

A VIEW OF REPRESENTATIVE ACTIONS, DERIVATIVE
AND CLASS, FROM A PLAINTIFF'S
ATTORNEY'S VANTAGE POINT

BY IRVING R. MORRIS*

I have enjoyed my presence here this morning. I regret I was not able to be here for your sessions yesterday. I compliment the people who have been in charge of making the arrangements. They have been very careful about most things. It may not be apparent to you but they've performed a service, for example, for the panelists. Each panelist has before him a handsome name card, visible at least through the first few rows. On the other side, so we shouldn't forget who we are, our names are printed, for which I personally am grateful.

When I say I enjoyed the session, I thought my good friend Dick Corroon's passionate presentation of the Levien against Sinclair litigation¹ was most moving when you realize how close he came to so much. I must feel for Richard.

Norm Veasey commented twice to you that the significant case of *Lutz v. Boas*² is not in your outline. The fact is it is in your outline, but not in Norm's section of it. You will find it in my section.³ It is indeed a significant case. Norm also made reference to the fact that the *Corporate Director's Guidebook*⁴ is not in the outline, but he should have noted that it is in the outline again in my section.

I ought to tell you where I come from to the issues under discussion at this session of the seminar. After law school I clerked for a couple of years for the late Paul Leahy, who was chief judge of the United States district court here in our district. Judge Leahy is the author of the case of *Speed v. Transamerica*,⁵ which is a granddaddy case in terms of responsibility of directors. It's a case that the Delaware Supreme Court the other day in *Lynch v. Vickers Energy Corporation*,⁶ reversing the lower court, at page 8 of the slip opinion, cited in commenting upon special knowledge which insiders have and what they may or may not do about it. The first citation the supreme court used is *Speed v. Transamerica*. I clerked with

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1. *Sinclair Oil Corp. v. Levien*, 280 A.2d 717 (Del. 1971), *aff'g*, 261 A.2d 911 (Del. Ch. 1969).

2. 39 Del. Ch. 585, 171 A.2d 381 (Ch. 1961).

3. Appendix G, this issue, *infra* at 401.

4. 32 Bus. Law. 5 (1976).

5. 235 F.2d 369 (3rd Cir. 1956).

6. No. 4605 (Del. Ch. Nov. 19, 1974).

Judge Leahy when *Speed* was written. Since clerking I've traveled — I don't know whether one would want to make a subjective judgment as to up or down — but I serve on the committee Norm Veasey referred to as the "august" committee. There are 23 of us who serve on it. It's the Committee on Corporate Laws of the ABA Section on Business, Banking and Law. My presence on that committee, I should add, is explained in the following way so that you won't think I'm completely over on the establishment side. Sam Arsht, who has labored long and arduously and well for that committee, came to me a couple years ago, and said he was concerned that there was no plaintiffs' lawyer on the group. He inquired whether or not I would be willing to serve. I said I would be honored to serve. So, I'm a minority voice on that committee. I lose votes roughly 22 to 1, but I try to make my presence known.

When our chairman and Dick Corroon talked about "speedy justice" in Delaware, I'm struck a wee bit by the lethargic movement in the particular case they cited. As I recall in one instance roughly 20 years ago, I filed a case on November 1st and we had the hearing on the settlement before then Chancellor Seitz on December 23rd. I think that was movement in the extreme. The court approved the settlement by the way and it was a good result.

My topic is "A View of Representative Actions, Derivative and Class, from a Plaintiff's Attorney's Vantage Point." There are four subsections to it. I suppose they could have been entitled "What Is The Animal?", "What Do You Do If One Attacks You?", "How Do You Get Rid Of It?", and, finally, "How Do You Avoid An Attack?" For want of anything else to do, I'll try to follow the outline. I do not consider my presentation to be above interrupting at all, so that if you would like to ask questions as I speak, please do not hesitate to interrupt. I'll give you my microphone so we can stimulate some discussion. Generally, when I've participated either as a registrant or a panelist in sessions of this kind, there have been many more questions than at least I've seen elicited so far from the people in attendance. My own experience is that at the very least there are questions masked in hypotheticals that are burning issues in one's shop or in one's corporation. Apparently the only person here in this crowd who has any such problem is Don Pease. I think he got about as good a response as one could expect on the questions he asked Dick Corroon. I dare say at 3:00 o'clock this afternoon Dick will tear himself away from this meeting if Don wants to arrange the conference with the people over at Du Pont who have the problem.

The first topic is "What is the animal we are talking about?" Representative suits are of two kinds. There is a derivative type and

there is a class type. The derivative type is one brought by a stockholder, who has to be a stockholder when he brings the action, has to have been a stockholder when the wrongdoing of which he's concerned and alleging occurred, and must remain a stockholder throughout the litigation. If there is any break in this continuous holding, the stockholder will be out of court provided the break is made known. When I say "provided the break is made known," I think of the case of *Paolozzi v. United Industrial Corporation*,⁷ in which Dick Corroon's partner, Dave Anderson, was involved. The fact is about half of the Delaware Bar got involved in it. Generally on the plaintiff's side you walk into a courtroom and you're there and it seems the world is sitting across the room from you in opposition. In any event, I had the case with a lawyer from New York and I had responsibility for its prosecution. I had met my client, the plaintiff, Colonel Paolozzi, and, indeed, he had been deposed early on in the litigation. The case went along and we made a partial settlement. The case continued and, finally, we reached an agreement with most of the remaining defendants — my recollection is save one — and that fellow's lawyer came in objecting to the settlement that we had reached with the remaining defendants. He insisted that he wanted further discovery, and, particularly, he wanted to examine the plaintiff. I noted the plaintiff had already been examined, but if he wanted to examine him again, there was no problem. I told the court we didn't even have to take the time of the court to set a date. The other lawyer and I would agree on a date and he could depose Colonel Paolozzi. The court was satisfied with that, and the lawyer and I went out in the corridor, I asked him for a couple of dates, he gave them to me, and I said I'd get back to him promptly. I called my forwarding lawyer in New York, told him that the defendant, now an objector to our settlement to substantially wrap up the litigation, wants to examine Colonel Paolozzi again. I asked him to call the Colonel and see whether either of the two dates I had been given were convenient, and, if not, to give me some other dates and we'll square this away promptly and get it behind us. He said, fine, he would call the Colonel. Roughly about an hour later my forwarding attorney called back and told me we had a problem. I asked what was the problem. He said Colonel Paolozzi died 18 months ago. That, indeed, presented a problem because we had already presented our settlement to the court. I immediately called then Chancellor Duffy and told him the facts. The facts prompted an opinion by Chancellor Duffy in which he suggested that a derivative case is not entirely the plaintiff's attorney's handiwork. A plaintiff

7. No. 1410 (Del Ch. Mar. 19, 1971).

does indeed serve a role in such litigation. The case had a happy ending. I was not summarily drummed out of the courtroom. I was lead counsel in the case, and the other plaintiffs' lawyers thought that it might be in the interest of everyone if I remained, and I did, and we eventually resolved the litigation.

The attitude of our court expressed in *Paolozzi v. United Industrial Corporation* should be compared with *Saylor v. Livesay*⁸ in the United States District Court for the Southern District of New York. In *Saylor*, a plaintiff was not happy with a settlement his lawyer had struck, believing it to be a good one, and fired the lawyer. The plaintiff objected to the settlement and didn't even want his lawyer to present it. The New York court's attitude was that the wrong was done to the corporation. The wrong did not "belong" in a derivative case to the plaintiff stockholder. Accordingly, the New York court's view was that the settlement should be presented, and if it were fair, as to which the court would make the judgment, then it would be enforced. In short, a plaintiff stockholder in a derivative case really doesn't have a veto power over whether or not a settlement should or shouldn't be made. I don't know that our courts have ever had the peculiar situation of the *Saylor* litigation before them.

Turning again to the outline, I move to the observations made about a derivative action appearing at pages [387] through the top of [391].⁹ The plaintiff stockholder need not be a stockholder of record. The plaintiff stockholder can be a holder who has his shares in the hands of a broker, and if a wrongdoing occurs, he can assert it. That makes good sense because he is indeed the beneficial owner and he has the economic interest. The record title holder, if he doesn't have the beneficial interest, may not be as intimately excited when wrongdoing occurs. The point about continuous ownership, I think I've covered.

You get into some interesting situations when the suit is brought and the outraged defendants think that there is no merit to it, and some situations where the defendants try to take over the litigation. Now, obviously, that cannot take place in any situation where the directors themselves are named parties defendants, because letting the defendants take over the case would leave the litigation in the hands of the defendants, and it's not been known that such a posture of a party defendant is one that results in a vigorous prosecution. Accordingly, absent a showing that it is truly an independent board of a corporation, the control of the litigation will remain in the

8. 274 F. Supp. 253 (S.D.N.Y. 1967), *rev'd*, 391 F.2d 965 (2d Cir. 1968).

9. Appendix G, this issue, *infra* at 387-91.

hands of the plaintiff stockholder who brings the suit and his lawyers. There have been efforts to take over litigation. In the *United Industrial* litigation the defendants attempted to do so but were not successful.

The *Aaron v. Parsons*¹⁰ litigation is another case where the corporation did act to prosecute the claim filed by the plaintiff stockholder and that has an interesting sidelight. I didn't cite *Aaron v. Parsons* in the section on fees in the outline, but it does have some bearing there in that the lawyer who filed the complaint — and thereafter the company in effect took over the litigation — I think it was out of state where they prosecuted and resolved it — sought a fee for his work. Our court of chancery recognized the plaintiff's attorney's effort and awarded him what the court thought was a reasonable allowance given the effort expended. The lawyer was decidedly disappointed with the allowance and appealed to our state supreme court seeking a larger allowance. The supreme court allows broad discretion to the trial bench and our court of chancery and said, in effect, the chancellor made his judgment and that's the end of the matter and rejected the appeal.

The abandonment of any litigation in Delaware cannot just be done unilaterally if a plaintiff decides in effect he's not going to move the litigation along or if his lawyer decides that he has other fish to fry. The cases are not dismissable either as a derivative or class action in Delaware without there being a notice except under certain circumstances.

Delaware's rules, including rules 23 and 23.1,¹¹ are closely fashioned after the federal rules. There are some differences, and here in the matter of notice is one. I think our Delaware rule makes much more sense than the federal rule. If you turn to page [398] — that's the bottom page in your outline¹² — you'll see the point that I'm making here about notice requirements under Delaware law. In Delaware we provide for an exception that is to me an ideal vehicle for getting rid of a case where you not infrequently have the following situation: You believe that a certain set of facts is true, you file an action, you get into discovery, and lo and behold you find the facts that you thought were true just turn out not to be so, or you can't prove them, and then you have the problem "What do you do with the action?" If you have to give a notice that will go out to all the stockholders in a derivative action under rule 23.1, or a notice

10. 37 Del. Ch. 184, 139 A.2d 365 (Ch.), *aff'd*, 37 Del. Ch. 407, 144 A.2d 155 (Sup. Ct. 1958).

11. DEL. R. CIV. PRO. 23, DEL. R. CIV. PRO. 23.1.

12. Appendix G, this issue, *infra* at 398.

that will go out to all the class members in a rule 23 case, you're going to immediately find that that is quite an expensive undertaking. The plaintiff is not about ready to encourage engaging that cost. The defendants and the corporation or corporations involved are not happy about picking up such a tab, and the last thing they want to do is advertise charges of wrongdoing, especially charges of wrongdoing which even the plaintiff says are not true. What our court of chancery has done is to provide in our rules 23 and 23.1 a procedure whereby, if the action is to be dismissed without prejudice as to the other stockholders in a rule 23.1 case, or to the other members of the class in a rule 23 case, and to be dismissed with prejudice to the plaintiff only, then the court is prepared to dismiss the case without notice, provided that no compensation has passed either directly or indirectly to the plaintiff or to the plaintiff's lawyer. Generally, our courts require an affidavit that there is no compensation passing and indeed no promise to pay any compensation. In short, the mechanism prevents a buy-out and at the same time affords a way of disposing of litigation that no one is really interested in prosecuting.

I turn now to the differentiation between a derivative action, which I talked about up to now substantially, and a class action. Both are representative actions. A derivative action is one where the plaintiff stockholder comes forward and asserts a right which he derives from the corporation itself because of the wrong to the corporation and the failure of the corporate management to take any action to remedy the alleged wrong. A class action is different in that the persons in the class have been injured as opposed to the corporation itself. In a class litigation the corporation involved may be and frequently is a real defendant. A typical situation giving rise to a class action occurs in a merger where a corporation is going out of existence, its stockholders receive a sum of money and are no longer stockholders of the entity in which they invested, which has gone out of existence or which has been merged out, and an attack is made that the price paid to the stockholders was not fair. The stockholders can band together as a class and the real defendant would be the corporation that survived that merger. A recent example of such a situation is *Lynch v. Vickers*,¹³ i.e., *Vickers II* to distinguish it from *Vickers I* in which the supreme court handed down its opinion this past Tuesday, which opinion is in your materials.

13. No. 70, 1977 (Del. Ch. Oct. 18, 1977).

In the outline at pages [391] through roughly the middle of [392]¹⁴ there appears essentially a restatement of what is in rule 23.¹⁵ I don't propose to take the time to go through each one of those items because in the time that is allotted to me I think there are some more interesting things to talk about — for example, fees. Generally, people like to talk about fees. Or another subject, "What do you do indeed if you are sued or attacked by this animal."

My friend and able lawyer from Chicago, Leo Herzl, answers the question as to what you should do and he has said this in print, and he says it in one word. He says "settle" and move on, and Leo is quite an able fellow. Indeed in the *Vickers* litigation we tried unsuccessfully to settle and now we just have to be content with a judgment, shortly I hope, in favor of the plaintiff, but sometimes those things happen.

If you are a secretary of a corporation that at the present time has never been sued and you don't have a procedure that is in place now that can be followed in the event of litigation, I suggest that when you leave here and return to your office you make yourself a hero by suggesting the prompt adoption of a procedure that would be followed in the event of litigation. The thought, for example, that a chief executive officer would learn that his company has been sued by picking up his morning paper or *Wall Street Journal* boggles my mind. I dare say he would wonder why he wasn't informed.

In the outline we've suggested certain things that might be considered as part of a procedure to be adopted and followed in the event of litigation. Essentially the procedure is notification to appropriate people and the development of a mechanism for monitoring the litigation. There are some practical techniques suggested. When a corporation is sued, I shouldn't think it's any different then when an individual is sued. The lawyer who is retained to represent the corporation has to know the facts, but somebody has to assemble those facts, somebody has to get the documents, somebody has to say "These are the people who know about the charges that have been made." Assembling the material is critical. You don't want to leave your lawyer in the unhappy predicament of learning the facts while he is attending the deposition of the chief executive officer and the facts are brought out by the plaintiff's lawyer. That can be a startling experience. So, accordingly, there has to be a somebody with the authority and capability of assembling the material in a form that is available and easily retrievable.

14. Appendix A, this issue, *infra* at 391-92.

15. DEL. R. CIV. PRO. 23.

The problem of securing documents from a corporation where the attorney/client privilege is asserted in a derivative or class action warrants comment. What has been developing — and in Delaware it is still a matter of first impression — is the extent to which the attorney/client privilege attaches to documents where the person seeking them is a plaintiff-stockholder or a former stockholder. In short, you have the interesting issue where a document was generated as a result of a conference between house counsel and an executive of a corporation, whether or not the document has to be disclosed to a plaintiff in a derivative or class action. What is occurring, and increasingly so, is recognition by the courts of a dual responsibility that the lawyer and the executive have by reason of their fiduciary responsibility. Not only does an executive manage the corporation with loyalty to it, but he manages the corporation on behalf of those people who have invested their money in the corporation. I would expect in line with those cases that we will see our judges in Delaware recognizing that dual position.

What do you do after the “animal” has attacked and how do you get rid of it? That’s the third section in the outline beginning at page [393].¹⁶ The section concerns the settlement of derivative and class representative actions. I think earlier in my remarks I used the pronoun “I” and then now I’ve gone to “we.” May I hasten to say that the reason I’ve done that is that Ira Conrad of my office and Richard Laibstain, who is a third year law student at Delaware Law School, participated in the preparation of this outline. I should like to thank them and note that any errors are theirs, and for any accuracies in the outline, I’ll take responsibility. Richard, incidentally, just before the start of this session, asked me if we are now ready for the high point of the conference. We’ll know a little later on about that.

The settlement of a derivative or class action is one that has been addressed by our courts in Delaware on numerous occasions. What you come down to is really a discretion factor that lies with both the trial court and the supreme court. The rules that are applicable were stated initially in the case of *In re Ortiz*.¹⁷ The rules have been repeatedly reenunciated and approved, and there have been some refinements to them, but I think what it all comes down to is that if you have effected a settlement which is fair, and when I say fair, I mean a negotiated one, and you present it to our court of chancery, and if those terms are fair and reasonable and satisfy the court of chancery, you’re pretty well home on it. Once our court of chancery has approved, and I stand to be corrected by my betters

16. Appendix G, this issue, *infra* at 393.

17. *In re Ortiz*’ Estate, 26 Del. Ch. 240, 27 A.2d 368 (Ch. 1942).

who are on the panel and the folks here in the audience, but I know of no approval of a settlement by our court of chancery which has ever been reversed by the supreme court. Moreover, I do not know of any case where our court of chancery has rejected a settlement where there has even been an appeal to the supreme court to seek a reversal of that rejection. There is wide discretion in the court of chancery as to what it will do when a settlement is presented to it.

Our courts have rejected settlements. It has not occurred with great frequency, because I think that the lawyers who have been involved in cases in the court of chancery know our judges, they know their cases, they have a sense of what is fair and what will pass muster. The instances of rejection, indeed, are few and of the four I know about, three of them are ones where the terms of the settlement as initially proposed and not approved by the court were thereafter renegotiated, improved, and the court in each instance approved the settlement as modified. The fourth instance is one that is current. It unhappily occurred earlier this year, and I am hopeful that the settlement will be improved and upon presentment will pass muster before the court. We're still negotiating, however.

The outline, I suggest, probably gives you as much detail, perhaps more, than what you might need as to the effect of a settlement. The effect of it is, of course, to provide *res judicata*. Our supreme court in *Rome v. Archer*¹⁸ held that, once litigation is settled and the settlement approved, anybody who was involved in the alleged wrongdoing is entitled to a release. In Delaware our courts take the view that there is no point in settling a case and then find it crop up again under a different guise with an attempt to go into the same set of facts which underlay the settled action.

The trial court's function is essentially that of exercising a business judgment as to whether or not the settlement as proposed is fair. The factors taken into account appear in the outline.¹⁹ The settlement of a case, our courts have frequently said, is not a rehearsal for a trial and it is not permitted to become even a mini-trial. In short, if an objector comes in and says he thinks there is great merit in the plaintiff's complaint as initially alleged, and here this plaintiff is willing to settle the case, and the objector wants to go full throttle on discovery, he will not have that opportunity in Delaware. If, however, the objector comes in and he is specific and has a certain precise area for discovery, our courts will give him an opportunity to do so. Our courts, however, will not permit the settlement procedure to be converted into a trial.

18. 41 Del. Ch. 404, 197 A.2d 49 (Sup. Ct. 1964).

19. Appendix G, this issue, *infra* at 396.

The role of our supreme court, however, in reviewing a settlement which has been approved over objection and then the objector takes an appeal to the supreme court — that has happened on a few instances but I don't know of any successful instances — is not to sit and decide anew whether or not that settlement that was approved by the trial court was fair or unfair. Rather, the supreme court views its role as one of looking at the record, reading what the trial court has said and making a judgment as to whether or not the trial court has abused its discretion. Our supreme court, and I think quite properly so, gives wide latitude to the trial court's judgment in passing upon a settlement. I suppose that some egregious situation could be conjured up where our supreme court would reverse the court of chancery's judgment in passing upon a settlement, but I don't think it would happen in Delaware with responsible lawyers as well as the able members of our trial bench. So I don't expect that we're going to have much law on that subject and that our present law, although not codified as such, as a practical matter is going to remain as stated in the outline.

The notice difference that I have commented upon earlier appears at page [398] in the outline²⁰ and we need not take of our time again about that.

Let us talk about counsel fees. In these settlements you have to assume a basic fact, namely, the litigation cannot be settled unless there is a benefit that has been obtained by that settlement. If a benefit is obtained, then the plaintiff is entitled to have his lawyer's fees paid and the expenses incurred in the prosecution of the case reimbursed to him.

The way the matter of fees comes up is, of course, the lawyers make an application to the court to be allowed a counsel fee and the reimbursement of the expenses of the litigation. Most cases, and I would say it is the rare exception, are undertaken on the plaintiff's side on a contingency basis. The full risk that the lawyer assumes is that he can work hard and long and arduously and not achieve a benefit — in which case that's his problem. If, on the other hand, he achieves a benefit, then he will be paid. Our courts, I would say, have been responsive to the recognition that derivative and class litigation, if it results in a benefit, should be rewarded as the effort should be and handsomely so. The reasons are that the risks are there, the opposition encountered generally is the cream of the crop on the other side, and if one is successful in obtaining a good result, then, indeed, recognition should be given to it in that form of compensation regarded by our society as the test of success, i.e., money.

20. *Id.* at 398.

The court, not the parties, makes the determination of what the allowance may be. I can have a suit, I can achieve a settlement which makes sense to me, generally measured by the amount of unhappiness I detect on the other side, and then I'll make an application to the court for an allowance based on the result. Suppose in the interim I engage in conversation with the lawyers on the other side as to what my application is going to be. In a derivative representative suit, the corporation which is going to be responsible for payment of the fee in most instances, if not all, does have an interest which is beyond mere curiosity as to what that application is going to be, since whatever the application is, if it is granted in its entirety or in whatever amount the court allows, the fee is going to reduce the benefit that the corporation will receive because the corporation is the beneficiary of any benefit in a derivative litigation.

In a class representative suit, the derivative situation doesn't obtain because the class is not the corporation. The class is the class of people who sustained the economic injury, a loss by reason of some action of wrongdoing in which the corporation itself may have participated. In a class suit, the court has the say, as it does in a derivative case, as to what the fee will be. But unlike the derivative action, the corporation really doesn't have standing, although I have been in courtrooms where in class litigation defendants are invited to express an opinion on fee allowances. There are very few things that judges will not listen to even though I don't think defendants have standing in a class situation to speak to the matter of fee allowances for the plaintiff's lawyer in a class situation.

If the board of directors at the time of the fee application is a disinterested board, then what the board's view is about the amount of the allowance will be given weight, and, if you will, great weight by our courts. That situation can obtain when, after the suit is filed against the then directors, these persons resign or are ousted as directors and are replaced by new directors who are not associated with the alleged wrongdoing. If the new directors make a judgment on fees, obviously if they were part and parcel of the negotiations of the settlement, they may also have some view about fees, our courts will take that view into account.

Our courts on occasion have inquired in settlement situations as to what the defendants' lawyers have been paid. That occurred in the *Chrysler*²¹ litigation.

21. *Dann v. Chrysler Corp.*, 41 Del. Ch. 438, 198 A.2d 185 (Ch. 1963), *aff'd sub nom.*, *Hoffman v. Dann*, 42 Del. Ch. 123, 205 A.2d 343 (Sup. Ct. 1964), *cert. denied*, 380 U.S. 973 (1965).

The test in Delaware in terms of measuring what the compensation should be is still substantially, I would say, the result achieved. Our courts have not gone, as the *Lindy*²² and *Grinnell*²³ cases hold, to an approach of saying, "Well, how many hours did you spend?" Not that our courts are not interested in time, but our courts look in my judgment where they should look, namely, "What is the result?" I mentioned the *UIC*²⁴ case earlier and I said that it was settled. The amount of time that I spent in that case, I think, resulted in a fee where the hourly compensation, as I recall, given the amount of time was not more than \$5 an hour, an absolute disaster so far as I was concerned, subject only to the exception that if we would have lost it and received nothing, that would have been worse. But there are other cases where you may not spend an enormous amount of time at all, but if you get a good result, I suggest that good result and not time should govern the amount of compensation the court should allow. Professor Hornstein years ago used the analogy, "Would you rather have a surgeon remove your appendix in a two hour operation or an eight minute operation?" Obviously you want a person who could go in there, know what he's about and do the job. Similarly so in a litigation which results in a benefit. I think contrary to *Lindy* and contrary to *Grinnell*, the lodestar of hours, I think, is a piece of goods that really does not help anybody at all. From my own observation, I think emphasizing time leads to a lot of additional expense and time which could be better spent elsewhere in this field of litigation.

In a situation where plaintiff alleges wrongdoing and the defendants promptly take action to remedy the wrong and moot the litigation, the plaintiff's attorney is still entitled to compensation. Taking corrective action is all good and well and management should do that — but I shouldn't think that any responsible persons, particularly those in attendance here, would take corrective action only out of a motivation of depriving the plaintiff of being able to receive his attorney's expense by way of a reasonable allowance. The Delaware rule in terms of compensation in a "mootness" case differs from that of many other jurisdictions — and indeed, I think I may be correct — of all other jurisdictions. In Delaware, the attitude of our courts is that if a claim is meritorious, and then the litigation is mooted, that the plaintiff's attorney is still entitled to receive a reasonable allowance. The reason that lies behind the Delaware rule

22. *Lindy Bros. Builders, Inc. v. American Radiator & Standard Sanitary C*, 382 F. Supp. 999 (E.D. Pa. 1974), *vacated and remanded, en banc*, 540 F.2d 102 (3rd Cir. 1976).

23. *City of Detroit v. Grinnell Corp.*, 495 F.2d 448 (2nd Cir. 1974).

24. No. 1410 (Del. Ch. Mar. 19, 1971). See text accompanying notes 7-8 *supra*.

is that our courts take the view that these corporations really exist, despite what some people might think, for the benefit of the stockholders. It is to the stockholders to whom the directors have the overriding responsibility. If that is indeed the case, then stockholders ought to be sensitive to what the managers of their money are doing with their money. Our courts encourage stockholders to be alert, to read the material, to vote, to take action. In many situations under Delaware law the majority vote of stockholders has significant legal consequences. Accordingly, if a plaintiff sees something wrong and takes action to remedy the wrong, then our courts are not going to deprive that stockholder from securing for his lawyer a reasonable allowance and the reimbursement of expenses just because the wrong is corrected. Our courts go a step farther down this road, namely, if it can be shown that there is a causal relationship between the filing of the litigation and the corrective action taken, our courts will increase the amount of the allowance. But as Dick Corroon and I know from our *Palley*²⁵ litigation, you just can't give the Rockefeller salute to the plaintiff's lawyer. Dick can tell you stories about my losers where he was on the other side — I think it was the *Chrysler*²⁶ litigation, which I think is the piece de resistance there. It had to be a rainy dark night, and they met in a cellar, and they concluded a settlement by which the defendants were going to be better off by reason of the settlement than they had been when the action was filed. So I came along and I suggested to the court that such a situation ought not to carry the day and be approved as a settlement. I said, "This is terrible, your Honor; these people are going to get more by reason of the settlement that Mr. Corroon has fashioned than they would have gotten if the settlement had never taken place." Dick got up and responded. He looked at the court and said, "Mr. Morris is precisely right, but that's the virtue of this settlement, because it provides incentive." I never knew what had happened to that area of my anatomy below my knees this morning.

The last section which I will try to cover very briefly, because I would like to have some questions, either from panelists, but since they may skewer me, I would prefer them from the audience, and I would be more pleased about being skewered by you than by them, is the section on preventive medicine on pages [401] and [402].²⁷

25. *Palley v. McDonnell Co.*, 295 A.2d 762 (Del. Ch. 1972), *aff'd*, *McDonnell Douglas Corp. v. Palley*, 310 A.2d 635 (Del. 1973).

26. *Dann v. Chrysler Corp.*, 41 Del. Ch. 438, 198 A.2d 185 (Ch. 1963), *aff'd sub nom.*, *Hoffman v. Dann*, 42 Del. Ch. 123, 205 A.2d 343 (Sup. Ct. 1964), *cert. denied*, 380 U.S. 973 (1965).

27. Appendix G, this issue, *infra* at 401-02.

There you will see the reference to *Lutz v. Boas*²⁸ and *The Corporate Directors' Guidebook*.²⁹ *Lutz v. Boas* indeed should be brought to the attention of every single director who goes on a board. I would say that the director ought to, even an experienced, knowledgeable, sophisticated person, ought to every now and again take a look at that one, because directors who do not direct are going to hurt their companies, they are going to hurt the people whose money they are handling, and finally they may do grave damage to themselves. In *Lutz v. Boas*, it had to be an unhappy day when the people there involved went on that board, and thought, "We're honored in the extreme," and then promptly forgot why they were there. So I suggest to you respectfully that that is reading which, if not known by your board people, they can read it periodically with some degree of advantage. *The Corporate Directors' Guidebook* I also urge. That is the work product of a subcommittee of the committee of the ABA on which I serve and Norm Veasey mentioned. The *Guidebook* has been criticized. It is not in final form. It has not yet been adopted by the ABA. It has not yet been adopted by the Section. But I suggest to you respectfully that whether or not it ever is adopted, the fact that it is out there and available, its teachings ought not to be ignored. I am aware of the criticism of the *Guidebook* that has come from the National Secretaries' group, and the concern that it places management in an odious position as if one didn't trust directors. I don't think that should be the attitude with which the *Guidebook* is received at all. I think it was intended to be helpful. I think it is helpful, and I think there will be refinements — we spent some time a couple of weeks ago out in Chicago going over some sections of it again, and there will be changes. By and large, our committee and our particular subcommittee, if they have their way, the thrust of the *Guidebook* will not be deflected — we don't think it should be — by the criticism we have heard so far, which doesn't mean we are unwilling to talk about it, discuss it, and, indeed, have more consideration given to it.

One other comment — under point 3 at page [402],³⁰ I have made a suggestion, which is not really seeking after business, but I am suggesting that in planning corporate moves, along with regular outside counsel and your accountants and your investment bankers and all the experts that you want to consult, that you might also give thought, if there is some concern among you that, "Will this fly in Topeka or indeed in the Court of Chancery of the State of

28. 39 Del. Ch. 585, 171 A.2d 381 (Ch. 1961).

29. 32 BUS. LAW. 5 (1976).

30. Appendix G, this issue, *infra* at 402.

Delaware," you might give thought to seeking the advice of lawyers on the plaintiff side who indeed might give you a different insight as to what a stockholder might say about what you are proposing.

I thank you for listening.

CHANCELLOR QUILLEN: Mr. Goldman.

MR. GOLDMAN: Irving, is it your view that under any circumstances, an unsuccessful plaintiff's attorney is entitled to a court-awarded fee, and if so under what circumstances.

MR. MORRIS: In the case of *Gottlieb v. Hayden Chemical*³¹ our supreme court held that there are only two situations where the cost of litigation incurred by a plaintiff may be placed upon a defendant: (1) where a fund is created by reason of the plaintiff's action, and (2) where the stockholders have been afforded a needed protection. That is the state of the law, that is the risk I assume when I undertake cases on the plaintiff side. I would love to say, well, I created a great deal of good law as the late Bob Barab did or helped to do in *Gottlieb v. Hayden Chemical*, but our courts will not recognize it as the basis for compensation. As to whether or not there should be an allowance without a benefit, there are days when the till is low that I think longingly that the answer to your question should be yes, but I will delay my despair and await those happy occasions when the court allows me that which I am reasonably entitled to.

CHANCELLOR QUILLEN: Since the till is obviously not low today, I would also add that I remember at least one chancery judge that insisted upon an affidavit of time, not that that was the exclusive measure — it certainly was not. Irv took great exception because there was a prominent New York lawyer on his side, and said, this isn't Irv Morris, this is John Smith. And I said, John Smith can file an affidavit too.

MR. MORRIS: There is, what I think, a fine enlightened opinion by then Chancellor Duffy, now Mr. Justice Duffy, which is directed to that point, which apparently from time to time has not been followed, which holds the view that I have expressed which of course is much more persuasive, namely, it is the result obtained and not the time spent which governs fee allowance.

MR. DREXLER: Irv, I wonder if you could address yourself briefly to the situation in a settlement of a class action suit where an intangible or a non-fund type of benefit is conferred upon the class and how that situation is handled with respect to attorneys' fees.

MR. MORRIS: That's a troubling situation. For example, I think what Dave [Drexler] has in mind is the following. You

31. *Gottlieb v. Hayden Chem. Corp.*, 34 Del. Ch. 436, 105 A.2d 461 (Sup. Ct. 1954).

represent a group of people to whom a tender offer has been made. You think the terms are unfair. You go before the court, and you seek to enjoin that tender offer on various grounds — failure to disclose, the terms are not fair, what have you. And the court agrees with you, the court says it's not going to let it happen, it's enjoined. You smile, you are successful, your wife's going to be happy at dinner when you tell her how good you are, the kids won't get beat up as severely as they might on other days. But then when you go in the next day you ask, "Well I have all this time, and I've gotten this good result, who is going to pay me?" This is a very troubling problem because the people you have benefited in the class, who didn't get ripped off because you prevented it, you never had them in one happy group, they didn't meet in the YMCA auditorium and raise a purse for you. If you go to the corporation, the corporation would say, "What are you talking about asking us for a fee. You didn't work for us, we didn't hire you, you haven't done anything for us at all." There ought to be perhaps a special fund in those instances, but there isn't. It's a difficult thing.

MR. BALOTTI: Iry, you know *Dillon v. Berg*,³² in the district court where that situation arose to a certain event. There was a proxy that was violative of federal law, and corrective action was taken by the court. Ultimately, counsel fees were applied for and the court awarded a fee to be paid by the corporation, but it was not a fee that covered all of the time and disbursements of the attorneys. So you are somewhat at risk when you take on litigation where you do not create a pot or a benefit easily measurable in dollars.

MR. MORRIS: If I may just add to that, you may create a benefit which is indeed real — "affording a needed protection" I think is the language of our supreme court in *Gottlieb v. Hayden Chemical*³³ — but it's still difficult as to where you go to get paid. In the *Dillon* litigation, to put numbers on it, and Frank Balotti will know because I think his shop was on the plaintiffs' side, I think the application was for \$225,000 for attorneys' fees plus expenses. I may be wrong, but when you are in that range, when you're off \$25,000 either way, it's really insignificant. Initially, I was in related litigation representing a plaintiff, and I did get paid but I was doing something else. Frank's colleagues out of New York were doing yet another thing, and the trial court when it was faced with their application, initially allowed, my recollection is, around \$25,000 and 10% of the out-of-pocket expenses, the total of which was \$60,000 or \$70,000. The disappointed lawyers appealed to the third circuit, and

32. 326 F. Supp. 1214 (D. Del.), *aff'd*, 453 F.2d 876 (3rd Cir. 1971).

33. *Gottlieb v. Hayden Chem. Corp.*, 34 Del. Ch. 436, 105 A.2d 461 (Sup. Ct. 1954).

the third circuit sent it back for specific findings. In the second decision on the fees, I think Chief Judge Latchum increased the allowance to somewhere around \$40,000, and I think he may have allowed more if not all of the out-of-pocket expenses. But I thought what was memorable about his second opinion was the way he concluded it. If he didn't use these words, certainly the thrust was there. "Look, members of the third circuit, I've done what I can, I've done all that I can. Now if you want to take it and reverse it again, you do something more at your end." It's a very difficult area for a plaintiff's lawyer, and I know plaintiffs' lawyers who have turned down such cases because they say, "I could work and if I am not retained and handsomely so, I may well be working for nothing even if I am successful."

MR. BALOTTI: I have to admit, that's not the part of the opinion that stands out most in my mind, Irv.

MR. MORRIS: Yes, but the other part is sad.

MR. DREXLER: Irv, if I can offer a comment there. The *Dillon v. Berg* case involved something that may be of interest here to some of our participants in the sense that occasionally (although I think Irv is addressing you as prospective defendants whom he looks upon eagerly) there comes the possibility that in your role as corporate secretary, it might be in your interest in a transaction to assume the role of plaintiff from your own corporate interest, rather than as a minority stockholder seeking recovery on behalf of a class, but pursuing some specific corporate interest of your own company. I think what happened in *Dillon v. Berg*, to a certain extent, was a feeling in the case where Mr. Balotti's clients were in fact contesting for corporate control with the defendants, and thus were pursuing their own interest. And when it came to the fee application, the court took into account that the interest of the plaintiff, qua himself, rather than the plaintiff as a stockholder, was being pursued and tried to come to some accommodation with that. The applicable rule was made pretty clear that that might be the rule in Delaware in the chancery court in a trust case not too many years ago, where a trustee came in and filed for an accounting, and when the fee application with respect to the expenses of that accounting were presented to the court, the defense successfully asserted to a substantial portion of those fees that the trustee had filed in the accounting for its own benefit rather than for the benefit of the trust beneficiary, and the fee was so adjusted. I think that principle would be applicable in a stockholder or class action, so that any corporation that gets into a struggle with another corporation and sues, uses a class action or derivative action as a device to pursue its own

individual interest, might find that it is not entitled to receive all the expenses and fees involved.

MR. LOWICKI: It may have been in part answered. I was going to ask you if your client has paid you, being subrogated to your fees . . . [inaudible].

MR. MORRIS: You see, Stan, I can recall only one instance where I ever received a retainer; I think it was \$2,500. The theory is that the allowance is to the plaintiff for the plaintiff to pay his lawyers. That is measured by the factors — result, time, complexity, standing of opposition, your own standing, and all the factors that go into determining a fee, which is not an easy matter either for a judge to resolve or for the lawyers who are presenting it. Most people I know who are on the plaintiffs' side as attorneys try to make a judgment, because they don't want to be embarrassed, they don't want a track record of going in and seeking X and being cut down. I am pleased to say that the number of instances that the allowance that I have sought has been reduced is very small in terms of numbers as opposed to times when I've gone in, evidenced what the benefit is, and then sought what I thought was fair and reasonable, and I've been pleased by finding that my judgment on that issue, as it was on the initial undertaking to try to undo the wrongdoing, was affirmed by the court.

MR. BALOTTI: In the *Lindy Brothers*³⁴ and the *Grinnell-type*³⁵ test though, what arrangements you have with your own client for payment of fees is one of the things that has to be disclosed and is taken into account by the court in awarding fees. It most often comes up, I suppose, Irv, in antitrust class action litigation rather than stockholders and securities.

CONFERENCE PARTICIPANT: Would it be in order to have a comment on whether the attorney/client privilege would ever apply to advice given by attorneys to the corporation where it is a derivative suit. In other words, I thought Mr. Morris indicated that there might be some movement in that direction as to whether in a derivative suit, the plaintiff, being representing in effect the corporation, would be entitled to all of that information or whether the attorney/client privilege would apply.

MR. MORRIS: That's the very issue that — well, let's see, it's a 1975 decision by Judge Wright, *Valenti v. Pepsico*,³⁶ and there's the

34. *Lindy Bros. Builders, Inc. v. American Radiator & Standard Safety Corp.*, 382 F. Supp. 999 (E.D. Pa. 1974), *vacated and remanded, en banc*, 540 F.2d 102 (3rd Cir. 1976).

35. *City of Detroit v. Grinnell Corp.*, 495 F.2d 448 (2nd Cir. 1974).

36. 68 F.R.D. 361 (D. Del. 1975).

prior case, *Garner v. Wolfenbarger*,³⁷ which I think is a fifth circuit decision. I think there's the trend, and I don't know how precisely it will be answered, but I think it will probably be answered by situations where documents are submitted to the court *in camera* and then the court will make a judgment as to what it's going to do. I think you're going to get a lot of ad hoc results, but I think we are now past the day when a plaintiff stockholder seeks conversations or documents and then the bar is put up because the lawyer was in the room when the discussion took place and can't have what was said, or a lawyer was either the sender or the recipient of the letter and therefore you can't get the document. I don't think that that absolute bar is ever again going to be the answer to this question. Similarly so, as I understand the cases, and there haven't been that many on it, that the plaintiff can't come along and say, "The attorney/client privilege is just out the window, because after all it is my corporation, I'm a stockholder in it, and therefore that attorney is as much working for me as he is for the corporate entity." There is going to be a balance somewhere along the line, but I think it's probably going to be on an ad hoc basis. And I think when the judge looks at the documents, if he thinks they are that meaningful, you're going to get the other exceptions that ordinarily come into attorney/client privilege anyway. If it's, "Sure, we can do this, so what if it violates the law," kind of thing, then I think the plaintiff's lawyer is going to see that document. But I don't think there are going to be many instances that blatant.

MR. GOLDMAN: I think it should be pointed out that there is a recent unreported opinion in chancery court which indicates that *Valenti* is not necessarily the law of Delaware and *Valenti* was not followed in that case. It was a [section] 225 action, and the attorney/client privilege was upheld. The ruling was by Vice Chancellor Hartnett.

CHANCELLOR QUILLEN: He's here, Irv, before you say anything.

MR. MORRIS: No, I'm just trying to think of the next occasion when I can try to be as helpful as I can to the court.

MR. BALOTTI: He followed another unreported opinion of the chancellor in rendering that ruling. The argument was made that an opinion by then Chancellor Quillen which permitted beneficiaries of a trust to examine privileged documents between the trustee and the attorney for the trustee, in which *Valenti* was cited with approval, the court of chancery had thus adopted the *Valenti* principle. But apparently, that is a one-shot situation where you are dealing with a

37. 430 F.2d 1093 (5th Cir. 1970), *cert. denied*, 401 U.S. 974 (1971).

trust beneficiary trustee situation, and it has not been adopted in corporate litigation so far.

CHANCELLOR QUILLEN: The communication in the trust case was prior to any litigation between the beneficiary and the trustee, and the communication was for tax advice for the benefit of the beneficiaries. It was a single letter.

MR. GOLDMAN: It should be pointed out that the trust was a private trust and not a public one.