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8 DAVID KINNEY, and DAVID SMILJKOVICH
9

10 **SUPERIOR COURT OF CALIFORNIA**
COUNTY OF SAN DIEGO – CENTRAL DIVISION

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

13 Plaintiffs,

14 vs.

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

18 Defendants.
19
20
21

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

**REPLY IN SUPPORT OF DEFENDANTS'
DEMURRER TO COMPLAINT**

[IMAGED FILE]

Judge: Hon. Joel R. Wohlfeil
Dept. C-73
Action Filed: October 13, 2015
Trial Date: Not Set

Date: April 1, 2016
Time: 9:00 a.m.
Department: C-73

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1 **I. DISCUSSION**

2 **A. Plaintiffs Failed Adequately To Plead Demand Futility**

3 **1. Plaintiffs' Extrinsic Evidence Cannot Be Used To Demonstrate Demand**
4 **Futility**

5 Defendants' demurrer regarding demand futility is straightforward: The Complaint fails to
6 allege demand futility "with particularity," as required by California Corporations Code section
7 800(b). The Complaint attempts to satisfy the demand requirement by alleging a majority of the
8 board members are not disinterested and independent. The Complaint alleges: "Because the
9 majority of the board members are engaged in the wrongdoing complained of herein, and any Board
10 action requires majority consent, a demand for action by Plaintiffs from the Board would be futile."
11 (Complaint ¶ 37.) However, to adequately allege demand futility based on such an allegation, the
12 Complaint must allege facts with particularity, specific to each director, showing that particular
13 director could not be expected to fairly evaluate the claims of the shareholder plaintiff. *Shields v.*
14 *Singelton*, 15 Cal. App. 4th 1611, 1622 (1993). The Complaint simply makes no effort to do so.

15 Plaintiffs' Opposition fails to argue the Complaint, as pled, satisfies this requirement.
16 Plaintiffs never point to any fact allegations in the Complaint specific as to each director, showing a
17 majority of the directors were interested and could not have fairly evaluated Plaintiffs' claims. As a
18 result, Plaintiffs effectively concede the Complaint fails to allege such facts, and the demurrer
19 should be sustained.

20 Instead, Plaintiffs' Opposition includes paragraph after paragraph of confusing factual
21 arguments supported by *extrinsic evidence*, rather than by citation to allegations actually included in
22 the Complaint. (See Opposition at 6-8.) It is axiomatic that the purpose of a general demurrer is to
23 determine the sufficiency of the complaint itself, and in ruling on the demurrer, the court considers
24 only the allegations of the complaint and matters properly subject to judicial notice. See, e.g., *Ion*
25 *Equip. Corp. v. Nelson*, 110 Cal. App. 3d 868, 881 (1980); *McKell v. Washington Mut., Inc.*, 142
26 Cal. App. 4th 1457, 1491 (2006).¹ As a result, all of Plaintiffs' extrinsic evidence, and the

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28 ¹ While there are rare exceptions in which extrinsic evidence may be considered, Plaintiffs do not argue any such exception applies as to the demand futility issue, nor could Plaintiffs credibly have taken such a position.

1 Opposition's factual arguments supported by such extrinsic evidence, is irrelevant and must be
2 ignored.²

3 For example, the Opposition argues demand would have been futile because the
4 Defendants refused to discuss the alleged wrongdoings and refused to have the derivative suit
5 presented at Board meetings for the Board's consideration. (Opposition at 6-7.) In support of this
6 argument, Plaintiffs cite to their own supporting declarations. (*See id.*) But nothing in those
7 declarations can be used to show the Complaint adequately alleges demand futility. Because the
8 Complaint does not allege such facts, (and putting aside whether such facts would establish demand
9 futility in any event), the entire argument is irrelevant.

10 **2. The Complaint Does Not Allege Other Directors Are Dominated By**
11 **Huffman**

12 The Opposition next argues demand on the Board would have been futile because defendant
13 David Huffman dominates the Board. (Opposition at 6.) Again, however, the Complaint never
14 alleges such domination as the basis for demand futility. The Complaint simply alleges, in
15 boilerplate fashion, that demand is futile because a majority of the Board members were engaged in
16 the alleged wrongdoing. (Complaint ¶ 37.) Because *the Complaint* does not allege Huffman
17 dominated the Board, and does not allege any facts specific as to each director to support such
18 alleged domination, this argument is meritless and must be ignored.

19 To support their "domination" argument, Plaintiffs argue "the lack of Declarations [sic]
20 from [defendants] Altamirano, Turner and Kinney in support of their own opposition [sic] only
21 substantiates Huffman's domination over the Board." (Opposition at 6.) But the fact that
22 Defendants chose not to file declarations from Altamirano, Turner and Kinney in support of
23 Defendants' demurrer has nothing to do with whether Huffman dominates the Board. The decision
24 as to what declarations are needed from each defendant to support a legal argument is a matter
25 decided by counsel. It has nothing to do with whether Huffman dominates other members of
26 Storix's Board. *See Bader v. Anderson*, 179 Cal. App. 4th 775, 834 (2009) (To show specified

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28 ² See Defendants' Objections to Plaintiffs' Declarations Filed In Opposition to Defendants' Demurrer to
Complaint, filed concurrently with this Reply.

1 directors lack independence because they are dominated by another, the plaintiff “is required to
2 present specific facts showing ‘that through personal or other relationship the directors are beholden
3 to the controlling person’” (internal citations omitted.)

4 Next, Plaintiffs try to support their “domination” argument with claims that (1) defendants’
5 alleged decision not to discuss Plaintiffs’ allegations was taken at Huffman’s direction, and (2) the
6 other Defendants always vote in support of Huffman and do not oppose him. (Opposition at 6.)
7 But again, even if these facts somehow showed Defendants are “beholden” to Huffman, as opposed
8 to merely sharing his viewpoint on what is best for the company, these arguments are irrelevant
9 because they are not alleged *in the Complaint*. Once again, Plaintiffs’ only support for these
10 arguments is the declarations Plaintiffs filed, not allegations in their pleading. None of these
11 arguments says anything about whether the Complaint adequately has pled demand futility.
12 Because the Complaint does not even allege Huffman dominated the Board, never mind alleging
13 such domination with particularity as required, Plaintiffs’ “domination” argument must be rejected.

14 **3. Plaintiffs’ Belated Argument They Made A Demand On The Board**
15 **Must Be Ignored Because The Complaint Specifically Alleges Plaintiffs**
16 **Did Not Make Such A Demand**

17 Finally, Plaintiffs argue the Complaint is sufficient because they actually did make a
18 demand on the Board after all, and their demand allegedly was rejected by the Board. (Opposition
19 at 7-8.) The fatal problem with this argument is that the Complaint expressly alleges the exact
20 opposite. The Complaint does not allege Defendants ever attempted to make a demand on the
21 Board. On the contrary, it alleges no such demand was ever made. The Complaint states,
22 “Plaintiffs did *not* demand action from the Board of Directors (the ‘Board’) of the Company in
23 prosecuting this action, because any such effort would have been futile.” (Complaint ¶ 37
24 (emphasis added).) That allegation is a judicial admission. Plaintiffs cannot abandon that position
25 and allege the exact opposite position now, by declaration, merely because it suddenly suits their
26 interests.³

27
28 ³ Once again, the extrinsic evidence in Plaintiffs’ declarations regarding an alleged demand on the Board must
be ignored because such extrinsic facts may not be considered in ruling on Defendants’ demurrer.

1 **4. Plaintiffs Should Not Be Given Leave To Amend**

2 Plaintiffs should not be given leave to amend their Complaint to adequately allege demand
3 futility. Plaintiffs already had the chance to make such an amendment and specifically chose not to
4 do so. Specifically, as part of the meet and confer process before Defendants filed their demurrer,
5 Defendants set out their demand futility argument and supporting authority to Plaintiffs’ counsel.
6 In response, Plaintiffs’ counsel acknowledged there was more they could allege regarding demand
7 futility, and they said Plaintiffs would file an amended complaint by a certain specified date.
8 However, that date came and went without an amended complaint being filed. A week later,
9 Plaintiffs’ counsel stated Plaintiffs decided not to amend their Complaint after all. (See Declaration
10 of David J. Aveni in support of Defendants’ Demurrer, dated February 29, 2016, ¶¶ 4-7.)

11 In short, after Plaintiffs understood the problem, they had a full and fair opportunity to
12 amend their complaint to address this exact issue, and they promised to do so. However, for
13 whatever reason, Plaintiffs reversed their decision, eschewing the opportunity to amend their
14 Complaint, and making this demurrer necessary. Having made that choice, Plaintiffs need not be
15 given another bite at the apple.

16 **B. Plaintiffs Cannot Adequately Represent The Interests Of The Company**

17 Defendants’ demurrer argues Plaintiffs are disqualified from serving as derivative plaintiffs
18 for three reasons. The first of these is that Johnson has a conflict of interest because he is a party in
19 two separate lawsuits against Storix, one of which he initiated. As a result, Johnson is disqualified
20 from representing Storix in this litigation.

21 While Plaintiffs have a lot to say about those other two lawsuits – that Johnson intends to
22 appeal his loss in the Copyright lawsuit; that discovery in the other lawsuit has not yet started; that
23 Storix has refused to settle one of the lawsuits with him, and so forth – none of that responds to
24 Defendants’ argument. Plaintiffs do not respond to Defendants’ actual legal position that Johnson
25 has an inherent conflict of interest due to these other lawsuits against Storix, and as a result he
26 cannot serve as a derivative plaintiff on Storix’s behalf. Plaintiffs do not address Defendants’ cited
27 authority, nor do they cite any authority of their own to argue Johnson somehow is an adequate
28 derivative plaintiff despite these lawsuits. In fact, other than a brief attempt to distinguish a single

1 one of Defendants cited cases on another issue, this section of Plaintiffs' Opposition does not cite
2 any legal authority at all.⁴ (See Opposition at 8-10.) Because Johnson is involved in two other
3 lawsuits against Storix, he has a conflict of interest and cannot fairly and adequately represent
4 Storix as a derivative Plaintiff. See, e.g., *Zarowitz v. Bank of America Corp.*, 866 F.2d 1164, 1165-
5 66 (9th Cir. 1988); *Robinson v. Computer Servicers, Inc.*, 75 F.R.D. 637, 641-43 (D. Ala. 1976)
6 (holding plaintiff was inadequate derivative representative of company where he "is in the
7 inherently anomalous position of arguing that he is an adequate representative of the shareholders .
8 . while at the same time he is suing [the company] for \$750,000 in monetary damages" and is
9 competing against the company.) Johnson's claims therefore must be dismissed.

10 Defendants' second argument regarding Plaintiffs' inadequacy to represent Storix is that
11 Johnson also has a conflict of interest because he threatened to open a competing business against
12 Storix. Remarkably, Johnson actually admits in his declaration that he made such threats. Faced
13 with Defendants' evidence of his prior threats to compete, Johnson admits, "*I had previously*
14 *threatened in emails to compete with Storix* if they (the board) would not cooperate"
15 (Declaration of Anthony Johnson in support of Opposition to Demurrer, dated Mar. 18, 2016
16 ("Johnson Decl."), ¶ 12 (emphasis added).) Having admitted he threatened to compete, Johnson
17 then tries to dodge the consequences by insisting he did not carry through on his threat, and never
18 actually opened a competing business.

19 But that explanation just does not hold up in light of the evidence. Johnson admits:

- 20 (1) He made repeated written threats to open a competing business against Storix
21 (Johnson Decl., ¶ 12);
- 22 (2) He took a copy of Storix's SBAdmin software home with him, without
23 authorization, after he ended his employment with Storix, and continued to make
24 changes to that software (Johnson Decl., ¶ 6; see also Memorandum of Points and
25

26 ⁴ The only case Plaintiffs address is *Hornreich v. Plant Indus., Inc.*, 535 F.2d 550 (9th Cir. 1976), which
27 Defendants cited merely for the proposition that on this conflict of interest issue, the court may consider extrinsic
28 evidence. Ironically, although Plaintiffs attempt to distinguish *Hornreich*, it is unclear why they did so, since they agree
with the proposition for which the case was cited. Plaintiffs do not dispute that extrinsic evidence is relevant to the
issue of whether Plaintiffs are fair and adequate derivative Plaintiffs, and in fact Plaintiffs also present extrinsic
evidence on this issue.

1 Authorities in Support of Defendants’ Demurrer, at 7; Smiljkovich Decl., Exhibit 2,
2 Exhibit 3, at pg. 1, 2, Exhibit 4, at pg. 1, 2);

- 3 (3) He created his own company, which he called JanStor Technologies; and
- 4 (4) He reserved two port numbers for JanStor Technologies, which would allow it to sell
5 software that works the exact same way as Storix’s SBAAdmin software.

6 This evidence shows Johnson was working to set up JanStor Technologies as a competing business
7 to sell its own version of Storix’s SBAAdmin software, just as Johnson said he would do.

8 Moreover, while Johnson now self-servingly insists he did nothing other than threaten to
9 compete, his private text messages to Plaintiff Sassi paint a very different picture. He outright told
10 Sassi in one of the messages that he was *actively working* to set up his competing business.
11 Johnson stated, “I’ve been working to get Storix [sic] new competitor set up.” (Declaration of
12 David Smiljkovich in support of Defendants’ Demurrer, dated Feb. 29, 2016 (“Smiljkovich Decl.”),
13 Exhibit 1.) This is not some threat he sent to Storix’s Board, either. This was a private text
14 message Johnson sent to Sassi, which he obviously never intended Storix or its officers and
15 directors to see. This text shows Johnson was not just making threats to Storix, he was actively
16 working to turn those threats into a reality.⁵ Johnson’s self-serving claim that his threats to open a
17 competing business were just threats simply is not credible.

18 In any event, whether Johnson actually carried out his threat to compete is not the central
19 issue. Just the fact he threatened to compete against Storix by itself creates a serious conflict of
20 interest. Johnson is a *current Storix Director* who owes Storix fiduciary duties including a duty of
21 loyalty. Johnson’s admission that he threatened to compete against Storix unless Storix gave in to
22 his demands is a serious breach of his obligations and creates an unavoidable conflict of interest
23 that prevents him from representing Storix. Thus, even if all of the other evidence that Johnson
24 worked to set up a competing company is ignored, Johnson’s damning admission that he threatened

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26 ⁵ In the meantime, Johnson also actually sent an email to Storix customers warning that he, not Storix, owns the
27 copyright to the SBAAdmin software and that the customers thus may be in possession of unauthorized and infringing
28 copies of the software. (Smiljkovich Decl., Exhibit 9.) This was yet another step Johnson took in violation of his
fiduciary duty to Storix, and which advanced his plan to compete against Storix by selling his own version of the
software. Johnson does not deny in his Opposition or in his declaration that he took these incredibly damaging steps
against Storix.

1 to compete disqualifies him from serving as a derivative plaintiff.

2 Defendants' third argument regarding Plaintiffs' inadequacy to represent Storix is that Sassi
3 is disqualified because she actively assisted Johnson in his copyright lawsuit against Storix. In their
4 Opposition, Plaintiffs largely misstate this issue. Plaintiffs apparently believe Defendants'
5 argument is that Sassi is disqualified because she has animosity toward Huffman as his ex-wife, and
6 because Sassi hid the fact that she was assisting Johnson in his lawsuit.⁶ (Opposition at 9-10.)
7 While both those facts certainly are relevant, they are not the central point.

8 The real issue Defendants raised is that Sassi is disqualified because she has been working
9 actively on Johnson's side to help him against Storix in the copyright lawsuit. As a result, Sassi is
10 tainted by the same conflict of interest as Johnson, from his ongoing litigation against Storix. In
11 other words, because Sassi has taken an active role in assisting Johnson in his litigation against
12 Storix – whether she tried to hide her involvement or not – she is no more an adequate derivative
13 plaintiff than Johnson is. Because that litigation bars Johnson as a derivative plaintiff, it bars Sassi
14 as well.

15 Sassi does not deny she assisted Johnson in his copyright litigation against Storix, and like
16 Johnson, Sassi has no response to Defendants' authority that such litigation against the company
17 disqualifies her as a derivative plaintiff. Consequently, Sassi has a conflict of interest, and she
18 cannot serve as a derivative plaintiff on Storix's behalf.

19 **II. CONCLUSION**

20 Plaintiffs lack standing to bring their claims, as they have failed adequately to plead demand

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22 ⁶ Sassi denies she attempted to hide that she was assisting Johnson, and argues defendant Smiljkovich knew
23 Sassi was speaking with Johnson all along. The text messages between Sassi and Johnson reveal Sassi's claim to be
24 false. Sassi and Johnson specifically discussed *hiding* the fact that Sassi was helping Johnson, presumably so
25 Defendants would continue to trust Sassi with confidential information about their litigation strategies. In one of the
26 messages, for example, Johnson discusses that Sassi's assistance should remain covert, if possible. Johnson wrote, "I
27 hope to keep your role quiet through to the end, but there is a good chance at some point our relationship will be
28 discovered." (Smiljkovich Decl., Exhibit 7.) Later, in another text message, Sassi and Johnson discussed the vote taken
at a shareholder meeting to elect the Board of Directors. During that meeting, Sassi revealed for the first time that she
was on Johnson's side by voting as a block with Johnson. While discussing the vote by text message, Sassi wrote to
Johnson, "Now the fount is dry as far as Smiljkovich is concerned." (Smiljkovich Decl., Exhibit 8.) In other words,
because Sassi voted with Johnson, Defendants now were aware her loyalty was to him, and Smiljkovich would no
longer share confidential information with her that she could secretly pass along to Johnson. These messages confirm
what common sense already makes clear – that Sassi was keeping her assistance to Johnson a secret so Defendants
would continue to trust her with confidential information that she could then pass along to Johnson behind their backs.

1 futility. Further, Plaintiffs cannot fairly and adequately represent Storix as derivative Plaintiffs
2 because they are actively working against Storix, both in litigation and by Johnson's effort to
3 compete directly against Storix, using Storix's own software. For these reasons, Defendants'
4 demurrer to the Complaint should be sustained.

5 Dated: March 24, 2016

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