

**COURT OF CHANCERY  
OF THE  
STATE OF DELAWARE**

WILLIAM B. CHANDLER III  
CHANCELLOR

COURT OF CHANCERY COURTHOUSE  
34 THE CIRCLE  
GEORGETOWN, DELAWARE 19947

Submitted: May 15, 2009  
Decided: June 12, 2009

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Re: *Gatz, et al. v. Ponsoldt, et al.*  
Civil Action No. 174-CC

Dear Counsel:

I have reviewed the submissions filed in connection with the proposed settlement of a class action brought by plaintiffs Edward E. Gatz and Donald D. Graham on behalf of shareholders of Regency Affiliates, Inc. (“Regency”), as well as an application for attorneys’ fees and expenses for services rendered by plaintiffs’ counsel in the prosecution of the litigation.

For the reasons set forth below, I approve the settlement, and award attorneys' fees and expenses in the amount of \$1,092,102.50, which amounts to 33% of the settlement common fund plus expenses.

## I. BACKGROUND

On May 2, 2002, plaintiffs initiated derivative and class action litigation in the United States District Court for the District of Nebraska against William R. Ponsoldt, Sr. ("Ponsoldt"), William R. Ponsoldt, Jr. ("Ponsoldt Jr."), Marc H. Baldinger ("Baldinger"), Stephanie Carey ("Carey"), and Martin J. Craffey ("Craffey") (collectively, the "Regency Director Defendants"), and Statesman Group, Inc. ("Statesman") seeking relief under The Organized Crime Control Act of 1970, and the Racketeer Influenced and Corrupt Organizations statute ("RICO"), and stating various other state law claims, including the breach of fiduciary duty (the "Nebraska Action"). On October 17, 2002, Regency announced the completion of a recapitalization involving defendant Royalty Holdings, L.L.C. ("Royalty"). As part of the recapitalization, defendants allegedly granted to Royalty a convertible note to acquire approximately 60% of the common stock of Regency at a discounted price, allowed Regency to repurchase from Statesman shares of Regency common stock, distributed \$4 million to Statesman, and effectively cancelled a \$2.44 million promissory note issued by Statesman to Regency.

On July 7, 2003, the Nebraska District Court transferred the case to the United States District Court for the District of Delaware. On September 23, 2003, the Regency Director Defendants and Statesman filed a motion to dismiss the complaint in the Delaware District Court. Plaintiffs moved the Delaware District Court for leave to file an amended complaint. The amended complaint alleged that Royalty received a convertible promissory note as part of the recapitalization, allowing it to acquire 1,750,000 shares of Regency common stock. This allegedly caused Regency's public shareholders' ownership interest to decrease from approximately 61.1% to approximately 40.7%. On December 18, 2003, the Delaware District Court denied plaintiffs' motion to file an amended complaint, dismissed plaintiffs' RICO claims under Rule 12(b)(6), and dismissed plaintiffs' other claims for lack of federal subject matter jurisdiction.

On January 20, 2004, plaintiffs filed their complaint in the Delaware Court of Chancery alleging breach of fiduciary duties in connection with the recapitalization, other recapitalization-related transactions, and unreasonable compensation paid to Ponsoldt, as well as aiding and abetting the breach of the fiduciary duties in connection with the recapitalization. On May 26, 2006, the

Court dismissed all of the plaintiffs' claims relating to the recapitalization on the grounds that those claims were derivative in nature and that plaintiffs had failed to make a pre-suit demand on Regency's board of directors as required by Court of Chancery Rule 23.1.

On June 14, 2006, plaintiffs appealed to the Delaware Supreme Court seeking review of this Court's holding dismissing plaintiffs' claims. On April 16, 2007, the Delaware Supreme Court held that plaintiffs' claims were direct in nature and reversed this Court's decision to dismiss. The case was remanded to this Court for further proceedings.

On January 16, 2008, the parties reached an agreement in principle to settle the action in the Court of Chancery, and the parties executed a memorandum of understanding on April 28, 2008, memorializing the terms of their agreement (the "Settlement Agreement"). On December 4, 2008, the parties sought approval of the Settlement Agreement. A hearing was held on March 16, 2009, after which the Court asked for further briefing to clarify the parties' positions.

Under the Settlement Agreement, defendants will pay \$3,000,000 (plus accrued interest), which will be distributed to the members of the shareholder class. In exchange for the cash payment, defendants received a dismissal of this action and release of all class members' claims relating to or arising from this action or the settlement. One condition of the settlement was that Regency was required to conduct an 8 *Del. C.* § 145 review to determine if the directors were entitled to indemnification from Regency with respect to the actions challenged in this suit. WolfBlock LLP was engaged to conduct this review which determined that since the directors acted in good faith and in a manner they reasonably believed to be in the best interests of Regency that they were entitled to indemnification. Therefore, the entire \$3,000,000 settlement payment was funded by Regency.

Additionally, plaintiffs' counsel requests the Court's approval of an award of attorneys' fees of 33% of the \$3,000,000 (\$990,000) settlement fund and expenses in the amount of \$102,102.50.

## II. ANALYSIS

### A. *Approving the Settlement*

This Court generally favors settlement of complicated litigation,<sup>1</sup> “[h]owever, the settlement of a class action is unique because the fiduciary nature of the class action requires the Court of Chancery to participate in the consummation of the settlement to the extent of determining its intrinsic fairness.”<sup>2</sup> Ultimately, this Court applies its own sound judgment in deciding whether to approve a class action settlement as fair and reasonable.<sup>3</sup> In doing so, the Court weighs and considers “the nature of the claim, the possible defenses to it, [and] the legal and factual obstacles facing the plaintiff in the event of a trial.”<sup>4</sup>

In deciding whether to settle their case, plaintiffs faced a relatively risky proposition that they would ultimately not prevail on their claims. Plaintiffs’ claims centered on the alleged harm that Regency’s shareholders suffered in connection with the recapitalization and other related events through the transfer of their voting power and equity interest in Regency to a third party, Royalty, without compensation and by reducing Regency’s shareholders from a majority to a minority ownership position. Substantial obstacles existed, however, that reduced the probability that plaintiffs would have been successful on the merits of their claims. Plaintiffs’ counsel was concerned about whether the recapitalization would be subject to entire fairness review or the less demanding standard of the business judgment rule.<sup>5</sup> In order to achieve the entire fairness standard, plaintiffs thought that they would have had to demonstrate that Ponsoldt was on both sides of the transaction in that he dominated and controlled both Statesman and Regency. Plaintiffs also believed that they had to show that the appointment of the special committee to overview the recapitalization transaction was a sham and not sufficient to shift the burden back to plaintiffs to show that the recapitalization was unfair. Plaintiffs believed that these standards would have been difficult for them to meet.

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<sup>1</sup> See, e.g., *In re Countrywide Corp. S’holders Litig.*, 2009 WL 846019, at \*10 (Del. Ch. Mar. 31, 2009).

<sup>2</sup> *Rome v. Archer*, 197 A.2d 49, 53 (Del. 1964); *Nottingham Partners*, 564 A.2d at 1102.

<sup>3</sup> *Rome*, 197 A.2d at 53.

<sup>4</sup> *Id.*

<sup>5</sup> See *In re Citigroup Inc. S’holder Derivative Litig.*, 964 A.2d 106, 124 (Del. Ch. 2009).

While facing these difficult hurdles to achieving success on the merits of their claims, plaintiffs nonetheless were able to obtain a cash settlement of \$3,000,000 for their shareholder class. Since plaintiffs' claims lacked a significant probability of success on the merits, the monetary benefits plaintiffs' obtained in settlement appear to be a reasonable benefit in light of the obstacles plaintiffs faced. Therefore, I conclude that the settlement is fair and reasonable and should be approved.

### *B. Plaintiffs' Counsel Fee Application*

Delaware maintains the policy of “insur[ing] that, even without a favorable adjudication, counsel will be compensated for the *beneficial results* they produced.”<sup>6</sup> This policy exists to “prevent frustration of the remedial policy of providing professional compensation for such suits when meritorious.”<sup>7</sup> In setting fee awards, this Court “must make an independent determination of reasonableness.”<sup>8</sup> In arriving at the specific amount for the award, and in assessing whether a fee is reasonable, the Court typically considers a number of factors, including: “(1) the results accomplished for the benefit of the shareholders; (2) the efforts of counsel and the time spent in connection with the case; (3) the contingent nature of the fee; (4) the difficulty of the litigation; and (5) the standing and ability of counsel involved.”<sup>9</sup> This Court has consistently noted that the most important factor in determining a fee award is the size of the benefit achieved.<sup>10</sup>

Here, plaintiffs' counsel produced a material cash benefit to the shareholder class, totaling \$3,000,000. To obtain that settlement, plaintiffs' counsel had to exert significant effort. Plaintiffs' counsel brought claims in federal court in Nebraska and Delaware, as well as in the Delaware Court of Chancery. Their claims were dismissed in the federal courts and initially in the Court of Chancery, but plaintiffs' counsel prevailed on appeal of the dismissal by this Court to the Delaware Supreme Court where counsel participated in two oral arguments. Plaintiffs' counsel has also taken a significant amount of discovery and deposed numerous witnesses.

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<sup>6</sup> *Allied Artists Pictures Corp. v. Baron*, 413 A.2d 876, 878 (Del. 1980) (emphasis added).

<sup>7</sup> *Id.*

<sup>8</sup> *Goodrich v. E.F. Hutton Group, Inc.*, 681 A.2d 1039, 1045-46 (Del. 1996).

<sup>9</sup> *In re Abercrombie & Fitch Co. S'holders Derivative Litig.*, 886 A.2d 1271, 1273 (Del. Supr. Oct. 26, 2005) (citing *Sugarland Indus. Inc. v. Thomas*, 420 A.2d 142 (Del. 1980)).

<sup>10</sup> *See, e.g., Seinfeld v. Coker*, 847 A.2d 330, 336 (Del. Ch. 2000).

Additionally, plaintiffs' counsel prosecuted this litigation on an entirely contingent basis.<sup>11</sup> In so doing, they expended a significant amount of time and resources pursuing this case. Plaintiffs' counsel spent approximately 6,107 hours pursuing the case in the federal courts, and 3,023 hours in the Court of Chancery. For their efforts in this Court alone, plaintiffs' counsel's time-based fee would be \$327.49. On an hourly rate, this fee request is very reasonable, if not below counsel's normal hourly rates. Also, plaintiffs' counsel incurred unreimbursed expenses of \$102,102.50. Moreover, as expressed in a percentage, the requested fee of 33% of the settlement fund is within the range of reasonable fee awards in other class action cases where the benefit of a common settlement fund was obtained.<sup>12</sup>

At the settlement hearing on March 16, 2009, this Court raised the concern that because of the indemnification agreement between Regency and the Regency Director Defendants the burden of the proposed settlement fund was, for all intents and purposes, being borne by the shareholders of Regency. Such an arrangement, if true, would not amount to any real benefit to the shareholder class because they would, essentially, be paying themselves. In their subsequent submissions, however, both Regency and plaintiffs have explained that since the recapitalization transaction took place in October 2002, the composition of Regency's shareholders has completely changed. Of the shareholder class that brought this lawsuit, Regency maintains that no more than 27%, and as little as 7%, remain as Regency shareholders. Accordingly, as much as 93%, and not less than 73%, of the proposed settlement payment will be borne by non-class members.<sup>13</sup> Thus, I am

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<sup>11</sup> This Court recognizes that attorneys are entitled to a significant fee when the fee is contingent on the outcome of the case. *See, e.g., Chrysler Corp. v. Dann*, 223 A.2d 384, 389 (Del. 1966); *see also In re First Interstate Bancorp Consol. S'holder Litig.*, 756 A.2d 353, 365 (Del. Ch. 1999).

<sup>12</sup> *See, e.g., Seinfeld v. Coker*, 847 A.2d 330, 337 (Del. Ch. 2000) ("Just this year, this Court awarded an attorneys fee equal to 33 percent of the fund.") (citing *In re Intek Global Corp. S'holders Litig.*, C.A. No. 17207, Strine, V.C. (Apr. 24, 2000)).

<sup>13</sup> Since 2002, Royalty now owns 50.5% of Regency's outstanding shares, the holders of the converted Series B shares own 12.5%, Raffles Associates own 2.9%, and the Regency Defendant Directors own 3.4%. Therefore, the foregoing account for over 69% of the new ownership (since 2002) of Regency and will indirectly bear 69% of the settlement payment to the shareholder class. Additionally, Regency's stock transfer ledger shows that 73% of Regency's currently outstanding common stock was issued after the recapitalization transaction. Regency's stock transfer ledger reflects changes in record ownership, not beneficial ownership, which, when taken into account, Regency believes has resulted in approximately 93% of its currently outstanding stock to be held by non-class members.

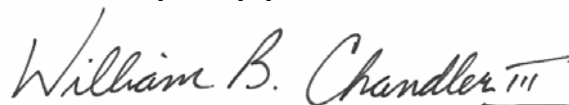
confident that the payment of the settlement fund will not be a circular transfer (minus attorney fees) that would result in a situation where the shareholder class was “paying themselves,” but rather an actual benefit to the shareholder class that was allegedly harmed by the recapitalization transaction.

On balance, and in the exercise of my discretion, I conclude that, given the obstacles they faced, an award of \$990,000 adequately compensates plaintiffs’ counsel for the benefit they provided the shareholder class and the effort they expended in this matter. Plaintiffs’ counsel will also be awarded their reasonable unreimbursed expenses, totaling \$102,102.50.

### III. CONCLUSION

For the foregoing reasons, I approve the settlement, and award attorneys’ fees in the amount of \$1,092,102.50 inclusive of expenses. I have entered the Order submitted by counsel at the settlement hearing.

Very truly yours,

A handwritten signature in cursive script that reads "William B. Chandler III". The signature is written in black ink and is positioned above the printed name.

William B. Chandler III

WBCIII:tet

xc: John M. Kerwin