COURT OF APPEALS OF NEW MEXICO
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IN THE COURT OF APPEALS OF THE STATE OF NEW MEXICO

PING LU; JILL MCKEON, RICHARD MCKEON, STEPHEN SPENCER, SPENCER STOPA; and JUDY C. WINNEGAR, on their own behalf and on behalf of a class of similarly situated persons,

Plaintiffs/Appellants,

v.

THE EDUCATION TRUST BOARD OF NEW MEXICO; THE EDUCATION PLAN TRUST OF NEW MEXICO; and THE STATE OF NEW MEXICO,

Defendants/Appellees.

No. 31,363

First Judicial District Court, County of Santa Fe

The Honorable Stephen Pfeffer

REPLY BRIEF OF APPELLANTS

ORAL ARGUMENT REQUESTED

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STATEMENT OF COMPLIANCE

This brief complies with Rule 12-213(F)(3) NMRA, in that the body of the brief contains 4,399 words, from the Introduction through the Conclusion, as

determined by Microsoft Word 2003. In compliance with Rules 12-213(F) and 12-305(C)(1) NMRA, this brief has been prepared in 14-point Times New Roman font, a proportionally spaced typeface that includes serifs.

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INTRODUCTION

The Parents have contracts with the State—contracts governing the investment of the Parents' college savings. Under those contracts, the Parents' savings were to be invested conservatively. The State breached that promise of conservative investment. Because of that breach, the Parents lost much of the money they were saving for college. They seek to hold the State liable for its breach, but the district court's ruling erroneously shields the State from liability.

There are two main grounds requiring reversal of the district court. Each of these grounds is enough on its own to require reversal.

First, the State, through statute, has made itself liable on written contracts. The Education Trust Act does not implicitly repeal that waiver of sovereign immunity, nor does it abrogate the State's contractual duties. Instead, it simply provides that no duties beyond those in the contracts shall be recognized. The State, by contrast, interprets the Act to immunize it from all possible liability. This is an absurd result, and one that the State reaches by failing to read the Act as a whole.

Second, the Act recognizes that the State has contractual duties. The State's breach of those duties depleted the Education Trust Fund of money to recompense the Parents. The State cannot rely on a breach of contract that depleted the Fund in order to evade liability for that very breach.

To this second argument, the State has failed to meaningfully respond. The State's silence is telling: it has no effective response and tacitly concedes the second argument.

While the State stays silent about this second ground for reversal, it nevertheless raises new arguments: the State argues that the contracts themselves shield it from liability, and that this is not a breach-of-contract case.

In what follows, the Parents will first address these new and fatally flawed arguments. These arguments fail because they do not honor the State's contractual duties.

The Parents, after showing why the State's position creates absurd consequences and cannot be squared with the State's waiver of sovereign immunity, will then turn back to the two main grounds for reversal that they have advanced. Nothing in the State's brief calls either of those grounds into question.

Finally, the Parents will discuss the State's "public policy" concerns against liability. These concerns, premised on an inaccurate account of the facts and mere conjecture, carry no weight.

ARGUMENT

I. The State Assumed Enforceable Contractual Duties That May Be Vindicated in a Breach-of-Contract Action.

The State contends that its contracts with the Parents immunize it from contractual liability, and it asserts that this case is really about a breach of fiduciary duty, not a breach of contract. These arguments have one thing in common: they fail to recognize and honor the State's contractual duties.

A. The Contracts Do Not Immunize the State from Contractual Liability.

The contracts provide that the State is not liable for losses incurred "as a result of participating in the New Mexico 529 program." [RP 79, 142] The Parents' losses, however, did not result from their participation in the 529 program. They resulted from the State's breach of contract, for which the State is indisputably liable. NMSA 1978, § 37-1-23(A). Because the contractual language bars liability for losses that occur solely because of participation in the 529 program—losses due to market fluctuations, for example—the language does not bar the Parents' suit.

The State, however, interprets the contracts to preclude liability for *any* loss. [AB 3, 8, 14] Under the State's interpretation, the language would preclude recovery not only for losses caused by mere participation, but also for losses caused by any

breach of contract. This interpretation ignores both the contracts and contract law itself.

Under this interpretation, the contracts themselves would immunize the State, the 529 program, and the Education Trust Board from all conceivable liability to the Parents, and thus no longer impose enforceable obligations. The contracts would then be illusory contracts—not contracts at all. *Bd. of Educ. v. James Hamilton Constr. Co.*, 119 N.M. 415, 420, 891 P.2d 556, 561 (1994).

If there is one thing that is clear from the agreements, it is that they are intended to be legally enforceable contracts. The participation agreements and plan descriptions are described as "binding agreement[s]" that come into effect once the 529 participant's application has been accepted. [RP 63, art. VII.11; RP 126, art. VII.11] This "binding" effect is made still clearer by the agreements' merger provision, which states that the agreements "supersede[] any prior agreement, oral or written, and any other communications between the parties hereto." [*Id.*] This merger provision was evidently drafted with the parol evidence rule in mind—a rule of contract law that would have been unnecessary to account for if the agreements had been something other than binding contracts.

Because the State's interpretation renders the contracts illusory, it also fails to acknowledge the very reason that the State, the Board, and the Parents entered into

them in the first place. There is no point in entering into an agreement if there is no remedy for its breach. The State's interpretation must therefore be rejected. *See Smith v. Tinley*, 100 N.M. 663, 665, 674 P.2d 1123, 1125 (1984) ("[A]n interpretation rendering a contract such that reasonable men would not enter into it is disfavored.").

Even if the contractual language could bear the State's construction, the Parents' construction would still prevail as a matter of law. When contractual language can bear two different interpretations—one that favors the drafter and another that does not—courts choose the interpretation that does not favor the drafter. *Id.* Here, the drafter is the Education Trust Board [RP 78, 141 (Board retains right to amend)], and under the State's interpretation the contract would favor the Board by shielding both the Board and the State from liability. Under the Parents' interpretation, by contrast, neither is shielded. Thus, the Parents' interpretation prevails.

B. The Parents Allege That the State Breached Binding Contracts, Not That It Breached Its Fiduciary Duties.

The State, again failing to honor and recognize its contractual duties, tries to recharacterize this lawsuit. It contends that this case is really about a breach of fiduciary duty, not a breach of contract. Because this lawsuit implicates valid, written contracts, the State's attempt to rest on tort immunity is unavailing.

The State, maintaining that a trustee is shielded from contract claims, emphasizes that the Education Trust Board is the trustee of the 529 program. [AB 14] The State, however, is not a trustee. Thus, even under the State's theory, only the *Board*, and not the *State*, could be shielded from contract claims.

The State's argument is also legally incorrect. "Conduct that breaches a fiduciary duty might *also* violate other legal rules; it might constitute a tort (such as fraud) or breach of contract." *In re Evangelist*, 760 F.2d 27, 31 (1st Cir. 1985) (Breyer, J.). The State signed binding contracts, breached its duties under those contracts, and caused the Parents damage. [RP 391–392, ¶¶ 91–94] These are the elements of a breach-of-contract claim. *Camino Real Mobile Home Park P'ship v. Wolfe*, 119 N.M. 436, 442, 891 P.2d 1190, 1196 (1995). As much as the State may wish that the Parents had brought fiduciary claims, they did not. "A defendant cannot force the plaintiff to accept the burden of proving theories upon which he does not wish to rely." *Enriquez v. Cochran*, 1998-NMCA-157, ¶ 71, 126 N.M. 196, 967 P.2d 1136 (1998); *cf. Adobe Masters, Inc. v. Downey*, 118 N.M. 547, 548, 883 P.2d 133, 134 (1994) (claims for substandard services rendered under contract may be brought under either negligence or breach-of-contract theory); *Vinnell Corp. v.*

State, 85 N.M. 311, 512 P.2d 71 (1973) (despite plaintiff's allegations of negligence, action was a contract action where it was based on a written contract).[1]

II. The State's Argument for Immunity Creates Absurd Results and Repeals an Earlier Statute.

The State's position conflicts with fundamental legal principles because it would create absurd results and repeal an earlier statute. For these reasons alone, the district court should be reversed.

A. Absurd Results Spring from the State's Argument for Immunity.

The Court should reject the State's position because it renders the Education Trust Act "absurd, unreasonable, [and] unjust." *State v. Santillanes*, 99 N.M. 89, 90, 654 P.2d 542, 543 (1982). Under the State's interpretation, the Parents have no recourse at all for breaches of their contracts, even if the State simply looted the Education Trust Fund. Indeed, the State admits that its reading leaves the Parents without a remedy. [AB 24 (noting that not even mandamus is available against the State)] The Legislature did not intend such an absurd and unjust result.

[1] The State also quotes language from the Declaration of Trust purporting to shield the Trustee from liability when "following any direction" given by an "investment manager." [AB 15] This language would apply, if at all, only to the Board and not the State. In addition, this is a new factual argument that would require determining whether the Board followed any of Oppenheimer's directions in this case.

B. Because Immunizing the State from Liability Would Necessarily Repeal an Earlier-Enacted Waiver of Sovereign Immunity, the State's Argument for Immunity Should Be Rejected.

The State, trying to get around the presumption against implied repeal, argues that because the Act does not wholly repeal Section 37-1-23(A)'s waiver of sovereign immunity for written contracts, it provides an "exception" to that waiver. [AB 6] According to the State, implied exceptions to an earlier statute, unlike implied repeals, are not disfavored. [*Id.*] New Mexico courts, however, draw no such distinction. What the State calls an implied exception,[2] the courts call an implied "partial repeal or amendment." *State ex rel. Sanchez v. Reese*, 79 N.M. 624, 626, 447 P.2d 504, 506 (1968). Implied partial repeals or amendments, like full repeals, are not "looked upon with favor." *Id.* Because the same presumption against implicit repeal applies here, *Kahrs v. Sanchez*, 1998-NMCA-037, ¶ 24, 125 N.M. 1, 956 P.2d 132, an implicit repeal will be found only where it is necessary to give effect to the Act. [BIC 15] Here, the Act does not impliedly repeal the State's earlier waiver of sovereign immunity. Rather, it simply provides that the Parents are afforded no guarantees above and beyond those in their contracts with the State. [BIC 25]

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[2] In their district court briefing [RP 474], the Parents used this term, which is functionally interchangeable with "partial repeal." The State is thus wrong to suggest [AB 6] that the question was not preserved. *Garcia ex rel. Garcia v. La Farge*, 119 N.M. 532, 540, 893 P.2d 428, 436 (1995).

Because an implicit repeal is not necessary to give effect to the Act, the State's interpretation cannot stand.

III. The Language of the Education Trust Act Does Not Forbid Recovery from Sources Other Than the Education Trust Fund.

The Education Trust Act does not preclude the Parents from recovering for their losses from any source other than the Education Trust Fund. The State's argument to the contrary is unpersuasive.

A. Because the State Fails to Read the Act as a Harmonious Whole, Its Interpretation Should Be Rejected.

According to the State, the first and second sentences of the Act's relevant provision, Section 21-21K-3(C), both do the same thing: they preclude certain kinds of contractual liability from encumbering certain funds. [AB 10–11] The first sentence, according to the State, forbids any liability of the 529 program from encumbering three specified funds.[3] [AB 11] The second sentence, under the State's reading, forbids liabilities that arise from the Parents' contracts from encumbering anything other than the Education Trust Fund. [*Id.*] But these parallel tasks call for parallel language, *State ex rel. Udall v. Colonial Penn Ins. Co.*, 112 N.M. 123, 128–

[3] Section 21-21K-3(C)'s first sentence does not implicitly prohibit the encumbrance of the general fund. [*Contra* AB 10 n.20] The State reads language into the Act that is not there, *State v. Trujillo*, 2009-NMSC-012, ¶¶ 11–12, 146 N.M. 14, 206 P.3d 125, and violates the *inclusio unius* canon. [BIC 20]

29 & n.7, 812 P.2d 777, 782–83 & n.7 (1991), and the two sentences do not have parallel language.

The first sentence forbids liabilities from encumbering certain funds:

> In no event shall any liability of, or contractual obligation incurred by, [the 529 program] obligate or encumber [three specified funds].

NMSA 1978, § 21-21K-3(C). By contrast, the second sentence merely disavows the affirmative "creat[ion]" of obligations by the Act:

> Nothing in the Education Trust Act *creates* any obligation . . . to fulfill the terms of any college investment agreement . . . out of any source other than the education trust fund.

Id. (emphasis added). It does not forbid obligations created *elsewhere*—such as in the Parents' contracts—from encumbering any fund.

If, as the State claims, the Legislature intended for the two sentences to have parallel tasks, it would have used parallel language. In that case, the second sentence would have read:

> In no event shall any obligation . . . to fulfill the terms of any college investment agreement . . . obligate or encumber any source other than the education trust fund.

That, of course, is not what the statute says. Because the State's interpretation cannot account for the markedly different language in each sentence, it cannot be accepted. *See, e.g.*, *State v. Juan*, 2010-NMSC-041, ¶ 39, 148 N.M. 747, 242 P.3d 314 ("[A]

statute must be construed so that no part of the statute is rendered surplusage or superfluous." (citation and quotation marks omitted)).

The State, however, says that because the Parents' contracts are authorized by the Education Trust Act, they are among those things "in the Education Trust Act" that do not "create[]" obligations. NMSA 1978, § 21-21K-3(C). Once again, the State's interpretation fails to read the Act as a whole because it renders its language inexplicable. The first sentence of Section 21-21K-3(C) states:

> In no event shall any liability of, or contractual obligation incurred by, *the program established pursuant to the provisions of the Education Trust Act* obligate or encumber [three specified funds].

Id. (emphasis added). Under the State's theory, "the program established pursuant to the provisions of the Education Trust Act" would be "in" the Act, since any entity that is authorized by the Act is "in" the Act. But if any entity authorized by the Act is "in" the Act, the Legislature could have written the first sentence simply as:

> In no event shall any liability in, or contractual obligation incurred by, *the Education Trust Act* obligate or encumber [three specified funds].

Instead of "the Education Trust Act," the Legislature chose a much more specific phrase: "the program established pursuant to the provisions of the Education Trust Act." *Id.* This phrase indicates that the Legislature drew a distinction between what the Act authorizes (addressed in the Provision's first sentence) and the Act itself (addressed in the second sentence). Because the State's reading of the Provision

obliterates this crucial difference in language, the Court should reject it. [BIC 19–20]

The State thus fails to harmonize the different language of the two sentences. *See State ex rel. Klineline v. Blackhurst*, 106 N.M. 732, 735, 749 P.2d 1111, 1114 (1988) (statutory language must be read together to produce "harmonious whole"). And yet the State accuses the Parents of failing to read the statute as "a harmonious whole." [AB 9] The State forgets that reading a statute as a harmonious whole requires analyzing different language differently. *See State v. Jade G.*, 2007-NMSC-010, ¶ 28, 141 N.M. 284, 154 P.3d 659 (when a statute uses certain words in one place but omits them elsewhere, that difference is presumed to be intentional); *Romero v. Valencia Cnty.*, 2003-NMCA-019, ¶¶ 8–10, 133 N.M. 214, 62 P.3d 305 (construing an enactment as a whole by contrasting different language used in different sections). The Parents account for the crucial differences in language within the Act. Because the State does not, its interpretation must be rejected.

B. The Parents' Interpretation of the Act Does Not Rely on the Difference Between the Words "Liability" and "Obligation."

The State contends that the Parents' interpretation turns on the difference between "liability" in Section 21-21K-3(C)'s first sentence and "obligation" in its second. [AB 11–12] The Parents make no such argument.

The *whole phrase* "any obligation, legal, moral or otherwise," NMSA 1978, § 21-21K-3(C), indicates the *purpose* of the Act's second sentence: to ensure that the Provision complies with the New Mexico Constitution's restrictions on indebtedness. [BIC 24] The Parents have never relied on the difference between "liability" and "obligation" to discern the meaning of the second sentence of Section 21-21K-3(C).

IV. The Fact that the State Depleted the Education Trust Fund Does Not Absolve It of Liability for Breach of Contract.

As the Parents pointed out in their Brief in Chief, the State is liable in full even if the Education Trust Fund were the sole source from which liability may be satisfied. [BIC 26–32] The facts supporting that conclusion are straightforward. The State assumed contractual duties over the Parents' investments in the Education Trust Fund. [RP 377–378, ¶¶ 29–30] The State breached these contractual duties. [RP 381–384, ¶¶ 42–52] This breach depleted the Education Trust Fund of the money necessary to satisfy the State's liability to the Parents. [BIC 27] Thus, the Education Trust Fund lacks sufficient money to satisfy the State's liability to the Parents only because the State breached its contractual duty.

To evade liability for its breach of contract, the State now relies on the depletion of funds caused by that very breach. There are three reasons why this reliance is misplaced.

First, as a matter of common sense, the State cannot use its own breach to bootstrap its way into contractual immunity and evade its contractual duties—contractual duties that the State necessarily retains even under its own reading of the Act. According to the State, the Act designates the Education Trust Fund as the sole source of funds from which "the terms of any college investment agreement" must be "fulfill[ed]." NMSA 1978, § 21-21K-3(C). If these "terms" were not binding contractual duties, the Act would not have to designate a source from which they must be "fulfill[ed]." But those duties are only binding if they can be enforced. And they can only be enforced by recognizing that, for purposes of the Parents' recovery, the Education Trust Fund extends not just to what is currently in the Fund, but what *would* be in the Fund if the State had not breached its contractual duties. [BIC 28]

Second, the Legislature deliberately chose not to limit the Parents' recovery to only what was *currently* in the Education Trust Fund. Like the Education Trust Act, the Ground Water Protection Act says that it "creates" no liability that must be satisfied from any source other than one particular fund—in the case of the Ground Water Protection Act, the "corrective action fund." NMSA 1978, § 74-6B-14. But unlike the Education Trust Act, the Ground Water Protection Act specifies that the state has no further responsibility "if the balance in the fund is insufficient to cover" costs that must be satisfied out of that designated fund. The Legislature knew how to

limit liability to the balance currently in a fund, but chose not to do so in the Education Trust Act. [BIC 31–32] The State offers no response to this argument.

Third, longstanding precedent shows that the State cannot escape liability just because its breach depleted the Education Trust Fund. *Crist v. Town of Gallup*, 51 N.M. 286, 183 P.2d 156 (1947) and *Gray v. City of Santa Fe*, 89 F.2d 406 (10th Cir. 1937) hold that when a breach of contract depletes the source of funds from which contractual liability must be paid, the breaching party is liable in full—even if liability is explicitly limited to that source.

While the State does not mention *Crist* or *Gray* by name, it apparently refers to them in one sentence: "Mandamus is analogous to the contract remedy of specific performance, and this explains the bond cases cited by Appellants." [AB 25] This is all that the State says about these two cases.

The State seems to be arguing that, just as *Crist* and *Gray* made specific performance available to plaintiff bondholders, so mandamus, a supposedly "analogous" remedy, is available to the Parents. But *Crist* and *Gray* did not address specific performance. Rather, they both stated that *damages*, rather than specific performance, were available to the plaintiffs. *See Crist*, 51 N.M. at 289, 183 P.2d at 158 (holding that an "action for damages" was available to the plaintiff); *Gray*, 89 F.2d at 412 (holding that the plaintiffs could replead to bring an "action for the

damages properly recoverable for the alleged breaches of contract"). Damages are not specific performance. *See, e.g.*, *McCoy v. Alsup*, 94 N.M. 255, 262, 609 P.2d 337, 344 (1980). The State's analogy gets the holding of *Crist* and *Gray* backwards.

The State also appears to argue that *Crist* and *Gray* are inapposite because they involved bonds. That distinction does not make a difference. A bond is a contract, 12 Am. Jur. 2d *Bonds* § 1, and neither *Crist* nor *Gray* made their holdings turn on the *kind* of contract at issue. In fact, *Gray* stated that it was addressing "breaches of contract." *Gray*, 89 F.2d at 412. Because the Parents and the State entered into contracts, *Crist* and *Gray* are on point.

V. It Is Just and Equitable to Recognize That the State Is Liable to the Parents for Its Breach of Contract.

A. Liability Is Consistent with Public Policy.

1. *The State's potential liability is sharply limited.*

The State says that recognizing its liability would end the 529 program because potential liability would be ruinous, and that "no sane Legislature" would have allowed the State to be liable to the Parents. [AB 23] This argument vastly inflates the State's potential liability.

The State reaches its inflated estimate because it wrongly assumes that the Parents' claim would make the State a guarantor against "market risk" [AB 21], and leave the State "on the hook for [the] *entire amount*" of the Education Trust Fund

[AB 19 (emphasis added)]. But recognizing the State's liability for breach of contract does not make the State the guarantor of the entire Trust Fund against market risk. Making the State a guarantor is *not* what the Parents contend for. They seek to hold the State to its promise of certain contractual duties, not to any particular result.

The State's estimate of its potential liability is inflated for another reason, too: it assumes that it alone would be liable for a breach of contract. But as the State's settlement with Oppenheimer shows, indemnification is available here, and will be available to the State in any similar breach-of-contract action. [RP 912]

2. *Because the State's potential liability is sharply limited, the Legislature's failure to fund the liability in advance proves nothing.*

The State's liability is limited—and perhaps ultimately nonexistent—since it has retained its right to seek full indemnification from Oppenheimer. [RP 912] The State's limited liability explains why the Legislature has not appropriated money in advance to satisfy liability to the Parents: unless the State fails to enforce its indemnification rights, it will be Oppenheimer, and not the State, that will have to fund the liability.

Of course, there is an even simpler explanation for this lack of advance appropriation: the Legislature did not expect that the State would breach its contracts with the Parents.

3. *Liability will not lead to a conflict with the Legislature.*

Contrary to the State's speculation, contractual liability will not create a conflict between the courts and the Legislature. In part, this argument fails because of what it obscures: if a judgment is entered against the State, there need not be a legislative appropriation, since the State can seek indemnification from Oppenheimer. [RP 912]

But at bottom, the State's speculation is just that: speculation. It unfairly assumes the worst of the Legislature—that the Legislature will refuse to pay a lawful judgment. It also wrongly assumes that recognizing the State's liability to the Parents would be a misunderstanding of the statute. [AB 22]

B. Recognizing the State's Liability Helps, Not Harms, the Victims of a Breach of Contract.

The State claims that recognizing its liability would leave the victims of a breach of contract worse off. Potential liability, it claims, would lead to delayed recovery because "the State would need to know the scope of its liability before it could pursue any indemnification or third-party claims." [AB 16] To be sure, indemnification cannot proceed until the State's liability has been determined—but

the alternative to this "delayed" recovery is no recovery at all for the victims of the State's breach of contract.[4] Perhaps the State is suggesting that potential liability would delay the State's own freestanding lawsuit against a third party. That suggestion is untrue. The State has *already* entered into a settlement with Oppenheimer that recovered a portion of the losses and preserved its indemnification rights.

The State's claim that this lawsuit has delayed the distribution of proceeds from the Oppenheimer settlement [AB 17] is factually incorrect and has no relevance to the legal issues before this Court. Under the State's settlement with Oppenheimer, 529 participants who did not fully release Oppenheimer would have to wait two years for their distribution. [RP 1263–1264] It is the State that agreed to settlement terms that delayed the distribution of funds. It is in no position to blame the Parents for questioning the settlement's fairness.

CONCLUSION

The State's statutory interpretation fails because it ignores the State's earlier waiver of sovereign immunity and does not account for crucial statutory language.

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[4] The State also claims that mandamus against the Board remains open even if its liability to the Parents is foreclosed. [AB 24] But mandamus will be unavailable, and the Parents will be left without recompense from *any* source, if the Board decides in future cases *not* to pursue an action against the 529 program manager (here, Oppenheimer).

Independently from that, the State must still be liable in full, for it cannot evade its contractual duties by breaching them. For these reasons and the others that the Parents have given, the district court's judgment should be reversed.

Respectfully submitted,

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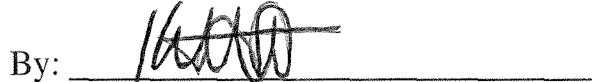
By: 
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CERTIFICATE OF SERVICE

I HEREBY CERTIFY that on the 27th day of April, 2012, I caused to be delivered a true and correct copy of the foregoing on the following counsel by U.S. mail, postage prepaid:

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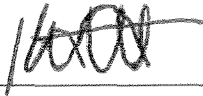

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