IN THE CIRCUIT COURT FOR MONTGOMERY COUNTY, MARYLAND

SHAO-CHANG CHEUNG, *et al.*	:	
	:	
Plaintiffs,	:	
	:	
v.	:	Case No. 346532
	:	Judge Ronald B. Rubin
KEK-YU HO, *et al.*	:	
	:	
Defendants.	:	
	:	

MOTION TO DISMISS AMENDED COMPLAINT BY DEFENDANTS KEK YU HO, CHEW MOI PUAH, AND SOOK CHUN HU

Defendants Kek Yu Ho, Chew Moi Puah, and Sook Chun Hu, by and through counsel, pursuant to Maryland Rule 2-322(b)(2), move to dismiss the Amended Complaint on grounds that, like the original Complaint, it still fails to state a claim upon which relief can be granted.

Having failed to timely muster up and file an opposition to the Defendants' Motions to Dismiss the original Complaint, having failed to obtain leave from the Court to extend the time for filing an opposition, and having unwittingly revealed to the parties and Court that Gregory Grant, Esq. was available all along to prepare an opposition, the Plaintiffs made the tactical decision to file an Amended Complaint.[1] But the Amended Complaint does not contain any material changes that counteract or defeat the various legal grounds for dismissal as set forth in the Defendants' original Motion to Dismiss filed June 22, 2011 (docket entry #23).

For purposes of this Motion, Plaintiffs Shao-Chang Cheung, Hsueh-Hua Wong, and Hseuh-Hui Lee are referred to as "Minority Stockholders" as they own 16.7% of the capital stock of Maxim Supermarket, Inc. (hereafter "Maxim"). Defendants Kek Yu Ho, Chew Moi Puah, and Sook Chun Hu are referred to collectively as the "Directors" of Maxim.

[1] The Amended Complaint substitutes for the original Complaint and seemingly moots the Defendants' Motion to Dismiss.

The Defendants request the Court to dismiss the entire Amended Complaint on grounds that (1) the Minority Stockholders failed to make a good faith effort to have Maxim act directly, known as making a "demand" upon the corporation; *Bender v. Schwartz*, 172 Md. App. 648, 665-66 (2007) (citations omitted); and (2) the Minority Stockholders failed to "clearly demonstrate, in a very particular manner" that a demand would be futile because the directors cannot respond to the demand in good faith under the business judgment rule. *Werbowsky v. Collomb*, 362 Md. 581, 620 (2001). Immediately after the Defendants received a draft derivative complaint on March 15, 2011, coupled with a buyout and settlement offer letter from counsel for the Minority Stockholders, even though a demand had not been made on Maxim, the Board of Directors was considering in good faith the claims which the Minority Stockholders had presented in the draft derivative complaint. In less than two weeks, Maxim formally engaged a valuation expert to advise the Board regarding the excessive compensation claims and other issues raised in the draft derivative complaint. Maxim's legal counsel promptly notified the Minority Stockholders' counsel on March 31, 2011, that Maxim had engaged a valuation expert to advise the Board of Directors and that the Directors would act prudently on behalf of all stockholders. Maxim engaged Valuation Services, Inc., a Member of the Zitelman Group (Principal – P. Richard Zitelman, CPA, CVA). But the Minority Stockholders rushed to file the derivative Complaint on April 15, 2011, before Valuation Services, Inc. could accomplish its work.

In furtherance of the Board's intention to address the claims of the Minority Stockholders in good faith under the business judgment rule, Maxim appointed A. Howard Metro, Esq.[2] of

[2] Mr. Metro has been engaged by other corporations to serve as special investigation counsel in connection with shareholder derivative claims. He has written and spoken about corporate investigations, most recently presenting a seminar on "Corporate Investigations: Best Practices in Shareholder Derivative Claims" at the Maryland State Bar Association Mid-Year Meeting in February 2011. He is a past president of the Montgomery County Bar Association and the Maryland Institute for Continuing Legal Education. He was an Honoree of the Daily Record's 2010 Leadership in Law Award, and has been

McMillan Metro as Special Investigation Counsel to serve as, and perform all the duties of, an independent Special Investigation Committee, to investigate the claims and issues raised in the Amended Complaint and to advise the corporation how to proceed regarding the allegations. Mr. Metro has been given broad authority and power by the corporation to take whatever steps or actions he deems reasonable and necessary to investigate the claims and allegations and to carry out his assignment. He has the authority to examine all company records, including records maintained by the company's accounting firm. He has the authority to meet and interview whomever he deems to have information relevant to his investigation. Mr. Metro is authorized to prepare a report of his findings and to make recommendations to the Board of Directors.

Mr. Metro has commenced his investigation. He has received corporate documents from Maxim. He has met separately with counsel for the Plaintiffs. He has received extensive letters from counsel for both sides setting forth their requests as to the scope and parameters of his investigation of the Plaintiffs' allegations. Counsel for the Plaintiffs has informed Mr. Metro in writing that they will participate in and cooperate with his investigation and they are amenable to procedures that will enhance a thorough and impartial investigation. *Accord, Grant letter to Metro, dated 8-1-11 (not attached).* Though the Plaintiffs object to Valuation Services, Inc., counsel for Maxim informed Mr. Metro in writing that "if it is your judgment that a compensation expert other than Mr. Zitelman should be engaged by you, Maxim will commit to paying the cost." *Accord, Willard letter to Metro, dated 7-25-11 (not attached).*

The Court should dismiss the Amended Complaint to allow a reasonable amount of time for the valuation expert and Special Investigation Counsel to complete their work, and for the Board of Directors to consider their advice and recommendations and act prudently on them.

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named in *Maryland Super Lawyers* and *Washington, D.C. Super Lawyers* for five consecutive years (2007 – 2011).

In addition, the Defendants request the Court to dismiss Count 8 because Maxim had corporate power and authority under the Articles of Incorporation and By-Laws to pay fees to the Directors and to enter into the transactions with H and P and Reserve; and "interested party" contracts and transactions are specifically permitted by the Articles of Incorporation and By-Laws.

The Defendants also request the Court to dismiss Count 1 for constructive fraud on grounds that (1) the Amended Complaint fails to plead any false representation made by the individual Defendants to Maxim; (2) the Amended Complaint fails to plead facts sufficient to satisfy other essential elements of constructive fraud; (3) Maxim did not rely upon the falsity of invoices, believing they were true, to pay H and P and Reserve since all of the officers and directors of Maxim are alleged to have created the so-called false invoices; and (4) claims based on acts prior to April 15, 2008, are barred by the statute of limitations.

The Defendants request the Court to dismiss all claims for punitive damages on grounds that (1) the legal standards for recovering punitive damages were not pleaded; and (2) punitive damages are not a legally cognizable claim based on judicial dissolution.

Finally, the Defendants request the Court to dismiss Count 1 on grounds that Maryland does not recognize a separate cause of action at law for monetary damages for breach of fiduciary duty.

The Court is referred to the attached Memorandum of Points and Authorities.

REQUEST FOR HEARING

Pursuant to Maryland Rule 2-311(f), the Defendants request a hearing on this Motion.

DATED: August 9, 2011

Respectfully submitted,

_____

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MEMORANDUM OF POINTS AND AUTHORITIES IN SUPPORT OF MOTION TO DISMISS AMENDED COMPLAINT OF DEFENDANTS HO, PUAH AND HU

DATED: August 9, 2011

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STATUTES & REGULATIONS

I. THE PARTIES

Maxim Supermarket, Inc. ("Maxim") was incorporated in Maryland on December 2, 2002. It is an Asian grocery store located at 460 Hungerford Drive, Rockville, Maryland 20850.

Defendants Kek Yu Ho ("Mr. Ho"), his wife, Chew Moi Puah ("Ms. Puah"), and Sook Chun Hu ("Ms. Hu") are referred to collectively as the "Majority Stockholders." Mr. Ho and Ms. Puah presently own together approximately 51% of the outstanding shares of capital stock of Maxim. Ms. Hu presently owns approximately 32% of the outstanding shares of capital stock.[1] In addition to being Majority Stockholders, they are the executive officers, directors, and managerial team of Maxim responsible for operating the business day-in and day-out.

Plaintiffs Shao Chang Cheung, Hsueh Hua Wong, and Hsueh Hui Lee are referred to as the Minority Stockholders. They originally owned 15% of the outstanding shares but as a result of redemptions, they presently own 16.7% of the capital stock. They became investors in Maxim in 2002 after it was formed. They live in New York and have not had any role in running the business of Maxim. Plaintiffs Wong and Lee are sisters.

Defendant H and P, LLC ("H and P") was incorporated in Maryland on March 15, 2006. The corporate charter was canceled on November 13, 2007. H and P had a consulting agreement with Maxim to accomplish certain business objectives of Maxim. H and P was owned by Mr. Ho and Ms. Puah.

Defendant Reserve Champion, L.L.C. ("Reserve") was incorporated in Maryland on May 31, 2007. Reserve had a consulting agreement with Maxim to accomplish certain business objectives of Maxim. Reserve was owned by Mr. Ho, Ms. Puah and Ms. Hu.

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[1] In 2002, when the corporation was organized, Ms. Hu owned 37.5% and Mr. Ho and Ms. Puah jointly owned 37.5% of the capital stock. The remainder was owned by investors. Over the years, there have been various stock redemptions of other investors that caused the ownership percentages of the Majority Stockholders to increase. In 2010, Mr. Ho purchased some of Ms. Puah's shares for $35 per share – the same buyout price offered by Maxim to the Minority Stockholders in March 2010.

II. INTRODUCTION

This shareholder derivative action is an effort by the three Minority Stockholders owning 16.7% of an Asian grocery store, Maxim, to gild the lily and elevate their dissatisfaction with their returns on investments to something more substantial. The Minority Stockholders challenge the business judgment of the corporation, its board of directors, and management dating back to the year 2002. The Minority Stockholders complain that the Defendants' compensation was excessive while closing their eyes to the back-breaking work, sweat and long hours of the Defendants running a grocery store 7 days a week from early in the morning until late at night. The Minority Stockholders complain that they did not receive dividends until 2008 and that the dividends they received were "paltry" compared to the compensation paid to Defendants Ho, Puah and Hu, who built the grocery store day-in and day-out. The Minority Stockholders claim that all of the compensation paid to the Defendants was "excessive" and should have been distributed instead as "profits" to all of the stockholders in the form of stock dividends. The Minority Stockholders voiced no dissatisfaction or grievance for 8 years about the absence of annual shareholders' meetings, financial performance data or the allocation of income to them on their annual Schedule K-1s. For 8 years, the Majority Stockholders never requested copies of minutes of meetings of the directors, the by-laws or the articles of incorporation; they voiced no objections about the promissory notes and the return of their capital or the interest rates paid to them on their loans. The Minority Stockholders never complained about the lack of dividends in the early years, and in 2008 when they started receiving dividends, they did not voice any dissatisfaction with the dividend amounts and the rates; nor did they question how the dividends were calculated. The Minority Stockholders never objected to the income allocated to them on their annual Schedule K-1s or the fact that they paid taxes on the income. And they never requested information about the compensation

being earned by the Defendants in their various roles. Now under the guise of a shareholder derivative action, the Minority Stockholders voice their dissatisfaction and seek "restitution" from the Defendants and ask the Court to direct Maxim to pay them a dividend.[2] (*See* Amended Complaint, Wherefore clause ¶A(6)).

III. ARGUMENT

1. THE AMENDED COMPLAINT SHOULD BE DISMISSED BECAUSE THE PLAINTIFFS FAILED TO MAKE A DEMAND OR CLEARLY DEMONSTRATE THAT A DEMAND WOULD BE FUTILE.

The Amended Complaint should be dismissed because the Plaintiffs did not make a demand upon the Board of Directors prior to commencing litigation or show that a demand, if made, was futile.[3] *Shenker v. Laureate Educ., Inc., 411 Md. 317, 344, 983 A.2d 408 (2009)* (citing *Bender v. Schwartz, 172 Md. App. 648, 666, 917 A.2d 142 (2007).* The Plaintiffs do not have standing to bring a derivative action because under Maryland law, a stockholder suing derivatively on behalf of the corporation must first make a demand upon the corporation to sue in its own name and the demand must have been refused. *Werbowsky v. Collomb*, 362 Md. 581, 620 (2001)*; Eisler v. Eastern State Corp.*, 182 Md. 329, 35 A.2d 118 (1943). This, the Plaintiffs have failed to do. As stated by the Court of Special Appeals of Maryland in *George Wasserman & Janice Wasserman Goldsten Family LLC v. Kay*, No. 2836 (Md. App., Feb. 9, 2011):

> In part because a derivative action intrudes on directors' managerial prerogatives, the law limits shareholders' ability to bring such actions. Before filing suit on behalf of the corporation, shareholders must first make a good faith effort to have the corporation act directly. *Bender*, 172 Md. App. at 665-666. This effort is known as making "demand" upon the corporation. Once demand is made, the board of directors must conduct an investigation into the allegations in the demand, and decide whether

[2] Notably absent from the Amended Complaint is the explanation that if compensation was excessive and "profits" should have been distributed, the Minority Stockholders would receive only 15% - 16.7% of the profits and the individual Defendants who are the Majority Stockholders nonetheless would receive 85% - 83.3% of the profits (fluctuating percentages due to the stock redemptions of other investors).

[3] The Court is referred to Appendix A for a full discussion of the core legal principles applicable to derivative actions in Maryland.

> litigation would be in the corporation's best interests. *Id*. at 666. The board can appoint a committee of disinterested directors to undertake this investigation. *Id.* If the corporation fails to bring suit, the shareholders may then bring a "demand refused" action. *Id*. The plaintiff can still allege that the board, in fact, did not act independently, or that the board's refusal to bring suit was wrong. *Id*. To determine whether the board wrongly refused to bring suit, courts review the board's investigation under the strict business judgment rule. *Id.* Under that rule, courts defer to the board or committee's decision not to bring suit "unless the stockholders can show either that the board or committee's investigation or decision was not conducted independently and in good faith, or that it was not within the realm of sound business judgment." *Id.*
>
> Shareholders can avoid the demand requirement only if demand is excused as "futile." *Id.* The futility exception is viewed as a
>
> > very limited exception, to be applied only when the allegations or evidence clearly demonstrate, in a very particular manner, either that (1) a demand, or a delay in awaiting a response to a demand, would cause irreparable harm to the corporation, or (2) a majority of the directors are so personally and directly conflicted or committed to the decision in dispute that they cannot reasonably be expected to respond to a demand in good faith and within the ambit of the business judgment rule.

Werbowsky, 362 Md. at 620.

The Plaintiffs concede that they did not make a demand upon Maxim prior to filing their derivative complaint. The Amended Complaint, ¶115, alleges that "[a]ny demand to bring this claim against Ho, Puah and Hu would have been futile" because they are the sole directors and control the voting majority, making it certain that they would not have authorized Maxim to sue any of them.[4] The Amended Complaint, ¶8, concedes that the draft derivative complaint was tendered with a settlement demand, but within two weeks of being informed by Maxim's counsel that an expert had been hired to evaluate the Plaintiffs' claims of excessive compensation, Plaintiffs made no further effort to communicate with Maxim because they had not been provided yet the name of the expert or the 2010 financial statements (Amended Complaint, ¶9).

[4] Similar allegations are repeated in Amended Complaint ¶ 126 and ¶ 147 with respect to suing H and P (Count 2 and Count 4), and in ¶ 158 and ¶ 167 with respect to suing Reserve (Count 5 and Count 6).

The fact that Maxim had not completed it 2010 tax return and K-1s for the stockholders, nor had immediately provided the name of the expert, does not show that making a demand was futile.

In accordance with *Bender v. Schwartz, supra, and George Wasserman & Janice Wasserman Goldsten Family LLC v. Kay, supra,* the Board of Directors is conducting an investigation into the allegations first made in the draft derivative complaint. It remains to be seen what Mr. Metro and Valuation Services, Inc. will decide and recommend; and it remains to be seen how Maxim will respond to their recommendations. But the law is clear – It is ONLY if Maxim fails to bring suit or fails in any other material way to act upon the demands of the Minority Stockholders can they then bring a "demand refused" action. They can allege that the Board did not act independently, or that the Board's refusal to bring suit was wrong (if that is what happens), but they cannot bring that action now. And they cannot proceed now with the derivative claims which they have asserted in their original Complaint and Amended Complaint because they failed to make a demand originally that was refused by Maxim (and the Directors). The uncontroverted fact is that when the Minority Stockholders made a demand, when they sent over their draft derivative complaint, the Board immediately began investigating the excessive compensation claims by hiring Valuation Services, Inc. Within a few months, it had hired Mr. Metro to spearhead the effort. The Court must dismiss the action.[5]

A. The Plaintiffs Have Failed to Allege Sufficient Facts Excusing the Demand Requirement.

Apart from alleging that Defendants Ho, Puah and Hu have voting control of Maxim, H and P, and Reserve, no other material allegations about a demand are made. The basis of their futility claim is that Defendants Ho, Puah and Hu have voting control (indeed, they collectively own 83.3% of the outstanding stock) and they are Directors of the corporation. These thin

[5] If the Minority Stockholders later bring a "demand refused" action, then the Board's investigation, its retention of Valuation Services, Inc. and Mr. Metro, and its acts or omissions in reliance upon the recommendations of both sets of experts, would be reviewed by the Court under the strict business judgment rule.

allegations in the Amended Complaint do not excuse the Minority Stockholders from making a demand because they do not meet the *Werbowsky* standards, 362 Md. at 620, for excusing a demand, to wit: they do not "clearly demonstrate, in a very particular manner either that:" (1) a delay in responding to a demand would cause irreparable harm to the corporation; or (2) that the directors cannot respond to the demand in good faith under the business judgment rule.

The Plaintiffs attempt to cure this defect in the original Complaint by alleging in the Amended Complaint that Mr. Metro and Valuation Services, Inc. are dependent on the will and control of Maxim's Board of Directors, who are interested parties, and that they do not have the authority or motivation to bring an action. Amended Complaint, ¶10 and ¶12. The deficiency in remains as the original Complaint was hastily filed before Maxim had a reasonable time to respond to the demands of the draft derivative complaint, and the Amended Complaint has been filed after Mr. Metro was engaged.

B. Maxim and The Board of Directors Responded in Good Faith to the Minority Stockholders' Requests for Information.

The history of the Plaintiffs' claims belies their "futility" excuse. In May or June of 2010, after Maxim made a buyout offer to the Minority Stockholders, they engaged legal counsel – specifically, Simon Nadler, Esq. of Shulman Rogers to advise them on the fairness of the offer. From June 11, 2010 through October 2010, Mr. Nadler made numerous requests for financial information and corporate records from Maxim. Maxim, through corporate counsel, Daniel S. Willard, Esq., responded to those requests and most of the documents sought were provided to the extent they existed. On July 23, 2010, Maxim even proposed in good faith a meeting together of the Minority Stockholders and the Directors with Maxim's accounting firm to answer

questions they might have about the financial condition of the business and the bases of a buyout offer made in March 2010.[6]

In a letter dated September 14, 2010, Mr. Nadler wrote to Mr. Willard, in pertinent part:

> Dear Dan:
>
> Our clients have now had an opportunity to review the information previously provided by Maxim Supermarket, Inc. ("Maxim"). The Minority Stockholders and I appreciate your efforts in working with Maxim, and in particular Mr. Ho and Ms. Lee (Maxim's accountant), to gather these documents.
>
> Not surprisingly, additional information is needed for the Minority Stockholders to adequately assess their ownership interest in Maxim and Mr. Ho's offer to purchase their stock.

The letter went on to chastise the Majority Stockholders for the manner in which they organized the business, did not have regular meetings, repaid loans and were paid compensation for their work. Maxim responded to the letter on September 28, 2010. A follow up letter from Mr. Nadler on October 12, 2010, reiterated much of the same chastisements and his demand for additional information. Mr. Ho and Ms. Puah, who were the founders, executive officers, directors and managerial team of Maxim, hired separate legal counsel, Daniel Ball, Esq. On January 11, 2011, through counsel, Mr. Ho and Ms. Puah provided detailed information to Mr. Nadler about the business of Maxim.[7]

C. The Minority Stockholders Submitted a Buyout Counteroffer and Settlement Proposal Two Months After Receiving Extensive Information About Maxim's Business.

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[6] Although the Amended Complaint makes it appear that Maxim refused to provide any information about the company to the Minority Stockholders until they hired a lawyer to make threats, nothing could be farther from the truth. From 2003 through 2010, the Minority Stockholders were provided annually Schedule K-1s reflecting their investments, ownership percentages, business income or loss, rental real estate income, interest payments, and dividend payments. The Minority Stockholders never questioned the financial information or sought additional financial or corporate information until June 2010, when they received a buy-out offer from Mr. Ho.

[7] Mr. Ball's letter, 24 pages in length, provided detailed information and explanations about (i) the business of Maxim, (ii) the origins of its organization and stockholders; (iii) loan repayments and dividend payments; (iv) subchapter S election; (v) prior stock redemptions and share purchases; (v) financial transactions with H and P and Reserve Champion; (vi) articles of incorporation and by-laws; (vii) the fairness of the buy-out offer made to the Minority Stockholders in March 2010; and (viii) made a renewal of Mr. Ho's buy-out offer with additional financial enhancements.

On March 14, 2011, counsel at Shulman Rogers, Gregory Grant, Esq., made a written settlement proposal to Mr. Ball purportedly cloaked under Maryland Rule 5-408. Attached to the proposal was a draft derivative complaint that Mr. Grant threatened to file for his clients "in the event that an acceptable resolution of their dispute with your clients is not quickly achieved." The letter went on to ask for *monetary compensation* for the Minority Stockholders and a buyout of his clients' shares. It did not make a demand upon Maxim to file the derivative complaint.

D. The Board of Directors Authorized Maxim to Engage a Valuation Expert After Seeing the Draft Derivative Complaint.

As a result of seeing the draft derivative complaint, and even though a demand had not been made on Maxim, the Directors considered in good faith the claims which the Minority Stockholders had presented therein. On March 23, 2011, Maxim formally engaged Valuation Services, Inc., a Member of the Zitelman Group (Principal – P. Richard Zitelman, CPA, CVA) regarding valuation, compensation and other issues related to Maxim and the claims being asserted by the Minority Stockholders. A copy of the Board of Director minutes confirming the engagement of Valuation Services, Inc. is attached hereto as Exhibit 1.

On March 31, 2011, Maxim, through counsel, Mr. Willard, responded to the settlement demands of Mr. Grant's letter of March 14, with the following letter (in pertinent part):

> Dear Mr. Grant:
>
> In light of the demands made upon Maxim Supermarket, Inc. in your letter of March 14, 2011, and the draft Complaint that accompanied it, the Board of Directors has engaged a valuation expert to advise the Board on the reasonableness of the compensation paid the Directors and Managerial Executives of the corporation. If the expert concludes that compensation was excessive, as the Minority Stockholders allege, the Board will act prudently on behalf of all stockholders.
>
> The Board of Directors has decided to defer filing its 2010 corporate tax return and the Schedule K-1s until it is able to consider the expert's conclusions. Prior to March 15, 2011, the corporation's accountant filed for an extension of the corporate tax return, enabling it to be filed up to and including September 15, 2011. The Minority and Majority Stockholders should consider filing for extensions of their 2010 individual tax returns because the K-1s will not be issued until after April 15, 2011. The Minority Stockholders may wish to consult their own tax advisors for advice.

Thus, within two weeks of receiving Mr. Grant's draft complaint and buyout counteroffer and demand for compensation for the Minority Stockholders, Maxim had engaged a valuation expert to advise the Board. Mr. Willard so notified Mr. Grant that Maxim would act prudently in the interests of all stockholders, including the Minority Stockholders, based on the conclusions of the valuation expert. This was a clear demonstration of Maxim's *bona fides* – the good faith exercise of its business judgment to seriously consider the derivative claims of the Minority Stockholders. Notwithstanding Maxim's earnest and diligent efforts, Mr. Grant wasted no time firing back a letter later in the day on March 31, 2011, misinterpreting the filing date of the Schedule K-1s and demanding the production of additional documents within 24 hours. Fifteen days later, on April 15, 2011, the Minority Stockholders rushed to file their derivative action.

E. The Amended Complaint Fails to Meet the Standards of Clearly Demonstrating Futility to Excuse the Demand Requirement.

The Plaintiffs' original Complaint and Amended Complaint make it exceptionally clear that they did not make a demand upon the Board of Directors because of their futility claim. To excuse a demand, they were required to clearly demonstrate, in a very particular manner that: "(1) a delay in responding to a demand would cause irreparable harm to the corporation;" This they failed to do.[8] If there was any urgency such as any irreparable harm to the corporation, the issue would have been raised by counsel earlier.

The other way to excuse a demand would have been for the Plaintiffs to clearly demonstrate, in a very particular manner: (2) that the directors cannot respond to the demand in

[8] For at least 6 months, the Minority Stockholders were requesting and evaluating financial information and documents from Maxim. There was no stated urgency in the process as the letters from their counsel were generally unhurried in time – Mr. Nadler typically took a minimum of several weeks each round to review and respond to correspondence or documents from Mr. Willard. Then after receiving Mr. Ball's letter on January 11, 2011, Shulman Rogers took two months, until March 15, to respond. The Amended Complaint does not allege that a delay in responding to a demand would cause irreparable harm to the corporation.

good faith under the business judgment rule. As showed in this Memorandum, however, the Directors responded quickly and in good faith once they received the draft derivative complaint.

F. In Further Exercise of Its Business Judgment, Maxim Has Engaged Special Investigation Counsel.

In addition, on June 14, 2011, the Board of Directors appointed a Special Investigation Counsel to serve as, and perform all the duties of, an independent Special Investigation Committee to advise the corporation how to proceed regarding the allegations made in the Complaint (and now Amended Complaint). Specifically, Maxim has engaged A. Howard Metro, Esq. of McMillan Metro as the Special Investigation Counsel to investigate the claims and issues raised in the derivative complaint. Mr. Metro has been given broad authority and power by the corporation to take whatever steps or actions he deems reasonable and necessary to investigate the claims and allegations and to carry out his assignment. He has the authority to examine all company records, including records maintained by the company's accounting firm. He has the authority to meet and interview whomever he deems to have information relevant to his investigation. Mr. Metro is authorized to prepare a report of his findings and to make recommendations to the Board of Directors. A copy of the Board of Director minutes authorizing Mr. Metro's appointment is attached hereto as Exhibit 2.

G. Making A Demand On The Board of Directors Would Not Have Been Futile.

When the Board of Directors considers the report of Valuation Services, Inc. and the recommendations of Mr. Metro, the Board can reasonably be expected to respond in good faith and within the ambit of the business judgment rule. *Werbowsky*, 362 Md. at 620. The corporation has demonstrated its good faith, first, by hiring the valuation expert, and second, by engaging the services of an independent Special Investigation Counsel to advise the Board on the course of action it should take with respect to the Minority Stockholders.

The Amended Complaint does not allege legally sufficient facts to excuse a demand on the Board of Directors, nor to deny the Board a reasonable amount of time to act upon it. In *Bender v. Schwartz*, 917 A.2d 142, 172 Md. App. 648 (Md. App. 2007), the underlying Circuit Court dismissed a shareholder derivative complaint because the facts alleged were insufficient to excuse a demand on the boards of directors. Several months later, the shareholders sent a demand letter to the directors to investigate the allegations and bring an action against the directors. As a result of that demand letter, the directors appointed special committees and new and independent directors. Here, Maxim's initial response to the draft derivative complaint was to promptly engage a valuation expert and inform the Minority Stockholders, through counsel, that the Board intended to act prudently on behalf of all stockholders based on the advice it would receive. Since the Complaint was filed, the Board of Directors has gone one step further by engaging Mr. Metro as Special Investigation Counsel.

Mr. Metro has commenced his investigation. He has received corporate documents from Maxim. He has met separately with counsel for the Plaintiffs. He has received extensive letters from counsel for both sides setting forth their requests as to the scope and parameters of his investigation of the Plaintiffs' allegations. Counsel for the Plaintiffs has informed Mr. Metro in writing that they will participate in and cooperate with his investigation and they are amenable to procedures that will enhance a thorough and impartial investigation. *Accord, Grant letter to Metro, dated 8-1-11 (not attached).* Though the Plaintiffs now object to Valuation Services, Inc., Mr. Willard informed Mr. Metro in writing that "if it is your judgment that a compensation expert other than Mr. Zitelman should be engaged by you, Maxim will commit to paying the cost." *Accord, Willard letter to Metro, dated 7-25-11 (not attached).* Judging these actions of Maxim and its Directors, a demand from the Minority Stockholders was not futile at all.

In *Boland v. Boland*, 194 Md. App. 477, 5 A.3d 106 (2010), a shareholders' derivative action based on a "demand refused", the corporations' board of directors appointed a Special Litigation Committee ("SLC") to investigate the derivative claims and determine whether to pursue them.[9] After five months of study, the SLC issued a report concluding that the claims had no merit and recommended that the corporations not pursue them and that claims be dismissed. The circuit court deferred to the SLC's decision under the business judgment rule. In *Boland*, five months to evaluate derivative claims based on allegations of self-dealing and excessive compensation was not considered to be too long a period of time.

The Amended Complaint should be dismissed. The Board of Directors will continue exercising their business judgment, investigate the derivative claims, obtain recommendations from Valuation Services, Inc. and Special Investigation Counsel, and act upon them in accordance with their business judgment.[10]

2. PLAINTIFFS CANNOT CLAIM UNJUST ENRICHMENT AGAINST DEFENDANTS HO, PUAH AND HU.

Plaintiffs' claims in Counts 2 and 5 that Defendants Ho, Puah and Hu have been unjustly enriched are unsupported by the facts alleged in the Amended Complaint and are legally

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[9] "If the corporation, after an investigation, fails to take the action requested by the shareholder(s) (i.e., to bring the suit), the shareholder(s) may bring a "demand refused" action. By making a demand, the shareholder(s) 'are deemed to have waived any claim they might otherwise have had that the board *cannot independently act* on the demand.' *Scattered Corp. v. Chicago Stock Exchange, Inc.*, 701 A.2d 70, 74 (1997) (emphasis added). The plaintiff may still allege, however, that the board *in fact* did not act independently or that demand was wrongly refused." *Id.* at 71; *Werbowsky*, 362 Md. at 619, 766 A.2d 123. Maxim has yet to reach this next stage because its investigation was not completed before the derivative lawsuit was filed.

[10] As stated in *Parish v. Milk Producers Assn.*, 250 Md. 24, 74, 242 A.2d 512 (1968), and reaffirmed several times since,

> It is well established that courts generally will not interfere with the internal management of a corporation at the request of a minority stockholder or a member. The conduct of the corporation's affairs [is] placed in the hands of the board of directors and if the majority of the board properly exercises its business judgment, the directors are not ordinarily liable.

It is well established in Maryland, and other jurisdictions, that courts generally will not interfere with the internal management of a corporation. *Devereux v. Berger*, 264 Md. 20, 31, 284 A.2d 605, 612 (1971).

insufficient. First, Maryland's three-year statute of limitations period for claims of unjust enrichment has run out as to the Defendants involvement with H and P, and will cut off any action relating to Reserve prior to April 15, 2008. Maxim, on whose behalf Plaintiffs bring these claims against Defendants Ho, Puah and Hu was a party to the transactions with H and P and Reserve and had knowledge of the transactions from their inception in 2007. Second, Plaintiffs have failed to allege facts necessary to meet the elements of a claim for unjust enrichment. Defendants incorporate by reference Sections 1 and 2 of the Memorandum of Points and Authorities in Support of the Motion to Dismiss Amended Complaint of Defendants H and P and Reserve. Inasmuch as Plaintiffs cannot meet the elements of unjust enrichment as to H and P and Reserve, their claims against Defendants Ho, Puah and Hu that flow against them from their unjust enrichment claims against H and P and Reserve similarly lack the essential elements.

3. PLAINTIFFS' COUNT 8 MUST BE DISMISSED BECAUSE MAXIM HAD CORPORATE POWER AND AUTHORITY TO PAY DIRECTORS' FEES AND ENTER INTO TRANSACTIONS WITH H AND P AND RESERVE.

Under Count 8 of the Amended Complaint, by claiming that Maxim had no corporate power or authority to pay the Board of Directors fees for their services and enter into transactions with H and P and Reserve, Plaintiffs, citing Md. Code Ann., Corps. & Assns. § 1-403(b)(1), ask the Court to set aside the consulting agreements between Maxim and H and P and Reserve and enjoin their performance. Amended Complaint, ¶ 179. However, Plaintiffs misread both Maxim's Articles of Incorporation and Maxim's By-Laws, which specifically permit Maxim to enter into such transactions. Accordingly, the Court should dismiss Plaintiffs' Count 8.

Plaintiffs allege that Article III, Section 11 of Maxim's By-Laws prohibit the payment of director's fees to Maxim's Board of Directors. Amended Complaint, ¶ 176, Ex. B. However, the language of Section 11 only makes mention of a "stated salary" for directors, not fees:

> No stated salary shall be paid to directors, as such, for their services, but by resolution of the Board of Directors a fixed sum and expenses of

> attendance, if any, may be allowed for attendance at each regular or special meeting of the Board; provided, however, that nothing herein contained shall be construed to preclude any director from serving the Corporation in any other capacity and receiving compensation therefor.

Amended Complaint, Ex. B. In fact, Section 11 allows for Maxim's Board of Directors, by resolution, to provide its directors with a fixed sum and expenses of attendance at each meeting of the Board, clearly distinguishing this type of fee payment from a "stated salary." Pursuant to this provision of the By-Laws, Maxim's Board of Directors, "due to the volume of the business" that Maxim was generating, decided to pay out a "director's fee" – not salary – to Maxim's directors starting in January 2006, as reflected in the minutes of Maxim's Board of Directors' meeting. Amended Complaint Ex. C. Section 11 of Maxim's By-Laws was silent as to the method or rate of distribution of the director's fee. The Board of Directors established a monthly payment schedule for the director's fee, rather than a per meeting fee or an annual lump sum payment – although any of these options could have been permitted under Maxim's By-Laws. Plaintiffs' claims to the contrary, Maxim's By-Laws clearly authorize Maxim's Board of Directors to pay a director's fee, as opposed to a salary, to Maxim's Board of Directors.[11]

Plaintiffs' challenge to Maxim's corporate authority to permit director's fees to be paid to its directors does not overcome the language of Maxim's By-Laws. Furthermore, Section 2-419(d)(2) of the Maryland Code, Corporations and Associations Article, specifically exempts from challenge "the fixing by the board of directors of reasonable compensation for a director,

[11] The distinction between director's salary and director's fees stems from the tax treatment of the remuneration. Corporate directors who receive no compensation other than fees for attendance at director's meetings are not in the employment of the corporation, and are therefore exempt from certain tax withholdings, given the treatment as self-employment income. A salary, on the other hand, would be treated as employment wages and subject to withholding taxes. *See* Internal Revenue Code Reg. § 31.3121(d)-1(b), 31.3306(i)-1(e) and 31.3401(c)-1(f) [FICA, FUTA and income tax withholding] (providing that corporate directors are not corporate employees and fees are treated as self-employment income).

whether as a director or in any other capacity." Md. Code Ann. § 2-419(d)(2). Plaintiffs' claim based on lack of corporate authority to permit director's fees must be dismissed.[12]

Plaintiffs also contend that Article 8, section 2 of Maxim's Articles of Incorporation and Article III, section 12(b) of Maxim's By-Laws prohibit Maxim from entering into agreements with H and P and Reserve, in which the directors had a financial interest, without the approval of a majority of disinterested directors. Amended Complaint, ¶ 178, Exs. A and B. However, the language of those provisions specifically permit such transactions.

Article 8, section 2 of the Articles of Incorporation specifically permits an officer and director to be an "interested party" in any contract or transaction with the corporation:

> (2) Any director, individually, or any firm of which any director may be an officer or director in which may be interested as the holder of any amount of its capital, stock or otherwise interested in, any contract or transaction of the Corporation, and in the absence of fraud no contract or other transaction shall be thereby affected or invalidated; provided, that in case a director, or a firm of which a director is a member, is so interested, such fact shall be disclosed or shall have known to the Board of Directors or a majority thereof; and any director of the Corporation who is also a director or officer or interested in such other corporation or association, or who, or the firm of which he is a member, is so interested, may be counted in determining the existence of a quorum at the meeting of the Board of Directors which shall authorize any such contract or transaction, as if he were not such a director or officer of such other corporation or association, or not so interested or a member of a firm not so interested.

Amended Complaint, Ex. A. The language could not be clearer. Contracts with a company in which a director of Maxim has an interest are permitted, so long as that fact is disclosed or is known to Maxim's Board of Directors or a majority of Maxim's Board of directors. The interests of Maxim's directors in H and P and Reserve were known to all of Maxim's directors, not just a majority, as well as to Maxim itself. The directors did not hide their interests from each other or

[12] Article IX, Section 2 of the By-Laws provides that "[t]he Board of Directors shall have power to make, adopt, amend and repeal, from time to time, by-laws of the Corporation". Thus, alternatively, payment of compensation to the Directors which was approved by all of the Directors is deemed an amendment *defacto* of the By-Laws under principles of corporate governance and internal management. The end result is the same -- the payments were permitted.

from Maxim, and the Board of Directors was fully informed of the interested directors' holdings in H and P and Reserve. Additionally, even the interested directors, under this section of the Articles of Incorporation, are counted in determining the existence of a quorum at a meeting of the Board of Directors to authorize the transaction, regardless of the director's interest. Because Maxim and its Board of Directors were fully apprised of the interests of the directors, Maxim had full authority to approve the contracts between Maxim and H and P and Reserve.

Article III, section 12 of Maxim's By-Laws also confirms this. Both section 12(a) and 12(b) permit Maxim to enter into transactions with interested directors:

> (a) No contract or other transaction between this Corporation [Maxim] and any other Corporation shall be impaired, affected or invalidated nor shall any director be liable in any way by reason of the fact that anyone or more of the directors of this Corporation is or are interested in, or is a director or officer, or are directors or officers of such other Corporation, provided that such facts are disclosed or made known to the Board of Directors.
>
> (b) Any director, personally and individually, may be a party to or may be interested in any contract or transaction of this Corporation, and no director shall be liable in any way by reason of such interest, provided that the fact of such interest be disclosed or made known to the Board of Directors, and provided that the Board of Directors shall authorize, approve or ratify such contract or transaction by the vote (not counting the vote of any such director) of a majority of a quorum, notwithstanding the presence of any such director at the meeting at which such action is taken. Such director or directors may be counted in determining the presence of a quorum at such meeting. This Section shall not be construed to impair or invalidate or in any way affect any contract or other transaction which would otherwise be valid under the law (common. statutory or otherwise) applicable thereto.

Amended Complaint, Exhibit B. Again, the language of Section 12(a) plainly states that any contract that Maxim enters into shall not be "impaired, affected or invalidated" simply because a director of Maxim is interested in or is a director or officer of the other party to the contract, provided that such facts are disclosed to the Board of Directors. Section 12(b) reiterates that a director of Maxim may be an interested party to a contract with Maxim, so long as it is disclosed to the Board of Directors. Consistent with Article 8 of Maxim's Articles of Incorporation,

Section 12(b) of the By-Laws further spells out that the interested directors may be counted in making up a quorum at any meeting of Maxim's Board of Directors to authorize and approve such contracts. A majority of the quorum of directors shall approve the contracts, even if the interested directors' votes are not counted. Despite Plaintiffs' contentions that authorization requires an approval of a "majority of disinterested directors," Amended Complaint, ¶ 177, it is simply a majority of a quorum of the directors that must approve the transactions. The contracts and transactions between Maxim and H and P and Reserve are the kinds of matters protected under Article 8 of Maxim's Articles of Incorporation and Article III, Section 12 of Maxim's By-Laws, especially since the Board of Directors was informed of the interested directors' holdings in H and P and Reserve. Article III, Section 12(b) specifically provides too that "no director shall be liable in any way by reason of such interest." Thus, Count 8 fails to state a claim upon which relief can be granted.

Moreover, Section 2-419 of the Corporations and Association Article, Maryland Code, provides that a contract or financial transaction between a corporation and any director(s) or entity in which the director(s) has a material financial interest is not void or voidable solely because (1) there is a common directorship or interest; (2) the director(s) was at a meeting of the board which authorized, approved or ratified the contract or transaction; or (3) the interested director(s) voted for the authorization, approval or ratification of the contract or transaction and the vote counted. Maxim's Articles of Incorporation specifically permit interested director transactions – and the authorization is without strings or adherence to any special requirements, statutory or otherwise. The Maryland Code speaks about interested director transactions in terms of fairness and reasonableness to the ***corporation,*** not fairness and reasonableness to any class of shareholders or to directors, officers, employees or shareholders who are not participants in the

interested contract or transactions. Md. Code Ann., Corps. & Assns. § 2-419(b)(2); *Sullivan v. Easco Corp.,* 656 F. Supp. 531, 535 (D. Md. 1987).

4. COUNT 1 SHOULD BE DISMISSED BECAUSE THE PLAINTIFFS FAIL TO PLEAD THE ESSENTIAL ELEMENTS OF FRAUD.

A. The Elements of a False Representation and Reasonable Reliance Were Not Pled.

Count 1 is styled as an action for Constructive Fraud/Breach of Fiduciary Duty but the Plaintiffs fail to plead all the essential elements of fraud.[13] Constructive fraud is defined as "a breach of a legal or equitable duty which, irrespective of the moral guilt of the fraud feasor, the law declares fraudulent because of its tendency to deceive others, to violate public or private confidence, or to injure public interests. Neither actual dishonesty of purpose nor intent to deceive is an essential element of constructive fraud." *Son v. Margolius, Mallios, Davis, Rider & Tomar*, 689 A.2d 645, 660-661 (Md. App. 1996), *quoting Scheve v. McPherson*, 44 Md.App. 398, 406, 408 A.2d 1071 (1979). "'Constructive fraud' is nonetheless fraud. *Id.* Therefore, the elements of fraud not resting on intent or dishonesty remain essential." *Id*.

The elements of fraud are: (1) a false representation made by the defendant to the plaintiff; (2) that the falsity was either known to the Defendant or the representation was made with reckless indifference as to its truth; (3) that the misrepresentation was made for the purpose of defrauding the plaintiff; (4) that the plaintiff relied upon the misrepresentation and had the right to rely upon it; and (5) that the plaintiff suffered actual damages resulting from the misrepresentation. *Md. Envtl. Trust v. Gaynor,* 370 Md. 89, 97 (2002); *Son v. Margolius, Mallios, Davis, Rider & Tomar*, 689 A.2d 645, 660 (Md. App. 1996). *Also see, Alleco Inc. v.*

[13] The genesis of a cause of action for constructive fraud is in the domain of property disputes. Constructive fraud primarily arises in the context of setting aside a deed or a tax sale decree, pursuant to specific statutory provisions. *City of College Park v. Jenkins*, 819 A.2d 1129, 1139 (Md. App. 2003). Constructive fraud is defined in Section 14-845 of the Tax-Property Article of the Maryland Code. The failure to provide notice to the owner of property of the sale of the property amounts to constructive fraud under the doctrine of *Jannenga v. Johnson*, 243 Md. 1, 220 A.2d 89 (1966).

Harry & Jeanette Weinberg Found., Inc., 340 Md. 176, 665 A.2d 1038 (1995); *Martens Chevrolet, Inc. v. Seney*, 292 Md. 328, 439 A.2d 534 (1982).

No where in the Amended Complaint do the Plaintiffs allege facts to show with specificity (1) that a false representation was made by each of the individual Defendants to Maxim; (2) that the false representation was known by each of the individual Defendants to be false or was made with reckless indifference as to its truth; (3) that the misrepresentation was made for the purpose of defrauding Maxim; (4) that Maxim reasonably relied upon the misrepresentation; and (5) that Maxim suffered actual damages resulting from the misrepresentation. It is axiomatic that the Plaintiffs must plead each false representation allegedly made by each of the individual Defendants in order to hold each Defendant liable. In common fraud parlance, the Plaintiffs are required to plead the "who", "what", "when" and "where" of the false representation purportedly made by each Defendant accused of fraud. The Plaintiffs must also plead how Maxim reasonably relied upon the misrepresentation to its utter detriment. None of these elements were properly pleaded.

At most, the Amended Complaint alleges that invoices issued by H and P and Reserve Champion to Maxim were false and that all of Maxim's officers and directors were involved in preparing the false invoices. Amended Complaint, ¶¶ 69, 70, 91, 92, 123, and 155. The Amended Complaint fails to plead how the invoices were a false representation made to Maxim when (1) Maxim agreed to pay H and P and Reserve Champion and all the officers and directors of Maxim were involved in allegedly preparing these so-called "false" invoices. More importantly, the Amended Complaint fails to plead how Maxim relied upon the *falsity* of the invoices to pay them. In ¶70 and ¶92, the Amended Complaint alleges that "[b]ecause all of Maxim's officers and directors were involved in preparing these false invoices (or consented to doing so), Maxim reasonably relied on them in paying [H and P; or Reserve Champion.]" If the

allegations are taken as true, if all of Maxim's officers and directors were involved in preparing false invoices, then Maxim could not have been deceived and could not have relied to its detriment upon the falsity of the invoices because Maxim had knowledge of the falsity – that is, the knowledge of all of its officers and directors is imputed to Maxim.

Although pleadings may be simple, they are required to contain statements of fact necessary to show the pleader is entitled to relief. *Walser v. Resthaven Memorial Gardens, Inc.*, 98 Md. App. 371, 633 A.2d 466 (1993), *cert denied*, 334 Md. 212, 638 A.2d 753 (1994). The Amended Complaint fails to allege any false representation made by the individual Defendants. It alleges only that invoices were false, but then pleads that all of Maxim's officers and directors knew that the invoices were false (before the invoices were paid) – thereby negating any inference that Maxim was reasonable in relying upon the falsity of the invoices.

In *Gross v. Sussex, Inc.*, 332 Md. 247, 257, 630 A.2d 1156 (1993), the Court of Appeals enumerated the elements of a prima facie claim for fraud under Maryland law. The fourth element, reliance, was enumerated this way:

> (4) that the person not only relied on the misrepresentation but had a right to rely upon it **with full belief in its truth**, and that the person would not have done the thing from which the damage resulted if the misrepresentation had not been made; (citations omitted) (emphasis added)

Applying this element here, there is no allegation that Maxim fully believed the invoices were true and that Maxim would not have paid the invoices, i.e., acted upon them in the same way, if Maxim had known they were false. Since Maxim could not have believed the invoices were true when, as alleged by the Plaintiffs, all of the officers and directors knew that the invoices were "false", the element of reasonable reliance is and will always be absent. *See also*, *City of College Park v. Jenkins*, 819 A.2d 1129, 1137 (Md. App. 2003), stating in its analysis that actual knowledge of fraud would be sufficient to negate any reliance claim in a constructive fraud case. The Plaintiffs have failed to adduce facts, and cannot adduce facts, as a matter of

law, which would support the claim of constructive fraud. In this case, Count 1 for Constructive Fraud/Breach of Fiduciary Duty must fail as a matter of law.

B. Claims Based on Acts Prior to April 15, 2008 Are Barred by the Statute of Limitations.

For reasons set forth in Section 2 above and in Sections 1 and 2 of the Memorandum of Points and Authorities in Support of the Motion to Dismiss Amended Complaint of Defendants H and P and Reserve, incorporated herein by reference, the Plaintiffs' claims for constructive fraud based on acts prior to April 15, 2008, such as the alleged false invoices, should be dismissed on statute of limitations grounds as they arose more than three years before the filing of the lawsuit.

5. PLAINTIFFS' CLAIMS FOR PUNITIVE DAMAGES SHOULD BE DISMISSED.

The Defendants incorporate by reference Section 3 of the Memorandum of Points and Authorities in Support of the Motion to Dismiss Amended Complaint of Defendants H and P and Reserve as those points and authorities are applicable to the punitive damages claims against individual Defendants Ho, Puah and Hu (Amended Complaint ¶ 114 and ¶179(F)). Furthermore, even if the Plaintiffs were successful in dissolving and destroying Maxim, punitive damages are not a cognizable remedy for dissolution under the judicial dissolution statute, Maryland Code, Corporations and Associations Article §3-413.

6. PLAINTIFFS CLAIMS FOR BREACH OF FIDUICARY DUTY SHOULD BE DISMISSED.

Maryland does not recognize a separate cause of action at law for monetary damages for breach of fiduciary duty, and therefore, Count 1 should be dismissed. Defendants incorporate by reference Section 2 of Defendant H and P and Reserve's Memorandum of Points and Authorities in Support of their Motion to Dismiss Amended Complaint.

DATED: August 9, 2011

Respectfully submitted,

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CERTIFICATE OF SERVICE

I hereby certify that on the 9th day of August, 2011, I caused a copy of the Motion to Dismiss Amended Complaint of Defendants Ho, Puah and Hu, Memorandum of Points and Authorities in Support thereof, Exhibits 1 and 2, Appendix, and proposed Order to be delivered by first class mail, postage prepaid, to:

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