

*Shaker, et al. v. Foxby Corp., et al.*

In *Shaker, et al. v. Foxby Corp., et al.*, 2005 WL 914385 (Md. Cir. Ct.), the Court considered the Defendants' motion to dismiss a claim alleging breaches of fiduciary duties against them and seeking declaratory and injunctive relief. In their complaint, the Plaintiffs challenged the election of three of the Defendants (the "Management Nominees") to the Board of Directors of Foxby Corp. ("Foxby") at the company's 2004 annual meeting, as well as certain bylaw provisions governing board election procedures.

At the Foxby 2004 annual meeting, three directors, labeled as Class I, II and V directors, were to be elected. It was undisputed that the Plaintiffs knew as of March 2004 that the Class II director would be elected at the meeting, or that they were on notice as of July 23, 2004, when Foxby filed a proxy statement with the Securities and Exchange Commission ("SEC") for the annual meeting, that the Class I and V directors would also be elected. The Plaintiffs also did not dispute the facial validity of the notice requirements of the bylaws. Rather, they disputed the validity if those provisions had been passed to interfere with shareholder voting rights. Thus, in deciding whether to grant or deny the defendants' motion, the Court first addressed the notice provisions in the bylaws of Foxby.

The Court, citing Md. Code Ann., Corps. & Ass'ns §2-504(f) (Repl. Vol. 1999 & Supp. 2005), first noted that bylaws may specify an advance notice requirement for director nominations. In this case, the Foxby's bylaws required that shareholders give notice of annual meeting business to the secretary within 90 days of mailing of the annual meeting notice. Further, the bylaws required notice of nominees for newly created director positions announced less than 120 days before the annual meeting be given within ten days of the public announcement. In each case, Plaintiff Shaker failed to comply with the notice requirements and the Defendants argued that the results of the 2004 annual meeting election should stand.

Although the Plaintiffs did not meet the notice requirements of the Foxby bylaws, the Court nevertheless analyzed their argument that the facially inoffensive notice provisions were enforced in a discriminatory manner. The Court found most compelling the Plaintiffs' argument that the Foxby bylaw notice provisions had a discriminatory impact on stockholders as applied to "control of the board" situations. While Plaintiff Shaker did have reason to know that the Class II director was open months prior to the notice deadline, the Court reasoned that he was not likely to engage in a costly proxy fight with Foxby management over one board position. It was not until the other two directorial positions were opened that a fight for board control would have become worthwhile. At that point, the Court conceded, Shaker and other stockholders only had ten days to give the board notice of a slate of candidates.

The Court looked to Delaware cases for analogous situations from which to form its opinion. In *Schnell v. Chris-Craft Indus., Inc.*, 285 A. 2d 437, 439 (De. 1971), where management had attempted to advance the date of an annual meeting to ward off a proxy contest with stockholders, the Supreme Court of Delaware nullified that action and held

that management was attempting to “utilize the corporate machinery and the Delaware law for the purpose of perpetuating itself in office” and “obstructing legitimate efforts of dissident stockholders in the exercise of their rights to undertake a proxy contest against management.” In *R.D. Hubbard v. Hollywood Park Realty Enterprises, Inc.*, 1991 WL 3151 (Del. Ch.), the Delaware Court held, in part, that occasions did arise where board inaction may operate inequitably, regardless of purpose or design. If that occurred, the Delaware Court was of the opinion that there existed equity power to grant relief to an aggrieved party in an appropriate case. The Court in this case came to the conclusion that Maryland law provided the same protections to shareholder voting rights as obtained in Delaware, in similar factual scenarios such as the case at bar. Under this backdrop, the Court held that Plaintiff Shaker had taken appropriate steps to notify the board and the SEC of his challenge to the Management Nominees. And, noting that Foxby’s Board of Directors responded to Shaker’s notice with a proxy contest that would have failed but for the invocation of the notice provisions, the Court held that application of those bylaw provisions by the Board of Directors brought the action within its equitable powers to determine if the Defendants had breached their fiduciary duties to shareholders by enforcing unreasonable or discriminatory bylaw provisions.

Following an analysis of the Foxby bylaw notice provisions, the Court turned to the remaining bylaw provisions alleged by the Plaintiffs to be for the sole purposes of destroying shareholder voting rights and preventing meaningful challenges to control of the Foxby board. The challenged bylaw provisions were characterized by the Court as “qualification and/or supermajority bylaws,” as well as one limiting judicial review of board election results. As neither party disputed the right of stockholders to elect directors at annual meetings under Maryland law (See Md. Code Ann. Corps. & Ass’ns §2-404(b) (Repl. Vol. 1999 & Supp. 2005)), the Court focused instead on what duties a corporation had to ensure fair voting procedures, and by whom and how those procedures could be challenged. The Court again turned to Delaware cases for support. Based on a review of *Blasius Indus. Inc. v. Atlas Corp.*, 564 A.2d 651 (Del. Ch. 1988), and *Arahamian v. HBO & Company*, 531 A. 2d 1204 (Del. Ch. 1987), in which it was stated that the corporate election process must be conducted with scrupulous fairness and that those in charge of the election machinery must be held to the highest standards of providing for and conducting corporate elections, the Court held that Maryland courts would give shareholder voting rights the same or similar status as is recognized by those Delaware cases.

The Defendants, while acknowledging that a stockholder could sue to enforce his rights, finally argued (i) that Plaintiff Shaker should have had to bring this action derivatively in the name of Foxby; and (ii) that directors of Maryland corporations did not owe fiduciaries to stockholders, but only to the corporation. However, the Court dismissed those arguments as unpersuasive, and held that the only cognizable injury was to Plaintiff Shaker’s right to participate in the corporate election, which clearly suggested that he was entitled to pursue this cause of action directly. Ultimately, the Court denied the Defendants’ motion to dismiss in its entirety, holding that the determination of whether the Foxby directors had in fact enacted fair bylaws was one better resolved following discovery.