

LEXSEE 2001 U.S. DIST. LEXIS 7097

**WILLIAM STEINER, individually and on behalf of himself and all others similarly situated, Plaintiff, - v. - DAVID H. WILLIAMS, JOHN D. CARIFA, WILLIAM H.M. DE GELSEY, REBA W. WILLIAMS, HELLMUT LONGIN, PETER MITTERBAUER, PETER NOWAK, REINHARD ORTNER, ANDRAS SIMOR, WALTER WOLFSBERGER, and THE AUSTRIA FUND, INC., Defendants. MARK LEVY, Plaintiff, - v. - SOUTHBROOK INTERNATIONAL INVESTMENTS, LTD., ELLIOT ASSOCIATES, L.P., WESTGATE INTERNATIONAL, L.P., ALEXANDER FINANCE, L.P., and ILLINOIS SUPERCONDUCTOR CORPORATION, Defendants.**

**99 Civ. 10186 (JSM), 99 Civ. 1479 (JSM)**

**UNITED STATES DISTRICT COURT FOR THE SOUTHERN DISTRICT OF NEW YORK**

*2001 U.S. Dist. LEXIS 7097*

**May 31, 2001, Decided**

**May 31, 2001, Filed**

**COUNSEL:** [\*1] For William Steiner: Joel C. Feffer, Wechsler Harwood Halebian & Feffer LLP, New York, New York.

For William Steiner: Gregory E. Keller, Harnes Keller LLP, New York, New York.

For Defendants: John L. Hardiman, Sullivan & Cromwell, New York, New York.

For Defendants: James H.R. Windels, Davis Polk & Wardwell, New York, New York.

For Mark Levy: Jeffrey S. Abraham, Abraham & Paskowitz, New York, New York.

For Mark Levy: Mitchell M.Z. Twersky, Fruchter & Twersky, New York, New York.

For Defendants: Philippe Adler, Friedman, Kaplan, Seiler & Adelman LLP, New York, New York.

For Defendants: John Landis, Foley & Lardner, Chicago, Illinois.

For Defendants: Fruman Jacobson, Sonnenschein Nath & Rosenthal, Chicago, Illinois.

For Defendants: Alan R. Friedman, Kramer Levin Naftalis & Frankel, New York, New York.

For Defendants: David Parker, Kleinberg, Kaplan, Wolff

& Cohen, New York, New York.

For Defendants: Herbert Teitelbaum, Robinson Silverman Pearce Aronsohn & Berman, New York, New York.

For Defendants: Gary Meyerhoff, Sonnenschein Nath & Rosenthal, New York, New York.

**JUDGES:** JOHN S. MARTIN, JR., U.S.D.J.

**OPINIONBY:** JOHN S. MARTIN, JR.

**OPINION:** [\*2]

**MEMORANDUM OPINION AND ORDER**

JOHN S. MARTIN, JR., District Judge:

These two cases present the common and often perplexing question of the amount of fees that should be awarded to counsel who have negotiated a settlement of a derivative or class action litigation.

The equitable fund doctrine provides that a court may award fees to attorneys who have created a common fund or conferred some other substantial benefit on a class of plaintiffs. In part, the rationale of fee awards in these cases is found in the equitable principle that "persons who obtain the benefit of a lawsuit without contributing to its cost are unjustly enriched at the successful litigant's expense." *Boeing Co. v. Van Gemert*, 444 U.S. 472, 478, 100 S. Ct. 745, 749, 62 L. Ed. 2d 676 (1980); see *Amalgamated Clothing & Textile Workers Union v. Wal-Mart Stores*,

*Inc.*, 54 F.3d 69, 71 (2d Cir. 1995). Awarding counsel fees in such cases also serves the salutary purpose of encouraging counsel to pursue meritorious claims on behalf of a class of individuals who could not afford to litigate their individual claims. See *Van Gemert v. Boeing Co.*, 573 F.2d 733, 737 (2d Cir. 1978), [\*3] rev'd en banc, 590 F.2d 433 (2d Cir. 1978), aff'd, *Boeing Co. v. Van Gemert*, 444 U.S. 472, 100 S. Ct. 745, 62 L. Ed. 2d 676, (1980) (Oakes, J. dissenting in part).

While the general principles to be applied in such cases are well-established, the public perception of their application to specific cases has provoked spirited debate, a prime example of which is provided by the majority and dissenting opinions in the Second Circuit's opinion in *Van Gemert*, 573 F.2d at 735-36. Writing for the majority, Judge Van Graafeiland observed:

Class actions, termed by some as "lawyer's lawsuits," see Developments in the Law Class Actions, 89 *Harv. L. Rev.* 1318, 1605 (1976), have received a good deal of criticism, and much of this has been directed at the substantial fees awarded to class attorneys. See, e.g., *Alpine Pharmacy, Inc. v. Chas. Pfizer & Co.*, 481 F.2d 1045, 1049-50 (2d Cir.), cert. denied, 414 U.S. 1092, 94 S. Ct. 722, 38 L. Ed. 2d 549 (1973). Terms such as "golden harvest of fees," *Free World Foreign Cars, Inc. v. Alfa Romeo, S.p.A.*, 55 F.R.D. 26, 30 (S.D.N.Y. 1972), [\*4] "astronomical fees," M. Blecher, Is the Class Action Rule Doing the Job? (Plaintiff's Viewpoint), 55 F.R.D. 365, 366 (1972), and "enormous fees," Comment, 54 *U. Det. J. Urb. L.* 598, 611 (1977), are used to describe the allowances, which often run into the millions of dollars. Critics point particularly to over-generous applications of the equitable fund doctrine, by means of which massive fees are awarded attorneys with too little regard for the interests of the class members. See *City of Detroit v. Grinnell Corp.*, 560 F.2d 1093, 1098 (2d Cir. 1977). This criticism, much of which is justified, prompts careful inquiry into whether it would be a misapplication of the equitable fund doctrine to permit counsel herein to collect part of their fees and expenses from the allocable shares of class members who claim none of the proceeds of the recovery.

Id.

Dissenting from this view, Judge Oakes responded:

I first disavow the rhetoric of the majority directed at class actions and "class action lawyers." Class actions often are valuable tools for the individual plaintiff seeking justice against a defendant whose resources [\*5] enable it to obtain the highest-paid lawyers to engage in such extensive discovery and other litigation techniques that one, two or three plaintiffs otherwise could never afford to conduct the lawsuit.

573 F.2d at 737.

The debate over the size of the fees awarded to counsel in such cases continues to this day. See, e.g., *Goldberger v. Integrated Res., Inc.*, 209 F.3d 43 (2d Cir. 2000); Richard Karp, Plaintiff Cry: Securities Class-Action Suits Recover Pennies for Victims, Pay Lawyers Big Bucks, *Barrons*, Apr. 9, 2001, available at 2001 WL-BARRONS 2281216; Getahn Ward, Judge OKs a Settlement in CCA Suits \$130M Deal Means Windfall for Attorneys, *The Tennessean*, Feb. 13, 2001, at 1 E, available at 2001 WL 7056249; Richard B. Schmitt, Stronger Role Is Urged for Judges in Class Actions, *Wall St. J.*, Nov. 1, 1999, at B5, available at 1999 WL-WSJ 24920019.

The two fee applications which the Court considers in this opinion are good examples of the balancing process that confronts the courts in such cases. In the first case, *Steiner v. Williams*, this Opinion will constitute the Court's ruling on counsel's fee request. In the second case, [\*6] *Levy v. Southbrook*, the Court granted the fee request from the bench at the time that it approved the settlement, but, because of the importance of the public perception of the award of counsel fees in such cases, the court indicated that an opinion setting forth the reasons for the award would be filed.

#### A. *Steiner v. Williams*

In this case, counsel undertook difficult litigation hoping that its attack on the defendants' restrictive bylaw provisions would aid an insurgent shareholder's efforts to gain control of The Austria Fund, Inc. These efforts became frustrated when the insurgent withdrew from the battle. As counsel explained in a letter to the court in support of their fee application:

Although plaintiff believed, and still believes, that he would prevail if the action was litigated to a conclusion, he agreed to settle because resolution of all of the corpo-

rate governance issues in question would not provide any additional benefit to the Fund in absence of a viable contest for control.

(Letter from Feffer to Martin, J. of 4/13/01, at 1-2.)

Thus, Plaintiff settled the action by accepting the agreement of the defendants to submit to the Fund's shareholders [\*7] a proposition calling for the amendment of the Fund's bylaws to delete the provision that required the Fund's Independent Directors to have a significant connection to Austria. After the Court approved the settlement, n1 the proposition was placed before the shareholders and was defeated, with only 15% of the shareholders voting in favor and 54% voting against.

n1 Approval was given only after the Court indicated that it would not approve the settlement unless the release that the class members were required to give was narrowed to conform to the limited relief provided for in the settlement.

While recognizing the limited nature of the relief that was obtained by their efforts, Plaintiff's counsel ask the Court to award them a fee of \$175,000.00 and expenses of \$5,529.16 to be paid by the defendants, who have agreed not to oppose the application.

#### B. Levy v. Southbrook

While the results obtained through counsel's efforts in *Steiner v. Williams* were underwhelming, counsel's efforts here provided [\*8] a bonanza to the corporation which was the beneficiary of this derivative action seeking the recovery of short-swing profits.

After making a demand on the Board of Directors of Illinois Semiconductor Company, which was rejected, Plaintiff's counsel commenced an action to recover short-swing profits from certain major shareholders of the company who had the ability to acquire more than 10% of the company's outstanding shares by converting their preferred stock into common stock. However, there was a provision in the defendants' Purchase Agreement, the so-called "conversion cap," that limited their conversion rights so as to prohibit them from owning more than 4.9% of the company's common stock at any one time. After the defendants moved to dismiss the complaint claiming that the 4.9% restriction on their conversion privileges insulated them from § 16(b) liability, Plaintiff moved to amend or supplement the complaint to allege that certain of the defendants should be deemed to be directors of the corporation by reason of their having been allowed to designate a director, and that those shareholders were members of a group whose aggregate shareholdings ex-

ceeded 10%. Plaintiff also added [\*9] a claim that the defendants dominated the company's board of directors and caused the directors to breach their fiduciary duty to the company by entering into transactions with the company that amounted to a waste of the company's assets.

The parties agreed that the Court should defer a ruling on the conversion cap issue pending a decision of the Second Circuit in a related case. The Court ruled on the remaining issues, denying the defendants' motions to dismiss based on a finding that there were factual issues presented.

After the Securities and Exchange Commission (the "SEC") filed an amicus brief in the Second Circuit in the related case that supported the defendants' position that the conversion cap provided protection from § 16(b) liability, the parties reached a settlement. Against what at the outset seemed overwhelming odds, Plaintiff's counsel obtained a settlement that resulted in total payments to the corporation of twenty million dollars. Counsel claimed that the settlement amount represented approximately 25% of the maximum possible recovery.

With the support of counsel for the corporation, which was the beneficiary of the settlement, Plaintiff's counsel applied for [\*10] a fee of 30% of the recovery, or \$6,000,000.00.

#### DISCUSSION

The first question that one might ask is: "Why should the Court care what fee is paid in these cases, since the payment will not come out of the plaintiffs' pockets but is being made by corporations who are represented by able counsel?" While as a general matter the courts do not monitor the contractual arrangements made by consenting adults or entities, courts do have a responsibility to monitor carefully fee agreements between plaintiff's counsel and defendants in class and derivative actions. As the Second Circuit observed in *Kaplan v. Rand*, 192 F.3d 60 (2d Cir. 1999):

It is no secret that in seeking court approval of their settlement proposal, plaintiffs' attorneys' and defendants' interests coalesce and mutual interest may result in mutual indulgence.

*Id.* at 67 (citing *Bell Atl. Corp. v. Bolger*, 2 F.3d 1304, 1310 (3d Cir. 1993)). Thus, these cases present a danger of "collusion—the temptation for the lawyers to agree to a less than optimal settlement 'in exchange for red-carpet treatment on fees.'" *Goldberger*, 209 F.3d at 53 (quoting [\*11] *Weinberger v. Great N. Nekoosa Corp.*, 925 F.2d

518, 524 (1st Cir. 1991)). As a result, the Second Circuit has advised that district judges acting on fee applications in such cases act "as a fiduciary who must serve as a guardian of the rights of absent class members." *City of Detroit v. Grinnell Corp.*, 560 F.2d 1093, 1099 (2d Cir. 1977), abrogated on other grounds by *Goldberger*, 209 F.3d 43 (2d Cir. 2000); see also *Jones v. Amalgamated Warbasse Houses, Inc.*, 721 F.2d 881, 884 (2d Cir. 1983) ("The judge's duty to safeguard the public interest is especially important when no class members are likely to object . . .").

There are two separate approaches that may be used in fixing the amount of the successful attorney's fee: one is simply to award counsel a percentage of the amount recovered; the other, the lodestar method, starts with the reasonable and necessary time charges of the attorney and then adjusts that figure up or down on the basis of various factors. In *Goldberger*, the Second Circuit instructed:

No matter which method is chosen, district courts should continue to be guided by the traditional [\*12] criteria in determining a reasonable common fund fee, including: "(1) the time and labor expended by counsel; (2) the magnitude and complexities of the litigation; (3) the risk of the litigation . . .; (4) the quality of representation; (5) the requested fee in relation to the settlement; and (6) public policy considerations."

*Goldberger*, 209 F.3d at 50 (quoting *In re Union Carbide Corp. Consumer Prods. Bus. Sec. Litig.*, 724 F. Supp. 160, 163 (S.D.N.Y. 1989)).

While all of these factors must be evaluated, in the end "the fees awarded in common fund cases may not exceed what is reasonable" under the circumstances. 209 F.3d at 47. Applying the test of reasonableness to the circumstance of these two cases leads to starkly different results.

#### A. *Steiner v. Williams*

Although the settlement in this action did not involve the payment of money by the defendants, counsel may nonetheless recover a fee if the settlement conferred a substantial non-monetary benefit on the corporation's shareholders. See *Amalgamated Clothing & Textile Workers Union v. Wal-Mart Stores, Inc.*, 54 F.3d 69 (2d Cir. 1995).

Applying the six-factor test [\*13] set forth in *Goldberger*, it is clear that: (1) counsel expended considerable time and labor pursuing this action; (2) while the magnitude of the litigation was not great, it did involve

complex issues; (3) the risk of the litigation was substantial; and (4) the quality of representation was excellent. However, counsel's request for a fee of \$175,000.00 founders on the fifth and sixth factors, i.e., the balancing of the requested fee against the value of the settlement and public policy considerations.

In order to award Plaintiff's counsel a fee, the Court must find that counsel's efforts have conferred a substantial benefit on the class. As Judge Decker observed in *Illinois v. Harper & Row Publishers, Inc.*, 55 F.R.D. 221, 224 (N.D. Ill. 1972):

If Rule 23 is to be preserved against deserved criticism, some attempt must be made by the court to suit the award of fees to the performance of individual counsel in light of the size of the settlement. Otherwise, the attorneys who are taking advantage of class actions to obtain lucrative fees will find themselves vulnerable to the criticism expressed in the Italian proverb, "A lawsuit is a fruit tree planted in [\*14] a lawyer's garden."

See also *Free World Foreign Cars, Inc. v. Alfa Romeo, S.p.A.*, 55 F.R.D. 26 (S.D.N.Y. 1972) (Weinfeld, J.).

In this case, counsel's efforts were diligent and well-motivated, but the only fruit of that labor was an agreement that the corporation place before the shareholders an extremely limited proposal to amend the by-laws. Plaintiff's counsel relies heavily on *Amalgamated Clothing & Textile Workers Union v. Wal-Mart Stores, Inc.*, in support of the argument that obtaining the agreement of a corporation to place a proposition before the shareholders for their vote may be a substantial benefit that justifies the award of counsel fees. However, Wal-Mart is distinguishable on several grounds.

First, in Wal-Mart, the plaintiffs won a summary judgment motion which granted them everything they sought in their complaint, i.e., an order requiring the corporation to include in its proxy material a proposal that would require the company to distribute a report on its equal opportunity and affirmative action policies. See *Wal-Mart*, 54 F.3d at 70-72. Here, however, the relief obtained in the settlement was substantially [\*15] less than Plaintiff sought in the complaint. Whereas the complaint in this case sought a declaration that certain defensive bylaw amendments adopted by the company in response to an insurgent's challenge to management were null and void, the only relief obtained by the settlement was the agreement to submit a relatively insignificant bylaw proposal to the shareholders. Thus, while the plaintiffs in Wal-

Mart won in court all that they sought in the complaint, the settlement here achieved none of the plaintiff's major goals. Indeed, the relief obtained here is so insubstantial that the Court is left with the nagging impression that, in an attempt to rid themselves of litigation that was going nowhere, the parties searched for a result that would have the least possible impact on the corporation but would still allow counsel a basis for arguing that they had conferred a benefit on the shareholders. Furthermore, Plaintiff's counsel has been admirably candid in acknowledging that once the insurgent shareholder withdrew from the battle "resolution of all of the corporate governance issues in question would not provide any additional benefit to the Fund."

Not only is the result here [\*16] far less substantial than that achieved by the plaintiffs' counsel in *Wal-Mart*, but the fee which counsel seeks here is more than three times the fee awarded in that case. See *Wal-Mart*, 54 F.3d at 71. Moreover, subsequent to *Wal-Mart*, in *Kaplan v. Rand*, 192 F.3d 60 (2d Cir. 1999), the Second Circuit, through the same author, Judge Miner, reversed a decision awarding counsel fees because it found that the settlement did not confer a substantial benefit on the shareholders. In this case, the resolution placed before the shareholders would have provided a limited benefit to the shareholders even if it had been adopted. The fact that it was rejected by a better than three-to-one margin of the voting shareholders does not necessarily reflect the value of placing this proposal before the shareholders, but it does suggest that the defendants knew that they were not giving up anything of value by agreeing to place this proposal before the shareholders.

While the right to vote on the resolution in question had some value and the Court could, with the aid of further submissions from the parties, place a monetary value on the benefit to the shareholders, [\*17] it is obvious that the value would be so small that any fee awarded as a percentage of that value would be an insult to counsel rather than a reward for their efforts. Thus, the Court is persuaded that it is better to award counsel no fee than to award one that denigrates the quality of their work. However, because a benefit was conferred on the shareholders, it is appropriate to order the corporation to reimburse counsel for their expenses in the amount requested, \$5,539.16.

Unfortunately, and despite the Court's respect for both the quality of the legal work of Plaintiff's counsel and for the candor counsel has demonstrated in connection with the fee application, the Court cannot conclude that counsel's efforts have resulted in a substantial benefit to the corporation. While the Court does not enjoy being cast in the role of Ebenezer Scrooge, it cannot abandon its fiduciary duty to protect the interest of shareholders or its obligation to maintain the public's confidence that deriva-

tive and class action litigation is not conducted solely for the benefit of lawyers. See *Schechtman v. Wolfson*, 244 F.2d 537, 540 (2d Cir. 1957) ("There should be some check on derivative [\*18] actions lest they be purely strike suits of great nuisance and no affirmative good . . .").

In applications for fees in cases such as this, counsel for plaintiffs regularly argue that they are entitled to fees well in excess of the amount of their time charges because in taking on contingent fee litigation they run the risk that, if the litigation is not successful, they will recover nothing. That argument has merit, and this case may be cited in the future as an example of attorneys who toiled diligently and well in a cause that ended without a substantial benefit to the corporation's shareholders and, therefore, without a fee to counsel.

#### B. *Levy v. Southbrook*

*Levy* represents the opposite extreme in the awarding of fees under the equitable fund doctrine. Counsel here is receiving a fee of \$6,000,000.00 because the corporation recovered \$20,000,000.00 which never would have been received were it not for counsel's diligence and ingenuity.

Turning specifically to the six factors to be considered: (1) although counsel expended considerable time and labor pursuing this action, counsel has conceded that the time charges were relatively insignificant when compared to [\*19] the fee requested; (2) while the magnitude of the litigation was not great, the factual issues were complex and the legal theories were novel and difficult; (3) the risk of the litigation was substantial; (4) the quality of representation was excellent; (5) balancing the requested fee of \$6,000,000.00 against a recovery of \$20,000,000.00 does not indicate that the request is excessive; and (6) given the important public policy goal served by § 16(b), the fee awarded should be substantial in order to encourage counsel to bring such suits in the future.

While all of the factors are important, the Second Circuit noted in *Goldberger*:

We have historically labeled the risk of success as perhaps the foremost factor to be considered in determining whether to award an enhancement.

*Goldberger*, 209 F.3d at 54 (citations omitted).

In undertaking this litigation, counsel took a tremendous risk that, in the end, nothing would be recovered. The theory on which Plaintiff's original complaint was based, that the conversion cap was invalid, was novel and risky. Indeed, all of the courts that had considered the

2001 U.S. Dist. LEXIS 7097, \*19

theory rejected it, and ultimately the SEC refused [\*20] to endorse it. The other theories on which Plaintiff relied were fact-intensive and hotly contested. Indeed, in denying the defendants' motion to dismiss, the Court noted that "it may well be that ultimately the complaint will not withstand a summary judgment motion or a trial . . . ."

Here, the shareholders of Illinois Semiconductor Company received a \$20,000,000.00 benefit as the sole result of the diligence and sagacity of Plaintiff's counsel.

Given the risks that counsel faced at the outset of their labors, awarding them 30% of the fruits of their labors is entirely appropriate.

**SO ORDERED.**

Dated: New York, New York

May 31, 2001

JOHN S. MARTIN, JR., U.S.D.J.