IN THE UNITED STATES DISTRICT COURT

FOR THE DISTRICT OF OREGON

QUANTUM TECHNOLOGY PARTNERS II, L.P., a Delaware limited partnership,

Plaintiff,

v.

ALTMAN BROWNING AND COMPANY, an Oregon corporation; BAKER GROUP LLP; KAY E. ALTMAN, an individual; MICHAEL J. BAKER, an individual; DAVID M. BROWNING, an individual; and DOES 1 through 20,

Defendants,

and

APEX DRIVE LABORATORIES, INC., a Delaware corporation,

Nominal Defendant.

08-CV-376-BR

OPINION AND ORDER

JOHN S. STEWART
ROBERT B. COLEMAN
TYLER J. STORTI
Stewart Sokol & Gray, LLC
2300 S.W. First Avenue
Suite 200
Portland, OR 97201
(503) 221-0699

Attorneys for Plaintiff

DAVID W. AXELROD
DEVON ZASTROW NEWMAN
Schwabe Williamson & Wyatt, PC
1600-1900 Pacwest Center
1211 S.W. Fifth Avenue
Portland, OR 97204
(503) 222-9981

Attorneys for Defendants Altman Browning and Company, Kay E. Altman, and David M. Browning

GARY I. GRENLEY
PAUL H. TRINCHERO
DAVID E. DEAN
Grenley Rotenberg Evans Bragg & Bodie PC
1211 S.W. Fifth Avenue
Suite 1100
Portland, OR 97204
(503) 241-0570

Attorneys for Defendants Baker Group LLP and Michael J. Baker

BROWN, Judge.

This matter comes before the Court on the Motion (#77) to Dismiss filed by Defendants Baker Group LLP and Michael J. Baker and the Motion (#79) to Dismiss and Joinder in the Corresponding Motions Filed by the Baker Group LLP of Defendants Altman Browning and Company (ABCO), Kay E. Altman, and David M.

Browning.

For the reasons that follow, the Court **GRANTS** Defendants' Motions.

BACKGROUND

The Court takes the following facts from Plaintiff Quantum Technology Partners II, L.P.'s Third Amended Complaint and from the parties' previous filings in this matter, and, accordingly, the Court accepts as true the allegations in the Third Amended Complaint and construes those facts in favor of Quantum.

At some point before 2004, Quantum purchased shares in Primotive Corporation for $590,000. At the time Quantum purchased its shares, Primotive was named Motile Corporation.

On February 25, 2004, Primotive's Board of Directors (BOD) and a majority of its shareholders voted to sell substantially all of Primotive's assets to Apex. In exchange for Primotive's assets, Apex issued 51% of its stock to the former shareholders of Primotive. Through this transaction, Quantum became an Apex shareholder.

On February 25, 2004, Apex also entered into a Services Agreement with ABCO in which Apex agreed ABCO would develop Primotive's technology. Pursuant to the Services Agreement, Apex issued the remaining 49% of its outstanding stock to the Baker Group. "[I]n exchange for the services ABCO agreed to perform

for Apex," the Baker Group assigned 8.9% of its shares to Laughlin LLC. Laughlin is not identified or further described in the parties' filings.

Under the terms of the Services Agreement, ABCO was required to accomplish specifically enumerated "milestones" by January 1, 2006, on which date the Services Agreement terminated. If ABCO did not accomplish the milestones, the Apex shares that were transferred to the Baker Group were subject to repurchase by Apex.

Baker, Altman, and Browning signed the Services Agreement on behalf of Apex in their capacities as Apex's President and Chief Executive Officer (CEO), Chief Financial Officer (CFO), and Chief Technical Officer (CTO) respectively. Baker, Altman, and Browning also signed the Services Agreement on behalf of ABCO acting in their capacities as ABCO's President and CEO, CFO, and CTO respectively.

In September 2004, Apex billed Holjeron Company $50,000 for a prototype project completed for Holjeron. Apex then paid the $50,000 to ABCO pursuant to the Services Agreement.

ABCO did not accomplish all of the milestones set out in the Services Agreement before January 1, 2006. As a result, Quantum delivered to the Baker Group and Laughlin a written consent of the majority of "non-interested shareholders" and the funds required for Apex to repurchase its shares.

At an Apex shareholder meeting on February 16, 2006, Quantum moved to affirm Apex's repurchase of the shares of the Baker Group and Laughlin, and "[t]he motion carried based upon a count of shares owned by a majority of the disinterested stockholders." Also at that meeting, Quantum noted the Services Agreement had expired by its own terms on January 1, 2006. Baker, however, asserted the directors of Apex (*i.e.*, Baker, Altman, and Browning) previously had extended the Services Agreement at a BOD meeting in December 2005.

In December 2006 Porteon Electric Vehicles, Inc., made a "substantial investment" in Apex and became Apex's largest shareholder. On January 25, 2007, Brad Hippert, President of Porteon, was elected to Apex's BOD.

On February 15, 2007, Quantum filed a complaint in Multnomah County Circuit Court in which it brought claims for fraudulent inducement, breach of fiduciary duty, abuse of control, gross mismanagement, waste of corporate assets, and unjust enrichment against the same individuals and entities that are defendants in this action based on the same facts underlying this action. On May 23, 2007, Quantum voluntarily dismissed the state-court action without prejudice.

On June 5, 2007, Quantum submitted to Apex a Demand for Investigation by Independent Directors of Apex Corporation in which Quantum demanded an investigation as to whether ABCO met

the milestones of the Services Agreement; whether the Services Agreement deadline had been validly extended; when the notes of the December 2005 BOD meeting were created; whether the actions taken at the February 16, 2006, stockholder meeting were "valid"; whether Apex received $50,000 from Holjeron and paid those funds to ABCO; and whether Defendants committed fraud, were self-dealing, breached their fiduciary duties, abused their control of Apex, grossly mismanaged Apex, wasted the corporate assets of Apex, violated Delaware corporate law, illegally converted the assets of Apex, and/or misrepresented ABCO's experience and skill to carry out the Services Agreement.

On July 10, 2007, Porteon's CEO Ken Montler and CFO James Boehlke met with Barry Dickman, Quantum's owner and manager, to discuss the possibility of Porteon purchasing Quantum's shares of Apex. After the meeting, Dickman sent Boehlke an email in which he rejected Porteon's suggestion, noted the settlement offer in the state-court action before Quantum voluntarily dismissed that case, advised he anticipated extensive legal fees if Quantum were to renew its action against Defendants, predicted discovery in such an action to be "monumental," and stated he did not "see how Apex survives past about October" due to the costs of such an action and the fact that no one would invest in Apex under a cloud of litigation.

On September 6, 2007, the BOD formed a Special Investigative

Committee (SIC) to investigate Quantum's June 5, 2007, Demand for Investigation.

On January 15, 2008, Hippert issued a report to Apex's shareholders regarding Quantum's June 2007 Demand. Hippert advised Apex's SIC hired independent outside counsel, Peter Glade, to investigate Quantum's Demand for Investigation and stated the SIC concluded pursuant to the investigation that "Quantum's claims have a tenuous foundation based on the facts." Hippert conceded Apex's BOD "could have kept better records of its deliberations" and "may have stretched the boundaries of its authority in some of its decisions." Hippert concluded, however, even though the BOD "may have made decisions that affected its own interests, the ultimate outcome of its management of [Apex] during the time in question was fair to [Apex]." Finally, Hippert noted "the diversion of resources to pursue litigation rather than advancing the core business of Apex would surely cripple [Apex] and inhibit the progress we are making." Hippert concluded, therefore, Apex would not take further action on Quantum's Demand for Investigation.

On January 23, 2008, Dickman emailed Glade to express his dissatisfaction with the investigation and to question Glade's objectivity. Glade forwarded Dickman's email to Hippert, expressed his discomfort with responding directly to Dickman, and reiterated the "scope and design" of the investigation "were free

from outside influence." Specifically, Glade stated "Browning, Altman and Baker played no role in limiting or expanding the investigation, and neither did anyone else."

On March 25, 2008, Quantum filed a Complaint in this Court against Defendants in which it brought derivative claims for (1) breach of fiduciary duty, (2) abuse of control, (3) gross mismanagement, (4) waste of corporate assets, (5) specific performance, and (6) unjust enrichment. Quantum also brought direct claims for (a) conspiracy to violate the Racketeering Influenced and Corrupt Organizations Act (RICO), 18 U.S.C. §§ 1961, *et seq*.; (b) violation of RICO, 18 U.S.C. § 1962(a), (b), and (c); and (c) fraudulent inducement.

On May 8, 2008, Quantum filed its First Amended Complaint to include more factual allegations to support its RICO claims.

On May 9, 2008, Defendants filed Motions to Dismiss Quantum's First Amended Complaint. After initial briefing, the Court permitted the parties to file supplemental briefs by September 26, 2008, to ensure the parties had an adequate opportunity to make their record as to the issues raised in Defendants' Motions. On September 26, 2008, Plaintiff filed a supplemental brief in opposition to Defendants' Motions. Defendants declined to file supplemental materials.

On October 3, 2008, the Court issued an Opinion and Order in which it granted Defendants' Motions to Dismiss and granted

Quantum leave to amend its First Amended Complaint to cure the deficiencies as to Quantum's derivative and fraudulent-inducement claims. The Court declined to allow Quantum to amend its First Amended Complaint as to its RICO claims.

On November 1, 2008, Quantum filed a Second Amended Complaint in which it asserted derivative claims against Defendants for (1) breach of fiduciary duty, (2) abuse of control, (3) gross mismanagement, (4) waste of corporate assets, (5) specific performance, (6) unjust enrichment, and (7) a direct claim for fraudulent inducement.

On December 30, 2008, Apex filed a Motion to Dismiss the derivative claims in the Second Amended Complaint. On that same day, the remaining Defendants filed Motions to Dismiss or in the Alternative for Summary Judgment as to all of Quantum's claims.

On January 15, 2009, Quantum filed a Motion for Leave to File a Third Amended Complaint to add a claim for breach of contract. Defendants objected on the grounds that, among other things, (1) under Delaware there is not a cause of action for damages for breach of contract between shareholders for violation of a corporation's bylaws; (2) Delaware law provides other remedies to contest a board of directors or shareholder vote; and (3) even if a breach of contract cause of action exists, it is a derivative rather than a direct claim and, therefore, should be dismissed for the same reasons the Court dismissed Quantum's

other derivative claims.

On May 7, 2009, the Court heard oral argument on the parties' Motions and took them under advisement. On June 24, 2009, the Court issued an Opinion and Order in which it granted Defendants' Motions to Dismiss. The Court concluded it could not fairly decide the issues raised by Defendants as to Quantum's proposed Third Amended Complaint as it had been submitted and, therefore, granted Quantum leave to file a Third Amended Complaint limited to a putative claim for breach of contract as set out by Quantum in its Motion for Leave to File Third Amended Complaint and granted Defendants leave to move to dismiss the Third Amended Complaint.

On July 7, 2009, Quantum filed a Third Amended Complaint in which it asserted a claim for breach of contract. On July 28, 2009, Defendants filed Motions to Dismiss Quantum's Third Amended Complaint.

STANDARDS

Dismissal under Federal Rule of Civil Procedure 12(b)(6) for failure to state a claim is proper only if the pleadings fail to allege enough facts to demonstrate a plausible entitlement to relief. *Bell Atlantic v. Twombly*, 550 U.S. 544, 555 (2007).

> While a complaint attacked by a Rule 12(b)(6) motion to dismiss does not need detailed factual allegations, a plaintiff's obligation to provide the "grounds" of his "entitle[ment] to relief"

> requires more than labels and conclusions, and a formulaic recitation of the elements of a cause of action will not do. Factual allegations must be enough to raise a right to relief above the speculative level on the assumption that all the allegations in the complaint are true (even if doubtful in fact).

Id. The court accepts as true the allegations in the complaint and construes them in favor of the plaintiff. *Intri-Plex Tech., Inc. v. Crest Group, Inc.*, 499 F.3d 1048, 1050 n.2 (9th Cir. 2007). "The court need not accept as true, however, allegations that contradict facts that may be judicially noticed by the court, and may consider documents that are referred to in the complaint whose authenticity no party questions." *Shwarz v. United States*, 234 F.3d 428, 435 (9th Cir. 2000)(citations omitted).

DISCUSSION

Quantum asserts a claim for breach of contract in its Third Amended Complaint as follows:

> Defendants breached their contractual obligations to Plaintiff under Article 3.12 of the Apex Bylaws by voting in favor of and ratifying approval of a transaction in which Defendants had an interest.
>
> As a direct and proximate result of the Defendants' breaches of their contractual obligations under the Apex Bylaws, Plaintiff has sustained significant damages as alleged herein. Specifically, but for Defendants breaches of their contractual obligations to Plaintiff under the Apex Bylaws, Apex would have purchased Defendants shares in Apex back from Defendants according to

> the terms of the services agreement, and Plaintiff's percentage share in Apex would be increased.

Third Am. Compl. ¶¶ 27-28.

Defendants Baker and Altman move to dismiss Quantum's Third Amended Complaint on the grounds that (1) under Delaware law there is not a cause of action for damages for breach of contract between shareholders for violation of a corporation's bylaws; (2) Delaware law provides other remedies to contest a board of directors or shareholder vote; and (3) even if a breach of contract cause of action exists, it is a derivative rather than a direct claim, and, therefore, should be dismissed for the same reasons the Court dismissed Quantum's other derivative claims.

I. Quantum has not established a cause of action exists under Delaware law for damages for breach of contract between shareholders based on violation of a company's bylaws.

As noted, Defendants contend Delaware law does not recognize a cause of action for damages between shareholders for breach of a corporation's bylaws.

Quantum, however, relies on *Centaur Partners, IV v. National Intergroup, Inc.*, 582 A.2d 923 (Del. 1990), to support its contention that Delaware law allows such a claim. Specifically, Quantum points out that the court in *Centaur Partners* stated "[c]orporate . . . by-laws are contracts among the shareholders of a corporation and the general rules of contract interpretation apply." *Id*. at 929. *Centaur Partners*, however, was not an

action for breach of contract but instead centered on the plaintiff's request for a declaratory judgment as to the percentage of shares required to amend the corporation's bylaws. The Court notes the Delaware court made this statement in the context of applying "general rules of contract interpretation" to resolve the dispute. *Id*. at 928. In addition, the cases the Delaware court cited to support the statement all arise in a similar posture: *i.e.*, all are cases in which the courts resolved requests for declaratory judgment and concluded rules of contract interpretation applied to interpret the provisions of corporate bylaws. *See Berlin v. Emerald Partners*, 552 A.2d 482, 488 (Del. 1988), and *Hibbert v. Hollywood Park, Inc.*, 457 A.2d 339, 342-43 (Del. 1983). The Delaware courts' interpretation of bylaws using the principles of contract construction, however, does not establish that the Delaware courts intended to recognize a cause of action for damages for breach of contract between shareholders for violations of corporate bylaws. Accordingly, the Court concludes neither *Centaur* nor the cases on which that court relied establish a shareholder may bring a breach-of-contract action under Delaware law for damages against other shareholders for violations of corporate bylaws.

Quantum also relies on *Kidsco, Inc. v. Dinsmore*, 674 A.2d 483 (Del. 1995). In that case, however, the plaintiffs sought preliminary injunction and "adjudication of the invalidity of [a]

by-law amendment as a matter of law." *Id*. at 490. Although the court noted the plaintiffs challenged the amendment of the bylaws "as a violation of their contract rights and as a breach of fiduciary duty," the court did not analyze the plaintiffs' claims as those for breach of contract nor did it address whether a breach-of-contract claim is permitted under Delaware law. Finally, in *Kidsco*, the plaintiffs did not seek damages, but rather equitable relief in the form of "an undoing" of the amendment.

Finally, Quantum relies on two cases from states other than Delaware to support its position. *See Procopio v. Fisher*, 83 A.D.2d 757 (N.Y.A.D. 1981) and *Leeds v. Harrison*, 72 A.2d 371 (N.J. Super. 1950). These cases, however, do not specifically recognize a cause of action for breach of contract between shareholders as for violation of a corporation's bylaws, and they were resolved under the laws of New York and New Jersey. Accordingly, they do not support Quantum's position.

In summary, the cases on which Quantum relies do not establish a shareholder may bring under Delaware law an action for damages for breach of contract against another shareholder for violations of a corporation's bylaws. In the absence of Delaware authority to establish this premise, this Court concludes Quantum has not established that Delaware recognizes a cause of action for damages for breach of contract between

shareholders for violations of a corporation's bylaws. Accordingly, the Court grants Defendants' Motions to Dismiss Quantum's Third Amended Complaint.

Because the Court concludes Quantum has not established that Delaware law recognizes a cause of action for damages for breach of contract between shareholders as to violation of a corporation's bylaws, the Court does not address Defendants' other contentions.

CONCLUSION

For these reasons, the Court **GRANTS** the Motion (#77) to Dismiss filed by Defendants Baker Group LLP and Michael J. Baker and the Motion (#79) to Dismiss and Joinder in the Corresponding Motions Filed by the Baker Group LLP of Defendants Altman Browning and Company, Kay E. Altman, and David M. Browning.

The Court **DIRECTS** Defendants to submit an appropriate judgment dismissing this matter with prejudice.

IT IS SO ORDERED.

DATED this 7th day of December, 2009.

/s/ Anna J. Brown

ANNA J. BROWN
United States District Judge

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DAVID W. AXELROD
DEVON ZASTROW NEWMAN
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BACKGROUND

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On May 8, 2008, Quantum filed its First Amended Complaint to include more factual allegations to support its RICO claims.

On May 9, 2008, Defendants filed Motions to Dismiss Quantum's First Amended Complaint. After initial briefing, the Court permitted the parties to file supplemental briefs by September 26, 2008, to ensure the parties had an adequate opportunity to make their record as to the issues raised in Defendants' Motions. On September 26, 2008, Plaintiff filed a supplemental brief in opposition to Defendants' Motions. Defendants declined to file supplemental materials.

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STANDARDS

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> While a complaint attacked by a Rule 12(b)(6) motion to dismiss does not need detailed factual allegations, a plaintiff's obligation to provide the "grounds" of his "entitle[ment] to relief"

> requires more than labels and conclusions, and a formulaic recitation of the elements of a cause of action will not do. Factual allegations must be enough to raise a right to relief above the speculative level on the assumption that all the allegations in the complaint are true (even if doubtful in fact).

Id. The court accepts as true the allegations in the complaint and construes them in favor of the plaintiff. *Intri-Plex Tech., Inc. v. Crest Group, Inc.*, 499 F.3d 1048, 1050 n.2 (9th Cir. 2007). "The court need not accept as true, however, allegations that contradict facts that may be judicially noticed by the court, and may consider documents that are referred to in the complaint whose authenticity no party questions." *Shwarz v. United States*, 234 F.3d 428, 435 (9th Cir. 2000)(citations omitted).

DISCUSSION

Quantum asserts a claim for breach of contract in its Third Amended Complaint as follows:

> Defendants breached their contractual obligations to Plaintiff under Article 3.12 of the Apex Bylaws by voting in favor of and ratifying approval of a transaction in which Defendants had an interest.
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> As a direct and proximate result of the Defendants' breaches of their contractual obligations under the Apex Bylaws, Plaintiff has sustained significant damages as alleged herein. Specifically, but for Defendants breaches of their contractual obligations to Plaintiff under the Apex Bylaws, Apex would have purchased Defendants shares in Apex back from Defendants according to

> the terms of the services agreement, and Plaintiff's percentage share in Apex would be increased.

Third Am. Compl. ¶¶ 27-28.

Defendants Baker and Altman move to dismiss Quantum's Third Amended Complaint on the grounds that (1) under Delaware law there is not a cause of action for damages for breach of contract between shareholders for violation of a corporation's bylaws; (2) Delaware law provides other remedies to contest a board of directors or shareholder vote; and (3) even if a breach of contract cause of action exists, it is a derivative rather than a direct claim, and, therefore, should be dismissed for the same reasons the Court dismissed Quantum's other derivative claims.

I. Quantum has not established a cause of action exists under Delaware law for damages for breach of contract between shareholders based on violation of a company's bylaws.

As noted, Defendants contend Delaware law does not recognize a cause of action for damages between shareholders for breach of a corporation's bylaws.

Quantum, however, relies on *Centaur Partners, IV v. National Intergroup, Inc.*, 582 A.2d 923 (Del. 1990), to support its contention that Delaware law allows such a claim. Specifically, Quantum points out that the court in *Centaur Partners* stated "[c]orporate . . . by-laws are contracts among the shareholders of a corporation and the general rules of contract interpretation apply." *Id*. at 929. *Centaur Partners*, however, was not an

action for breach of contract but instead centered on the plaintiff's request for a declaratory judgment as to the percentage of shares required to amend the corporation's bylaws. The Court notes the Delaware court made this statement in the context of applying "general rules of contract interpretation" to resolve the dispute. *Id*. at 928. In addition, the cases the Delaware court cited to support the statement all arise in a similar posture: *i.e.*, all are cases in which the courts resolved requests for declaratory judgment and concluded rules of contract interpretation applied to interpret the provisions of corporate bylaws. *See Berlin v. Emerald Partners*, 552 A.2d 482, 488 (Del. 1988), and *Hibbert v. Hollywood Park, Inc.*, 457 A.2d 339, 342-43 (Del. 1983). The Delaware courts' interpretation of bylaws using the principles of contract construction, however, does not establish that the Delaware courts intended to recognize a cause of action for damages for breach of contract between shareholders for violations of corporate bylaws. Accordingly, the Court concludes neither *Centaur* nor the cases on which that court relied establish a shareholder may bring a breach-of-contract action under Delaware law for damages against other shareholders for violations of corporate bylaws.

Quantum also relies on *Kidsco, Inc. v. Dinsmore*, 674 A.2d 483 (Del. 1995). In that case, however, the plaintiffs sought preliminary injunction and "adjudication of the invalidity of [a]

by-law amendment as a matter of law." *Id*. at 490. Although the court noted the plaintiffs challenged the amendment of the bylaws "as a violation of their contract rights and as a breach of fiduciary duty," the court did not analyze the plaintiffs' claims as those for breach of contract nor did it address whether a breach-of-contract claim is permitted under Delaware law. Finally, in *Kidsco*, the plaintiffs did not seek damages, but rather equitable relief in the form of "an undoing" of the amendment.

Finally, Quantum relies on two cases from states other than Delaware to support its position. *See Procopio v. Fisher*, 83 A.D.2d 757 (N.Y.A.D. 1981) and *Leeds v. Harrison*, 72 A.2d 371 (N.J. Super. 1950). These cases, however, do not specifically recognize a cause of action for breach of contract between shareholders as for violation of a corporation's bylaws, and they were resolved under the laws of New York and New Jersey. Accordingly, they do not support Quantum's position.

In summary, the cases on which Quantum relies do not establish a shareholder may bring under Delaware law an action for damages for breach of contract against another shareholder for violations of a corporation's bylaws. In the absence of Delaware authority to establish this premise, this Court concludes Quantum has not established that Delaware recognizes a cause of action for damages for breach of contract between

shareholders for violations of a corporation's bylaws. Accordingly, the Court grants Defendants' Motions to Dismiss Quantum's Third Amended Complaint.

Because the Court concludes Quantum has not established that Delaware law recognizes a cause of action for damages for breach of contract between shareholders as to violation of a corporation's bylaws, the Court does not address Defendants' other contentions.

CONCLUSION

For these reasons, the Court **GRANTS** the Motion (#77) to Dismiss filed by Defendants Baker Group LLP and Michael J. Baker and the Motion (#79) to Dismiss and Joinder in the Corresponding Motions Filed by the Baker Group LLP of Defendants Altman Browning and Company, Kay E. Altman, and David M. Browning.

The Court **DIRECTS** Defendants to submit an appropriate judgment dismissing this matter with prejudice.

IT IS SO ORDERED.

DATED this 7th day of December, 2009.

/s/ Anna J. Brown

ANNA J. BROWN
United States District Judge