IN THE UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

NO. 05-15704
D.C. No. CV-03-03231-SI

HEIDE BETZ,	*
	*
Appellant	*
	*
vs.	*
	*
TRAINER WORTHAM & COMPANY, INC., DAVID P. COMO, FIRST REPUBLIC BANK, a Nevada Corporation, and **ROBERT VILE**	*
	*
Respondents	*
	*

* *

APPELLANT'S OPENING BRIEF
On Appeal from the United States District Court, Northern District of California, San Francisco Division
The Honorable Susan Illston, District Judge

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JURISDICTIONAL STATEMENT

In this action for securities fraud and related state claims, jurisdiction in the district court was based on 28 U.S.C. §§1331 and 1337, §10B of the Securities and Exchange Act of 1934 (15 U.S.C. §78j(b)), and Rule 10b-5 of the Securities and Exchange Commission (17 C.F.R.§240.10b-5).

The district court granted Defendants' motion for summary judgment on April 5, 2005 (Excerpts of Record (ER) 758), and issued judgment on the same day (ER 770). That judgment is a final judgment disposing of all the parties' claims.

On April 21, 2005, Plaintiff timely filed notice of appeal from that judgment (ER 771). This Court has jurisdiction to hear this appeal under 28 U.S.C.A. §1291, which provides that: "The courts of appeals * * * shall have jurisdiction of appeals from all final decisions of the district courts * * * *"

ISSUES PRESENTED FOR REVIEW

I. Is there a triable issue of fact on the question of whether Betz knew or should have known that Defendants committed fraud before July 11, 2001, where up to that time Betz had received account statements showing that Defendants had failed to perform their promise to maintain the value of her portfolio, but Betz had no information indicating that Defendants' promise was based on a deliberate lie?

II. Where a cause of action alleges that Defendants were professional investment managers who breached their fiduciary duty by promising an unsophisticated, retired art consultant that they would use their experience and expertise to invest her retirement money in conservative securities suitable for her needs, but instead invested in speculative high-technology and communications stocks, is the "gravemen" of this cause of action just what it says it is — breach of fiduciary duty (which carries a four-year statute of limitations) — or is it something else: negligence (which carries a two-year statute of limitations), even though this cause of action makes no mention of negligence?

III. Is there a triable issue of fact on the question of whether Betz should have known that Defendants breached the implied covenant of good faith and fair dealing before July 11, 2001, under California law, which holds that “In the presence of a fiduciary relationship, the usual duty of diligence to discover facts giving rise to a cause of action does not exist”?

IV. Is there a triable issue of fact on the question of whether Betz should have known that Defendants made negligent misrepresentations before July 11, 2001, under California law, which holds that “In the presence of a fiduciary relationship, the usual duty of diligence to discover facts giving rise to a cause of action does not exist”?

V. Where Defendants continuously lied to Betz throughout the entire period from June of 1999 to June of 2002, does the statute of limitations for fraudulent and unfair business practices begin to run in June of 1999, or in June of 2002?

STATEMENT OF THE CASE

The original Complaint in this case was filed in the court below on July 11, 2003. ER 1. A First Amended Complaint was filed (ER 10), but this was dismissed (ER 25). A Second Amended Complaint (SAC) was then filed (ER 36), and Defendants' motion to dismiss this SAC was denied (ER 60).

The Second Amended Complaint alleges the following facts.

Defendant Trainer Wortham is an investment management company directed and managed by Defendant First Republic Bank, and Defendants Como and Vile work for Trainer Wortham. ER 37.

Plaintiff Heide Betz owned an estate of $2.2 million. ER 40. She also owed a large debt to First Republic Bank. ER 41. Castro worked for First Republic Bank. ER 41.

Como, Vile, and Castro told Betz that if she gave Trainer Wortham control over her estate, they would invest the money so that she would receive income of $15,000 per month without depleting her capital. ER 39. This was false, and these people knew that it was impossible for $2.2 million to generate this much income without depleting capital. ER 39. But they lied to Betz in order to induce her to give Trainer Wortham control over Betz's estate, so they could garner commissions, so they could pay a secret kickback from Trainer Wortham to First Republic Bank, and so First Republic could obtain repayment of its loan to Betz. ER 39. Betz was to use $7,500 of the monthly income to pay off the loan to First Republic. ER 40.

She advised these people that the $2.2 million was all the money she had, that she was completely dependent on income from this money for her support, that she was completely unsophisticated in investment matters, and that she would be completely dependent on these people for their expertise and advice. ER 40. They falsely told her that they would invest her money in accordance with generally accepted investment principles and accepted guidelines (such as Standard & Poor's). ER 40-42.

In reliance on these lies, on June 7, 1999, Betz entered into an oral Portfolio Management Agreement with Trainer Wortham, giving Defendants the power to invest her $2.2 million estate. ER 39, 43.

Thereafter, in willful violation of industry-accepted guidelines for investments for retired persons such as Betz, Defendants invested 100% of Betz's money in stocks, even though Defendants knew that such heavy investment in stocks was unsuitable for a person in Betz's position. ER 44. In addition, instead of buying stocks in blue chip, safe, dividend-paying companies, Defendants spent 63% of Betz's money buying stock in high risk technology and telecommunication companies that paid no dividends and earned no profits, such as Lucent, QWEST, and MCI/Worldcom. ER 46. Defendants also recommended that Betz purchase more equities on margin, thereby substantially increasing her risk of depleting her estate, and Betz followed this recommendation. ER 50.

When the stock market turned downward, the value of Betz's investments dropped sharply, and she lost more than $2 million. ER 53. Betz did not discover Defendants' lies until March of 2002. ER 52.

The SAC alleges that Defendants thereby committed securities fraud under federal law (Count 1, ER 37), and alleges the following claims under pendant state law: breach of fiduciary duty (Count II, ER 53), breach of the implied covenant of good faith and fair dealing implied into the Portfolio Management Agreement (Count III, ER 55), negligent misrepresentation (Count IV, ER 56), and fraudulent and unfair business practices (Count V, ER 57).

Defendants filed an answer to the SAC (ER 61). After both parties engaged in discovery, Plaintiff moved for partial summary judgment (ER 71) and Defendants filed a motion for summary judgment (ER 237). The district court denied Plaintiff's motion and granted Defendants' motion for summary judgment, holding that all of Betz's claims were barred by various statutes of limitations (ER 758).

On April 5, 2005, the court issued judgment (ER 770). On April 21, 2005, Plaintiff filed notice of appeal from that judgment (ER 771).

STATEMENT OF FACTS

This Statement of Facts draws from various declarations and exhibits presented to the district court on the motion for summary judgment. In accordance with well-established rules, it focuses on the evidence that supports the party opposing the motion for summary judgment (Plaintiff Betz) — and all reasonable inferences therefrom. *Anderson v. Liberty Lobby*, 477 U.S. 242, 255 (1986). This is proper, as the issue here is whether there is one or more triable issue of fact that should be decided by a jury — and not which side is more believable. "Credibility determinations, the weighing of the evidence, and the drawing of legitimate inferences from the facts are jury functions, not those of a judge ruling on a motion for summary judgment." *Id*. at 255.

In early 1999, Plaintiff Heide Betz, a retired art consultant and dealer, was selling her house and buying a co-op to live in. ER 666:6; 675:10-12. Betz was seeking a real estate loan to purchase the co-op, and she met with Carmen Castro (agent of Defendant First Republic Bank) for this purpose. ER 705:17-25.

When Castro learned that Betz had obtained $2.2 million from the sale of her house, Castro suggested that Betz meet with Defendant David Como, an agent for Defendant Trainer Wortham. ER 705:20-25. First Republic

Bank owns Trainer Wortham. ER 705:11. Up to this time, Betz had no plan to invest any money with Trainer Wortham. ER 705:20-21.

In May or June of 1999, Betz met with Como. ER 705:26-27. Betz told Como and Castro that the $2.2 million was all the cash she had and that she had no regular income, and that she had sold her home in order to generate enough income to live on. ER 705:27-706:3; ER 670:9-18.

"I told David Como that I knew absolutely nothing about the stock market or financial markets and I repeated that many times over the next months that this was all the cash that I had and I could not afford to lose it." ER 706:3-6. Castro admitted that Betz "had repeatedly told us that she knew nothing about the stock market or bond market." ER 713:21-23.

Castro and Como recommended that she invest her money with Trainer Wortham. ER 671:4-7.

During subsequent meetings, Como and Castro told Betz that she would need about $15,000 per month for her support. ER 706:12-16. They told Betz that she could withdraw the $15,000 each month without having to touch the growth of her portfolio. ER 300:21-25. This $15,000 would be in addition to growth in the value of the investment, which would grow to about $2.7 million on one year and to $4 million in 5 years. ER 668:11-17.

On June 7, 1999, Betz entered into an oral Portfolio Management Agreement, giving Defendants control over her $2.2 million. ER 705:16-19. They agreed that "David Como would invest my 2.2 million dollars cash in such a fashion that I would receive $15,000 a month from the profit of the investment and that he would not touch the principal." ER 677:17-20.[1]

In November of 1999, Betz needed to pay a tax bill on the sale of her house. ER 706:20-24. Como and Castro suggested that she borrow money on margin instead of selling some securities. ER 706:20-24. Betz did not understand "margin." ER 706:24-25. Como explained it to her, but "I still did not understand either what that really meant or the logic of it." ER 325:10-17. Betz initially wanted simply to take the money out of her portfolio to pay the tax bill, but Como said "No, you must go on margin. This is not how we do business." ER 680:4-21. Castro told Betz to follow Trainer Wortham's advice to go on margin, because "They're the experts." ER 681:3-10. Betz followed their advice, because "I didn't think I had a choice." ER 706:25-27; 680:9; 326:8-9. Castro later admitted that "maybe we shouldn't have borrowed on margin." ER 715:5-8.

[1] Betz and Trainer Wortham also entered into a written agreement on June 7, 1999. ER 380-384. That agreement contains no "integration" or "merger" clause. It provides that Trainer Wortham "will remit .25% of the gross investment advisory fee to First Republic Bank (the 'bank') for its referral services." ER 380.

Betz received monthly reports from Defendants. ER 691:1-2. She understood only the “bottom line” — the total value of her portfolio. ER 691:5-6. She did not know whether she had invested in stocks or bonds, and never discussed investing in bonds with Como, because “Mr. Como told me that he was completely in charge and knew what he was doing. And I trusted that he knew what he was doing, so I did not discuss that, no.” ER 691:13-18. Betz could not explain what a “stock” is, nor what a “bond” is. ER 691:7-9; 299:24-300:10.

Betz relied solely on Como and Castro for financial advice. ER 298:18-24. “I trusted everything that David Como said to me. I was never, ever consulted on purchase of the type of stock or the specific investment portfolio that David Como planned to invest my $2.2 million cash in. I continually advised David Como and Carmen Castro that I was not familiar with the stock market nor investment strategies and that I would rely on them for their investment advice.” ER 706:15-20.

In March or April of 2001, Betz spoke with Defendant Robert Vile, another Trainer Wortham agent, to express her dismay that the value of her portfolio had dropped below $2.2 million. ER 706:27-707:4. “Robert Vile assured me that this was temporary and stated that within a year or less the market would recover and my account would be back to $2.2 million.” ER

707:4-6. Vile "assured me that he knew exactly what he was doing to bring this back up to at least 2.2, if not more, in no time." ER 694:20-695:1. Vile also told Betz that the portfolio's value was dropping because of Betz's monthly withdrawals — even though the withdrawals were part of the original agreement. ER 681:18-22. But Vile nevertheless told Betz that "we know what we are doing. This is temporary. We're going to – we're watching your account. And it's temporary. We're taking care of everything. Don't worry about it." ER 696:16-24.

And even in March of 2001, when the value of Betz's portfolio had dropped to $848,000, Vile assured Betz that the drop "was temporary" and promised her that the value "within no time it would be back up [to $2 million] and that they knew what they were doing." ER 697:20-25; 698:14-20; 699:2-8.

David Como "continually advised me that there was nothing wrong with the portfolio and that the value would be back up very soon." ER 707:13-14; 693:8-11. And Carmen Castro "always reassured me that Robert Vile and David Como knew what they were doing and that I should not worry about my portfolio," that "things are going great," and that "I do not need to do anything with my account, that nothing is wrong with the account, and that Charles Moore, the president of defendant Trainer

Wortham & Company would meet with me and see that my account is replenished." ER 709:19-26; 700:4-11.

In March, April, or May of 2001[2], Castro told Betz that "we have a serious problem with the way this portfolio has been managed", but the president of Trainer Wortham (Charles Moore) would take care of the problem because it was the right thing to do and because they valued client relations. ER 707:6-12. There was no evidence that Castro ever advised Betz that Como or Vile had deliberately lied to Betz.

In late May of 2002, Mr. Moore sent word to Betz that Betz should "be patient with them and not take any legal action and respect their time frame." ER 707:18-21. Betz agreed to do so. ER 707:21.

In June of 2002, however, Moore (through Castro) told Betz that Trainer Wortham and First Republic Bank "were not going to do anything at all." ER 707:21-24. Betz then realized that Defendants' representations and promises had been false and merely attempts to induce her not to take legal action. ER 707:24-26.

Charles Moore, President of Trainer Wortham, later testified that a portfolio of about $2 million invested in equities would earn about two

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[2] Betz's Declaration, at ER 707:14-18, says that this meeting occurred in 2002, but this appears to be in error. At her deposition, Betz testified that the meeting took place in 2001 (ER 350:7-355:7), and the District Court accepted 2001 as the correct year (ER 760:27).

percent in 1999 — about $40,000 per year. ER 717:14-20. Moore admitted that there was no way $2 million could earn $15,000 a month: “This doesn’t make sense.” ER 717:14-20. Como made a similar admission. ER 719:17-24, 723:4-23.

SUMMARY OF ARGUMENT

The District Court erred in holding that there is no triable issue of fact regarding Count I, Betz's federal claim for securities fraud. A reasonable jury could find that Betz did not know and should not have known of Defendants' fraud more than two years prior to the filing of the complaint. The District Court ruled that the account statements Betz received in February of 2000 and thereafter were "storm warnings" of fraud. But those account statements told Betz only that Defendants had failed to fulfill their promise to keep the value of her portfolio from falling below $2.2 million. Those account statements gave Betz no indication that Defendants had *deliberately lied* when they made that promise. Therefore, these account statements were not "storm warnings" of *fraud*. And even if they were, Betz reasonably investigated this possibility by making inquiries to the very experts that Defendants themselves had told her to trust.

The law does not require an unsophisticated investor to immediately file a lawsuit for fraud against a sophisticated financial advisor as soon as the value of her account declines. Such a policy would increase meritless litigation rather than encourage parties to work out their differences amicably.

The District Court erred in finding no triable issue of fact on Count II, Betz's state law claim for breach of fiduciary duty, which carries a four-year statute of limitations. The District Court ruled that a two-year statute of limitations applies to this claim, because the "gravamen" of Count II was really negligence, not breach of fiduciary duty. But nowhere does Count II allege negligence. Instead, Count II alleges that Defendants induced Betz to place her confidence in their experience and expertise to manage her assets, thereby creating a fiduciary duty under California law, and that Defendants breached this duty by investing her assets in speculative stocks that were unsuitable for Betz's stated needs. The fact that Defendants might also have been negligent in doing so does not change the gravamen of Count II.

And even if the gravemen of Count II is something other than what it explicitly states (breach of fiduciary duty), that something would be *fraud*, not negligence, because Count II expressly alleges that Defendants lied to Betz. As fraud carries a three-year statute of limitations, Count II is not time-barred.

The District Court erred in finding no triable issue of fact regarding Count III (breach of implied covenant of good faith and fair dealing) and Court IV (negligent misrepresentation), both of which carry a two-year statute of limitations. The court overlooked the California rule that "In the presence of a fiduciary relationship, the usual duty of diligence to discover facts giving rise to a cause of action does not exist."

The District Court erred in finding no triable issue of fact regarding Count V, for unfair and fraudulent business practices, which carries a four-year statute of limitations. The court assumed that the statute began running in February of 1999, when Defendants made their false promises. But in fact Defendants made false promises and reassurances to Betz *continuously* from 1999 to June of 2002, which is well within the four years before the complaint was filed.

ARGUMENT

I. STANDARD OF REVIEW

An appeal from a summary judgment is reviewed *de novo*. *Jones v. Union Pacific R.R.*, 968 F.2d 937, 940 (9th Cir. 1992).

II. THERE IS A TRIABLE ISSUE OF FACT REGARDING WHETHER THE STATUTE OF LIMITATIONS HAD RUN ON BETZ'S FEDERAL CLAIM FOR *SECURITIES FRAUD.*

The statute of limitations for Betz's federal §10(b) claim for securities fraud is five years after the fraud or two years after the "discovery" of the fraud, whichever is earlier. 28 U.S.C. §1658(b). In their motion for summary judgment, Defendants argued that the "discovery" period applies here. Because the original complaint was filed on July 11, 2003, the two-year statute of limitations would bar Betz's suit only if Defendants prove that Betz "discovered" Defendants' fraud before July 11, 2001.

Betz in fact "discovered" the fraud in June of 2002, when Moore (through Castro) told Betz that Trainer Wortham would not deliver on its promises to make her account whole. ER 707:21-24.

Defendants invoked the rule that the statute of limitations began to run "once the investor, in the exercise of reasonable diligence, should have discovered the facts underlying the alleged fraud." *Sterlin v. Biomune*

Systems, 154 F.3d 1191, 1201 (10th Cir. 1998); *Berry v. Valence Technology, Inc.*, 175 F.3d 699, 704 (9th Circuit, 1999). Defendants argued that Betz *should* have discovered their fraud before July 11, 2001.

This Court has held that "the question of when fraud is discovered is for the trier of fact," that because of this "the party seeking summary disposition has an *extremely difficult burden* to show that there exists no issue of material fact regarding notice," and that "summary disposition of this issue is discouraged." *S.E.C. v. Seaboard Finance*, 677 F.2d 1301, 1309 (9th Cir. 1982) (emphasis added).

Nevertheless, the District Court found that there is no triable issue of fact as to whether Betz should have discovered Defendants' fraud before July 11, 2001. ER 764-766. This, we contend, was error.

A. The Test for Discovery

Defendants made no claim that Betz *actually* discovered their fraud before July 11, 2001. They claimed only that she *should have* discovered their fraud by then, whereupon Betz could then have filed a lawsuit for fraud.

This issue may be determined as a matter of law "only when the uncontroverted evidence irrefutably demonstrates that the plaintiff discovered or should have discovered" the fraud at a particular point in time. *Kramas v. Security Gas & Oil Inc.*, 672 F.2d 766, 770 (9th Cir.1982), *cert. denied*, 459 U.S. 1035 (1982); *Meadows v. Pacific Inland Securities Corp.*, 36 F.Supp.2d 1240, 1246 (S.D. Cal. 1999); *Washington v. Baenziger*, 673 F.Supp. 1478, 1485 (N.D. Cal. 1987).

According to the cases, the statute of limitations began to run when Betz had sufficient information to file a lawsuit against Defendants for fraud. This would occur only when *both* (1) there were "storm warnings" that should have alerted Betz to the possibility of fraud, *and* (2) she then had time to investigate these "storm warnings" and acquire sufficient evidence to prove that fraud had indeed occurred. "We hold, therefore, that following the receipt of sufficient storm warnings, a plaintiff's cause of action is deemed to accrue when, exercising reasonable diligence, she would have unearthed the fraud." *Young v. Lepone*, 305 F.3d 1, 9-10 (1st Cir. 2002).

This two-part rule is designed to ensure that "the applicable statute of limitations should not precipitate groundless or premature suits by requiring plaintiffs to file suit before they can discover with the exercise of reasonable diligence the necessary facts to support their claims." *Sterlin v. Biomune Systems*, *supra*, 154 F.3d at 1202. The Ninth Circuit Court of Appeals has said that it would adopt this two-part test. *Berry v. Valence Technology, Inc.*, *supra*, 175 F.3d at 704.

In the present case, the District Court purported to apply these two parts, but we respectfully submit that its application was erroneous.

B. There Is A Triable Issue of Fact Regarding "Storm Warnings."

The District Court found that Betz received "storm warnings" of Defendants' fraud "in February of 2000, when plaintiff received the first of thirty account statements between that month and July 2001 showing that her portfolio had declined below the value of her original $2.2 million investment. These accounts directly contradicted the alleged oral representation made by defendants." ER 765:5-8.

True, the accounts did appear to show that Defendants had *failed to perform their promise* to keep the principal intact, but they do *not* show that Defendants committed *fraud*, i.e., that Defendants had intentionally *lied* about their intentions to perform this promise.

Suppose A lends B $1,000 on B's promise: "I'll pay you back on March 1." B's failure to pay the $1,000 on March would subject him to a suit for breach of contract, but without more evidence, this would *not* subject him to a suit for *fraud*. B's failure to pay would not even be a "storm warning" of potential fraud. An attorney who filed a suit for fraud on these facts would be subject to Rule 11 sanctions. Breaches of contract are common and ordinary, and the overwhelming majority of such breaches are not based any fraudulent intent *ab initio*.

Betz was naturally disappointed and disturbed that the "bottom lines" on her accounts had dropped, but this gave her no reason to believe that the Defendants had *lied* to her. Financial experts such as Moore and Como might have known that it was impossible for her $2.2 million to generate $15,000 a month without investing in risky stocks that might well decrease in value, but Betz had no reason to know this. To hold her to this knowledge would simply reward Defendants for their fraud.

Defendants have therefore failed to sustain their "extremely difficult burden" of presenting evidence showing — "irrefutably"— that these accounts were "storm warnings" of *fraud*.

Similarly, when Castro told Betz in March of 2001 that "we have a serious problem with the way this portfolio has been managed" (ER 707:6-12), this gave Betz no reason to believe that Defendants had lied to her back at the beginning, in June of 1999, when Defendants set up her account. Castro's statement indicated mismanagement, perhaps a breach of contract, perhaps negligence — but not fraud.

At a minimum, there was a triable issue of fact on the issue of "storm warnings." The District Court's ruling to the contrary was erroneous.

<u>C. There Is A Triable Issue of Fact Regarding When Betz Would Have Discovered Facts Showing Fraud.</u>

"Storm warnings" alone, of course, cannot trigger the statute of limitations, because one cannot file a federal lawsuit based on mere "storm warnings." Without evidence of scienter, no suit for fraud may be brought. *Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 193 (1976); *Demarco v. Lehman Brothers, Inc.*, 309 F.Supp.2d 631, 637 (S.D.N.Y. 2004). Indeed, filing such a suit would be unethical, subjecting her attorney to severe sanctions. See Fed.Rules Civ. Proc., Rule 11.

Even assuming that the monthly accounts gave Betz "storm warnings" of fraud, the statute of limitations would not begin to run until the expiration of sufficient time to enable a reasonable investor to investigate these "storm warnings" and uncover enough evidence of fraud to file a lawsuit for fraud. *Young v. Lepone, supra*, 305 F.3d at 9-10.

What was this time? While the District Court purported to address this issue, it really did not. The Court noted that Como, Vile, Castro, and Moore had given Betz assurances that her account would recover, but held that these assurances "did not toll the statute of limitations." ER 765:19-

766:22. With respect, we submit that the District Court misunderstood the second half of the two-part test.

The District Court assumed that "storm warnings" trigger the statute of limitations, and that "reasonably diligent investigation" tolls the statute. This is not correct. "Storm warnings" alone do *not* trigger the statute. Only "storm warnings" *plus* passage of a reasonable time to investigate trigger the statute — because only an investigation that uncovers firm evidence of fraud will permit the filing of a lawsuit for fraud. Otherwise, application of the statute of limitations would "precipitate groundless or premature suits by requiring plaintiffs to file suit before they can discover with the exercise of reasonable diligence the necessary facts to support their claims." *Sterlin v. Biomune Systems*, *supra*, 154 F.3d at1202.

We submit that a reasonable jury could find that Betz conducted a reasonably diligent investigation by making inquiries to Como and Vile, the "experts," according to what Castro had told Betz. "They're the experts." ER 327:10. Indeed, Como himself had told Betz, "that he was completely in charge and knew what he was doing." ER 299:13-18. And Vile too had told Betz that "we know what we are doing." ER 332:16-24. See *S.E.C. v. Seaboard Finance*, *supra*, 677 F.2d at 1310 (where plaintiff questioned defendants and received assurances, “whether this constituted reasonable diligence is uncertain,” so summary judgment improper).

In addition, a naïve investor such as Betz may rely on assurances that are meant to *supplant* rather than *supplement* the written reports. In *McCoy v. Goldberg*, 748 F.Supp. 146, 158-159 (S.D.N.Y. 1990), the court held:

> While defendants are correct in asserting that an investor cannot rely on "reassuring comments" made by an investment advisor in lieu of examining the furnished prospectus, *Zola v. Gordon*, 685 F.Supp. 354, 366 (S.D.N.Y.1988) (*citing Volk v. D.A. Davidson & Co.*, 816 F.2d 1406 (9th Cir.1987)), such is not the case here. Defendants' statements to plaintiff regarding the content of the prospectuses were intended to supplant, rather than to supplement, the reading of the offering documents.

A reasonable jury could find that Castro, Como, and Vile intended to induce Betz to rely on their assurances instead of the written reports, thereby supplanting them rather than supplementing them.

But even assuming the District Court were correct in ruling that Betz’s reliance on the assurances of the experts (the very experts who had persuaded her to trust them) was not a sufficient investigation, the District Court failed to follow this determination with an answer to the relevant questions: what *should* Betz have done, and how long would this have taken? Should she have asked federal or state law enforcement agencies to investigate? If so, how long would it have taken to get a response from these agencies? Should she have consulted a lawyer? But a lawyer could not have filed a lawsuit based on mere "storm warnings," and without a lawsuit and its attendant discovery devices, how could the lawyer uncover evidence of fraud, and how long would this have taken?

The District Court failed to address these vital issues. And if it had done so, it would have had to have found a triable issue of fact. Indeed, the very difficulty of these issues is why this Court has held that "the question of when fraud is discovered is for the trier of fact" and that "summary disposition of this issue is discouraged." *S.E.C. v. Seaboard Finance*, *supra*, 677 F.2d at 1309.

The District Court noted this Court's opinion in *Vucinich v. Paine, Webber, Jackson & Curtis, Inc.*, 739 F.2d 1434 (9th Cir. 1984). There, the district court granted summary judgment based on the statute of limitations, but this Court reversed:

> Vucinich filed suit in June 1982. More than three years prior to this date, she had become aware that the market was running against her. Additionally, she had been receiving monthly statements which, had she been able to interpret them, would have indicated that the value of her account was declining. *She claims, however, that she could not decipher the statements and that she relied on Moore's continuing reassurance that a longer time was needed to realize gains from his strategy.* By June 1980 Vucinich had received several margin calls, requiring her to liquidate certain stocks. Also by this date, she had been independently told by a friend that short positions were speculative.
>
> The statutes of limitations begin to run when one should have been put on notice of the fraud or misrepresentation. Under California law, the statute of limitations may be tolled by a broker reassuring his

client on concerns relevant to the possible misrepresentation. *See Twomey v. Mitchum, Jones and Templeton, Inc.*, 262 Cal.App.2d 690, 723-29, 69 Cal.Rptr. 222 (1968). *Whether the events existing as of June 1979 and June 1980 were sufficient to put Vucinich on notice and whether the reassuring statements of defendant reasonably affected that notice is a disputed question of fact requiring determination by the district court.*

Reversed and remanded. [*Id.* at 1436-1437; emphasis added.]

Vucinich was an unsophisticated investor who could not read financial statements and relied on defendants' assurances — just like Betz.

The case is indistinguishable from the present case, but the District Court nevertheless purported to distinguish *Vucinich* with a single sentence: "The Court of Appeals has expressly held, however, that *Vucinich* does not compel denial of summary judgment where a plaintiff is a sophisticated investor who monitors his or her monthly statements. See *Davis v. Birr, Wilson & Co.*, 849 F.2d 1369-1370 (9th Cir. 1988)." ER 766:10-14. This sentence is baffling. What is the relevance of a case (*Davis*) in which the plaintiff was a "sophisticated investor"? Castro admitted that Betz "had repeatedly told us that she knew nothing about the stock market or bond market." ER 713:21-23. And Betz "monitored" her monthly statements by looking only at the "bottom line" — the total value of her account — because she did not understand the nature of the investments that made up that account. ER 691:5-6. Betz did not even know the difference between a stock and a bond. ER 691:7-9; 299:24-300:10. This is a far cry from the "sophisticated investor" whose suit was barred in *Davis*:

> In this case Davis was well-educated and had recently invested large sums of money with other brokers. He received monthly statements of his account, followed his investments, and made suggestions concerning them. In connection with one of his investments, *Davis acknowledged that he was "an experienced and sophisticated investor*." This is not a case like *Vucinich v. Paine, Webber, Jackson & Curtis, Inc.*, 803 F.2d 454 (9th Cir.1986), in which we held there were questions of fact concerning the tolling of a statute for a naive investor who claimed that she was lulled into inaction by the defendant. [*Davis v. Birr, Wilson & Co.*, 849 F.2d 1369, 1370 (9th Cir. 1988); emphasis added.]

The District Court also relied on several other cases, but only one of these was decided by this Court: *Volk v. D.A. Davidson & Co.*, 816 F.2d 1406 (9th Cir. 1987). But there is no indication in the *Volk* opinion that the investors were unsophisticated, as were Vucinich and Betz. And as *McCoy*, *supra*, noted, there was no indication in *Volk* of assurances that were intended to supplant, rather than supplement, the written reports.

This Court's approach in *Vucinich* makes perfect sense. A sophisticated investor might select his own stocks and bonds, adjuring the services of financial experts and avoiding the fees they charge. Firms such as Trainer Wortham are set up primarily to assist investors who feel that they are *not* able to make these decisions by themselves and *are* willing to pay the firm's fees to fill in this knowledge gap.

Indeed, Trainer Wortham promotes itself to investors by lauding its "Experience" ("continuity of investment professionals"), "Accountability" ("sole business is investment management") and "Integrity" ("commitment to meeting the financial needs and goals of our clients"). ER 400. Trainer Wortham and similar firms send the message to financially unsophisticated clients: "You are not financial experts, but we are — so trust us to invest your money safely and profitably in ways that you do not understand." Vucinich believed the message, and so did Betz, and neither one should be penalized by the very naiveté that defendants deliberately sought to exploit.

As the court stated in *McCoy v. Goldberg*, *supra,* 748 F.Supp. at 152, "After luring plaintiff into ignorant reliance, defendants cannot now avail themselves of the doctrine of constructive knowledge." And in *Carruth v. Fritch*, 36 Cal.2d 426 (1950), the California Supreme Court held: "The purpose of the statute of limitations is to protect a defendant from the prosecution of a stale claim; it may never be used to assure the success of his fraud." [*Id*. at 433-434]

The District Court erred in ruling that there was no triable issue of fact on the issue of when Betz would have discovered facts showing fraud.

III. THERE IS A TRIABLE ISSUE OF FACT REGARDING WHETHER THE STATUTE OF LIMITATIONS HAD RUN ON BETZ'S STATE LAW CLAIM FOR *BREACH OF FIDUCIARY DUTY*.

Count II of the SAC alleges that the oral Management Agreement imposed a fiduciary relationship on Defendants to Betz, and that Defendants breached their fiduciary duty to Betz by failing to place her money in suitable investments, by recommending that she trade on an unsuitable margin account, and by not disclosing to her that Trainer Wortham was going to kick back a secret referral fee to First Republic. ER 53-55.

In California, the statute of limitations on breach of fiduciary duty is four years. Calif. Code of Civil Procedure §343. The District Court held, however, that the "gravamen" of this count is negligence, and not breach of fiduciary duty, and therefore California's two-year statute of limitations for negligence claims applies, so this claim is time-barred. ER 768:6-19.

There are two independent reasons why this ruling was erroneous: (1) the "gravamen" of Count II is exactly what it says it is — breach of fiduciary duty — and therefore California's four-year statute of limitations applies, and (2) if the gravamen of Count II is not breach of fiduciary duty, then the gravamen is fraud, which carries a three-year statute of limitations.

A. The "Gravamen" of Count II Was Breach of Fiduciary Duty, And Therefore A Four-Year Statute of Limitations Applies.

In California, the statute of limitations on a claim for breach of fiduciary duty is four years (Calif. Code of Civil Procedure §343), and this four years begins to run when the plaintiff "discovered, or in the exercise of reasonable diligence could have discovered, that facts have been concealed." *Stalberg v. Western Title Ins. Co.*, 230 Cal.App.3d 1223, 1230 (1991).

Therefore, even if the District Court were correct in its ruling that Betz should have discovered Defendants' fraud as early as February of 2000, this was less than four years prior to the filing of her complaint (on July 11, 2003). February of 2000 was when Betz received her first account statement showing that the value of her portfolio had dropped below $2.2 million, and there was no earlier date on which it might reasonably be argued that she should have known of Defendants' breach of fiduciary duty.

Therefore, it would seem that Count II was filed well within California's statute of limitations for breach of fiduciary duty.

But the District Court held that Count II is in fact not what it purports to be, but is something else: a claim for negligence. This was error.

The District Court correctly noted that under California law, the statute of limitations is determined by the "gravamen" of the cause of action rather than its form — at least where the form is used to disguise the true gravamen of the cause of action. See *Hydro-Mill Co. v. Hayward, Tilton and Rolapp Ins. Associates*, 115 Cal.App.4th 1145, 1154 (2004).

The gravamen of Count II is exactly what it says it is: breach of fiduciary duty.

In *Hydro-Mill Co. v. Hayward, Tilton and Rolapp Ins. Associates, supra*, 115 Cal.App.4th at 1156-1157 (2004), the court explained when a fiduciary duty exists under California law:

> A fiduciary relationship has been defined as "any relation existing between parties to a transaction wherein one of the parties is ... duty bound to act with the utmost good faith for the benefit of the other party. Such a relation ordinarily arises where a confidence is reposed by one person in the integrity of another, and in such a relation the party in whom the confidence is reposed, if he voluntarily accepts or assumes to accept the confidence, can take no advantage from his acts relating to the interest of the other party without the latter's knowledge or consent."

Count II alleges just such a relationship. ¶28 of Count II incorporates the prior allegations of the SAC, and ¶30 alleges:

> That by reason of the Management Agreement, a fiduciary relationship was created between plaintiff and defendants whereby defendants owed to plaintiff a fiduciary duty to act in plaintiff's best interests, that this fiduciary duty imposed upon defendants a duty to manage plaintiff's account in a manner that was consistent with plaintiff's financial data, financial needs and plaintiff's long-term objectives and, further, consistent with plaintiff's age, her future retirement date and her total assets; and further, a duty to disclose to plaintiff the risk of any unsuitable investments and to keep plaintiff properly appraised of the status of her account. [ER 54].

And then ¶31 of the SAC alleges "That the defendants breached their fiduciary duty to plaintiff by not fully investigating their suggested plan of investments to ensure its suitability for plaintiff, by not allocating her investment in a manner that was consistent with recognized guidelines for a investor of plaintiff's age, financial condition, financial needs and plaintiff's inexperience in investment decisions. . . ." ER 54.

Thus, Count II alleges that Defendants owed Betz a fiduciary duty in certain specific ways, and then alleges that they breached that duty by failing to perform in those same ways. This breach was also negligent, probably — as most breaches of fiduciary duty are. But the fact that a claim may state a cause of action under more than one theory of law does *not* mean that the "gravamen" of the cause of action is not what it asserts itself to be. Negligence and breach of fiduciary duty naturally overlap, but neither the District Court nor Defendants cited any authority for the notion that this overlap changes the gravamen of a claim of breach of fiduciary duty.

California cases holding that the gravamen of a claim for breach of fiduciary duty was some other claim usually involve a plaintiff's attempt to present a weak or non-existent claim for breach of fiduciary duty as a disguise for some other claim with a shorter statute of limitations. For example, in *City of Vista v. Robert Thomas Securities, Inc.*, 84 Cal.App.4th

882 (2000), plaintiff purchased securities through defendant broker, and then plaintiff claimed that defendant had defrauded plaintiff by engaging in price collusion with other brokers. The court reversed the trial court's grant of summary judgment against the fraud claim, but held that a claim for breach of fiduciary duty was barred by the statute of limitations, because the gravamen of the complaint was fraud. *Id.* at 889. There seemed to be no serious argument that there was *any* fiduciary relationship between the broker and the plaintiff, and this cause of action was probably added solely in an effort to take advantage of a longer statute of limitations.

Here, by contrast, the fiduciary relationship not just the gravamen of Count II — it was its essence. Trainer Wortham had continuously urged Betz to place her trust in Trainer Wortham's expertise and reliability, and then they violated this trust. This breach of fiduciary duty was real, substantial, and the very essence of Count II of the SAC.

Indeed, this case is quite similar to *Davis & Cox v. Summa Corp.*, 751 F.2d 1507 (9th Cir. 1985), where a counterclaim asserted that a corporate director had acted negligently, but framed this as a cause of action for breach of fiduciary duty. This was proper, according to this Court, as "The gravamen of Summa's counterclaim was Davis' breach of fiduciary duties as a director, rather than his professional malpractice." *Id*. at 1520. In *Federal*

Deposit Ins. Corp. v. McSweeney, 976 F.2d 532 (9th Cir. 1992), certiorari denied, 508 U.S. 950, this Court followed *Davis & Cox*.

The fact that this breach might also have constituted negligence does not bar Betz from claiming breach of fiduciary duty. "A breach of contract is of course actionable regardless of whether the act is independently wrongful as a tort." Witkin, Calif. Procedure, *Actions*, §139.

Because the statute of limitations on Count II was four years, not two, the District Court erred in ruling that there was no triable issue of fact on Count II.

B. Alternatively, The Gravamen of Count II Is Fraud, Not Negligence, And Therefore A Three-Year Statute of Limitations Applies.

If the gravemen of Count II is something other than what it purports to be — breach of fiduciary duty — that something would be fraud, not negligence, because Count II expressly incorporates ¶10 of the SAC, which alleges that Defendants *lied* to Betz. ER 39-40. There is *no* paragraph alleging negligence in Count II or in any part of the SAC that is incorporated into Count II.

California Code of Civil Procedure §338, subsection (d), provides that the statute of limitations for fraud is three years from "the discovery, by the aggrieved party, of the facts constituting the fraud. . . ."

Let us assume that this Court finds that Betz should have learned of Defendants' fraud earlier than the date on which she says she learned of it (June of 2002, when Castro told Betz that Trainer Wortham and First Republic Bank "were not going to do anything at all." ER 707:21-24.) If so, then the proper date should *not* be February of 2000, when Betz began to receive account statements showing that the value of her portfolio had fallen below $2.2 million. That does not show that Defendants committed fraud by intentionally lying to Betz. No, the earliest possible date on which this Court might conceivably find notice of fraud was March of 2001, when Castro told Betz that "we have a serious problem with the way this portfolio has been managed", but the president of Trainer Wortham (Charles Moore) would take care of the problem because it was the right thing to do and because they valued client relations. ER 707:6-12.

March of 2001 was within three years of the date the complaint was filed: July 11, 2003. Therefore, Count II was timely filed, and the District Court erred in ruling that it was time-barred.

IV. THERE IS A TRIABLE ISSUE OF FACT REGARDING WHETHER THE STATUTE OF LIMITATIONS HAD RUN ON BETZ'S STATE LAW CLAIM FOR *BREACH OF THE IMPLIED COVENANT OF GOOD FAITH AND FAIR DEALING.*

Count III of the SAC alleges that inherent in the Management Agreement is an implied covenant of good faith and fair dealing,[3] and Defendants breached this covenant by failing to place her money in suitable investments, by recommending that she trade on an unsuitable margin account, and by not disclosing to her that Trainer Wortham was going to kick back a secret referral fee to First Republic. ER 55-56.

The District Court held that this is a claim for breach of an oral agreement, carrying a two year statute of limitations under California law (Calif. Code of Civil Procedure §339, subsection 1), which therefore bars this claim. ER 767:15-20.

But California law provides for a "discovery" rule for breach of a covenant in an oral contract, at least where the breach is based on a claim of

[3] Under California's implied covenant of good faith and fair dealing,

> There is implied in every contract a covenant by each party not to do anything which will deprive the other parties thereto of the benefits of the contract. . . . [T]his covenant not only imposes upon each contracting party the duty to refrain from doing anything which would render performance of the contract impossible by any act of his own, but also the duty to do everything that the contract presupposes that he will do to accomplish its purpose. [*Harm v. Frasher*, 181 Cal.App.2d 405, 417 (1960)]

negligence, as is the case here. In *Seelenfreund v. Terminix of Northern Cal., Inc.,* 84 Cal.App.3d 133, 136 (1978), the court held that **"**the statute of limitations began to run when appellant knew or should have known that the contract had been negligently breached."

As this Court has recognized, in California, "where a fiduciary relationship exists, 'facts which would ordinarily require investigation may not excite suspicion, and ... the same degree of diligence is not required.'" *Upingco v. Hong Kong Macau Corp.*, 935 F.2d 1043, 1045 (9th Cir. 1991).

In *Electronic Equipment Express, Inc. v. Donald H. Seiler & Co.*, 122 Cal.App.3d 834 (1981), the court held that under California law, "the same degree of diligence is not required where a fiduciary relationship exists between the parties at the time the alleged acts of negligence occur." *Id.* at 855. The court upheld a jury instruction that stated:

> In the presence of a fiduciary relationship, the usual duty of diligence to discover facts giving rise to a cause of action does not exist. Since a fiduciary has a duty to make a full disclosure of the facts which might materially affect the rights of the parties, the party to whom the fiduciary duty is owed is entitled to rely on the fiduciary making a full disclosure, and cannot be penalized by failure to investigate circumstances which, in the absence of a fiduciary relationship, might cause a reasonable man to investigate. [*Id.* at 855]

The same theme was noted in *Sanchez v. South Hoover Hospital*, 18 Cal.3d 93 (1976), where the court held:

> [T]he patient is fully entitled to rely upon the physician's professional skill and judgment while under his care, and has little choice but to do so. It follows, accordingly, that during the continuance of this professional relationship, which is fiduciary in nature, the degree of diligence required of a patient in ferreting out and learning of the negligent causes of his condition is diminished. This principle is not confined to the physician-patient relationship alone but exists in other contexts as well, in which it is generally held that existence of the trust relationship limits the duty of inquiry. [*Id.* at 102; internal citations omitted.]

In this situation, there is at least a triable issue of fact regarding whether Betz should have believed that Defendants negligently breached their implied covenant of good faith and fair dealing before June of 2002, when Castro finally told Betz that Trainer Wortham and First Republic Bank “were not going to do anything at all.” (ER 707:21-24), and Betz then realized that Defendants’ representations and promises had been false and merely attempts to induce her not to take legal action. ER 707:24-26.

Alternatively, the implied covenant of good faith and fair dealing is also implied into the *written* agreement entered into by Betz and Trainer Wortham on June 7, 1999. See ER 380-384. A four-year statute of limitations applies to breach of written agreements (California Code of Civil Procedure §337), and Defendants breached that covenant within four years of the filing of the complaint.

V. THERE IS A TRIABLE ISSUE OF FACT REGARDING WHETHER THE STATUTE OF LIMITATIONS HAD RUN ON BETZ'S STATE LAW CLAIM FOR *NEGLIGENT MISREPRESENTATION*.

Count IV of the SAC alleges that Defendants negligently and falsely represented to Betz that her $2.2 million could be invested in conservative securities while still enabling her to withdraw $15,000 each month. ER 56-57.

The District Court held that California Code of Civil Procedure §337(1) imposes a two-year statute of limitations on this claim, and therefore the claim is untimely. ER 767:22-768:4.

The statute of limitations for negligence in California is two years. Calif. Code of Civil Procedure §337(1). But, "Under California's discovery rule, the accrual date of a cause of action is delayed until the plaintiff is aware of her injury and its negligent cause." *Hopkins v. Dow Corning Corp.*, 33 F.3d 1116, 1120 (9th Cir. 1994). See also *Norgart v. Upjohn Co.,* 21 Cal.4th 383, 389 (1999).

As discussed above, the District Court applied the federal discovery rule improperly. If the Court agrees with the argument above, then it should hold that the District Court also ruled erroneously on Count IV, because under California law, "the same degree of diligence is not required where a fiduciary relationship exists between the parties at the time the alleged acts of negligence occur." *Electronic Equipment Express, Inc. v. Donald H. Seiler & Co.*, *supra*, 122 Cal.App.3d at 855.

In this situation, there is at least a triable issue of fact regarding whether Betz should have known that Defendants were negligent before June of 2002, when Castro finally told Betz that Trainer Wortham and First Republic Bank "were not going to do anything at all" (ER 707:21-24), and Betz then realized that Defendants' representations and promises had been false and merely attempts to induce her not to take legal action. ER 707:24-26.

VI. THERE IS A TRIABLE ISSUE OF FACT REGARDING WHETHER THE STATUTE OF LIMITATIONS HAD RUN ON BETZ'S STATE LAW CLAIM FOR *UNFAIR BUSINESS PRACTICES*.

Count V of the SAC alleges that Defendants engaged in unfair and fraudulent business practices by making the false promises to Betz previously alleged and by paying the secret kickback to First Republic Bank. ER 57-59.

The District Court held that California Business & Professions Code §17208 imposes a four-year statute of limitations on this claim, which accrued in June of 1999, so it too is time-barred. ER 768:21-769:11. This was error.

Defendants' misrepresentations to Betz occurred not just at the outset of their relationship, but *continuously throughout the entire time they held her money*. See ER 707:24-708:2. Therefore, under California law, the statute of limitations did not begin to run until the last of these continuous misrepresentations occurred (in June of 2002, when Castro told Betz that Trainer Wortham and First Republic Bank "were not going to do anything at all." ER 707:21-24. In *Suh v. Yang*, 987 F.Supp. 783, 795 (N.D. Cal. 1997), the court interpreted California's unfair competition law, holding that "Plaintiff's claim for unfair competition would not be barred by the four year statute of limitations since the alleged wrongs (i.e., the wrongful use and dilution of Suh's service marks) are multiple, continuous acts, and some of these acts have occurred within the limitations period."

The payment of the secret kickback was, presumably, not continuous, but a one-time payment. The District Court assumed that this occurred in June of 1999, when Betz signed a written agreement with Trainer Wortham that mentions a "referral fee." But this agreement states that Trainer Wortham "will remit" such a fee to First Republic, not that Trainer Wortham "has remitted" the fee (ER 380), and there is nothing in the record that indicates *when* this payment was in fact made. As payments are normally made about 30 days after billing, it may reasonably be inferred that this payment was made in the middle of July of 1999, which would be within four years before the complaint was filed on July 11, 2003. See *Anderson v. Liberty Lobby, supra*, 477 U.S. at 242, 255 (1986) (on motion for summary judgment, court considers evidence that supports the party opposing the motion for summary judgment — and all reasonable inferences therefrom).

In sum, the District Court erred in ruling that there is no triable issue of fact on Count V.

CONCLUSION

The District Court's grant of summary judgment should be reversed.

Respectfully submitted,

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STATEMENT OF COMPLIANCE WITH RULE 32(A)(7)

This brief is 9,047 words long, which is less than the 14,000 word limit imposed by Rule 32(A)(7).

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____
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