

SETH W. HAMOT and ANDREW R. SIEGEL

Plaintiffs,

v.

TELOS CORPORATION

Defendant.

* * * * *

TELOS CORPORATION

Counter-Plaintiff,

v.

SETH W. HAMOT and ANDREW R. SIEGEL

Counter-Defendants.

MEMORANDUM OPINION

Now before the Court is the motion of plaintiffs/counter-defendants Seth W. Hamot and Andrew R. Siegel (“Hamot” and “Siegel”) to dismiss counterclaims¹ filed in this action by defendant/counter-plaintiff Telos Corporation (“Telos”). Before it addresses the sufficiency of the allegations contained in the counterclaims under the traditional Maryland standard applicable to motions to dismiss, Hamot and Siegel contend that the Court must first analyze Telos’ counterclaims in light of the protections accorded Hamot’s and Siegel’s actions by the First Amendment to the United States Constitution.

¹ At oral argument, counsel for both sides agreed that the Court should treat the present motion as directed at the First Amended Counterclaims filed on June 20, 2008.

Counter-defendants assert that Telos' counterclaims are essentially premised upon directors Hamot's and Siegel's "threat to sue any Telos auditor that will not classify the ERPS² as current liabilities." First Amended Counterclaims ("FAC") ¶ 63. Arguing that the Petition Clause of the First Amendment immunizes such "threats to sue" where they are predicated upon good faith claims, counter-defendants would have the Court dismiss Telos' counterclaims for failure to state a claim upon which relief may be granted.

The argument advanced by counter-defendants here is that their actions are protected by the *Noerr-Pennington* Doctrine whose application was first articulated in a series of antitrust actions before the United States Supreme Court. *See E.R.R. Presidents Conference v. Noerr Motor Freight, Inc.*, 365 U.S. 127, 137-38 (1961); *United Mine Workers v. Pennington*, 381 U.S. 657, 670 (1965); *California Motor Transport Co. v. Trucking Unlimited*, 404 U.S. 508, 510-515 (1972). The doctrine essentially provides immunity for litigation and, by logical extension, threats of litigation under the Petition Clause of the First Amendment, unless the underlying claims are objectively baseless or exempted from immunity as a mere sham. *P.R.E.I.I. v. Columbia Pictures Industries, Inc.*, 508 U.S. 49, 51 (1993). Counter-defendants in the present action contend that Telos has failed to plead adequately the sham exception to the *Noerr-Pennington* Doctrine and that its counterclaims are thereby barred. The Court disagrees.

Even a cursory review of Telos' FAC reveals Telos' contention that Hamot's and Siegel's litigation threats are objectively baseless. *See, e.g.*, FAC ¶¶ 48, 58, 59, 60, 66 and 68.³

² Cumulative 12% Exchangeable Redeemable Preferred Shares of Telos Corporation.

³ ¶ 68 also alleges that Hamot and Siegel are motivated by an "improper and unlawful purpose." Thus, the second prong of the *Noerr-Pennington* analysis is satisfied.

Indeed, Telos' FAC details at length the efforts of Hamot and Siegel, acting independently or through the Costa Brava Partnership, to disrupt the business activities of Telos Corporation, including the unsuccessful shareholder litigation in this Court, the efforts to hinder the replacement of independent directors on Telos' board in 2006, the attempts to interfere with Telos' primary lender, Wells Fargo Foothill, Inc., a series of allegedly abusive SEC filings and, finally, the threats to sue Telos' independent auditors. As the United States Supreme Court has said, in the context of the *Noerr-Pennington* Doctrine:

One claim, which a court or agency may think baseless, may go unnoticed; but a pattern of baseless, repetitive claims may emerge which leaves the factfinder to conclude that the administrative and judicial processes have been abused. That may be a difficult line to discern and draw. But once it is drawn, the case is established that abuse of those processes produced an illegal result, *viz.*, effectively barring respondents from access to the agencies and courts.

California Motor Transport Co., 404 U.S. at 513. Thus, the Supreme Court has adopted the view that such a pattern of baseless, repetitive claims can be deemed objectively baseless for purposes of the *Noerr-Pennington* analysis.

Assuming the applicability of the doctrine, the gravamen of counter-defendants' argument is that this Court may not proceed to the second prong of the *Noerr-Pennington* Doctrine to consider Hamot's and Siegel's subjective motivations until satisfying itself that their threats of suit were objectively baseless. Relying exclusively on the jury verdict in the Virginia litigation,⁴ counter-defendants contend that Telos cannot meet the sham litigation exception to the *Noerr-Pennington* Doctrine because, as the Supreme Court has said, "[o]ne cannot come

⁴ The record before this Court contains no other evidence suggesting that there is merit to Hamot's and Siegel's argument that Telos' accounting for its ERPS obligations is inaccurate or misleading.

before a court and argue that litigation that terminated in one's opponent's favor is 'objectively baseless in the sense that no reasonable litigant could realistically expect success on the merits.'" *P.R.E.I.I.*, 508 U.S. at 61. While that is no doubt accurate as a general principle supporting the immunity of good faith claims where the doctrine is applicable, there is nothing in the Supreme Court jurisprudence which compels this Court to parse an ambiguous jury verdict in a foreign jurisdiction to determine whether it was logically predicated upon evidence supportive of the claims made here by counter-defendants upon which they threaten suit. Under the circumstances of this case, the Court believes it is justified at this early motions stage of the proceedings to assume the truth of Telos' allegations that the counter-defendants' claims are objectively baseless. Accordingly, counter-defendants' motion fails on this issue because counter-plaintiff, as previously stated, has pled adequately the sham exception.

The Supreme Court has not had occasion to consider the *Noerr-Pennington* Doctrine outside the context of antitrust litigation, although its extension into other areas of litigation has been the subject of controversy in the lower federal courts and in legal literature. At least one commentator has taken the position that

The *Noerr* decision was strictly a matter of statutory interpretation – a construction of the Sherman Act – and not a declaration of standards by which First Amendment cases should be reviewed. The Court acknowledged that a holding that the Sherman Act applied to political activity “would raise important constitutional questions. The right of petition is one of the freedoms protected by the Bill of Rights and we cannot, of course, lightly impute to Congress an intent to invade these freedoms.” But the Court did not state that there is a constitutional right to antitrust immunity when petitioning is involved, or that there should be a case-by-case review of the competing interests. Instead, the Court declared only that a plaintiff harmed by petitioning activity may not recover *under the Sherman Act*; it expressly avoided ruling on the railroads' insistence that their activities were protected by the First

Amendment.

Robert A. Zauzmer, *The Misapplication of the Noerr-Pennington Doctrine in Non-Antitrust Right to Petition Cases*, 36 Stan. L. Rev. 1243, 1250 (1984) (emphasis in original) (internal citations omitted). Thus, debate has ensued over whether *Noerr* and *Pennington* were constitutional decisions that balanced antitrust policies against the First Amendment right to petition, finding the latter to be paramount, or merely rulings that the Sherman Act was not meant to reach political activities. Justice Douglas' opinion in the *California Motor* case clearly invoked the doctrine and went on to discuss it in the context of First Amendment jurisprudence. This was an action for injunctive relief and damages under the Clayton Act brought by highway carriers against other carriers, charging a conspiracy to monopolize the transportation of goods by instituting state and federal proceedings to resist and defeat applications by the plaintiffs to acquire, transfer or register operating rights. Speaking for the Supreme Court, Justice Douglas said:

We conclude that it would be destructive of rights of association and of petition to hold that groups with common interests may not, without violating the antitrust laws, use the channels and procedures of state and federal agencies and courts to advocate their causes and points of view respecting resolution of their business and economic interests *vis-a-vis* their competitors.

We said, however, in *Noerr* that there may be instances where the alleged conspiracy "is a mere sham to cover what is actually nothing more than an attempt to interfere directly with the business relationships of the competitor and the application of the Sherman Act would be justified."

404 U.S. at 510-511 (citing *Noerr*, 365 U.S. at 533).

More important to this Court's determination of the applicability of the *Noerr-Pennington* Doctrine to the present case are two related factors. First, because the Supreme Court has not had occasion to decide what effect the right to petition the government has upon common law tort

actions, the lower federal courts have grappled with the doctrine's extension into those areas. Secondly, in analyzing extensions of *Noerr-Pennington* to non-antitrust cases, the federal courts have focused upon the litigants' First Amendment rights to petition the government for changes in executive or legislative policy. For example, in *Sierra Club v. Butz*, the United States District Court for the Northern District of California stated: "This court agrees that when a suit based on interference with advantageous relationship is brought against a party whose 'interference' consisted of petitioning a governmental body to alter its previous policy a privilege is created by the guarantee of the First Amendment." 349 F.Supp. 934, 938 (N.D. Cal. 1972). Moreover, the United States Court of Appeals for the Third Circuit has expressed that:

The rule that liability cannot be imposed for damage caused by inducing legislative, administrative or judicial action is applicable here. The conduct on which this suit is based is protected by the firmly rooted principle, endemic to a democratic government, that enactment of and adherence to law is the responsibility of all. The problem is not too much citizen involvement but too little. Thus, we hold that as a matter of law, defendants' actions in calling Brownsville's violations to the attention of state and federal authorities and eliciting public interest cannot serve as the basis of tort liability.

Brownsville Golden Age Nursing Home, Inc. v. Wells, 839 F.2d 155, 160 (3rd Cir. 1988). In a more recent decision, the Third Circuit has elaborated on those principles, stating:

Thus, the purpose of *Noerr-Pennington* as applied in areas outside the antitrust field is the protection of the right to petition. Immunity from liability is necessary so as not to chill the exercise of that right. The question presented by this case is whether immunity from the burden of suit is also necessary to avoid an unconstitutional chill of the right to petition.

. . . .
. . . The courts have never recognized, however, that an immunity *from suit* was necessary to prevent an unacceptable chill of those First Amendment rights. Indeed, the law appears to be to the contrary.

We, Inc. v. City of Philadelphia, 174 F.3rd 322, 327 (3rd Cir. 1999) (emphasis in original).

Thus, it appears that the federal courts have extended the *Noerr-Pennington* analysis beyond the antitrust field to bar litigation arising from injuries received as a consequence of First Amendment petitioning activity, regardless of the underlying cause of action. What is not clear from the *Noerr-Pennington* cases and their progeny is that the doctrine can be set up as a bar to claims based on threats of suit from private individuals over private interests, not in furtherance of any identifiable petitioning activity. Viewed in this context, the Court finds it highly questionable that the federal courts would apply the *Noerr-Pennington* Doctrine in the present case.

For these reasons, the Court will go on to consider the FAC in light of the traditional Maryland standards for determining a preliminary motion to dismiss.

Counter-defendants seek to dismiss the counterclaims on the following grounds: 1) that Telos fails to plead adequately tortious interference with contracts because either no facts have been alleged demonstrating a contract or the auditor engagements could be terminated at-will by the auditors⁵, and even assuming the contracts existed and were not at-will, no nexus has been shown between counter-defendants' allegedly unlawful behavior and any injury suffered by Telos and no breach has been shown; 2) that claims for tortious interference with business relations do not arise when a director seeks answers to substantive questions or disagreements regarding the company's accounting and/or when the individual has a legitimate business or economic interest in the underlying contract and is acting pursuant thereto or to protect those interests; and 3) breach of

⁵ Counter-defendants contend that terminable-at-will contracts are treated much like no contract for purposes of analyzing interference claims. The Court believes that the auditor engagements here are more akin to services contracts which do enjoy legal protection from the kinds of interference here alleged. *Compare Sharrow v. State Farm Mutual*, 306 Md. 754, 765 (1986).

fiduciary duty is not a recognized independent claim in Maryland, and even assuming it is, Telos has not alleged sufficient facts of a breach.

In considering a motion to dismiss counterclaims, the Court assumes the truth of all well-pleaded facts and draws all reasonable inferences in favor of the counter-plaintiff. *Manikhi v. Mass Transit Admin.*, 360 Md. 333, 344-45 (2000). The facts comprising a counter-plaintiff's causes of action must be pled with specificity. *Adamson v. Corr. Med. Servs., Inc.*, 359 Md. 245, 249 (2000). Dismissal is appropriate when no relief can be granted as a matter of law. *Lubore v. RPM Assocs. Inc.*, 109 Md. App. 312, 322 (1996).

Counts one and two of the FAC allege tortious interference with contractual relationships with outside auditors Reznick Group ("Reznick") and Goodman & Company, LLP ("Goodman"). Contrary to the counter-defendants' belief, Telos has pleaded adequately facts showing the existence of contracts between Telos and the auditors,⁶ FAC ¶¶ 43, 50, 63, 75-77, and Telos as well has alleged actions on the part of Hamot and Siegel that, if proven to be true, rise to the level of actionable interference. Those alleged acts of interference include multiple e-mails and letters sent to both auditors accusing Telos of unlawfully funneling money to Telos' majority shareholder; multiple Schedule 13-D filings with the SEC alleging misclassification of the ERPS; a letter writing campaign to convince Goodman to withdraw its former audit opinions; and communicating directly with

⁶ Specifically, at the hearing, counter-defendants alleged that the Goodman contract not to withdraw prior audit opinions did not come into existence until March 27, 2008. Since Hamot and Siegel did not send their letter seeking withdrawal of former audit opinions until March 28, 2008, they claim they lacked the requisite knowledge of the contract with Goodman and so could not have tortiously interfered with that contract as alleged by Telos. For the purposes of a motion to dismiss, counter-plaintiff is only required to plead the existence of a contract between Telos and Goodman. A "continuing contractual obligation" between Goodman and Telos is alleged, as is the knowledge of that contract on the part of counter-defendants and injury resulting from counter-defendants' actions. FAC ¶¶ 77-81.

Reznick, allegedly violating the Sarbanes-Oxley Act, SEC Rule 1362-2, and the Audit Committee Charter, in an attempt to reclassify the ERPS treatment in the 2007 audit report. FAC ¶¶ 31, 34, 44, 53-60. When viewed in the light most favorable to counter-plaintiff, these facts plead sufficiently an action for tortious interference with contract.

The Court similarly finds that Telos has stated viable claims for tortious interference with business relations in counts three and four. A typical tortious interference claim involves three parties, one of whom is not involved in the underlying relationship. *See, e.g., K&K Management, Inc. v. Lee*, 316 Md. 137, 155-56 (1989). Here Telos has alleged adequately that the relationship with Goodman and Reznick was managed by Telos' Audit Committee, which was specifically formed for that purpose. FAC ¶¶ 51-52. This Committee oversight, Telos points out, is required by SEC Rule 10A-3(b)(2). The counterclaims also indicate behavior by Hamot and Siegel that, if proven to be true, could be considered wrongful conduct by a finder of fact. *See K&K Management*, 316 Md. at 166. Hamot and Siegel contend that they have a legitimate interest in the business relations with Reznick and Goodman and, consequently, they cannot tortiously interfere with those relationships. Counter-defendants can point to no case law establishing that directors of corporations, by virtue of their position, cannot interfere with contracts held by the corporation. Considering Telos' allegations in their totality, a factfinder could infer wrongful or harmful conduct on the part of Hamot and Siegel. *See* FAC ¶¶ 55-62. Thus, the counts will survive counter-defendants' motion.

The same can be said for Telos' claims of breach of fiduciary duty in counts five and six.⁷ There is no dispute as to the fact that Hamot and Siegel, as Class D directors, owe a fiduciary duty to Telos and its shareholders. Md. Code Ann., Corps. & Ass'ns § 2-405.1 (2008). At issue here is whether they breached those duties in attempting to change the classification of the ERPS through the alleged harassment of the outside auditors. Facts that go to the issue of breach include Hamot's and Siegel's refusal, as directors or otherwise, to answer questions put forward by other members of the board of Telos regarding counter-defendants' allegedly unauthorized communications with Reznick and their continuation of that communication irrespective of the board's reaction. FAC ¶¶ 60-62. These allegations, coupled with the fact that Hamot and Siegel are holders of the ERPS in question and interested directors, support the inference that Hamot and Siegel put their own interests before those of the corporation and its other shareholders in violation of their fiduciary duties.⁸ See Md. Code Ann., Corps. & Ass'ns § 2-405.1(a); *Indurated Concrete Corp. v. Abbott*, 195 Md. 496, 503 (1950).

For the foregoing reasons, counter-defendants' motion to dismiss the counterclaims is **DENIED** as to all counts.

⁷ Both parties have conceded that breach of fiduciary duty is not recognized as an independent tort under Maryland law. Because the Court is assuming the truth of the facts alleged in the other counterclaims, those same facts will provide tortious conduct to support a claim for breach of fiduciary duty.

⁸ The precarious situation in which constituency directors such as counter-defendants Hamot and Siegel find themselves has been the subject of quite recent commentary. See E. Norman Veasey & Christine T. Di Guglielmo, *How Many Masters Can a Director Serve? A Look at the Tensions Facing Constituency Directors*, 63 Bus. Law. 761 (2008).

/s/ ajm

ALBERT J. MATRICCIANI, JR.

Judge

July 24, 2008

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