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

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Re: *Kuo v. Genius Products, Inc., et al.*
Civil Action No. 3329-CC

Dear Counsel:

I have reviewed your submissions seeking and objecting to an award of attorneys' fees and expenses for services rendered by plaintiff's counsel in the prosecution of this litigation. A minority stockholder of Genius Products, Inc. ("Genius"), Betty Kuo, brought this action following the October 9, 2007 announcement of Genius's proposed reverse stock split. Kuo sought damages, alleging that Genius's board of directors violated its fiduciary duties and that the price offered by Genius in the proposed transaction to buy-out fractional shareholders was insufficient and unfair. Ultimately, Genius decided to abandon the proposed transaction, rendering plaintiff's complaint moot. Kuo contends, however, that her lawsuit caused Genius to abandon the proposed transaction. Kuo insists that her lawsuit provided a substantial benefit to Genius's stockholders, which entitles plaintiff's counsel to an appropriate fee award. I conclude that defendants have failed to fully rebut the presumption that, at a minimum, plaintiff's claims contributed to Genius's decision to abandon the reverse stock split. Thus,

for the reasons set forth below, I award attorneys' fees in the amount of $100,000 inclusive of expenses.

## I. BACKGROUND

Genius is a Delaware corporation that is actively engaged in acquiring, producing, and licensing an extensive library of motion pictures, television programming, and other entertainment. The Weinstein Company Holdings LLC ("WCH") and W-G Holding Corp. ("W-G"), both affiliates of The Weinstein Company LLC, control Genius through ownership of Genius Series W Preferred Stock. WCH and W-G appointed five of the seven members of the Genius board of directors.

On October 9, 2007, Genius issued a press release announcing that its board approved a reverse stock split of Genius's common stock in an attempt to meet the minimum stock price of $5.00 required to list its stock on NASDAQ. On October 29, 2007, Genius's controlling stockholders approved the reverse stock split and gave the Genius board one year, until October 29, 2008, to select an exchange ratio and effect the reverse split, or alternatively abandon the transaction. On October 31, 2007, Genius filed a "Notice of Stockholder Action by Written Consent" ("Notice") with the Securities and Exchange Commission. The Notice informed stockholders that Genius would not issue fractional shares with the reverse split. Stockholders with less than one post-split share would be cashed out, as would the fractional interests of stockholders whose shares were not evenly divisible by the reverse stock split ratio (originally set at 1 to 8). The cash amount paid to the stockholders was to be equal to their fractional interest multiplied by the closing trading price of the common stock on the trading day immediately before the date of the split.

On November 2, 2007, Kuo commenced this action, alleging that Genius's board of directors breached its fiduciary duties and that the reverse stock split violated 8 *Del. C.* § 155(2), which requires Genius to pay stockholders "fair value" for their fractional interests. Defendants Genius, its board of directors, WCH, and W-G filed their answer on December 21, 2007. At the same time, Genius entered into settlement negotiations with Kuo. During the course of the negotiations, Genius's stock price began to fall. Genius claims that its stock price fell to such a level that it effectively eliminated the chance of a NASDAQ listing. Genius then announced that it was abandoning the reverse stock split. On October 29, 2008, the option to effect the reverse split expired. On November 7, 2008, the parties filed a stipulation and order of dismissal, recognizing plaintiff's claims as moot.

On November 17, 2008, plaintiff filed a request for an award of attorneys' fees and expenses.

## II. ANALYSIS

This Court may grant attorneys' fees in a mooted class action under the common corporate benefit doctrine.[1] "Under this doctrine, a litigant who confers a common monetary benefit upon an ascertainable stockholder class is entitled to an award of counsel fees and expenses for its efforts in creating the benefit."[2] In order to be awarded fees under the corporate benefit doctrine, an applicant must show: (1) the suit was meritorious when filed; (2) the action producing the benefit to the corporation was taken by the defendants before a judicial resolution was achieved; and (3) the resulting corporate benefit was causally related to the lawsuit.[3]

Defendants contend, however, that Kuo's lawsuit did not cause Genius's board to abandon the reverse stock split. In fact, defendants maintain that Genius's falling stock price was the sole factor that led to the decision to abandon the transaction. Thus, defendants argue that plaintiff's counsel is not entitled to a fee award. The law in Delaware is clear on this issue. A corporate defendant that, after a complaint is filed, takes action that renders the claims asserted in the complaint moot bears the burden of persuasion to show that no causal connection existed between the initiation of the suit and any later benefit to the stockholders.[4] A strong presumption in favor of plaintiff's counsel exists in these types of cases. Defendants "must demonstrate that the stockholders' suit 'did not in *any way* cause [its] action.'"[5] Defendants have not met this burden.

Although defendants, by affidavit, insist that Genius abandoned the reverse stock split "solely" because of the "sharp decline in the Company's stock price,"[6] Genius's actions suggest that Kuo's lawsuit at least contributed to the board's decision. Almost immediately after Kuo filed her lawsuit, Genius instigated settlement negotiations with Kuo's counsel. Not only does such action suggest that Genius did not consider the suit frivolous, it also suggests that Genius was at least

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[1] *Cal-Maine Foods, Inc. v. Pyles*, 858 A.2d 927, 928-29 (Del. 2004).
[2] *United Vanguard Fund, Inc. v. Takecare, Inc.*, 693 A.2d 1076, 1079 (Del. 1997).
[3] *Id.*
[4] *Id.* at 1080.
[5] *Cal-Maine*, 858 A.2d at 929 (quoting *Allied Artists Pictures Corp. v. Baron*, 413 A.2d 876, 880 (Del.1980)).
[6] Defs.' Br. Opp'n to Pl.'s Fee Application 8, 10.

somewhat concerned about its liability to its potential fractional stockholders. If Genius thought the suit to be frivolous or of minor importance then logic suggests that it would have taken a hard-line approach and moved for an immediate dismissal of the case. The lack of such action provides evidence, which the words of defendants' affidavit fail to rebut, that Kuo's lawsuit at least contributed in part to Genius's decision to abandon the reverse stock split.

Furthermore, the facts of this case cause me to doubt defendants' contention that Genius's decision to abandon the reverse stock split was due solely to the decline in Genius's stock price. Defendants argue that Genius's board of directors received advice from its financial advisor, Goldman Sachs, that because the stock price often falls after a reverse stock split Genius should do the transaction only if it resulted in a stock price of around $15 per share. To achieve such a result, according to defendants, Genius's stock price had to be at least $1.90 per share at the time of the 1 to 8 reverse stock split. Genius argues that because the stock price fell below the $1.90 threshold the transaction would not have achieved its goal. Even if I assume that Goldman Sachs's advice was correct and Genius needed to achieve a $15 per share post-transaction outcome, rather than NASDAQ's required $5 threshold to list securities on its exchange, the problem with defendants' assertion is that they do not state why Genius could only effectuate a 1 to 8 reverse stock split. Why could it not do a 1 to 10 split? Or a 1 to 20 split? At any stock price Genius could have engineered a reverse stock split to achieve its desired outcome of $15 per share. The economics of a stock split are the same regardless of the magnitude of the split. A reverse stock split simply reduces the amount of the stock in circulation, resulting in fewer shares comprising the residual ownership of the company. Defendants have failed to provide sufficient evidence for why Genius needed to obtain a $15 per share outcome rather than NASDAQ's required $5 per share, and why they could only do a 1 to 8 reverse stock split to achieve that goal.

Moreover, in February 2008, after the parties had practically agreed to a settlement based upon the rounding up of the fractional interests, defendants abruptly ended settlement negotiations, arguing that there was insufficient time to present a settlement to the Court before the consummation of the reverse stock split. At that time, Genius's stock was trading at $1.32 per share. Evidence of Genius's willingness to complete the transaction when its stock was trading well below $1.90 undermines defendants' claim that Genius, acting on advice of its

financial advisor, abandoned the transaction solely because its stock price fell below the $1.90 threshold.[7]

The relevant inquiry is whether defendants have rebutted the strong presumption that Kuo's lawsuit did somehow affect or influence Genius's decision to abandon the transaction. Given that Genius immediately engaged in settlement negotiations with Kuo, and has failed to convincingly establish that because of the decline in its stock price it could not have completed the transaction, I conclude that Kuo's lawsuit played at least some part in Genius's decision to abandon the reverse stock split. Accordingly, I find that defendants have failed to establish that no causal connection existed between the initiation of the suit and any later benefit to the stockholders.

I next turn to the amount of the fee award. It has long been the policy of Delaware to "insure[] that, even without a favorable adjudication, counsel will be compensated for the *beneficial results* they produced."[8] This policy exists to "prevent frustration of the remedial policy of providing professional compensation for such suits when meritorious."[9] In arriving at the specific amount for the award, *Sugarland* rejected a more mechanical approach, establishing that the Court must exercise its sound discretion to determine fee awards.[10] 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."[11] This Court has consistently noted that the most important factor in determining a fee award is the magnitude of the benefit achieved.[12]

Plaintiff's counsel is requesting a fee award of $200,000 plus $2,440.67 in expenses. That appears to be an overly generous fee award in light of the benefit achieved and effort expended. In line with the *Sugarland* factors, plaintiff's

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[7] Genius's attempt to complete the reverse stock split in February and March of 2008 immediately preceded Genius's announcement of its negative quarterly financial results on March 17, 2008. The announcement triggered a one-day decline in Genius's stock price of 25%. The stock price has not recovered from this decline.
[8] *Allied Artists*, 413 A.2d at 878 (emphasis added).
[9] *Id.*
[10] *Sugarland Indus. Inc. v. Thomas*, 420 A.2d 142 (Del. 1980).
[11] *In re Abercrombie & Fitch Co. S'holders Derivative Litig.*, 886 A.2d 1271, 1273 (Del. Oct. 26, 2005) (citing *Sugarland*, 420 A.2d 142).
[12] *See, e.g., Seinfeld v. Coker*, 847 A.2d 330, 336 (Del. Ch. Dec. 4, 2000).

counsel has expended modest efforts in this case. Plaintiff's counsel filed its complaint and then immediately entered into settlement negotiations with defendants. No substantive motion was argued before the Court and, in fact, no briefs or papers (beside this motion for fees) were ever filed with the Court. Plaintiff's counsel contends that they spent 140 hours on this case, but they fail to distinguish how many of those hours were spent in filing the motion for fees rather than substantively working for the benefit of Genius's shareholders.

A fee award of $200,000 perhaps would be acceptable if a substantial corporate benefit was bestowed upon Genius's shareholders solely on account of plaintiff's counsel's actions.[13] I am unconvinced, however, that a significant benefit was obtained or that counsel's actions were solely responsible for the aborted transaction. In her complaint, Kuo alleged that the fractional shareholders would not have received fair compensation for their interests that would have been cashed out in the reverse stock split. To remedy this alleged injustice, Kuo sought monetary damages. Kuo did not seek to enjoin the transaction. At most, Kuo was partially responsible for preventing Genius's shareholders from receiving slightly less compensation for their fractional shares than they might otherwise have received if the transaction had been completed. But it is not possible to know how much less Genius's shareholders would have received because no independent appraisal of the shares was conducted. Nevertheless, for purposes of determining a fee award I conclude that such benefit would have been relatively insignificant.[14] A modest benefit obtained with little effort does not warrant a significant fee. Accordingly, based on the *Sugarland* factors, I conclude that plaintiff's counsel is entitled to a fee of $100,000, inclusive of expenses.

## III. CONCLUSION

For the foregoing reasons, I award attorneys' fees to plaintiff's counsel in the amount of $100,000, inclusive of expenses.

[13] A fee award of $200,000 would result in a per hour rate of approximately $1,450 per hour.
[14] Plaintiff's counsel has refused to quantify the value of the corporate benefit they obtained for Genius's shareholders. Defendants, on the other hand, have attempted to calculate this amount, which they contend would have resulted in an aggregate payment of $2,100 for all the fractional interests.

IT IS SO ORDERED

Very truly yours,

William B. Chandler III

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