restatement (Third) of Trusts § 3 cmt. c (2003); *see also Barboza v. Cal. Ass'n of Prof. Firefighters*, 799 F.3d 1257, 1265 (9th Cir. 2015) (explaining that "'the person who holds title to the property [incurs] duties to deal with it for the benefit of charity'" and that the "'trustee' [is] simply the person, including a corporation or unincorporated association, 'who holds property in trust'" (quoting Rest. §§ 2, 3)). And here, Fidelity has made binding admissions stating that *Fidelity Charitable the entity* (not the Board of Trustees that governs it) holds title to the donated assets. Fidelity Charitable is thus the appropriate defendant here.

From the outset of this case, Fidelity has argued that the federal law governing DAFs requires the "sponsoring organization" itself—"the entity that maintains the fund"—to "*own[] and control[]*" the assets. MTD, ECF No. 21 at 12 & n.2. To that end, Fidelity Charitable's Answer stated that "it is a Massachusetts 501(c)(3) non-profit corporation" (ECF No. 46 ¶ 19), a juridical entity with the power to be sued and hold title to property, and further "admit[ted] that it holds title to the assets in the Fidelity Charitable DAFs" (*id.* ¶ 30). *See also, e.g.*, MIL No. 5, ECF No. 216 at 3 (donated assets were "indisputably . . . Fidelity Charitable's ***own property***" (emphasis in original)). These assertions "are considered judicial admissions conclusively binding on the party who made them." *Am. Title Ins. Co. v. Lacelaw Corp.*, 861 F.2d 224, 226 (9th Cir. 1988). They demonstrate that Fidelity Charitable—the title-holder that owns and controls the DAF assets—is the proper defendant here.[5]

Plaintiffs meet all of the requirements for surcharge. Fidelity's motion should be denied.

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[5] At minimum, Fidelity's admission that the *entity* holds title to the assets demonstrates that its Board of Trustees acts via Fidelity Charitable the *entity*, and thus Fidelity Charitable is the appropriate defendant. In any event, this is again a federal Rule 19 indispensable party issue, yet Fidelity makes no sufficient showing of this defense under the relevant federal principles.

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Respectfully submitted,

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