

Schettino et al. v. Modanlo

In *Schettino, et al. v. Modanlo, et al.*, 2005 WL 914376 (Md. Cir. Ct.), the Circuit Court for Montgomery County considered Third Party Plaintiff Modanlo's Motion to Reconsider Ruling on Post-Trial Motions. While many issues were raised in action, the Court focused on the principal question of whether Third Party Defendant/Counter Plaintiff Ahan, a stockholder of Final Analysis, Inc. ("FAI"), had standing to maintain an action individually against Modanlo for an injury suffered by the corporation.

The claims which led to Ahan's successful judgment at trial arose out of the interest both Ahan and Modanlo held in two corporations, Final Analysis, Inc. ("FAI") and Final Analysis Communications Systems ("FACS"). Each man owned fifty percent of all outstanding shares of FAI, which in turn owned a controlling interest in FACS and all of its voting stock. Because neither Ahan nor Modanlo owned a majority of stock in FAI, neither had absolute control over FAI, and, in turn, over FACS. Absent agreement between Ahan and Modanlo, the two companies could not take any action. Eventually, as it became more difficult for the men to agree on decisions to be made by the companies, Ahan and Modanlo realized that the existence of the companies was in jeopardy.

To circumvent this pending danger to the companies, Ahan and Modanlo entered into a Memorandum of Agreement (the "Memo"), and later a Shareholder's Agreement, whereby they attempted to restructure FAI and FACS in a manner so as to break the impasse between the men while also preserving their respective investments in both companies. Alleging breach of the Shareholder's Agreement by Modanlo, Ahan claimed that as a result of Modanlo's actions, his shares in FAI and his interest in FACS became worthless. Thus, he sued to recover lost profits as damages for the breach of contract or, in the alternative, a breach of independent fiduciary duty.

In deciding on the Motion to Reconsider, the Court focused on whether Ahan had standing to bring any claim against Modanlo for an injury to FAI/FACS. Both Modanlo and Ahan cited *Waller v. Waller*, 187 Md. 18 (1946), the pivotal Maryland case on the issue. Modanlo read that case as holding that where a stockholder suffered no injury distinct from that suffered by the corporation, he could not recover against a director for an injury to the corporation. On the other hand, Ahan interpreted the case as standing for the proposition that where a duty to a stockholder existed independent of the duty that a director owed to the corporation, the stockholder could bring an action against the director for the breach of that duty even though the company suffered the same or similar injury as the shareholder. The Court indicated that support for both Ahan's and Modanlo's positions could be found in that opinion.

The trial court in *Waller* dismissed a claim brought by an officer/shareholder of the M. Waller Corporation against the secretary and sales manager of the company based on the general rule that only a corporation can bring an action at law for an injury done to it, even though the injury indirectly or incidentally results in diminishing or destroying the value of stock. The Court of Appeals affirmed that decision, stating that the rule is

advantageous because (i) it avoids the possibility of multiple lawsuits by affected stockholders, and (ii) any damages recovered would first be available to pay any debts of the corporation and only thereafter be distributed to shareholders in proportion to their shares. However, in reaching its decision, the Court of Appeals in *Waller* stated that the general rule did not bar a stockholder from bringing suit against an officer or director of a corporation for a violation of duties owing to the corporation if the acts also violated a contract or duty owing directly from the officer to the injured shareholder. The dismissal of the *Waller* case by the Court was upheld by the Court of Appeals because no such duty owing directly to the Plaintiff was found.

In order to determine whether an analysis of the nature of the injury to a stockholder or the nature of the duty owed to a stockholder controlled the decision on whether Ahan could maintain his individual action, the Court reviewed some of the cases cited in *Waller*. In *General Rubber Co. v. Benedict*, 215 N.Y. 18 (1915), where General Rubber Co. filed suit against the Defendant alleging that he knew about a misappropriation of a subsidiary company's funds and acquiesced in it, the Court of Appeals of New York held that an action by General Rubber Co., as a shareholder in the subsidiary, would lie. Although the Court of Appeals of New York observed that generally a shareholder can not maintain an action against a third party for an injury done to a corporation, it held that the principle would not apply where the wrongful acts are not only wrongs against the corporation but also are violations of a duty arising from contract or otherwise, and owing directly by the wrongdoer to the stockholders.

Other cases cited in *Waller*, *Blakeslee v. Sottile*, 194 N.Y.S. 752 (1922), and *Ritchie v. McMullen*, 79 F. 522 (1897), further led the Court in *Modanlo* to conclude that in order to determine if Ahan had standing to bring the action in this case, *Waller* dictated that the focus of the analysis be placed on the duty owed to the stockholder and not the injury suffered by the stockholder. *Modanlo*, in an attempt to keep alive his assertion that Ahan should not have been allowed to bring an action individually against him in this case, subsequently offered several additional cases for the Court's consideration, citing *Danielewicz v. Arnold*, 137 Md. App. 601 (2001) and a previous action involving Ahan, *Ahan and Protolxe LLC v. George Grammas and Gardner, Carten & Douglass*, 2004 WL 2724111 (Md. Cir. Ct.). However, the Court held that the Plaintiffs in those cases clearly lacked standing to bring individual actions because they had failed to show duties owed by directors or officers of the respective companies directly to them. Ultimately, the Court denied the Motion to Reconsider, holding that Ahan had established that a contractual relationship existed between himself and *Modanlo* and noting that it had previously ruled that *Modanlo* owed Ahan an independent fiduciary duty. Thus, Ahan's individual action against *Modanlo* was proper and the jury verdict was allowed to stand.