

07-3750-cv
Halebian v. Berv

1 UNITED STATES COURT OF APPEALS

2 FOR THE SECOND CIRCUIT

3
4 August Term, 2008

5 (Argued: February 5, 2009 Decided: December 29, 2009)

6 Docket No. 07-3750-cv

7 -----
8 JOHN HALEBIAN,

9 Plaintiff-Appellant,

10 - v. -

11 ELLIOT J. BERV, DONALD M. CARLTON, A. BENTON COCANOUGH, MARK T.
12 FINN, STEPHEN RANDOLPH GROSS, DIANA R. HARRINGTON, SUSAN B.
13 KERLEY, ALAN G. MERTEN, R. RICHARDSON PETTIT,

14 Defendants-Appellees,

15 CITIFUNDS TRUST III,

16 Nominal Defendant-Appellee.*

17 -----
18 Before: SACK and PARKER, Circuit Judges, and STANCEU, Judge.**

19 Appeal from a judgment of the United States District
20 Court for the Southern District of New York (Naomi Reice
21 Buchwald, Judge) dismissing a three-count complaint arising from
22 the renegotiation of certain investment advisory agreements. We
23 reserve decision while certifying to the Supreme Judicial Court
24 of Massachusetts a question as to the circumstances under which

* The Clerk of Court is directed to amend the official caption as set forth above.

** The Honorable Timothy C. Stanceu, of the United States Court of International Trade, sitting by designation.

1 the business judgment rule may be asserted in response to a
2 shareholder derivative suit under the Massachusetts Business
3 Corporation Act.

4 Question certified; decision reserved.

5 JOEL C. FEFFER (Daniella Quitt, James G.
6 Flynn, on the brief) Harwood Feffer LLP,
7 New York, NY, for Plaintiff-Appellant.

8 JAMES S. DITTMAR, Goodwin Procter LLP,
9 Boston, MA (Michael K. Isenman, Matthew
10 Hoffman, Goodwin Procter LLP,
11 Washington, DC, on the brief) for
12 Defendants-Appellees.

13 SACK, Circuit Judge:

14 John Halebian, a shareholder of an investment fund
15 within CitiFunds Trust III ("CitiTrust" or the "Trust"), appeals
16 from a judgment of the United States District Court for the
17 Southern District of New York (Naomi Reice Buchwald, Judge). The
18 court dismissed his three-count complaint against members of the
19 Trust's board of trustees, the defendants here, in connection
20 with the sale of an adviser of the Trust and the approval of new
21 investment advisory contracts following that sale. Claim One,
22 styled as a derivative claim on behalf of the Trust, alleges that
23 the defendants breached their fiduciary duties to the Trust "in
24 considering the . . . transaction and in recommending the new
25 advisory agreements." Complaint ¶ 54, Halebian v. Berv, No. 06
26 Civ. 4099 (S.D.N.Y. filed May 30, 2006) (Doc. No. 1) ("Compl.").
27 Claims Two and Three, styled as direct claims, allege that the
28 defendants violated federal and state law by issuing materially

1 false and misleading statements encouraging their shareholders to
2 approve the new investment advisory contracts.

3 We conclude that we cannot decide the propriety of the
4 district court's dismissal of Count One without resolving a
5 question of Massachusetts law which appears to us to be one of
6 first impression. We think that issue would best be decided by
7 the Massachusetts Supreme Judicial Court in the first instance.
8 Accordingly, we certify that question to the Supreme Judicial
9 Court. Although we are of the view that dismissal of Counts Two
10 and Three was proper, in light of our decision to certify a
11 question to the Supreme Judicial Court in connection with Count
12 One and because our resolution of the propriety of the district
13 court's dismissal of Counts Two and Three also involves the
14 application of Massachusetts law, we think it the more prudent
15 course to reserve judgment in this respect, too, pending the
16 Supreme Judicial Court's response to the question certified.

17 **BACKGROUND**

18 The following recitation is based on Halebian's
19 complaint and other documents "integral" to that complaint, see
20 Chambers v. Time Warner, Inc., 282 F.3d 147, 153 (2d Cir. 2002),
21 the factual assertions of which, for purposes of this discussion,
22 we assume to be true, see Ashcroft v. Iqbal, 129 S. Ct. 1937,
23 1949 (2009). Halebian is a citizen of New York State. At all
24 relevant times, he owned shares in the Citi New York Tax Free
25 Reserves Fund (the "New York Fund"), one of six "series
26 portfolios," or mutual funds (the "Funds"), contained in the

1 Trust. See Compl. ¶ 7. CitiTrust is a Massachusetts business
2 trust with its principal place of business in Maryland. Id. ¶ 8.
3 CitiTrust is "named as a nominal defendant . . . solely in a
4 derivative capacity." Id. ¶ 9. The actual defendants, none of
5 whom is a New York citizen, are members of CitiTrust's Board of
6 Trustees (the "Board"). Id. ¶¶ 10-19.

7 The Transaction

8 On June 23, 2005, Citigroup sold substantially all of
9 its asset management business, including a subsidiary that served
10 as an adviser to CitiTrust, to Legg Mason, Inc. Id. ¶ 32. In
11 connection with this transaction (the "Transaction"), the Funds'
12 existing advisory contracts were terminated and new contracts
13 were executed with the Funds' new advisers, id. ¶ 33, for which
14 the Funds' shareholders' approval was required, id. ¶ 34. In
15 August 2005, the Board approved the Funds' new investment
16 advisory agreements with Legg Mason. Id. ¶ 39. Thereafter, the
17 Board issued a proxy statement to its shareholders describing the
18 advisory agreements and recommending that they vote to approve
19 the new agreements, id. ¶¶ 34-35, which they did, id. ¶ 61.

20 Two aspects of the Transaction are relevant to this
21 appeal. First, the new advisory agreements authorize the payment
22 of "soft dollars." Id. ¶ 43.¹ As described by the district
23 court, soft-dollar payments "permit the advisor to select brokers

¹ The prior advisory agreements also permitted soft-dollar payments. See Halebian v. Berv, 631 F. Supp. 2d 284, 289 (S.D.N.Y. 2007).

1 or dealers who provide both brokerage and research services to
2 the Funds, even though the commissions charged by such brokers or
3 dealers might be higher than those charged by other brokers or
4 dealers who provide execution only or execution and research
5 services." Halebian v. Bery, 631 F. Supp. 2d 284, 289 (S.D.N.Y.
6 2007).

7 Second, the voting procedures employ "echo voting," in
8 which Citigroup-affiliated service agents who were record holders
9 of shares for which instructions had not been received would vote
10 those shares "in the same proportion as the votes received from
11 its customers for which instructions have been received." Compl.
12 ¶ 45 (internal quotation marks omitted).²

13 The Demand Letter and the Board's Response

14 On February 8, 2006, Halebian, through counsel,
15 expressed his dissatisfaction with the Transaction by letter to
16 the Board. Compl. ¶ 48. He asserted that in connection with the

² This practice is described in the Trust's most recent prospectus, in the "Trust Instrument" (the source of the shareholders' contractual rights), and in the relevant proxy statement. Halebian, 631 F. Supp. 2d at 289 n.2. The proxy statement notified the shareholders that:

With respect to any shares for which a Citigroup-affiliated service agent (other than a broker-dealer) is the holder of record and for which it does not receive voting instructions from its customers, such service agent intends to vote those shares in the same proportion as the votes received from its customers for which instructions have been received.

Id. at 289.

1 Transaction and contrary to its fiduciary duty, the Board "placed
2 the interests of Citigroup before those of the Fund and . . .
3 [its] shareholders" and "failed to avail itself of the
4 opportunity presented to seek to negotiate lower fees" on behalf
5 of the Trust "or to seek competing bids from other qualified
6 investment advisers." Letter from Joel C. Feffer to the Bd. of
7 Trs. of the Citi N.Y. Tax Free Reserves Series of Citi Funds
8 Trust III 1-2 (Feb. 8, 2006). The letter demanded "that the
9 board take action which would include, among other things, the
10 institution of an action for breach of fiduciary duty against any
11 and all persons who are responsible for the board's dereliction
12 of its duties in connection with the . . . transaction" and that
13 "appropriate remedial measures . . . be undertaken, including
14 seeking bids for the advisory contract from other qualified
15 investment advisers, negotiating new terms more favorable to the
16 [New York] Fund with Legg Mason, or both." Id. at 2.

17 The demand letter noted that "shareholder approval does
18 not appear to have been obtained properly," presumably a
19 reference to the echo voting practices described in the proxy
20 statement. The letter did not, however, make a demand with
21 respect to this purported impropriety because, the letter said,
22 the impropriety "gives rise to direct, rather than derivative,
23 claims." Id. at 1 n.1.

24 The Board acknowledged receipt of the demand letter.
25 Compl. ¶ 49. It later advised Halebian that it had created a
26 "Demand Review Committee" to review his complaint, and that the

1 committee had retained counsel. Id. ¶ 50. Throughout this
2 period of time, counsel for both Halebian and the Demand Review
3 Committee remained in communication with one another.

4 Halebian's Complaint

5 On May 30, 2006, more than ninety days after the date
6 of Halebian's original demand letter, not having received a
7 definitive response from the Demand Review Committee, Halebian
8 filed a three-count complaint in the United States District Court
9 for the Southern District of New York. In it, he alleges that
10 following his demand letter, Halebian waited "the statutory time
11 required" -- ninety days -- before filing his derivative claim;³
12 that such a period "provide[d] more than adequate time" for the
13 Board to have reviewed Halebian's demand and have taken action;
14 and that "[n]ot surprisingly, defendants have failed to take
15 action against themselves." Compl. ¶ 51.

16 Claim One, styled as a derivative claim for breach of
17 fiduciary duty, alleges that members of the Board breached their
18 fiduciary duties of good faith and loyalty under Massachusetts
19 law in their "consider[ation of] the Citigroup/Legg Mason
20 transaction and in recommending the new advisory agreements."
21 Id. ¶ 54. The complaint alleges that the "[d]efendants limited
22 their consideration to whether the . . . transaction would be

³ As discussed in greater detail below, prior to the filing of a derivative claim under Massachusetts law, a shareholder must give the corporation the opportunity to resolve the issue that forms the basis of the claim. See Mass. Gen. Laws ch. 156D, § 7.42.

1 worse for CitiTrust's beneficiaries than their current situation"
2 and "made no effort to investigate whether a transaction could be
3 fashioned which would benefit CitiTrust's beneficiaries, either
4 with Legg Mason or another asset manager." Id. ¶ 36. Halebian
5 contends that the soft-dollar arrangements allow for the payment
6 of "higher than necessary brokerage commissions," id. ¶ 43,
7 referring to those payments as "kickback[s]," id. ¶ 44.⁴

8 Claim Two, styled as a direct claim on behalf of
9 Halebian and members of a class of "all persons and entities who
10 held shares of beneficial interest in CitiTrust on August 22,
11 2005 (the 'Class')," id. ¶ 26, alleges that the proxy statement
12 at issue violated section 20(a) of the Investment Company Act of
13 1940 (the "ICA"), 15 U.S.C. § 80a-20(a), because it contained
14 material misstatements and omissions. First, the echo voting
15 procedures described in the proxy statement violated federal law
16 -- section 15(a) of the ICA, 15 U.S.C. § 80a-15(a) -- and
17 unspecified provisions of Massachusetts law, and that the proxy
18 statement was misleading because it did not so state. Compl. ¶¶

⁴ In 2006, the SEC issued an Interpretive Release that provides guidance on the use of "soft dollars" under section 28(e) of the Securities Exchange Act of 1934, 15 U.S.C. § 78bb(e)(1). It provides "a safe harbor that allows money managers to use client funds to purchase 'brokerage and research services' for their managed accounts under certain circumstances without breaching their fiduciary duties to clients." Commission Guidance Regarding Client Commission Practices Under Section 28(e) of the Securities Exchange Act of 1934, Exchange Act Release No. 54,165, 71 Fed. Reg. 41,978, 41,978 (July 24, 2006). To qualify under the safe-harbor provision, money managers must "make a good faith determination that the commissions paid are reasonable in relation to the value of the brokerage and research services received." Id. at 41,991.

1 47, 60. Second, the proxy statement failed to disclose that by
2 virtue of the Transaction, assets of CitiTrust were
3 "diver[ted] . . . for the benefit of others," id. ¶ 60,
4 presumably via soft dollar payments. Based on this "material
5 false and misleading information," Halebian alleges, the
6 "[d]efendants secured approval of the new advisory agreements."
7 Id. ¶ 61.

8 Claim Three, also styled as a direct claim on behalf of
9 Halebian and members of the Class, id. ¶ 26, asserts that the
10 trustees violated Massachusetts law, id. ¶ 64, by failing fully
11 and fairly to disclose in the proxy statement all material
12 information within their control, namely, the "[im]propriety of
13 the[] voting procedures" and "the diversion of CitiTrust assets
14 for the benefit of others," id. ¶ 65.

15 The complaint seeks declaratory and injunctive relief
16 and compensatory damages. See Compl. at 20-21, "Prayer for
17 Relief."

18 Board's Post-Complaint Conduct

19 By resolution dated July 12, 2006, some six weeks after
20 the timely filing of Halebian's complaint, the Board expressly
21 declined to accede to Halebian's demand, effectively rejecting
22 it. See Res. of the Bd. of Trs. of CitiFunds Trust III 27
23 (July 12, 2006). The Board stated that it had "studied a large
24 volume of information on the quality and costs of the adviser's
25 services, including a study that indicated the Fund's management
26 fee was in the lowest quintile measured against fees for similar

1 funds, and concluded that the fees were reasonable." Id. at 22.
2 The Board further "found no authority for the proposition that
3 the 1940 Act or Massachusetts law forbids the use of echo voting
4 by a record holder of shares in a vote to approve an advisory
5 contract with a registered mutual fund" and noted that "[e]cho
6 voting is a common practice in the financial industry [the]
7 utility [of which practice] has been recognized both by the
8 Securities and Exchange Commission and the New York Stock
9 Exchange." Id. at 25. According to the Board, "the balance of
10 the Trust's interests weighs against taking the action requested
11 in the Demand Letter." Id. at 26. On that basis, the Board
12 declined to institute any action against its members. It
13 directed its counsel to move to dismiss Halebian's derivative
14 claim instead. Id. at 27-28.

15 On October 24, 2006, defendants' counsel moved
16 pursuant to, inter alia, Federal Rule of Civil Procedure 12(b)(6)
17 to dismiss the complaint.

18 The District Court Opinion

19 By Memorandum and Order dated July 31, 2007, the
20 district court granted the defendants' motion to dismiss. See
21 Halebian, 631 F. Supp. 2d at 303.

22 In addressing Count One, the court acknowledged that
23 Halebian had satisfied Massachusetts's statutory universal demand
24 requirement for derivative actions by demanding that the Trust
25 rectify the alleged improprieties in the Legg-Mason transaction
26 and then waiting the requisite 90 days before filing his suit.

1 See Mass. Gen. Laws ch. 156D, § 7.42. The district court
2 nonetheless dismissed Count One on two other bases.

3 First, the court concluded that the complaint failed to
4 comply with Rule 23.1 of the Federal Rules of Civil Procedure
5 because it "asserts no basis for 'plaintiff's failure to obtain
6 the action' from the board as required by Rule 23.1." Halebian,
7 631 F. Supp. 2d at 297-98 (quoting Fed. R. Civ. P. 23.1 (2006)).

8 Second, the court concluded that dismissal was
9 appropriate pursuant to a then-recently enacted provision of
10 Massachusetts law authorizing the dismissal of derivative actions
11 based on the corporation's good-faith business judgment that
12 prosecution of the action would not be in its best interests.

13 See Mass. Gen. Laws ch. 156D, § 7.44(a). The district court
14 acknowledged that section 7.44, by its terms, applies only to
15 derivative proceedings "commenced after rejection of a demand"
16 and that Halebian's suit had been filed before any rejection of
17 his demand. See id. Nonetheless, the court concluded that
18 dismissal pursuant to section 7.44 would be required "as long as
19 [CitiTrust] rejected the demand after a good faith review,"
20 irrespective of whether that rejection post-dated the timely
21 filing of a derivative claim. Halebian, 631 F. Supp. 2d at 294.
22 Upon concluding that section 7.44 applied, the district court
23 dismissed Count One based on its finding that the section's
24 various preconditions had been met -- "an independent group [of
25 the Trust's leadership] has determined in good faith after
26 conducting a reasonable inquiry that the maintenance of the

1 proceeding is not in the [Trust's] best interest." See id. at
2 295-96 (citing Mass. Gen. Laws ch. 156D, § 7.44(a)).

3 The district court then addressed Counts Two and Three
4 in tandem, concluding that although Halebian had styled both as
5 direct claims they were in fact derivative claims "because they
6 seek to redress an alleged injury to the Funds." Id. at 302. In
7 light of Halebian's failure to make a demand on the corporation
8 with respect to either of these claims, as is required under
9 Massachusetts's law for any properly filed derivative claim, see
10 Mass. Gen. Laws ch. 156D, § 7.42, the district court dismissed
11 both of them, Halebian, 631 F. Supp. 2d at 303. As an
12 alternative basis for dismissal, the court concluded that Counts
13 Two and Three "sound[ed] in fraud" and failed to meet the
14 "heightened standard of pleading for claims which sound in fraud"
15 as required by Rule 9(b) of the Federal Rules of Civil Procedure.
16 Id.

17 The district court also concluded that Claim Two --
18 Halebian's "direct" claim for violation of section 20(a) of the
19 ICA -- failed because, under Alexander v. Sandoval, 532 U.S. 275
20 (2000), and its progeny, see, e.g., Olmstead v. Pruco Life Ins.
21 Co., 283 F.3d 429 (2d Cir. 2002), no federal private right of
22 action is available for a violation of section 20(a). Halebian,
23 631 F. Supp. 2d at 298-301.

24 Halebian appeals. We reserve judgment pending a
25 response by the Supreme Judicial Court of Massachusetts to a
26 question of Massachusetts law that we certify to it.

1 **DISCUSSION**

2 I. Standard of Review

3 We review dismissals pursuant to Rule 12(b)(6) of the
4 Federal Rules of Civil Procedure de novo. See Velez v. Levy, 401
5 F.3d 75, 84 (2d Cir. 2005). Where "determination of the
6 sufficiency of allegations of futility depends on the
7 circumstances of the individual case, the standard of review for
8 dismissals based on Fed. R. Civ. P. 23.1 is abuse of discretion."
9 Scalisi v. Fund Asset Mgmt., L.P., 380 F.3d 133, 137 (2d Cir.
10 2004) (internal quotation marks omitted). Where, however, "a
11 challenge is made to the legal precepts applied by the district
12 court in making a discretionary determination, plenary review of
13 the district court's choice and interpretation of those legal
14 precepts is appropriate." Id.

15 II. Federal Procedural Requirements

16 A. Rule 12(b)(6)

17 In accordance with the Supreme Court's decision in Bell
18 Atlantic Corp. v. Twombly, 550 U.S. 544 (2007), we apply a
19 "plausibility standard" to evaluate whether dismissal pursuant to
20 Rule 12(b)(6) of the Federal Rules of Civil Procedure is
21 appropriate. Id. at 560. That standard is guided by "[t]wo
22 working principles." Ashcroft v. Iqbal, 129 S. Ct. 1937, 1949
23 (2009). First, "a court must accept as true all [factual]
24 allegations contained in a complaint" but need not accept "legal
25 conclusions." Id. For this reason, "[t]hreadbare recitals of
26 the elements of a cause of action, supported by mere conclusory

1 statements, do not suffice" to insulate a claim against
2 dismissal. Id. Second, a complaint must "state[] a plausible
3 claim for relief." Id. at 1950. "Determining whether a
4 complaint [does so] will . . . be a context-specific task that
5 requires the reviewing court to draw on its judicial experience
6 and common sense." Id.

7 B. Rule 23.1

8 In addition to meeting the generally applicable rules
9 for pleading under the Federal Rules of Civil Procedure, the
10 pleading of derivative actions must satisfy the requirements set
11 forth in Rule 23.1 of the Rules. Fed. R. Civ. P. 23.1. Rule
12 23.1 applies "when one or more shareholders or members of a
13 corporation or an unincorporated association bring a derivative
14 action to enforce a right that the corporation or association may
15 properly assert but has failed to enforce." Fed. R. Civ. P.
16 23.1(a). Complaints asserting derivative claims must "state with
17 particularity . . . any effort by the plaintiff to obtain the
18 desired action from the directors or comparable authority and, if
19 necessary, from the shareholders or members; and . . . the
20 reasons for not obtaining the action or not making the effort."
21 Fed. R. Civ. P. 23.1(b)(3).

22 Rule 23.1 is a "rule of pleading that creates a federal
23 standard as to the specificity of facts alleged with regard to
24 efforts made to urge a corporation's directors to bring the
25 action in question." RCM Secs. Fund, Inc. v. Stanton, 928 F.2d
26 1318, 1330 (2d Cir. 1991). It does not "'abridge, enlarge or

1 modify any substantive right.'" Kamen v. Kemper Fin. Servs.,
2 Inc., 500 U.S. 90, 95 (1991) (quoting 28 U.S.C. § 2072(b)). The
3 underlying demand requirement, by contrast, "in delimiting the
4 respective powers of the individual shareholder and of the
5 directors to control corporate litigation[,] clearly is a matter
6 of 'substance,' not 'procedure.'" Id. at 96-97 (citing Daily
7 Income Fund, Inc. v. Fox, 464 U.S. 523, 543-44 & n.2 (1984)
8 (Stevens, J., concurring in judgment)). It is therefore governed
9 by state law. See Shady Grove Orthopedic Assocs., P.A. v.
10 Allstate Ins. Co., 549 F.3d 137, 141-42 (2d Cir. 2008)
11 ("[F]ederal courts . . . apply state substantive law and federal
12 procedural law to any issue or claim which has its source
13 in state law." (internal quotation marks omitted)), cert. denied,
14 129 S. Ct. 2160 (2009).

15 III. Massachusetts Substantive Requirements

16 Even where an underlying cause of action is based on
17 the ICA, as Claim Two is, whether the action is properly
18 classified as derivative or direct is ordinarily determined by
19 state law. See, e.g., Strougo v. Bassini, 282 F.3d 162, 169 (2d
20 Cir. 2002) ("We must fill a gap in the ICA with rules borrowed
21 from state law unless . . . application of those rules would
22 frustrate the specific federal policy objectives underlying the
23 ICA."); id. at 176 ("The expectations of private parties that
24 state law will govern their corporate disputes is even higher
25 when the federal statute invoked does not on its face provide
26 notice to the parties of a possibility of a federal private suit

1 and thereby suggest that federal law may be applied."); see
2 also Burks v. Lasker, 441 U.S. 471, 478 (1979) ("Congress has
3 never indicated that the entire corpus of state corporation law
4 is to be replaced simply because a plaintiff's cause of action is
5 based upon a federal statute."); Lapidus v. Hecht, 232 F.3d 679,
6 682 (9th Cir. 2000) (relying on Massachusetts state law to
7 determine whether the plaintiffs' claims brought under the ICA
8 were direct or derivative).

9 A. Claim Classification

10 Under Massachusetts law, a claim based on a "duty owed
11 to the corporation, not to individual stockholders[,]" is
12 properly characterized as derivative, not direct. Bessette v.
13 Bessette, 385 Mass. 806, 809, 434 N.E.2d 206, 208 (1982); see
14 also Robertson v. Gaston Snow & Ely Bartlett, 404 Mass. 515, 525
15 n.5, 536 N.E.2d 344, 350 n.5 (1989) (observing that any claim by
16 a shareholder alleging a breach of duty to the corporation must
17 be through a derivative action). In other words, a derivative
18 claim is one where the plaintiff is not "enforc[ing] any personal
19 rights" and has "no direct or personal interest in the suit,
20 excepting as the value of [the plaintiff's] stock might be
21 enhanced." Shaw v. Harding, 306 Mass. 441, 448, 28 N.E.2d 469,
22 473 (1940).

23 Harm to a corporation may manifest itself as harm to
24 its shareholders in the form of a lower stock price. But the
25 "wrong underlying a derivative action is indirect, at least as to
26 the shareholders. It adversely affects them merely as they are

1 the owners of the corporate stock; only the corporation itself
2 suffers the direct wrong." Jackson v. Stuhlfire, 28 Mass. App.
3 Ct. 924, 925, 547 N.E.2d 1146, 1148 (1990) (emphasis in original)
4 (internal quotation marks omitted). Therefore, "[t]o bring a
5 direct action under Massachusetts law, a plaintiff must allege an
6 injury distinct from that suffered by shareholders generally or a
7 wrong involving one of his or her contractual rights as a
8 shareholder, such as the right to vote." Lapidus, 232 F.3d at
9 683.⁵

10 B. Demand Requirement for Derivative Claims

11 Courts have traditionally required "as a precondition
12 for [a derivative] suit that the shareholder demonstrate that the
13 corporation itself had refused to proceed after suitable demand."
14 Scalisi, 380 F.3d at 138 (citations and internal quotation marks
15 omitted).⁶ As the Massachusetts Supreme Judicial Court

⁵ Massachusetts law appears to comport with the approach of federal law in this regard. In determining whether a suit is derivative for purposes of the Federal Rules of Civil Procedure, "the term 'derivative action' . . . has long been understood to apply only to those actions in which the right claimed by the shareholder is one the corporation could itself have enforced in court." Daily Income Fund, Inc., 464 U.S. at 529. The Supreme Court has characterized derivative actions as "permit[ting] an individual shareholder to bring 'suit to enforce a corporate cause of action against officers, directors, and third parties.'" Kamen, 500 U.S. at 95 (quoting Ross v. Bernhard, 396 U.S. 531, 534 (1970)) (emphasis in original); accord Cohen v. Beneficial Indus. Loan Corp., 337 U.S. 541, 548 (1949) (Through a derivative action, a stockholder may "step into the corporation's shoes and . . . seek in its right the restitution he could not demand in his own.").

⁶ A derivative action has been described as an "equitable device" developed "to enable shareholders to enforce a corporate right . . . that the corporation had either failed or refused to assert on its own behalf." Scalisi, 380 F.3d at 138 (internal

1 explained, "[t]he rationale behind the demand requirement is
2 that, as a basic principle of corporate governance, the board of
3 directors or majority of shareholders should set the
4 corporation's business policy, including the decision whether to
5 pursue a lawsuit." Harhen v. Brown, 431 Mass. 838, 844, 730
6 N.E.2d 859, 865 (2000); accord RCM Secs. Fund, 928 F.2d at 1326
7 ("Whether a corporation should bring a lawsuit is a business
8 decision, and the directors are, under the laws of every state,
9 responsible for the conduct of the corporation's business,
10 including the decision to litigate. A shareholder demand that
11 the corporation bring litigation is thus a method by which the
12 appropriate corporate authority may be consulted about litigation
13 to be brought in the name of the corporation." (citations and
14 internal quotation marks omitted)).

15 Thus, so long as it is exercising its good faith
16 business judgment, a corporation is ordinarily entitled to decide
17 through its board of directors that refusing, in part or in
18 whole, the demand to take action would be in its best interests.
19 See Harhen, 431 Mass. at 846, 730 N.E.2d at 866 ("It is axiomatic
20 that the decision of a disinterested board to refuse demand
21 receives the protection of the business judgment rule.").

quotation marks and citation omitted); cf. Hirshberg v. Appel,
266 Mass. 98, 100, 164 N.E. 915, 915 (1929) ("The law is settled
that for such injury to a corporation, a stockholder has no right
to maintain an action at law. A suit for redress must be brought
by the corporation."). It is "an exception to the normal rule
that the proper party to bring a suit on behalf of a corporation
is the corporation itself, acting through its directors or a
majority of its shareholders." Daily Income Fund, 464 U.S. at
542.

1 State law generally determines whether, in an action
2 classified as derivative, a pre-suit demand is necessary, and if
3 so, whether the demand made was adequate. "Where a state claim
4 is involved, . . . the source of the demand requirement must be
5 the law of the state of incorporation." RCM Secs. Fund, 928 F.2d
6 at 1327. If a federal derivative claim is involved, however, the
7 "contours of the demand requirement . . . are governed by federal
8 law." Kamen, 500 U.S. at 97 (emphasis omitted). But "[i]t does
9 not follow . . . that the content of such a rule must be wholly
10 the product of a federal court's own devising." Id. at 98. In
11 "areas [such as corporation law] in which private parties have
12 entered legal relationships with the expectation that their
13 rights and obligations would be governed by state-law standards,"
14 we entertain a strong presumption that "state law should be
15 incorporated into federal common law." Id. We will therefore
16 incorporate state law governing pre-suit demand if that law is
17 not "inconsistent with the policies underlying" federal
18 securities law. Id. at 107.⁷

19 C. Massachusetts Business Corporation Act

⁷ As noted, "Rule 23.1 [of the Federal Rules of Civil Procedure] is a rule of pleading [regarding] the specificity of facts alleged with regard to efforts made to urge a corporation's directors to bring the action in question," but "the adequacy of those efforts is to be determined by state law absent a finding that application of state law would be inconsistent with a federal policy underlying a federal claim in the action." RCM Secs. Fund, 928 F.2d at 1330; accord Abramowitz v. Posner, 672 F.2d 1025, 1026 (2d Cir. 1982) (noting that "the authority of disinterested directors to terminate shareholder derivative litigation is governed by applicable state law, provided that such law is consistent with the policies of the federal acts upon which the action is based").

1 Several years ago, the Massachusetts Legislature
2 enacted a comprehensive statute governing Massachusetts
3 corporations. The Massachusetts Business Corporation Act (the
4 "Act"), enacted on November 26, 2003, see 2003 Mass. Acts ch.
5 127, and made effective as of July 1, 2004, see 2004 Mass. Acts
6 ch. 178, § 49, is codified as Chapter 156D of Title XXII of the
7 General Laws of Massachusetts. Subdivision D of Part 7 of the
8 Act contains various provisions governing derivative suits, see
9 Mass. Gen. Laws ch. 156D, §§ 7.40-7.47, three of which are
10 pertinent here.

11 First, the Act adopts a "universal demand requirement,"
12 Johnston v. Box, 453 Mass. 569, 578 n.15, 903 N.E.2d 1115, 1123
13 n.15 (2009), requiring that a shareholder make a written demand
14 upon the corporation and then wait a specified period of time
15 before filing any derivative action on behalf of the corporation.
16 See Mass. Gen. Laws ch. 156D, § 7.42; accord Forsythe v. Sun Life
17 Fin., Inc., 417 F. Supp. 2d 100, 110 n.13 (D. Mass. 2006).
18 Section 7.42 prohibits, without exception, the filing of any
19 derivative action absent such written demand. See Mass. Gen.
20 Laws ch. 156D, § 7.42; accord ING Principal Prot. Funds
21 Derivative Litig., 369 F. Supp. 2d 163, 170 (D. Mass. 2005).
22 Section 7.42 therefore abrogates prior common law exceptions to
23 the demand requirement. See, e.g., Pupecki v. James Madison
24 Corp., 376 Mass. 212, 218, 382 N.E.2d 1030, 1034 (1978)
25 (reflecting previous common law doctrine that demand is

1 unnecessary "if it is clear that [such a demand] would be
2 futile").

3 Second, the Act authorizes a court to stay any
4 derivative proceeding to allow a corporation to conclude its
5 inquiry into the allegations made in the demand or complaint.
6 See Mass. Gen. Laws ch. 156D, § 7.43. Section 7.43 provides that
7 "[i]f the corporation commences an inquiry into the allegations
8 made in the demand or complaint, the court may stay any
9 derivative proceeding for a period as the court considers
10 appropriate." Id.

11 Third, the Act sets forth a procedure by which a
12 corporation can seek dismissal of derivative actions that it
13 concludes would not be in its best interests to prosecute. See
14 id. § 7.44. Section 7.44 mandates dismissal of any "derivative
15 proceeding commenced after rejection of a demand" by motion of
16 the corporation if the court finds that the corporation, by
17 "majority vote of independent directors present at a meeting of
18 the board of directors," concluded "in good faith after
19 conducting a reasonable inquiry" that the derivative proceeding
20 "is not in the best interests of the corporation." Id. §
21 7.44(a), (b)(1).

22 The corporation must support such a motion with a
23 written filing "setting forth facts" that demonstrate that "a
24 majority of the board of directors was independent at the time of
25 the determination by the independent directors" and that the
26 decision was made "in good faith after . . . a reasonable

1 inquiry." Id. § 7.44(d). Upon the filing of a proper motion,
2 "[a]ll discovery proceedings shall be stayed" pending the court's
3 resolution of that motion, except that "the court, on motion and
4 after a hearing and for good cause shown, may order that
5 specified discovery be conducted." Id. Where the corporation's
6 pleadings are proper, the court must dismiss the derivative
7 action "unless the plaintiff has alleged with particularity facts
8 rebutting the corporation's filing in its complaint or an amended
9 complaint or in a written filing with the court." Id.

10 IV. Counts Two and Three

11 We first address Halebian's argument that the district
12 court erred in characterizing Counts Two and Three as derivative,
13 despite the fact that the complaint styles them as direct, and
14 dismissing both for failure to comply with Massachusetts's
15 universal demand requirement. See id. § 7.42.⁸ The court
16 concluded that the claims were derivative because they "fail[] to
17 articulate a theory by which the alleged harm to shareholders
18 which resulted from the [allegations] was separate and
19 independent from the harm allegedly resulting to the Fund
20 itself." Halebian, 631 F. Supp. 2d at 303.

21 One aspect of both Counts Two and Three is undoubtedly
22 derivative -- that the Board violated its fiduciary duties by

⁸ Halebian does not contest that, assuming the claims are in fact derivative, they fail to comply with section 7.42. Nor does he contest the district court's conclusion that "[t]he nature or character of a claim against a corporation is determined according to the law of the state of the corporation, and not dictated by the form the plaintiff chooses to plead in his or her complaint." Halebian, 631 F. Supp. 2d at 301.

1 failing to disclose "the diversion of CitiTrust assets for the
2 benefit of others." Compl. ¶¶ 60, 65. This is plainly an
3 attempt to restate a classic derivative claim -- that the
4 corporation was harmed because its assets were diverted, thereby
5 harming the corporation's shareholders. See, e.g., Demoulas v.
6 Demoulas Super Mkts., Inc., 424 Mass. 501, 517, 677 N.E.2d 159,
7 172 (1997); P'ship Equities, Inc. v. Marten, 15 Mass. App. Ct.
8 42, 50, 443 N.E.2d 134, 138 (1982). The district court did not
9 err in rejecting Counts Two and Three insofar as they contain
10 such allegations.

11 The counts, insofar as they relate to the "propriety of
12 the[] voting procedures," Compl. ¶ 65; see also id. ¶ 60, are
13 more difficult to classify. Halebian contends that the proxy
14 statement was "materially false and misleading because it
15 fail[ed] to advise beneficial holders that the use of echo voting
16 to approve an investment advisory agreement violate[ed] both the
17 ICA and Massachusetts law." Halebian Br. 36. He describes these
18 claims as "paradigmatic direct claims because they involve a
19 beneficial holder's right to cast an informed vote." Id. at 35.
20 He insists that "the harm caused by a violation of a holder's
21 right to cast an informed vote is inherently 'separate and
22 independent' from any harm caused [to] CitiTrust simply because
23 CitiTrust has no right to cast any vote, much less an informed
24 vote." Because CitiTrust issued the allegedly improper proxy
25 statement, he says, it could not be harmed by a misrepresentation
26 in that statement. Id. at 43-44.

1 Indeed, Massachusetts's highest court has long
2 recognized corporations' shareholders' "right to vote" their
3 shares. See Seibert v. Milton Bradley Co., 380 Mass. 656, 662,
4 405 N.E.2d 131, 135 (1980); Ky. Package Store, Inc v. Checani,
5 331 Mass. 125, 129, 117 N.E.2d 139, 142 (1954). By statute,
6 Massachusetts law provides, as a general default rule, that "each
7 outstanding share, regardless of class, is entitled to 1 vote on
8 each matter voted on at a shareholders' meeting, . . . each
9 fractional share is entitled to a proportional vote," and "[o]nly
10 shares are entitled to vote." Mass. Gen. Law ch. 156D,
11 § 7.21(a). Therefore, shareholders of a corporation, not the
12 corporation itself, are entitled to vote. Relatedly, shares that
13 are "owned . . . by another entity of which the corporation
14 owns . . . a majority of the voting interests" are not entitled
15 to vote. Id. § 7.21(b). In effect, voting those shares would
16 constitute voting by the corporate entity itself, which is
17 forbidden.⁹

18 Federal courts interpreting Massachusetts law have
19 observed that although injuries that are not distinct to each
20 affected shareholder generally give rise to derivative claims,
21 not all indistinct injuries do so. As the Ninth Circuit has
22 pointed out, to assert a direct claim, "it is unnecessary to
23 allege an injury distinct from that suffered by shareholders
24 generally if the alleged injury is predicated upon a violation of

⁹ A corporation is, however, entitled to "vote any shares, including its own shares, held by it, directly or indirectly, in a fiduciary capacity." Mass. Gen. Laws ch. 156D, § 7.21(c).

1 a shareholder's voting rights." Lapidus, 232 F.3d at 683. A
2 district court in the District of Massachusetts has explained:

3 [W]hat differentiates a direct from a
4 derivative suit is neither the nature of the
5 damages that result from the defendant's
6 alleged conduct, nor the identity of the
7 party who sustained the brunt of the damages,
8 but rather the source of the claim of right
9 itself. If the right flows from the breach
10 of a duty owed by the defendants to the
11 corporation, the harm to the investor flows
12 through the corporation, and a suit brought
13 by the shareholder to redress the harm is one
14 "derivative" of the right retained by the
15 corporation. If the right flows from the
16 breach of a duty owed directly to the
17 plaintiff independent of the plaintiff's
18 status as a shareholder, investor, or
19 creditor of the corporation, the suit is
20 "direct."

21 Stegall v. Ladner, 394 F. Supp. 2d 358, 364 (D. Mass. 2005)
22 (internal quotation marks omitted); accord Blasberg v. Oxbow
23 Power Corp., 934 F. Supp. 21, 26 (D. Mass. 1996); Weber v. King,
24 110 F. Supp. 2d 124, 132 (E.D.N.Y. 2000); cf. Strougo, 282 F.3d
25 at 171 ("To sue directly under Maryland law, a shareholder must
26 allege an injury distinct from an injury to the corporation, not
27 from that of other shareholders."). For these reasons, the fact
28 "[t]hat many investors might have been misled . . . or that the
29 plaintiff might only be minimally injured[] does not [alone]
30 convert the claim to a derivative one." Blasberg, 934 F. Supp.
31 at 26.

32 Based on these principles, Halebian asserts that any
33 claim of the use of improper voting procedures necessarily states
34 a direct rather than a derivative claim. Relying on Delaware
35 law, see Sarin v. Ochsner, 48 Mass. App. Ct. 421, 423, 721 N.E.2d

1 932, 934-35 (2000) (applying Delaware law to determine whether
2 claims were direct or derivative), he also insists that
3 Massachusetts shareholders have not only the right to vote, but
4 the "right to cast an informed vote." In re J.P. Morgan Chase &
5 Co. S'holder Litig., 906 A.2d 766, 772 (Del. 2006); accord In re
6 Tyson Foods, Inc., 919 A.2d 563, 601 (Del. Ch. 2007) ("Where a
7 shareholder has been denied one of the most critical rights he or
8 she possesses [as a shareholder] -- the right to a fully informed
9 vote -- the harm suffered is almost always an individual, not
10 corporate, harm.").¹⁰

11 Halebian points us to no appellate court in
12 Massachusetts that has specifically embraced Delaware law in this
13 regard, and our research has revealed none. Cf. Weitman v.
14 Tutor, 24 Mass. L. Rptr. 343 (Mass. Super. Ct. 2008) (noting that
15 "a shareholder's right to make an informed vote may, in some
16 circumstances, provide a basis for injunctive relief" (citing
17 Eisenberg v. Chicago Milwaukee Corp., 537 A.2d 1051, 1062 (Del.
18 Ch. 1987))); Sealy Mattress Co. of N.J., Inc. v. Sealy, Inc., 532
19 A.2d 1324, 1342 (Del. Ch. 1987). Even were we to conclude that
20 Massachusetts law tracks Delaware law in this regard, however, we
21 would remain unpersuaded that Counts Two and Three can stand as
22 individual claims. We do not think that Halebian has alleged an

¹⁰ Delaware courts have also recognized, as a corollary, that shareholders have the "right not to attend a meeting" and the "right not to vote on any matter," i.e., the "right to withhold [the shareholder's] vote on any particular proposal." Berlin v. Emerald Partners, 552 A.2d 482, 493 (Del. 1988) (emphasis added) (internal quotation marks omitted).

1 actionable non-disclosure claim under either Massachusetts or
2 federal law.

3 The essence of Halebian's claim is not that the
4 defendants failed to inform him and others similarly situated
5 that the voting procedures incorporated echo voting, but that
6 echo voting is unlawful. Many courts have expressed reluctance
7 to conclude that a proxy statement is misleading "when it fail[s]
8 to disclose a legal theory with which the corporation did not
9 agree and which was never called to its attention." Ash v. LFE
10 Corp., 525 F.2d 215, 220 (3d Cir. 1975); see also Bolger v. First
11 State Fin. Servs., 759 F. Supp. 182, 194 (D. N.J. 1991)

12 ("[C]ompanies have no duty to disclose legal theories as to how a
13 given transaction violated the law."); Freedman v. Barrow, 427 F.
14 Supp. 1129, 1144 (S.D.N.Y. 1976) ("Failure to disclose a legal
15 theory with which those soliciting do not agree and which was not
16 called to their attention at the proper time does not violate"
17 federal rules prohibiting untrue statements of material fact);
18 Goldberger v. Baker, 442 F. Supp. 659, 667 (S.D.N.Y. 1977)

19 (noting that "the allegation that the [proxy] statement failed to
20 disclose the 'legal significance' of the [proposed] option plan"
21 at issue was "so vague as to defy analysis"); Voegel v. Magnavox
22 Co., 439 F. Supp. 935, 941 (D. Del. 1977) ("A proxy statement,
23 based upon the opinion of properly qualified outside
24 counsel . . ., even if the opinion is wrong, cannot be deemed to
25 be a misrepresentation or concealment of a material
26 fact"); cf. Maldonado v. Flynn, 597 F.2d 789, 796, 798

1 (2d Cir. 1979) (citing Ash and Goldberger with approval, but
2 concluding that the proxy statements at issue were misleading
3 based on nondisclosure of "factual information 'impugning the
4 honesty, loyalty or competency of directors' in their dealings
5 with the corporation to which they owe a fiduciary duty" -- that
6 "senior officers [were able] to avoid the adverse personal tax
7 effect of the [transaction at issue], known to them through
8 inside information, while depriving the Corporation of a
9 corresponding tax benefit").

10 There is no indication that the alleged unlawfulness of
11 echo voting under section 15(a) of the ICA or Massachusetts law
12 was called to the attention of the Board by Halebian or anyone
13 else prior to the institution of this lawsuit. And the Board has
14 consistently and strenuously denied that echo voting violates
15 these laws.¹¹ Since the Board was apparently not of the view,
16 nor had it been told, that using a Citigroup-affiliated service
17 agent other than a broker-dealer to echo vote shares violated the
18 ICA or Massachusetts law, or indeed any law, its failure to

¹¹ In connection with the demand-review process, the corporation found "no authority for the proposition that the 1940 Act or Massachusetts law forbids the use of echo voting by a record holder of shares in a vote to approve an advisory contract with a mutual fund" and noted that "[e]cho voting is a common practice in the financial industry whose utility has been recognized both by the Securities and Exchange Commission and the New York Stock Exchange." See Res. of the Bd. of Trs. of CitiFunds Trust III 25 (July 12, 2006). Although Halebian vehemently insists that echo voting, in this context, is unlawful, we note that he has failed to cite any court decision that has so suggested or held. We do not address the merits of Halebian's claim that echo voting violates section 15 of the ICA and Massachusetts law.

1 inform shareholders to the contrary does not appear to us to have
2 been potentially false and misleading so as to be cognizable
3 under Massachusetts or federal law.¹²

4 V. Count One

5 The parties agree that Count One asserts a derivative
6 claim under Massachusetts law, and that the complaint was filed
7 in accordance with section 7.42's universal demand requirement.
8 We therefore must decide whether dismissal of the claim pursuant
9 to section 7.44 was proper. We conclude that dismissal was not
10 required because of Halebian's failure to meet federal procedural
11 requirements. We decline to resolve in the first instance, at
12 least at this time, however, whether dismissal was required under
13 Massachusetts law. Instead, we certify that question of
14 Massachusetts law, which is critical to the resolution of this
15 appeal, to the Supreme Judicial Court of Massachusetts.

16 A. Federal Procedural Law

17 The district court decided that the complaint required
18 dismissal because it did not comply with Rule 23.1 of the Federal
19 Rules of Civil Procedure. Were this conclusion correct, we would
20 have no need to address the court's alternate conclusion that

¹² We note that Halebian's contention that the proxy statement should also have disclosed that the Securities Exchange Commission and the New York Stock Exchange ("NYSE") have ruled that NYSE member broker-dealers may not echo vote shares to obtain shareholder approval of an investment company's investment advisory contract with a new investment advisor is utterly without merit, as the proxy statement explicitly contains this information. See Finn Declaration Exhibit D ("Schedule 14A"), at 8, Halebian v. Bery, No. 06 Civ. 4099 (S.D.N.Y. filed May 30, 2006) (Doc. No. 22).

1 dismissal of Count One was also required under Massachusetts law.
2 We conclude, however, that the district court erred with respect
3 to Rule 23.1.

4 Rule 23.1 is a "rule of pleading that creates a federal
5 standard as to the specificity of facts alleged with regard to
6 efforts made to urge a corporation's directors to bring the
7 action in question." RCM Secs. Fund, 928 F.2d at 1330. It "is
8 not the source of any such requirement." Daily Income Fund, 464
9 U.S. at 543 (Stevens, J., concurring in judgment). State law is
10 the source. The federal rule "merely requires that the complaint
11 in such a case allege the facts that will enable a federal court
12 to decide whether such a demand requirement has been satisfied,"
13 concerning itself "solely with the adequacy of the pleadings."
14 Id. at 543-44.

15 The district court dismissed Count One for failure to
16 state "the reasons for not obtaining the [desired] action" from
17 the Board as required by Rule 23.1. Fed. R. Civ. P.
18 23.1(b) (3) (B); see also Halebian, 631 F. Supp. 2d at 295-98.
19 Halebian's demand allegations, however, set forth all the
20 information needed to determine whether, as a matter of
21 Massachusetts law, the complaint was filed in accordance with
22 Massachusetts's universal demand rule. See Mass. Gen. Laws Ch.
23 156D, § 7.42.

24 For a derivative proceeding to have been properly filed
25 pursuant to section 7.42, Halebian had to have made "written
26 demand . . . upon the corporation to take suitable action" and

1 waited "90 days . . . from the date the demand was made" to file
2 suit. Id. Halebian's complaint alleges both. And Halebian's
3 complaint specifically alleges the reason that the corporation
4 declined to accede to his demands -- that the members of the
5 board were motivated by self-interest to reject his demand.
6 Nothing else was required to allow the court to determine
7 whether, as a matter of Massachusetts law, Halebian's complaint
8 was properly filed. Halebian's complaint satisfies the
9 heightened pleading requirements of Rule 23.1 on this score.

10 Count One therefore stands or falls on whether it was
11 properly dismissed pursuant to Massachusetts substantive law.

12 B. State Substantive Law

13 Halebian contends that the district court erred in
14 concluding that section 7.44 and its protection for a board of
15 directors' good faith decision that litigation is not in the
16 defendant corporation's best interests applied in this case.¹³
17 He initiated this action following the expiration of the post-
18 demand statutory waiting period set forth in section 7.42, but
19 before the corporation rejected his demand. And section 7.44, by
20 its terms, applies to "derivative proceeding[s] commenced after
21 rejection of a demand." Mass. Gen. Laws Ch. 156D, § 7.44(a)
22 (emphasis added). The district court nonetheless held that

¹³ He also argues in the alternative that even if section 7.44 applied the district court erred by barring him from seeking discovery and by failing to convert the corporation's motion to dismiss to a motion for summary judgment. At this stage of the proceedings, however, we need only address Halebian's first argument.

1 section 7.44 applies, concluding that the section is applicable
2 to derivative proceedings commenced before rejection of a demand
3 "as long as [the corporation's board] rejected the demand after a
4 good faith review." Halebian, 631 F. Supp. 2d at 294.

5 Relying on statutory commentaries, the district court
6 concluded that the state legislature contemplated "that section
7 7.44 could be applicable to cases . . . where a plaintiff has
8 waited the requisite ninety days after the written demand to file
9 a complaint, but the corporation did not reject the demand until
10 after the filing of the complaint" because in some situations "a
11 board would need more than ninety days to evaluate a
12 shareholder's demand before determining whether to pursue the
13 litigation." Id. at 295.¹⁴

14 The district court also explained that reading section
15 7.44 as written, and thereby preventing corporations that "had

¹⁴ The decision by a corporation to reject a demand, according to the commentary to section 7.44, "'can be made prior to the commencement of the suit in response to a demand or after commencement upon examination of the allegations of the complaint."' Halebian, 631 F. Supp. 2d at 295 (quoting Mass. Gen. Law Ann. ch. 156D, § 7.44, cmt. background (emphasis added by the district court)). A related commentary to the neighboring universal-demand-requirement provision in section 7.42 notes that although the statutory waiting provisions set forth in that section had been "'chosen as a reasonable minimum time[] within which the board of directors [or] the shareholders can meet, direct the necessary inquiry into the charges, receive the results of the inquiry, and make its or their decision,'" nonetheless "'[i]n some instances a longer period may be required,'" and that in those instances the corporation "'may request counsel for the shareholder to delay filing suit until the inquiry is completed or, if [the] suit is commenced, the corporation can apply to the court for a stay under § 7.43.'" Halebian, 631 F. Supp. 2d at 295 (quoting Mass. Gen. Law Ann. ch. 156D, § 7.42, cmt. 3).

1 not completed a good faith, reasonable inquiry into the efficacy
2 of the maintenance of the derivative proceeding after ninety
3 days" from being "able to avail themselves of Massachusetts'
4 codification of the business judgment rule," would "render[]
5 meaningless" section 7.43, the stay provision. Id. The court
6 considered this to be a "curious result" that would encourage "a
7 race to the courthouse for shareholder plaintiffs, as filing on
8 the ninety-first day after a written demand would automatically
9 foreclose corporate boards that otherwise were proceeding
10 appropriately in response to the demand from availing themselves
11 of section 7.44." Id.

12 We have doubts about the district court's reasoning in
13 this regard. Assuming arguendo that relevant statutory
14 commentary and policy arguments suggest otherwise, it is a well-
15 established principle of Massachusetts law that when "the
16 language of the statute is clear, we must enforce it according to
17 its terms." Town of Milford v. Boyd, 434 Mass. 754, 757-58, 752
18 N.E.2d 732, 735 (2001) (internal quotation marks omitted). Here,
19 the relevant provision of section 7.44 is clear enough -- it
20 applies to "derivative proceeding[s] commenced after rejection of
21 a demand." Mass. Gen. Laws Ch. 156D, § 7.44. By negative
22 implication, the section would appear not to apply to derivative
23 proceedings commenced before rejection of a demand. The district
24 court's reading in effect excised the statutory phrase:
25 "commenced after rejection of a demand."

1 We recognize, of course, that under Massachusetts law,
2 as elsewhere, context matters. "[S]tatutes . . . enacted
3 together . . . as part of a carefully-crafted statutory
4 plan . . . must be construed together so as to constitute a
5 harmonious whole consistent with the legislative purpose."
6 Commonwealth v. Renderos, 440 Mass. 422, 432-33, 799 N.E.2d 97,
7 106 (2003) (internal quotation marks omitted). But we remain
8 unconvinced that the statutory context required the district
9 court to take the path that it did.

10 To be sure, and as the district court noted, the
11 commentary to section 7.44 clearly anticipates that in some
12 instances, a corporation might require more than ninety days to
13 investigate and respond to the shareholder's demand. And, as the
14 district court explained, section 7.43 might be rendered
15 meaningless if section 7.44 were categorically inapplicable to
16 corporations that did not complete their investigations prior to
17 institution of the derivative proceeding. To this extent, the
18 terms of section 7.44 may need to bend to accommodate contrary
19 statutory provisions.

20 But here, no stay was sought or obtained. And the
21 district court's reading of section 7.44, ignoring its language
22 appearing to limit its application to suits commenced after
23 rejection of a demand by a board directors, seems to leave
24 section 7.43 with little purpose, if any. If a corporation can
25 invoke section 7.44 at any time based on a good-faith rejection
26 of the demand even after the litigation is under way and without

1 a stay in place, then there would appear to be little need for
2 the stay provision of section 7.43.

3 If, by contrast, section 7.43 operates to extend the
4 time period within which a corporation is able to invoke section
5 7.44, then the stay provision would play a critical role in the
6 statutory scheme. Construing these two sections together, it may
7 well be that 7.44 applies to timely derivative actions filed
8 before the rejection of the demand that serves as the basis for
9 the action not in all circumstances, as the district court's
10 ruling suggests, but only when such an action was actually stayed
11 in accordance with section 7.43.

12 This reading, although not without its difficulties,¹⁵
13 appears to be consistent with other statutory commentary,
14 including commentary that the district court itself identified.
15 According to the commentary to section 7.42, where a corporation
16 needs more time than the provisions of section 7.42 give it to
17 investigate, and perhaps reject, the shareholder demand, it "'may
18 request counsel for the shareholder to delay filing suit until
19 the inquiry is completed or, if [the] suit is commenced, . . .
20 apply to the court for a stay under § 7.43.'" Halebian, 631 F.
21 Supp. 2d at 295 (citing Mass. Gen. Law Ann. ch. 156D, § 7.42,
22 cmt. 3 (alteration in original)). Similarly, commentary to
23 section 7.43 notes that the "court may in its discretion stay the

¹⁵ For example, this reading leaves unresolved the issue of whether a stay must be sought or entered within a certain period of time following the filing of the original complaint in order to toll the provisions of section 7.44.

1 proceeding for such period as the court deems appropriate" where
2 "the complaint is filed 90 days after demand but the inquiry into
3 the matters raised by the demand has not been completed or where
4 a demand has not been investigated but the corporation commences
5 the inquiry after the complaint has been filed." See Mass. Gen.
6 Law Ann. ch. 156D, § 7.43, cmt. (West 2009).

7 Both passages suggest that the Massachusetts
8 Legislature anticipated that a corporation that had not completed
9 its investigation following the expiration of the period set
10 forth in section 7.42 and which was unwilling or unable to
11 convince the shareholder to refrain from filing suit would seek
12 court approval for further delays to permit further
13 investigation. And as a result of court supervision as a
14 condition of extending the time within which a demand can be
15 investigated, the legislature seems to have anticipated that the
16 court would "monitor the course of the [corporation's] inquiry to
17 ensure that it is proceeding expeditiously and in good faith."
18 Id. Reading section 7.44 as written except insofar as it is
19 modified by the operation of section 7.43 seems to us to be
20 consistent with this commentary.

21 Moreover, such a reading does not, we think, pose an
22 unfair hardship on Massachusetts corporations. Rather it would
23 appear to facilitate the Massachusetts Legislature's goal, as
24 stated in the statutory commentary, to ensure that derivative
25 actions are dismissed so long as the corporation "promptly

1 determine[s]" to reject the demand. Mass. Gen. Law Ann. ch.
2 156D, § 7.44, cmt. (West 2009).

3 VI. Certification

4 We have endeavored to identify relevant issues raised
5 with respect to the Massachusetts Business Corporation Act and to
6 proffer our best reading of section 7.44. We think it
7 appropriate, however, to reserve judgment and certify a question
8 necessary to the resolution of this appeal to the Supreme
9 Judicial Court pursuant to Massachusetts Supreme Judicial Court
10 Rule 1:03.¹⁶ We do so because the appeal presents "unsettled and
11 significant questions of state law [that] will control the
12 outcome of [the] case." Colavito v. N.Y. Organ Donor Network,
13 Inc., 438 F.3d 214, 229 (2d Cir. 2006) (internal quotation marks
14 omitted); accord Boston Gas Co. v. Century Indem. Co., 529 F.3d
15 8, 15 (1st Cir. 2008); Nieves v. Univ. of P.R., 7 F.3d 270, 274
16 (1st Cir. 1993). A proper reading of the Massachusetts Business

¹⁶ The Rule provides in part:

§ 1. Authority to Answer Certain Questions of Law. This court may answer questions of law certified to it by the Supreme Court of the United States, a Court of Appeals of the United States, or of the District of Columbia, or a United States District Court, or the highest appellate court of any other state when requested by the certifying court if there are involved in any proceeding before it questions of law of this state which may be determinative of the cause then pending in the certifying court and as to which it appears to the certifying court there is no controlling precedent in the decisions of this court.

1 Corporation Act is, it seems to us, important to the effective
2 regulation by the Commonwealth of Massachusetts of corporations,
3 and, in this case, business trusts, incorporated under its laws,
4 and to our knowledge, no appellate court has ever discussed
5 section 7.44 or section 7.43, let alone at any length or as they
6 apply to the situation presented in this appeal. The First
7 Circuit, more intimately familiar than are we with the workings
8 of the Supreme Judicial Court, has observed that the court "has
9 indicated a willingness, under such circumstances, to answer
10 certified questions." Foxworth v. St. Amand, 570 F.3d 414, 437
11 (1st Cir. 2009).

12 We therefore certify the following question to the
13 Supreme Judicial Court of Massachusetts for its consideration:

14 Under Massachusetts law, can the business
15 judgment rule, established under Mass. Gen.
16 Laws ch. 156D, § 7.44, be applied to dismiss
17 a derivative complaint filed timely under
18 section 7.42 but prior to a corporation's
19 rejection of the demand that serves as the
20 basis for the suit?

21 We certify that this question is to the best of our
22 understanding determinative of a claim in this case and that it
23 appears to us that there is no controlling precedent in either
24 the decisions or rules of practice of the Supreme Judicial Court.

25 We respectfully invite any additional guidance about
26 relevant Massachusetts law or practice that the Supreme Judicial
27 Court may wish to offer in responding to the certified question.
28 The certified question may be deemed to cover any pertinent
29 further issues of Massachusetts law that the Supreme Judicial

1 Court thinks is appropriate and advisable to address, including
2 those issues addressed in the portion of our opinion discussing
3 the propriety of the district court's dismissal of Counts Two and
4 Three. For this reason, although we have stated our conclusions
5 with respect to Counts Two and Three as though they were
6 definitive, we reserve decision on all issues on appeal pending
7 the Supreme Judicial Court's response to our certification.

8 This Court will issue a Certification Order pursuant to
9 Massachusetts Supreme Judicial Court Rule 1:03. The Clerk of
10 this Court is directed to forward to the Supreme Judicial Court
11 of Massachusetts, under the official seal of this Court, the
12 Certification Order, this opinion, and the briefs and appendices
13 filed by the parties. Pending the receipt of a response, this
14 Court and this panel shall retain appellate jurisdiction.

15 **CONCLUSION**

16 For the foregoing reasons, we reserve judgment and
17 certify the stated question to the Supreme Judicial Court of
18 Massachusetts.