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ELECTRONICALLY FILED
Superior Court of California,
County of San Diego

03/24/2016 at 04:53:00 PM

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8 SUPERIOR COURT OF THE STATE OF CALIFORNIA

9 COUNTY OF SAN DIEGO - CENTRAL DIVISION

10 ANTHONY JOHNSON, and ROBIN SASSI,
derivatively on behalf of STORIX, INC., a
11 California corporation,

12 Plaintiffs,

13 v.

14 DAVID HUFFMAN, an individual, RICHARD
TURNER, an individual, MANUEL
15 ALTAMIRANO, an individual, DAVID KINNEY,
an individual, DAVID SMILJKOVICH, an
16 individual and DOES 1-20,

17 Defendants.

Case No. 37-2015-00034545-CU-BT-CTL

REPLY MEMORANDUM OF POINTS
AND AUTHORITIES IN SUPPORT OF
NOMINAL DEFENDANT STORIX,
INC.'S DEMURRER TO COMPLAINT

IMAGED FILE

Date: April 1, 2016
Time: 9:00 a.m.
Dept: C-73
Judge: Hon. Joel R. Wohlfeil

Complaint Filed: October 13, 2015
Trial Date: Not Yet Set.

19 **I. PRELIMINARY STATEMENT**

20 Storix Inc.'s demurrer to the complaint is based on two grounds: (1) the failure of Plaintiffs
21 Anthony Johnson ("Johnson") and Robin Sassi ("Sassi"; together with Johnson, "Plaintiffs") to
22 allege facts establishing that a demand was made or that demand futility exists, and (2) Johnson
23 and Sassi's inadequacy as derivative plaintiffs in light of their track record of hostility toward and
24 harmful acts against Storix. The opposition fails to overcome either of those bases for demurrer.

25 First, facts establishing demand futility must first be *pleaded* before a plaintiff may proceed
26 with a derivative action. Confronted with their clear failure to allege facts showing demand
27 futility, Plaintiffs have submitted information that is clearly beyond the four corners of their
28 complaint. When such extrinsic (and in many instances inadmissible and/or inappropriate)

1 evidence is properly ignored, it is clear that Plaintiffs have not satisfied their obligation to allege
2 facts establishing demand futility and the demurrer should be sustained on that basis.

3 In contrast to the issue of demand futility, the court may look beyond the four corners of the
4 complaint when ruling on the separate issue of Plaintiffs' inadequacy as derivative plaintiffs. On
5 that separate issue, the Plaintiffs' opposition does not squarely address the overt hostility Plaintiffs
6 have shown to the corporation whose rights they pretend to enforce. Instead, the Plaintiffs actually
7 underscore their individual anger and hostility toward company management, and the individual
8 nature of their claims for which a derivative form of suit is simply not appropriate.

9 Finally, if there was any doubt as to Plaintiffs' inadequacy as derivative plaintiffs, the
10 opposition makes it clear that they are not suited to protect, much less enforce, the interests of the
11 company. While pretending to look out for the interests of Storix, Inc., Plaintiffs have submitted
12 sensitive and confidential information as exhibits to their opposition without making any effort to
13 seal or redact such information. Indeed, the exhibits submitted by Plaintiffs include documents
14 containing Storix's sensitive financial and technical information, social security numbers of Storix
15 employees and documents marked "Confidential" which were produced by Storix subject to a
16 Protective Order in the Copyright Action pending in the District Court.

17 For these reasons, Plaintiffs' opposition does not overcome the demurrer, but actually
18 underscores the reasons that Plaintiffs should not be allowed to proceed with this action.

19 **II. DISCUSSION**

20 **A. Plaintiffs Fail to Adequately Allege Demand Futility with Particularity, and**
21 **Cannot Rely on Extrinsic Evidence to Do So**

22 Whether a derivative plaintiff adequately pleads demand futility must be determined by
23 reviewing the four corners of the complaint. Rather than rely on the four corners of the complaint,
24 Plaintiffs improperly seek to rely on extrinsic evidence and allegations to try to salvage their
25 demand futility claim. It is an express requirements that demand futility must be pleaded with
26 particularity. Cal. Corp. Code § 800(b)(2). Plaintiffs' rambling narrative of extrinsic facts is not
27 based on the content of the complaint. Accordingly, while the court may consider extrinsic
28 evidence in assessing a plaintiff's ability to adequately serve as a derivative plaintiff on the

1 company's behalf (discussed in § II.C, *infra*), it may not do so when assessing allegations of
2 demand futility. Plaintiffs simply cannot rely on any of those improper citations to extrinsic
3 evidence to try to explain their demand futility theory, even if any of such facts may be judicially
4 noticeable (which is disputed).¹

5 In truth, Plaintiffs point to only four paragraphs in the Complaint as containing allegations
6 relevant to demand futility:

- 7 • Paragraph 4 – regarding Huffman's role as chairman, CEO and president of Storix;
- 8 • Paragraph 28 – regarding the company's decision to conduct board meetings
9 telephonically, and to limit the time for board members to discuss a given topic to 3
10 minutes;
- 11 • Paragraph 30 – regarding the company's supposed refusal to supply "detailed financial
12 information" to Plaintiffs upon request;

13 Those three paragraphs have no bearing on demand futility, or at least Plaintiffs have not connected
14 the dots to explain how such facts establish demand futility. The fourth paragraph cited by
15 Plaintiffs in support of their demand futility argument, paragraph 37, is the only one to even
16 addresses the topic, but is the same general language Storix noted in its demurrer as lacking
17 particularity. (*See* Storix's Memorandum, p. 9). That paragraph generally alleges demand futility
18 without the requisite details, and by itself cannot save Plaintiffs' complaint.

19 Plaintiffs' claim that the company has exhibited "deaf ears," ostensibly making the required
20 demand futile, is based entirely on a single generalized accusation that the board is comprised of a
21 majority of individual defendants who are somehow predisposed to reject Plaintiffs' claims. That
22 broad theory cannot survive a demurrer, because it does not provide the requisite level of details to
23 rely on the demand futility exception. *See, e.g., Bader v. Anderson*, 179 Cal.App.4th 775, 790
24 (2009)("However, given the requirement under section 800(b)(2) that allegations be made 'with
25 particularity,' it is clear that general averments that the directors were involved in a conspiracy or
26 aided and abetted the wrongful acts complained of will not suffice to show demand futility."
27 (Underline added)).

28 ¹ In fact, Storix is separately asserting objections to the exhibits and declarations filed by Plaintiffs.

1 While Plaintiffs have packed their opposition with vitriol and seek to introduce new,
2 unsubstantiated allegations and accusations against Storix and its attorneys², they have not
3 presented a basis to overrule the demurrer. Plaintiffs failed to adequately plead demand futility
4 with the requisite clarity required, and therefore the demurrer should be sustained as to the entire
5 complaint.

6 **B. Plaintiffs Cannot Establish Demand Futility as Their Opposition Confirms**
7 **They are Merely Challenging Business Judgments, and Have Pled No Facts to**
8 **Overcome the Presumption**

9 Plaintiffs now reveal that the entire purpose supposedly underlying this derivative claim is
10 to challenge business decisions with which they apparently disagree. Those claims refute their
11 ability to rely on demand futility. In their opposition, Plaintiffs state that:

12 **“Plaintiffs sue only to compel the entity to do what is in its best interest:**
13 **update and maintain its sole product** to meet current security threats,
14 **rather than funnel money into unwarranted and wasteful officer salaries.**
15 **Plaintiffs thus have as their only objective to keep the product viable**
16 **and valuable,** and protect the interests of the entity and its shareholders.”
17 Opposition, p. 10 (Emphasis added).

18 As noted in the demurrer, a Plaintiff must establish a reasonable doubt that the challenged
19 transaction is otherwise the product of a valid exercise of business judgment. *See* Demurrer, p. 8-9.
20 The test for demand futility is whether the facts show a reasonable doubt that (1) the directors are
21 disinterested and independent, and (2) the challenged transaction was otherwise the product of a
22 valid exercise of business judgment. *See Oakland Raiders v. National Football League*, 93
23 Cal.App.4th 572, 587 (2001); *Bader v. Anderson*, 179 Cal.App.4th 775, 790 (2009). Not only have
24 Plaintiffs failed to allege particularized facts why each director could not act independently, but
25 they do not allege facts raising a reasonable doubt that such activities were not part of the valid
26 exercise of business judgments.

27 ² This demurrer is not the appropriate vehicle for challenging the many irrelevant, inaccurate, unsubstantiated, and
28 frankly false, accusations and mischaracterizations of fact leveled by Plaintiffs in their opposition. Consequently,
Storix disputes such “facts” but, in the interest of brevity and relevance, is not providing a refutation of such statements
on a line-by-line basis, as for present purposes of the demurrer it is sufficient to show that the complaint lacks the
requisite details. However, Storix does not intend to and does not waive its right or ability to challenge such facts and
accusations at an appropriate time, and reserves all rights to do so.

1 The business judgment rule is a judicial policy of deference to the business judgment of
2 corporate directors in the exercise of their broad discretion in making corporate decisions. *Lee v.*
3 *Interinsurance Exchange*, 50 Cal.App.4th 694, 711 (1996). The rule is based on the premise that
4 the business managers, rather than the courts, are best suited to judge whether a particular act or
5 transaction is helpful to the conduct of the business or expedient for the attainment of its purposes.
6 *Id.* The rule establishes a *presumption* that directors' decisions are based on sound business
7 judgment, and it prohibits courts interference in business decisions made by the directors in good
8 faith and in the absence of a conflict of interest. *Id.* In most cases, the presumption created by the
9 business judgment rule can be rebutted only by affirmative allegations of facts which, if proven,
10 would establish fraud, bad faith, overreaching or an unreasonable failure to investigate material
11 facts. *Id.* at 715. Interference with the discretion of directors is not warranted in doubtful cases. *Id.*

12 Product design, management and support are quintessential business judgments of company
13 management. That is all Plaintiffs complain about here—that Storix management rejected Plaintiff
14 Johnson's proposed software version in favor of an alternative design plan. There were many
15 reasons for doing so, all related to sound business judgments. Regardless, Plaintiffs fail to
16 establish bad faith, fraud or unreasonableness in rejecting Johnson's proposed software design
17 option. Accordingly, the supposed "only objective" underlying Plaintiffs' lawsuit is not one that
18 can support a demand futility allegation, as it was presumptively the product of the exercise of
19 sound business judgment, and Plaintiffs have not established otherwise.

20 None of the other complaints regarding Storix's operations amount to a legitimate basis for
21 a derivative complaint. For instance, they allege they disagree with the Company's decision to
22 conduct board meetings telephonically. Complaint at ¶ 28. They complain about the
23 implementation of time limits on discussion topics during meetings. *Id.* Plaintiffs complain about
24 other amendments to the By-Laws regarding procedural matters. *Id.* at ¶ 29. Plaintiffs are truly
25 asserting complaints regarding their individual disagreements with Company decisions and
26 directions. However, such do not justify a derivative complaint. They fail to present any reason to
27 disregard the business judgment rule, or why the demand futility exception should apply.
28 Accordingly, the demurrer should be sustained.

1 **C. Plaintiffs' Opposition Emphasizes the Fact that Plaintiffs Cannot Adequately**
2 **Represent the Company; Instead it is Clear they are Seeking to Enforce**
3 **Individual Interests**

4 In their effort to couch the remaining board of directors as sufficiently adverse to excuse the
5 making of a demand, Plaintiffs have in fact emphasized why they themselves are not adequate
6 representatives of Storix to serve as derivative plaintiffs. Plaintiffs' arguments make it loud and
7 clear that they are just seeking to gain individual advantages, instead of benefitting the company.

8 Plaintiffs' various disloyal conduct remains an insurmountable obstacle for them to
9 adequately represent the Company's interests as derivative plaintiffs. Rather than refute the details
10 regarding Johnson and Sassi's conflicted status, they embellish and support such a conclusion.

11 First, Johnson sued the Company for copyright infringement, claiming that the Company
12 had no right to sell its primary product. The Company won, but had to incur significant attorneys'
13 fees in defending against Johnson's baseless claims. While Johnson's characterization of the
14 copyright litigation as anything other than a complete and total victory for the Company finds no
15 basis in logic or reality, it is clear that the litigation he filed put him directly adverse to Storix.
16 Even after losing at trial, Johnson continues to try to undermine the Company's ownership rights
17 with respect to its intellectual property, including the software copyrights that a unanimous jury
18 found to be owned 100% by Storix. Johnson's pursuit of an appeal on this matter only further
19 solidifies his position as a conflicted director and shareholder who is seeking to harm the
20 Company's interests.

21 Second, Johnson mischaracterizes the status of the case Storix filed against him for his
22 breach of fiduciary duty owed to Storix. The Company sued Johnson for engaging in disloyal
23 conduct, and that case remains very much alive, but is not yet at issue, as Storix filed a First
24 Amended Complaint on March 14, 2016. Johnson has not yet answered the pleading. A Case
25 Management Conference is set for March 25, 2016, and Storix expects discovery to proceed in
26 short order thereafter. Notably, Storix has focused its efforts on defending (and winning) the
27 copyright litigation Johnson filed against the Company, and so has not pursued discovery while the
28 pleadings are finalized in the breach of fiduciary duty litigation. If anything, that plan conserved

1 Company resources. It is entirely disingenuous for Johnson, on one hand, to complain about Storix
2 expending resources for “frivolous litigation” and then argue that Storix is not adequately pursuing
3 such case.

4 As to Sassi, Plaintiffs misconstrue the asserted basis for her conflicted status. Storix does
5 not rely on her past marriage to Mr. Huffman, or any alleged bad blood between them, to contend
6 that she cannot serve as a suitable company representative. Rather, her disloyal acts and support of
7 Johnson’s efforts to undermine the Company, all to the Company’s detriment, are sufficient to
8 establish that she is not an adequate representative for a derivative claim. Like Johnson, Sassi is
9 seeking personal benefit and control over company operations. Storix has provided evidence of her
10 prior efforts to assist Johnson in his copyright suit against the Company and his efforts to oust the
11 current management of Storix. That is not in the Company’s interest, nor the proper purpose for a
12 derivative claim.

13 **D. Plaintiffs Disclosed Confidential Company Information and Violated Employee**
14 **Privacy**

15 As further evidence of their incapacity to serve as Company representatives in derivative
16 litigation, Plaintiffs violated not only the rules of this Court, but also the Protective Order in place
17 in the federal copyright litigation, and their duties to maintain the confidences of the Company.
18 Plaintiffs filed a number of exhibits in support of their Opposition that are troubling because of the
19 information revealed.³

20 For instance, Plaintiffs filed – as a matter of public record – Storix’s confidential
21 communications with its bank which included credit card applications bearing sensitive financial
22 information, Tax ID numbers, and Social Security Numbers. *See, e.g.*, Plaintiffs’ Ex. 6. This
23 action violates Cal. Rules of Court, Rule 1.20(b), which states in relevant part:

24 “To protect personal privacy and other legitimate interests, parties
25 and their attorneys must not include, or must redact where
26 inclusion is necessary, the following identifiers from all pleadings
27 and other papers filed in the court’s public file, whether filed in
28 paper or electronic form, unless otherwise provided by law or
ordered by the court:

³ Plaintiffs’ counsel has indicated they are working to withdraw such information. If they do not, Storix may file a motion asking to seal these exhibits to their oppositions.

1 (A) Social security numbers. If an individual's social security
2 number is required in a pleading or other paper filed in the public
file, only the last four digits of that number may be used.

3 (B) Financial account numbers. If financial account numbers are
4 required in a pleading or other paper filed in the public file, only
the last four digits of these numbers may be used.”

5 Moreover, Exhibit 6 was produced to Johnson in the copyright litigation and marked
6 “CONFIDENTIAL” under the terms of the protective order in that case. That Protective Order
7 provides that such marked documents “must not be disclosed by the receiving Party ... or their
8 respective counsel to anyone other than those persons designated within this order ... and in any
9 event, must not be used for any purpose other than in connection with this litigation.” *See*
10 Declaration of Paul Tyrell, Ex. 7, filed herewith. As a result, Plaintiffs’ filing violates both the
11 California Rules of Court and the District Court’s Protective Order.

12 Moreover, Johnson submitted exhibits revealing a number of details regarding Storix’s
13 software development and code details. *See, e.g.,* Plaintiffs’ Exs. 1 & 3. The code produced by
14 Storix in the copyright litigation was designated “CONFIDENTIAL – FOR COUNSEL ONLY.”
15 Its use was also subject to the terms of the protective order. Storix will be addressing this matter
16 with the District Court. Just as troubling as their disregard of explicit court orders is Plaintiffs’
17 inability to maintain the secrecy of confidential Company information, including its financial
18 information and trade secrets, which are privileged from discovery and disclosure. *See* Evid. C. §
19 1060. Plaintiffs’ desire to exact revenge on the Company has blinded them from their duty to
20 maintain its secrets. Neither Johnson nor Sassi can adequately represent the Company as a
21 derivative plaintiff.


22 **III. CONCLUSION**

23 Plaintiffs present no justification for overruling Storix’s demurrer. First, Plaintiffs cannot
24 establish that their case is being pursued on behalf of the company for its benefit as they are
25 conflicted directors that are pursuing personal disputes and grievances for individual gain. They
26 are not adequate representatives of Storix for purposes of a derivative suit. Second, they lack
27 standing as a result of their failure to make a demand on the board to investigate their allegations,
28

1 or to plead particularized facts regarding demand futility. They cite no details with respect to how
2 each director is incapable of addressing their demand. Further, they cannot overcome application
3 of the business judgment rule, as their sole grounds for pursuing this action, i.e., controlling
4 software product design, is a quintessential business decision with which the Court should not
5 interfere. For the foregoing reasons, and those stated in Storix's opening brief, the demurrer should
6 be sustained in its entirety. Further, since the flaws in Plaintiffs' case cannot be overcome with
7 further pleading, leave to amend should be denied.

8
9 DATED: March 24, 2016

PROCOPIO, CORY, HARGREAVES & SAVITCH
LLP

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11 By: 
12 Paul A. Tyrell
13 Sean M. Sullivan
14 Attorneys for Storix, Inc.

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