SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK

THE PEOPLE OF THE STATE OF NEW YORK, by ERIC T. SCHNEIDERMAN, Attorney General of the State of New York, Plaintiffs, - against - JOHN C. MOORE, ROBERT HINKLE, MICHAEL LAKOW, DIANA PIKULSKI, HAYWARD R. PRESSMAN, LESLIE PRIGGEN, JOHN S. RAINEY, MARGARET SANTULLI, AND THOROUGHBRED RETIREMENT FOUNDATION, INC., Defendants.	Index No. 401004-12 Assigned to: **ORAL ARGUMENT REQUESTED**

PLAINTIFFS' MEMORANDUM OF LAW IN OPPOSITION TO DEFENDANTS' MOTION TO DISMISS THE VERIFIED COMPLAINT

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Plaintiffs, the People of the State of New York, by their attorney, ERIC T. SCHNEIDERMAN, Attorney General of the State of New York ("Attorney General"), respectfully submit this Memorandum of Law, together with the accompanying affidavits and the exhibits thereto,[1] in opposition to Defendants' motion to dismiss Plaintiffs' Verified Complaint.[2]

PRELIMINARY STATEMENT

Defendants' meritless "motion to dismiss" is clearly intended more for its desired public relations value than as a serious filing with the remotest possibility of success in a court of law. Defendants devote almost no attention to the serious allegations of the Attorney General's Complaint. Instead, they dwell at length on what they describe as their impeccable standing and reputations, and on the supposedly "inexplicable" decision of the Attorney General to commence this action.

Far from being inexplicable, the Complaint -- as well as the substantial evidentiary material submitted herewith -- demonstrate beyond question that this action was commenced for a simple, compelling reason: the horses' welfare demanded it. For years, the leadership of the Thoroughbred Retirement Foundation, Inc. ("TRF") recklessly took in far more horses than the organization could support. For years, the TRF has tried, and too often failed, to support its oversized herd on an amount per horse per day that is far below the standards in the equine rescue industry. Indeed, for all their invective and posturing, Defendants do not deny that their average per horse expenditure barely reaches $3 per day, nor do they dare suggest any

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[1] Plaintiffs' Memorandum of Law is accompanied by the affidavits of David E. Nachman, sworn to May 22, 2012 ("Nachman Aff."), Stacey Huntington, D.V.M., sworn to April 30, 2012 ("Huntington Aff."), Anne Lear, sworn to April 27, 2012 ("Lear Aff."), David R. Fix, sworn to April 30, 2012 ("Fix Aff."), Suzanne Peugeot, sworn to May 14, 2012 ("Peugeot Aff."), and Julie Walawender, sworn to May 17, 2012 ("Walawender Aff."). The Verified Complaint ("Complaint" or "Compl.") is attached as Exhibit A to Mr. Nachman's affidavit.

[2] The Defendants are John C. Moore, Robert Hinkle, Michael Lakow, Diana Pikulski, Hayward R. Pressman, Leslie Priggen, John S. Rainey, Margaret Santulli (collectively, the "Director Defendants") and TRF. With the exception of Mr. Rainey, a former director, the Director Defendants are current directors of TRF. Compl. ¶¶ 21-24.

responsible observer would regard that paltry sum as adequate.

The stark mismatch that TRF's board allowed to develop between TRF's financial resources and the size of its herd has had predictably disastrous consequences: substantial numbers of underfed horses, inadequate veterinary care, failure to provide the basic hoof and dental care that horses require, horses going without vaccinations, untreated wounds , horses going missing and remaining unaccounted for, and even deaths from neglect.

These undeniable facts come not only from the sworn statement of the highly accredited independent veterinarian who personally examined most of TRF's horses before she was summarily fired by TRF's board, but also from one of its own employees: the manager of a well-run Virginia farm to which TRF transfers horses for re-feeding and other restorative care after they have been mistreated at other TRF facilities. In a powerfully detailed sworn statement, this conscientious TRF employee has come forward to describe how TRF has continued to neglect the welfare of horses at certain facilities, and how its chronic inability to pay its bills on time has strained even her own farm's ability to provide proper care to the horses.

Defendants' effort to distract attention away from their long-running neglect and mistreatment of these living beings rests principally on a collection of notarized statements from TRF's farm managers and regular attending veterinarians, most of whom report, in the most summary and conclusory terms, that present conditions at the farms after one of the mildest winters in U.S. history are generally fine. These reports, and their seeming unanimity, are not creditable. They are proffered by farms financially beholden to TRF and an organization that repeatedly represented to the Attorney General, in the course of a year-long investigation, that there were no issues with respect to the health and welfare of TRF's herd. These repeated assurances turned out to be false: at the very times they were made, TRF was neglecting horses

in New York, and allowing ill-treated horses to deteriorate further at a Kentucky farm that should have been closed last year.

Putting aside their factual distortions, Defendants' motion fails as a matter of law. This is, first, a motion to dismiss, where the well-pleaded facts of the Complaint are deemed true, and the sole issue is the sufficiency of the pleaded causes of action. Defendants disregard this basic axiom, absurdly pretending that the Complaint's highly detailed factual allegations should be ignored because Defendants have a document, that they themselves authored, which they say "debunk[s]" the 2011 herd examinations that exposed so many of TRF's deficiencies, or because, having previously received false assurances about the herd's condition, the Attorney General was obliged to wait for yet more self-serving "evidence" on that score. Second, even treated as a motion for summary judgment, the Defendants' application not only comes before legitimate discovery, but already is doomed by the obvious presence of disputed material facts. Third, the Defendants are just wrong in arguing that no New York court has upheld the removal of a not-for-profit's board members except in cases of self-dealing and misappropriation of charitable assets. The New York Court of Appeals has done precisely that, applying a legal standard -- "for cause" -- that is easily met here by the conduct of the current TRF board. Defendants ask this Court to read out of the statute books the Attorney General's enforcement powers and express authority to seek removal of directors "for cause," and hold instead that TRF's directors are answerable to no one but themselves for fostering the severe and continued neglect of living animals.

Lastly, Defendants confine their (erroneous) legal arguments to but two of the Attorney General's five pleaded causes of action, for removal and breach of the fiduciary duty of care under the Not-for-Profit Corporation Law ("N-PCL"). In doing so, Defendants have chosen to

ignore the broad remedial authority the Attorney General has under the Estates, Powers and Trusts Law ("EPTL") to bring appropriate proceedings to safeguard the proper administration of New York charities, as well as his authority under other provisions of the N-PCL to hold directors to account for violations of their statutory duties in the administration of endowment funds and other charitable assets. Defendants' motion is meritless and should be denied.

STATEMENT OF FACTS

The factual allegations of the Complaint supporting Plaintiffs' claims, along with the substantial evidentiary material accompanying this memorandum, are summarized below.

I. The Director Defendants Recklessly Over-Expanded the TRF Herd

The TRF board recklessly allowed the size of the TRF herd to grow unchecked for years, far beyond the size its finances could support, consciously disregarding the impact this overexpansion would have on the health and welfare of the living creatures that it is the mission of this charity to protect. Compl. ¶¶ 29, 34-41. As a result, TRF's finances progressively deteriorated: TRF has had negative cash flow in each year since 2005, a six- or seven-figure operating loss in all but two of those years, and is regularly months late in making payments to the farms and other providers that take care of its horses. *Id.* ¶¶ 34-37. Defendants now have admitted that the TRF board "'clearly recognized' as early as late 2005 that the TRF had to reduce the size of its herd." Br. at 16.[3] Despite knowing it could not afford to take on additional horses, TRF's leadership accepted *over 500 new horses* into the herd between 2006 and 2010, Compl. ¶¶ 37-38, a fact uncontested by Defendants and conclusively demonstrated by the year-by-year herd count submitted with their motion. *See* Ostrager Aff. Ex. D ("Intakes").

The Director Defendants seek to camouflage these years of reckless overexpansion by

[3] "Br." refers to Defendants' Memorandum of Law in Support of Defendant Directors' Motion to Dismiss Plaintiffs' Verified Complaint, dated May 11, 2012; "Ostrager Aff.," "Moore Aff." and "Gagliano Aff." refer respectively to the affidavits of Barry Ostrager, John C. Moore III and James Gagliano submitted therewith by Defendants.

emphasizing the decline in overall herd size from a peak of 1,348 in 2006, to 1,029 today. Br. at 6-7, 16-17. Yet it is the hundreds of deaths in the TRF herd since 2006, not any responsible action by TRF's directors, that account for this decline in absolute terms.[4] Moreover, Defendants have admitted publicly that the herd remains hundreds of horses too large: an October 2011 TRF press release, describing the "crisis" confronting TRF, quoted then CEO Rob Hinkle as stating that "TRF needs both to increase donations and to reduce herd costs by immediately placing as many as 200 to 300 horses in Foster Care." Ostrager Aff. Ex. O; Compl. ¶ 78.

Defendants tout the "moratorium on the acceptance of new horses" the directors adopted by resolution in February 2011 (Br. at 17), but do not dispute that they subsequently accepted over 20 new horses into the TRF herd, including horses belonging to Mr. Moore and Mr. Pressman personally. Compl. ¶¶ 39-40. These self-dealing transactions violated the moratorium and stand to save these directors each tens of thousands of dollars in future horse care costs.

II. TRF's Substandard and Chronically Late Payments to Its Boarding Facilities and Its Inadequate Supervision Put the Herd at Risk

The Director Defendants endangered the TRF herd by cutting horse care spending to substandard levels, regularly failing to pay the boarding facilities and other vendors who care for the horses on time, and not adequately supervising the care provided to its horses.

Having over-expanded the herd for years, the Director Defendants resorted to drastic cutbacks in horse care expenditures, at the expense of the TRF herd's health and welfare, despite repeated warnings that their spending on the horses was dangerously low. Compl. ¶¶ 44-49. In late 2009, the TRF board instituted a $3 daily per-horse payment (the "per diem") for the care of

[4] *See* Compl. ¶ 57; Ostrager Aff. Ex. D (showing 344 "Deaths" after 2006). Defendants' claim that "the number of deaths leveled off and fell along with the overall population" after 2006 (Br. at 16) is an outright falsehood, as shown by TRF's herd count summary, which shows that the annual number of deaths in TRF's herd roughly *quadrupled* from 2006 to 2010 in both absolute and proportional terms: from "23" in 2006 (1.7% of the herd), to "90" in 2010 (7.9% of the herd). *See* Ostrager Aff. Ex. D.

its herd by the satellite farms, the sum that most of the farms continue to receive today. *Id.* ¶¶ 44, 49. This per diem is grossly inadequate to cover the costs of providing proper care to a retired Thoroughbred race horse and far below acceptable industry standards: the American Veterinary Medical Association estimated the average cost of "basic care" at $5 per day in 2008; and in the December 2011 report of the New York State Task Force on Retired Racehorses, other horse rescue programs all reported average daily costs ranging from $6.85 to $10, more than *double or triple* TRF's standard per diem. *Id.* ¶¶ 46, 47; Nachman Aff. Ex. M at 11; Huntington Aff. ¶¶ 56, 66. Tellingly, nowhere in Defendants' papers do they dispute that the $3 per diem is inadequate and makes TRF an extreme outlier in the equine rescue community.

In addition to spending far too little on its horses, TRF also does not pay on time: it is regularly several months late paying the bills that boarding facilities and other horse care providers submit to TRF.[5] Compl. ¶ 36; Lear Aff. ¶¶ 36-38. Veterinarians, farriers (who care for horses' hooves) and other vendors have refused to visit or supply TRF horses and facilities because of its payment delays and defaults. Compl. ¶¶ 56, 63; Lear Aff. ¶¶ 36-38.

TRF's substandard spending and payment delinquencies place an enormous strain on its boarding facilities, which must find ways to supplement TRF's payments in order to provide proper care to the horses. *See* Lear Aff. ¶¶ 10-11, 34, 44; Walawender Aff. ¶ 9. Not all TRF facilities succeed. A December 2010 survey by a former TRF employee revealed that only four of the 17 reporting facilities were up-to-date on all four elements of basic maintenance care (farrier, worming, vaccine, dental), and several were seriously delinquent in multiple categories: "TRF was leaving it up to them to front the money for basic horse care, or to tap into their own

[5] Defendants' claim that TRF has been able to "stay current or near-current" since 2011 (Br. at 8, 19) is false, as demonstrated, *inter alia*, by Defendants' own "Aged Accounts Payable Report," showing that TRF had over $100,000 in accounts payable that were not "current" as of May 9, 2012, including over $35,000 in payables more than 60 days overdue. *See* Ostrager Aff. Ex. I at 2. The total non-current amount likely is much higher, since the report covers only 13 of TRF's farms and none of its correctional facilities or other vendors. *Id.*

resources, or to seek donations to pay these expenses, and the farm managers were responding to the shortfall by cutting back on basic care." Walawender Aff. ¶¶ 5-9, Ex. A.

TRF's board left many of its facilities not only underfunded, but also largely unsupervised. In recent years, TRF has failed to track the herd's current condition and whether, or how regularly, its facilities provide basic care to the horses. Compl. ¶¶ 50-52. By January 2012, according to internal meeting minutes, TRF still had made "no progress" in "tracking current condition, trims, vaccines, worming, dental, etc. in the herd database." Compl. ¶ 52.

III. TRF Neglected Its Horses in 2011, and Again This Year

The Defendants' strident claim that TRF's horses "consistently benefit from proper care" (Br. at 11) is a grotesque distortion of the facts. In reality, the TRF board's substandard spending on the herd and its persistent failures of oversight have placed the entire TRF herd at risk and caused the neglect, suffering, and even death, of retired race horses. Compl. ¶¶ 54-66. In early 2011, just months after the year the Director Defendants now tout as a relative financial success for TRF (Br. at 7), the disastrous consequences of their conduct were exposed by herd inspections conducted by a veterinarian, Stacey Huntington, D.V.M. Compl. ¶¶ 55-56, 58-59. Nor did the Director Defendants put an end to the suffering of TRF horses in 2011: the Attorney General's investigation has uncovered evidence of serious neglect at a correctional facility in New York and a satellite farm in Kentucky as recently as February and March 2012. *Id.* ¶¶ 62-66. The continued neglect is all the more disturbing in light of the repeated assurances that the herd was in good condition, now proven false, that the Attorney General received from Defendants throughout the investigation.

A. Dr. Huntington's 2011 TRF Herd Inspections Uncovered Severe Neglect and Widespread Basic Care Shortcomings

Between January and March 2011, Dr. Huntington, a highly experienced equine veterinarian hired by TRF to inspect its herd, identified serious deficiencies in the care provided to and the condition of many of the TRF horses and farm facilities she visited.[6] *See* Compl. ¶¶ 55-56, 58-59; Huntington Aff. ¶¶ 13-23. Dr. Huntington evaluated the horses using the Henneke Scoring System, a standardized system for determining a body condition score ("BCS"), and found hundreds of horses that did not meet TRF's own standards for proper care, including over 10% of the inspected herd with a score below 4.[7] Huntington Aff. ¶¶ 17, 22, 53. She also found that 98% of the herd had not received one or more types of required maintenance (vaccinations, wormers, dental, farrier), and referred dozens of horses for emergency dental and farrier work. *Id.* ¶ 21. The most problematic TRF facilities Dr. Huntington inspected reported long delinquent or inadequate TRF payments. *Id.* ¶¶ 30-31, 33, 45, 48, 57.

Dr. Huntington also found especially severe neglect in the TRF herd at several facilities with horses in need of intensive care and re-feeding due to malnutrition, and multiple instances of horses unaccounted for and deaths from neglect. Compl. ¶¶ 58-59.

- One TRF satellite farm in Oklahoma, the 4-H Ranch, could not produce 16 of the 63 TRF horses expected to be found there, and many of the horses recovered were emaciated. Huntington Aff. ¶¶ 32-43, Ex. 1. Dr. Huntington concluded that some of the missing horses likely died during a recent blizzard from exposure without adequate shelter, *id.* ¶ 39, a conclusion the ranch owner shared and communicated to TRF. Compl. ¶ 58.

[6] Dr. Huntington has over 20 years of experience as an equine veterinarian, has been licensed in three states, and has served as a law enforcement consultant and expert witness in multiple investigations and cases of animal abuse and neglect. *See* Huntington Aff. ¶¶ 1-7.

[7] TRF now makes the revisionist argument that the acceptable BCS range for its horses is 4 to 6. Br. at 12. For many years, however, TRF's satellite farm contracts required that its horses be maintained at a score between 5 and 7. Compl. ¶ 55; Lear Aff. ¶ 26; Huntington Aff. ¶ 17. The webpage to which Defendants point indicates only that "4-6" may be a normal range for a "Thoroughbred racehorse," Ostrager Aff. Ex. M, whereas TRF's horses are retired and, in TRF's own words, "live outside 24 hours a day, seven days a week." Br. at 13. Thoroughbreds thus exposed to the elements need additional fat cover to avoid adverse consequences. *See, e.g.*, Huntington Aff. ¶ 39.

- Dr. Huntington also found over 30 neglected and inadequately fed horses at Deer Valley Farm, a TRF satellite farm in Kentucky owned and operated by Sam Detweiler, including approximately 15 horses that were very thin or emaciated to the degree that their lives were in danger. Huntington Aff. ¶¶ 44-45, 62, Ex. 4. At the time, Mr. Detweiler was receiving a $2.50 per diem from TRF. *Id.* ¶ 45. Shortly after Dr. Huntington's inspection, three horses she had identified as dangerously underweight died as a consequence of the neglect. *Id.* ¶¶ 46-47, 63-64.

In her March 2011 report to the TRF board, Dr. Huntington recommended closing its facility at the Detweiler farm. Compl. ¶ 59; Huntington Aff. ¶ 54, Ex. 6 at 3.

On March 18, 2011, one day after an article about TRF's mistreated horses appeared in *The New York Times*, the TRF board fired Dr. Huntington before she could complete her inspections. Compl. ¶ 61; Huntington Aff. ¶¶ 49-50, Ex. 5. Defendants' claims that Dr. Huntington's findings have since been "discredited" and "debunked" are based on nothing but a self-serving, unsworn and unsigned April 2011 document "prepared by the TRF" (Br. at 12), which actually accepts several of her key findings.[8] In fact, TRF directors immediately recognized their culpability for the neglect. When Dr. Huntington informed TRF that she was reporting 4-H Ranch to an Oklahoma sheriff, one TRF director wrote another, "TRF is going to be partially at fault also due to our lack of mgmt and fiscal responsibility." Compl. ¶ 58. Internal e-mails show that TRF's leadership *knew* going into the winter of 2011 there would be problems in the herd, notwithstanding its now vaunted 2010 financial results (Br. at 7, 19).[9]

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[8] *See* Ostrager Aff. Ex. L. TRF "agrees that there were signifcant [sic] problems" at the Detweiler farm, the 4-H Ranch and another Oklahoma farm. *Id.* at 3-5. Defendants' attempt to recast neglect uncovered by Dr. Huntington as the normal symptoms of old age (Br. at 13) is untenable: she found that over 80% of the horses she evaluated were not elderly (*i.e.*, over 17) and "body conditions scores did not correlate with age." Huntington Aff. ¶ 53.

[9] In December 2010, Ms. Pikulski wrote to TRF's then Interim Herd Manager, in response to her concerns about a TRF satellite farm, "Windmill is just the problem of the day. This winter will bring other problems. We are going to have problems at Diane Templemeyer's. We will always have these problems because of the size and age of the herd and the economics." Walawender Aff. ¶ 11, Ex. B at 1. Ms. Walawender responded, "It just seems like we have too many horses and not enough money, that's the problem, not so much the age of the herd because most of the herd is between 10 and 15 years old." *Id.* *See* Moore Aff. ¶ 14 ("TRF's herd averages 13 years of age.").

B. Contrary to TRF's Assurances, the Neglect Continued In Recent Months

The Attorney General's investigation has uncovered evidence of the TRF board's ongoing failure to take proper care of its horses, including at Wallkill Correctional Facility in New York and the Detweiler farm in Kentucky, Compl. ¶¶ 62-66, demonstrating the falsity of Defendants' claim "that all TRF horses receive excellent care" (Br. at 14).

1. Neglect and Mismanagement at TRF's "Flagship" Wallkill Facility

Numerous horses at Wallkill, which TRF's Chairman calls its "flagship correctional care facility" (Moore ¶ 6), have been neglected to the point that they had to be transferred to another facility for re-feeding and other restorative care; deprived of basic maintenance care for months, and even years; and not provided veterinary attention for wounds and injuries. Compl. ¶¶ 63-64. On several occasions in recent years, including December 2011, TRF transferred batches of ailing horses from Wallkill to the Shaffer Place Farm, a TRF satellite farm in Virginia managed by Anne Lear, an experienced horsewoman and longtime TRF employee. *See* Lear Aff. ¶¶ 4-13, 16-18. Many of these horses have arrived underweight or otherwise not in good condition, but the December 2011 shipment of six horses "was the worst [Ms. Lear] had ever seen coming from Wallkill," all severely underweight, with visibly protruding ribs, mangy coats, untreated sores and other obvious signs of neglect. *Id.* ¶¶ 16-18, Ex. 2 (photographs).

Horses at Wallkill have continued to suffer neglect since December 2011. After witnessing a 28-year-old horse that her family had placed there in 2003 decline precipitously over the course of the winter, a retired New York social worker re-adopted the horse in February 2012; the horse had become emaciated and lame in the front and back, and its coat had changed to a faded red color. *See* Peugeot Aff. ¶¶ 1-25, Exs. 1-4 (photographs). After three months of care and re-feeding at a non-TRF facility, the horse (Après Coup) has regained significant weight (from a BCS of 1 when she left Wallkill, to a BCS of 3.5) and her original brown color. *Id.* ¶¶

26-33, Exs. 5-6 (veterinarian report and photographs).

TRF's operations at Wallkill have been marked by a persistent failure to provide basic horse care on a regular basis, including a years-long period when the herd received no dental care, long past when the need had become urgent for many horses.[10] Compl. ¶¶ 63-64. When the Ulster County SPCA inspected the herd in February 2012, its investigator found about 65 percent of the TRF horses in need of farrier and dental services (a conclusion shared by the facility manager), several underweight horses, and one horse with an open and untended dirty wound. Fix Aff. ¶¶ 1-4, Exs. 1-2 (report and photographs).[11]

2. The Removal of the Herd from TRF's Detweiler Facility

Far from taking "swift action" to address the severe neglect that Dr. Huntington uncovered at the Detweiler farm in March 2011 (Br. at 12, 13), when she recommended its closure, the Director Defendants recklessly allowed the TRF herd to remain at the Kentucky facility and continue to deteriorate *for a full year*, through another winter, before removing the herd in February and March 2012. Compl. ¶¶ 65-66.[12] They had known of the continuing problems at Detweiler in 2011, and after removing six horses in June 2011 even discussed the "urgency" of removing more horses, but failed to take sufficient action to protect the horses until this year, when the balance were removed. *Id.*; Lear Aff. ¶¶ 14-15, 19-21, 28. The first batch of Detweiler horses transferred to the Shaffer Place Farm arrived with protruding ribs, patches of

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[10] Per Defendants' own submissions from Wallkill: "[d]ue to lack of funding, some of the herd are not routinely vaccinated" and "only the minority of the herd receives dentals," and "it has not always been the case[that] all of the horses are up to date on dental work, vaccinations and hoof care." Ostrager Aff. Ex. A, Tabs 23, 45.

[11] Defendants have argued that the Attorney General has "focused on a handful of super-annuated horses which need special care," and that older horses "will continue to inevitably decline with age," Ostrager Aff. Ex. R at 1-2, ignoring the fact that even an older horse can suffer neglect, but may improve when reintroduced to proper care. *See, e.g.*, Peugeot Aff. ¶¶ 12-33 (recovery of 28-year-old horse removed from Wallkill). In any event, Defendants admit that the TRF herd is not old and "averages 13 years of age." Moore Aff. ¶ 14.

[12] The persistent neglect of TRF horses at the Detweiler farm also highlights the shortcomings of TRF's vaunted "comprehensive monitoring system" (Br. at 15); according to the "TRF Inspection Record" submitted by Defendants, Detweiler was the most frequently visited farm since January 2011. *See* Ostrager Aff. Ex. N.

hair missing, untreated sores, and split and untrimmed hooves. Lear Aff. ¶¶ 19-22; Ex. 4 (photographs). Subsequent shipments from Detweiler included more underweight horses; horses in need of immediate farrier care, with severe and infected scratches on their legs, and with overgrown teeth; and one approximately seven-year-old horse so severely lame that a veterinarian recommended he be euthanized. *Id.* ¶¶ 23-30. None of the horses were accompanied by customary records concerning basic horse care. *Id.* ¶ 31.

Far from having "comprehensively addressed" the critical situation that existed at the Detweiler farm as early as March 2011 (Br. at 13), the Director Defendants sat by until the herd's situation became truly dire following another winter. Notably, nowhere in Defendants' motion papers do they disclose to the Court the recent closure of the Detweiler facility.

3. TRF Offered False Assurances of the Herd's Good Condition

TRF's sensationalist claim that the Attorney General is "knowingly and intentionally making false allegations that would constitute actionable libel if the allegations were not contained in a complaint" (Br. at 2) is not only wrong, but designed to distract attention from the Director Defendants' own misrepresentations to the Court, the Attorney General, and the public. Throughout the period when, as discussed above, TRF was aware of serious problems at its Wallkill and Detweiler facilities, it offered repeated and demonstrably false assurances to the Attorney General that there were "no serious issues" and the herd was in "excellent condition."[13] During the investigation, TRF's board also sought to conceal the charity's true financial condition from the Attorney General through deceptive submissions. *See* Compl. ¶¶ 74-76.

[13] *See, e.g.*, Nachman Aff. ¶ 6, Ex. B (August 2011: "there is presently no issue with respect to the health and welfare of the herd;" September 2011: "there is no evidence that there is a basis to be concerned about the TRF's stewardship of the animals in its care;" December 2011: "there are no serious issues, and no issues that we are not aware of, and the overall herd is in good condition;" January 2012: TRF "anticipates no issues, in any respect, with the management of the herd;" April 2012: "The TRF herd remains in excellent condition . . . .").

Especially in light of the evidence of ongoing neglect of TRF's horses and the history of false assurances regarding the herd's condition, the Attorney General was not obligated to wait its suit in response to Defendants' renewed representations regarding the condition of the horses.[14] Not surprisingly, it turns out that Defendants' so-called "clear and convincing evidence" of the herd's "nearly perfect condition" (Br. at 2, 14) is little more than a collection of (i) notarized facility accreditation forms completed by hand by TRF facilities' regular veterinarians, offering cursory numerical ratings of the overall facility without detailed support, and (ii) notarized letters written by TRF facility managers and owners, who are beholden to TRF for salaries, per diems and other financial support. *See* Ostrager Aff. Ex. A.[15] Most of the so-called veterinary "reports" give no indication that any horses were examined individually: one lists a question mark ("?") in the field for "number of horses." *Id.* Tab 2.

V. TRF's Financial Condition Is Desperate

After years of overexpansion and stagnated fundraising, TRF's finances are in such disrepair that they impede its fulfillment of its charitable mission. Defendants' assertion that "TRF is not in financial crisis" (Br. at 7) is belied by the uncontested fact that TRF is over $1.5 million in debt (Compl. ¶ 73) and Defendants' admission that in 2011 the board borrowed $1 million in part to meet operating expenses and repay existing debt, including personal loans made by two of the Director Defendants. Br. at 8, 19, 23 n.13; Compl. ¶¶ 68-69. Defendants point to TRF's 2010 financial results (Br. at 7) but do not contest the fact that TRF ended 2011

[14] Contrary to Defendants' oft-repeated claim (*e.g.*, Br. at 2, 5, 7, 11, 15), at no point did the Attorney General refuse to accept for review and consideration any materials TRF chose to provide. *See* Nachman Aff. ¶¶ 4-12.

[15] The reliability of these reports cannot be assumed, as demonstrated for example by the discrepancy between the Walkill farm manager's claim that "[t]here has never been a case of a horse at the Wallkill facility not having enough to eat" (Ostrager Aff. Ex. A Tab 45) and the sworn statements submitted herewith detailing evidence of underweight horses removed from Wallkill in recent months. *See supra* at 10-11.

with an operating deficit of approximately $500,000.[16] Compl. ¶ 35. TRF was so desperate for cash in late 2011 that the Director Defendants repeatedly invaded its restricted $7 million Endowment Fund, in violation of its express spending limits.[17] Compl. ¶ 72. As set forth above, TRF is chronically insolvent and remains significantly in arrears to its satellite farms, which depend on these payments to meet the needs of TRF's horses. *See supra* at 6-7. Defendants' defensive assertion that many other charities "operate at a loss or in insolvency" (Br. at 19 n.10) characteristically overlooks the unique role that TRF has in being *solely* responsible for the health and welfare of the hundreds of live animals it has taken in.

The Director Defendants' self-aggrandizing claims that they are "among the most respected members of the thoroughbred community" and that TRF has an "endorsement" and "moral and financial support" from "every major New York thoroughbred breeding and racing stakeholder" (Br. at 3, 5, 6; Moore Aff. ¶ 11) wildly exaggerate the support that TRF receives under its current leadership. By far the bulk of the specific recent pledges and donations Defendants cite is restricted to a new, expanded rehabilitation program at Wallkill that, according to TRF's counsel, is limited to former race horses that are "not part of the TRF herd." Ostrager Aff. Ex. Q at 4.[18] While TRF is a national organization, with horses at facilities "across

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[16] Defendants also misread their own 2010 financial statement as showing "net positive cash flow of $661,956" (Br. at 7), when in fact that figure refers to the "Change in Net Assets." Ostrager Aff. Ex. F at 3. The relevant section of the financial statement, the "Statement of Cash Flows," shows that in 2010 TRF had negative cash flow of $29,351 ("Decrease in Cash and Cash Equivalents"). *Id.* at 5.

[17] Defendants' claim that the executors of the Paul Mellon estate, who donated TRF's endowment fund, "recognized the legality of every transaction related to the endowment about which the Attorney General complains" (Br. at 4) is farcical. TRF recently sued one of the executors for allegedly defaming TRF by objecting to TRF's use of the endowment. *See The Thoroughbred Ret. Found. v. Terry*, Index No. 150012/2012 (Sup. Ct. N.Y. Co.).

[18] *See* Compl. ¶ 78; Moore Aff. ¶¶ 11-12; Gagliano Aff. ¶¶ 5-6. TRF also makes the unsupported claim that it has "recently been named a beneficiary of the Thoroughbred Aftercare Alliance" ("TAA") (Br. at 22), failing to mention that in order to obtain TAA funding TRF first would have to be accredited by that organization. *See* Gagliano Aff. ¶ 10. In 2011, TRF earned the opprobrium of the ASPCA after TRF failed to meet the ASPCA's request that TRF obtain accreditation from another industry consortium: the ASPCA refused to consider TRF for additional funding and publicly criticized "'T.R.F.'s animal care oversight and that they were not adhering to operational best practices.'" Compl. ¶ 53.

the United States" (Br. at 6), its claimed base of support is limited largely to a handful of New York State industry organizations, two closely affiliated with its counsel, one of which is mired in scandal.[19] TRF's purported industry "support" has not prevented it from sinking deeper into debt, or stemmed the exodus of more than 25 directors from the TRF board since 2006 that has left in place a diehard core of just 7 directors, three of whom are current or former TRF employees. Compl. ¶¶ 8, 21-24.

Defendants point insistently to an "important partnership" TRF recently concluded to relocate up to 100 horses on a trial basis to a "60,000 acre ranch in Colorado," "resulting in substantial savings to the TRF while maintaining excellent care for the TRF's horses" (Br. at 17-18). This rhetoric does not withstand even cursory scrutiny. This so-called "partnership" is by its express terms a "grazing only contract, and all other expenses related to the care of all TRF horses shall be the sole responsibility of TRF." Ostrager Aff. Ex. P at 1. While admitting that TRF's board plans to spend *even less* on horses relocated to the Colorado ranch than the already substandard amounts that TRF spends per horse, Defendants fail to explain how turning retired race horses loose on a ranch the size of Brooklyn, pursuant to a contractual arrangement that makes no provision for staff to care for the horses, will "ensur[e] proper care for all horses relocated" there. Br. at 18 n.9. *See also* Huntington Aff. ¶¶ 67-77 (concerns about impact on TRF herd).[20] This "partnership" represents yet another effort by the Director Defendants to cut

[19] *See, e.g.*, Nachman Aff. ¶ 19, Ex. N (James M. Odato, *NYRA jousts with state*, ALBANY TIMES UNION, May 17, 2012). Defendants do not disclose that TRF's own counsel is a member of the board of directors of the New York Racing Association, Inc. ("NYRA") and President of the New York Thoroughbred Breeders, Inc. ("NYTB"). *Id.* ¶ 20, Ex. O (Press Release, "NYTB Seats 2012 Board, Ostrager Re-elected President.").

[20] Defendants' spurious claim that the Attorney General misrepresented communications with the owner of the Colorado ranch (Br. at 18 n.8) is based on a deliberate misreading of Mr. Nachman's statement in a letter to Mr. Ostrager that the ranch owner denied having offered "program support" to TRF (Ostrager Aff. Ex. Q, Attach. 1), which contradicted TRF's earlier statement in a January 26, 2012 press release that he "would be donating a large portion of care and services" to TRF. *See* Nachman Aff. ¶ 8, Ex. E. Defendants do not now claim that the ranch owner offered or made a charitable donation to TRF. As the executed contract shows, the owner has not committed to make *any* donation to TRF, which is responsible for all horse care expenses. *See* Ostrager Aff. Ex. P at 1.

costs on the backs of the horses, rather than implement viable solutions to the crisis caused by their own reckless conduct and persistent oversight failures. Compl. ¶¶ 79-80.

ARGUMENT

DEFENDANTS' MOTION TO DISMISS SHOULD BE DENIED BECAUSE THE VERIFIED COMPLAINT ASSERTS VALID CAUSES OF ACTION

The Attorney General has a "wide range of supervisory powers," which "include the right to proceed against the directors or trustees of a charitable organization" under the N-PCL and EPTL. *Lefkowitz v. Lebensfeld*, 68 A.D.2d 488, 497-98 (1st Dep't 1979), *aff'd*, 51 N.Y.2d 442 (1980). *See also People v. Grasso*, 54 A.D.3d 180, 191 (1st Dep't 2008) (N-PCL "grants to the Attorney General extensive supervisory and enforcement authority . . . over not-for-profit corporations" because of "the significant public interest in the[ir] management and affairs").

Defendants move to dismiss the Complaint on the bases that (I) "a defense is founded upon documentary evidence," under CPLR Rule 3211(a)(1), and (II) that "the pleading fails to state a cause of action," under Rule 3211(a)(7). Br. at 9-10. The former is frivolous, as Defendants have submitted no such evidence, and all of Plaintiffs' causes of action are valid and supported by non-conclusory allegations in the Complaint, which must be accepted as true on this motion to dismiss.

I. Defendants Have Submitted No "Documentary Evidence" Justifying Dismissal

Defendants' submissions do not justify dismissal because the materials do not constitute "documentary evidence" within the meaning of CPLR Rule 3211(a)(1) and, in any event, do not conclusively establish any defense to Plaintiffs' claims as a matter of law. "A motion to dismiss pursuant to CPLR 3211(a)(1) will be granted only if the 'documentary evidence resolves all factual issues as a matter of law, and conclusively disposes of the plaintiff's claim.'" *Fontanetta v. Doe 1*, 73 A.D.3d 78, 83-84 (2d Dep't 2010) (citations omitted). *Accord Beal Savings Bank v.*

Sommer, 8 N.Y.3d 318, 324 (2007). "[I]f the court does not find [the movants'] submissions 'documentary', it will have to deny the motion.'" *Fontanetta*, 73 A.D.3d at 84 (quoting SIEGEL, PRACTICE COMMENTARIES, CPLR C3211:10, at 22). Judicial records, mortgages, deeds, contracts, and other papers "the contents of which are 'essentially undeniable,'" may qualify as documentary evidence. *Id.* at 84-85 (citation omitted). Types of written materials that do not qualify as documentary evidence include "affidavits," "deposition and trial testimony," "letters, summaries, opinions" and "e-mails." *Id.* at 85-87 (collecting cases).

The materials Defendants submit in support of their motion do not begin to approach the standard for "documentary evidence" that could support dismissal under Rule 3211(a)(1).[21] Defendants seek to rely primarily on an assortment of so-called "affidavits and affirmations attached to the Ostrager Affidavit as Exhibit A" (Br. at 11), which cannot sustain dismissal under the Rule because "affidavits submitted by a defendant do not constitute documentary evidence upon which a proponent of dismissal can rely." *Crepin v. Fogarty*, 59 A.D.3d 837, 837 (3d Dep't 2009) (citation omitted). *See also Fontanetta*, 73 A.D.3d at 86 (same). Defendants' Rule 3211(a)(1) motion must, therefore, be denied.[22]

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[21] Defendants' materials consist almost entirely of materials that do not constitute "documentary evidence" for purposes of Rule 3211(a)(1): affidavits and affirmations (Moore Aff., Gagliano Aff., Ostrager Aff. Ex. A); TRF internal memorandum, meeting minutes, financial statements and operations records (Ostrager Aff. Exs. B, C, D, F, H, I, L, N, T, Y); letters and opinions (Exs. E, G, J, Q, R, S, U); a draft contract amendment (Ex. K); and a press release and website screenshots (Ex. M, O, V, W). Even if TRF's organizational documents (Ex. B) and the two contracts Defendants submit (Exs. P, X) constitute "documentary evidence," they are not dispositive of Plaintiffs' claims. *See Penquin Tenants Corp. v. Ellenberg*, 25 A.D.3d 345, 345-46 (1st Dep't 2006) (motion to dismiss denied "[b]ecause the documentary evidence of the [contract] was not dispositive" on contested legal point).

[22] Even if the instant motion were converted to a motion for summary judgment, due to the submission of materials extrinsic to the Complaint, there are genuine issues of material fact that would defeat Defendants' motion on each cause of action. Here, the parties have not been given notice that conversion will occur, as required by CPLR Rule 3211(c), and the Court should decline any invitation to convert since the case is "in its earliest stages, and no discovery has been had." *SPI Comms. V. WTZA-TV Assocs. Ltd. P'ship*, 229 A.D.2d 644, 645 (3rd Dep't 1996).

II. Plaintiffs Have Asserted Valid Causes of Action

Defendants have raised only two grounds for dismissal of Plaintiffs' claims pursuant to CPLR Rule 3211(a)(7): (1) that Plaintiffs' claims for removal of directors require a showing of fraud or intentional wrongdoing, and (2) that the presumption of the business judgment rule defeats all Plaintiffs' claims. *See* Br. at 10, 22-25. Defendants are incorrect on both counts.

In addition, Defendants make no arguments at all concerning Plaintiffs' fourth and fifth causes of action: breach of statutory duties in the administration of charitable assets under N-PCL §§ 513, 553 and 720, and improper administration of a not-for-profit corporation under EPTL § 8-1.4. Compl. ¶¶ 92-102. They have, therefore, abandoned their motion with respect to these claims.[23]

Defendants also gloss over the well-settled standard for determining a motion to dismiss for failure to state a cause of action:

> When determining a motion to dismiss, the court must "accept the facts as alleged in the complaint as true, accord plaintiffs the benefit of every possible favorable inference, and determine only whether the facts as alleged fit within any cognizable legal theory."

Goldman v. Metro. Life Ins. Co., 5 N.Y.3d 561, 570-71 (2005) (citations omitted); *see also GPS Global Pkg. Sol'ns, LLC v. 151 W. 17th St. Condo.*, 93 A.D.3d 463 (1st Dep't 2012). The Complaint is replete with specific, detailed factual allegations that must be accepted as true and are more than sufficient to support the Attorney General's claims.

[23] It is long settled that the Attorney General's broad authority over charities includes the power to sue a not-for-profit corporation to enforce donor-imposed restrictions on gifts to the corporation, including endowment spending restrictions. *See, e.g., St. Joseph's Hospital v. Bennett*, 281 N.Y. 115, 119 (1939). Defendants are not permitted to address these causes of action in their reply papers. "The function of reply papers is to address arguments made in opposition to the position taken by the movant and not to permit the movant to introduce new arguments in support of, or new grounds for the motion." *Dannasch v. Bifulco*, 184 A.D.2d 415 (1st Dep't 1992) (citations omitted).

A. Plaintiffs State a Valid Claim for Removal of TRF's Directors "For Cause" Under Sections 112(a)(4) and 706(d) of the N-PCL

Plaintiffs seek to remove TRF's directors "for cause," pursuant to the Attorney General's express statutory authority under N-PCL §§ 112(a)(4) and 706(d), a standard easily met here by the Director Defendants' entire course of conduct and interference with TRF's fulfillment of its charitable purpose. Compl. ¶¶ 14, 29, 34-83. Defendants assert, incorrectly, that "[t]here is not a single reported New York case in which a director of a not-for-profit corporation has been removed without a showing of fraud or intentional wrongdoing." Br. at 10. No less than the Court of Appeals has upheld removal of a life member and trustee (equivalent to a director) of a charitable corporation when there was no suggestion of fraud, intentional wrongdoing, or even self-dealing. In *Matter of Grace v. Grace Institute*, 19 N.Y.2d 307 (1967), the Court of Appeals found that the petitioner was properly removed by the corporation's board "for cause" because his "conduct was so inimical to the corporate interests as to require his removal," on the basis that he "had embarked on a course of conduct designed to involve the Institute in endless and costly litigation and that the suits were undertaken for the purpose of harassing the Institute and its members." *Id.* at 314, 315. It further held, "Once [a life member] breaches that condition [of "faithfully serv[ing] the" charity] and engages in activities that obstruct and interfere with the operation of the corporation and the purposes for which the Legislature created it, he may be removed." *Id.* at 315.[24]

TRF's directors are subject to removal "for cause" under Sections 112(a)(4) and 706(d) of the N-PCL on the basis of their consistent and intractable course of conduct that has been far more "inimical to [TRF's] interests" than the conduct at issue in *Grace*, with tragic consequences

[24] *See also Abberger v. Kulp*, 156 Misc. 210, 212 (Sup. Ct. Erie Co. 1935) (a director may be removed "for cause" for "acting in a manner inimical to the interests of the corporation"); *Fox v. Cody*, 141 Misc. 552, 554 (Sup. Ct. N.Y. Co. 1930) (removal is proper "where a director has been unfaithful to his trust, or has misconducted himself in such a manner as to render it necessary for the corporation to dispense with his services as a director").

for TRF's horses. These statutes grant the Attorney General the same power to remove a director "for cause" that the board in *Grace* had to remove a life member and trustee. The Complaint sets forth a years-long series of actions and omissions on the part of the Director Defendants that has damaged, and if permitted to continue may destroy, TRF's ability to fulfill its charitable mission of protecting horses from neglect and mistreatment. These directors' conduct -- marked by a reckless overexpansion of TRF's herd, repeated oversight failures, and irresponsible financial transactions involving TRF's restricted endowment fund -- has resulted in the organization's financial ruin and the severe neglect, and in some instances death, of horses. Removal of TRF's current, failed leadership is critical in order for TRF to have any chance of regaining "its position as the gold standard of thoroughbred aftercare." Br. at 4.

In their motion, Defendants take the extreme position that as not-for-profit board members, TRF's directors are accountable to no one but themselves, and cannot be removed from their positions absent fraud or intentional wrongdoing, *even if they are running the charity into the ground.* Br. at 10. In making this bold claim, Defendants ignore the Attorney General's independent authority to seek the removal of directors "for cause" under N-PCL §§ 112(a)(4) and 706(d). This enforcement power is part of a larger statutory scheme: "The state legislature has given the Attorney General broad supervisory and oversight responsibilities over charitable assets and their fiduciaries, as enumerated in the Not–for–Profit Corporation Law, the EPTL and the Executive Law." *In re McDonell*, 195 Misc. 2d 277, 278 (Sup. Ct. N.Y. Co. 2002) (citing N-PCL §§ 112, 720; EPTL §§ 8-1.1(f), 8-1.4; EXEC. LAW Art. 7-A). The Attorney General's enforcement role is particularly critical here because the directors of a not-for-profit corporation without members, like TRF, can be voted out *only* by their fellow directors.[25] *See* N-PCL §

[25] Notably, in the case of a not-for-profit corporation *with* members, the Attorney General's statutory right to seek removal of directors "for cause" is shared by "10 percent of the members." N-PCL § 706(d).

706(a)-(c). The self-perpetuating nature of the board of a not-for-profit without members compels the Attorney General, as the primary regulator of New York charities, to exercise his right and duty to seek removal of directors where "cause" exists. Defendants' motion asks the Court to upend the statutory scheme and hold that directors are invulnerable to removal in the absence of fraud or intentional wrongdoing, even where they violate their duties as directors, obstruct a charity's fulfillment of its mission, and imperil the welfare of live animals.

B. Plaintiffs Have Stated Valid Claims Under Section 8-1.4(m) of the EPTL to Secure the Proper Administration of TRF

Defendants also entirely ignore Plaintiffs' separate and independent claim to secure the proper administration of a charitable organization under Section 8-1.4(m) of the EPTL, which authorizes the Attorney General to "institute appropriate proceedings . . . to secure the proper administration of any trust, corporation or other relationship to which this section applies."[26] Compl. ¶¶ 99-102. The Court of Appeals has recognized that "8-1.4 grants supervisory power over charities and other entities and allows the Attorney-General to institute proceedings to secure proper administration of such entities." *Lefkowitz*, 51 N.Y.2d at 447. "The powers and duties of the attorney general provided in this section are in addition to all other powers and duties he or she may have," EPTL § 8-1.4(m), including his powers under the N-PCL.[27] The statute also instructs that Section 8-1.4 "shall be liberally construed so as to effectuate its general purpose of protecting the public interest in charitable uses, purposes and dispositions." *Id.* § 8-1.4(n).

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[26] As a "non-profit corporation organized under the laws of this state for charitable purposes," EPTL § 8-1.4(a), TRF is a corporation to which Section 8-1.4 applies. Compl. ¶ 25.

[27] *See, e.g., Koppel v. L.I. Soc'y for the Prev. of Cruelty to Children*, 163 Misc. 2d 654, 659 (Sup. Ct. N.Y. Co. 1994) ("In addition [to N-PCL §§ 112(a)(1) and (a)(3)], EPTL § 8-1.4 authorizes the Attorney General to institute proceedings to secure the proper administration of non-profit corporations.").

The Attorney General's fifth cause of action states a valid claim under Section 8-1.4(m) for relief that will "secure the proper administration of" TRF going forward, including removal of the current board and injunctive relief barring the acceptance of new horses into the herd and curtailing the board's invasions of TRF's endowment fund. This relief is appropriate in light of the improper administration of TRF and its assets by the Director Defendants and will serve to protect the public interest in TRF's charitable assets and its fulfillment of its mission.

C. Plaintiffs' Claims Cannot Be Dismissed Because the Business Judgment Rule Presumption is Overcome

Defendants' principal argument rests on a misapplication of the business judgment rule to the pleaded facts of this case. Br. at 22. The business judgment rule is a rebuttable presumption that protects directors from liability for actions taken in good faith. *See People v. Grasso*, 11 N.Y.3d 64, 70 (2008); *Higgins v. NYSE, Inc.*, 10 Misc. 3d 257, 282 (Sup. Ct. N.Y. Co. 2005); N-PCL § 717(b). On a motion to dismiss under CPLR Rule 3211(a)(7) premised on the business judgment rule, a "complaint will be sustained if it contains allegations sufficient to demonstrate that directors did not act in good faith or were otherwise interested, as 'pre-discovery dismissal of pleadings in the name of the business judgment rule is inappropriate.'" *Higgins*, 10 Misc. 3d at 282 (quoting *Ackerman v. 305 E. 40th Owners Corp.*, 189 A.D.2d 665, 667 (1st Dep't 1993)). The absence of good faith may be demonstrated by alleging "wantonly negligent, even reckless conduct," which the Court of Appeals has held is not protected by the business judgment rule. *Giblin v. Murphy*, 73 N.Y.2d 769, 771-72 (1988) (citations omitted). *See, e.g.*, *Herman v. BBR Worldwide Trans. Parts Distrib., Inc.*, 2005 WL 6214712, at n.10 (Sup. Ct. N.Y. Co. June 7, 2005) (Gammerman, J.) (same).

Plaintiffs' claims overcome the presumption of the business judgment rule because the Complaint alleges that the Director Defendants' challenged course of conduct was undertaken

recklessly, "in conscious disregard of the risks they posed to TRF's horses and the organization's ability to fulfill its charitable purpose," Compl. ¶ 85, not least through "the reckless failure of TRF's board . . . to ensure that TRF maintain a herd no larger than it can support." *Id.* ¶ 2. Far from alleging mere "mismanagement" and "dysfunction" (Br. at 25), the Complaint lays out how the Director Defendants knowingly disregarded "[c]lear warnings that, since at least 2005 or 2006, TRF could no longer afford to accept new horses into its herd," and "repeated warnings that its per diems are inadequate to cover the cost of providing proper care to retired Thoroughbred race horses." *Id.* ¶¶ 37, 48. *See also id.* ¶¶ 34, 38-41, 45-47, 54-66. TRF's charitable purpose is to provide an appropriate home for all the horses it accepts into its herd and protect them from neglect, *id.* ¶ 29, and "[i]t is axiomatic that the Board of Directors is charged with the duty to ensure that the mission of the charitable corporation is carried out." *Manhattan Eye, Ear & Throat Hosp. v. Spitzer*, 186 Misc. 2d 126, 152 (Sup. Ct. N.Y. Co. 1999). The Director Defendants' "wantonly negligent, even reckless conduct," *Giblin*, 73 N.Y.2d at 771-72, as alleged in the Complaint, clearly demonstrates an absence of good faith. Accordingly, these Defendants are not entitled to the business judgment rule's protections.[28]

Defendants argue in a footnote that the business judgment rule protects them from liability for securing a $1 million line of credit with the income stream on TRF's restricted endowment fund, and agreeing not to materially diminish the fund without the lender's approval, because the TRF board obtained legal advice concerning the loan. Br. at 21 n.11. N-PCL § 717(b) provides that directors "acting in good faith, may rely on information, opinions, reports or

[28] Defendants misapprehend the holding in *Grasso* that provisions of Section 720 of the N-PCL, under which Plaintiffs assert claims for breach of fiduciary duty, are "fault-based." 11 N.Y.3d at 71. Br. at 23. In *Grasso*, "fault" is used, in contrast to "a type of strict liability" for ultra vires acts, to denote the level of knowledge or intentionality required to impose liability under the business judgment rule. *Id.* As noted above, that threshold is met by a director's "wantonly negligent, even reckless conduct." *Giblin*, 73 N.Y.2d at 771-72. The Director Defendants' reliance on *People v. Lawrence*, 903 N.Y.S.2d 618 (4th Dep't 2010) (Br. at 23) is misplaced for the same reason.

statements . . . prepared or presented by . . . counsel, public accountants or other persons as to matters which the directors or officers believe to be within such person's professional or expert competence." Obtaining such advice, however, does "not bulletproof the board." *In re NYSE/Archipelago Merger Litig.*, 12 Misc. 3d 1184(A), 2005 WL 4279476, *14 (Sup. Ct. N.Y. Co. Dec. 5, 2005) (fairness opinion) (citing *Bernstein v. Kelso*, 231 A.D.2d 314, 321 (1st Dep't 1997)). Reliance on the advice "must be reasonable," *id.*, and the TRF directors' purported reliance on an opinion from Virginia counsel "without question, investigation or scrutiny," *id.*, was inherently unreasonable: the letter warned explicitly of the possibility that "some aspect of New York corporate law governing the Foundation compels a different result," as indeed it does. Compl. ¶¶ 71, 93-95. Nor did the opinion address granting a bank control over an endowment corpus. *Id.* ¶ 71. TRF's directors failed to obtain an opinion on New York law, and a director is not entitled to rely on an opinion without making "reasonable inquiry into material matters." *Hanson Trust PLC v. ML SCM Acq'n Inc.*, 781 F.2d 264, 275 (2d Cir. 1986).

D. The Business Judgment Rule Does Not Apply to Plaintiffs' Claims for Breach of the Duty of Loyalty and for Removal

Finally, Defendants' argument fails to recognize that the presumption of the business judgment rule does not even apply to several of the Attorney General's claims -- in particular, those for breach of the fiduciary duty of loyalty (third cause of action) and for removal under the N-PCL and EPTL (first and fifth causes of action).

With respect to Plaintiffs' third cause of action concerning the $1 million line of credit, Mr. Moore and Mr. Rainey are not entitled to the presumption of the business judgment rule because they both were "interested" in securing funds for TRF to ensure that there would be sufficient cash to repay the personal loans they had made to the organization. Compl. ¶¶ 68-69. These directors violated their duty of undivided loyalty to TRF first by arranging and approving

the line of credit, and then by repaying themselves out of the proceeds. *Id.* ¶¶ 88-91. The duty of loyalty is an "'inflexible'" rule that requires "'avoidance of situations in which a fiduciary's personal interest possibly conflicts with the interest of those owed a fiduciary duty.'" *Wisell v. Indo-Med Comm., Inc.*, 2006 WL 1160136, *7 (Sup. Ct. Nassau Co. May 2, 2006) (citation omitted). The conduct of individual directors who, like Mr. Moore and Mr. Rainey, do not "'possess a disinterested independence'" is not entitled to the protection of the business judgment rule. *S.H. & Helen R. Scheuer Fam. Fnd., Inc. v. 61 Assocs.*, 179 A.D.2d 65, 69 (1st Dep't 1992) (quoting *Auerbach v. Bennett*, 47 N.Y.2d 619, 631 (1979)).[29] As creditors of TRF (already deep in debt and chronically insolvent by early 2011), Mr. Moore and Mr. Rainey had an interest in TRF obtaining additional cash and repaying their loans ahead of other creditors, including TRF's boarding facilities. Compl. ¶¶ 68-69.

The business judgment rule also does not apply to Plaintiffs' first and fifth causes of action seeking the removal of TRF's board. The business judgment rule is intended, as Defendants point out, "to protect the directors of not-for-profit corporations from liability" (Br. at 22 n.12; emphasis added), not removal. *See, e.g.*, N-PCL § 717(b) ("Persons who so perform their duties shall have no liability . . . ."). As discussed above, N-PCL §§ 112(a)(4) and 706(d) authorize removal simply "for cause," regardless of whether directors are subject to liability for the conduct constituting "cause." Likewise, EPTL § 8-1.4(m) is a statute fundamentally concerned, not with liability for past conduct, but with "secur[ing] the proper administration" of the charity going forward. Removal of TRF's current board is necessary if TRF is to fulfill its charitable purpose of protecting horses from neglect in the many years remaining in the lives of the more than 1,000 Thoroughbreds entrusted to its care.

[29] *See also Marx v. Akers*, 88 N.Y.2d 189, 190 (1996) ("Directors are self-interested in a challenged transaction where they will receive a direct financial benefit from the transaction which is different from the benefit to shareholders generally.").

CONCLUSION

For the reasons set forth above, Plaintiffs respectfully request that the Court deny Defendants' motion in its entirety.

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