IN THE SUPREME COURT OF THE STATE OF NEVADA

CHARLES JESSEPH AND CHARLES CHURCHWELL, Appellants, v. DIGITAL ALLY, INC., Respondent.	)	Case No.: 78480

APPEAL FROM ORDER GRANTING MOTION TO DISMISS
THE EIGHTH JUDICIAL DISTRICT COURT
STATE OF NEVADA, CLARK COUNTY
HONORABLE ELIZABETH GONZALEZ

JOINT APPENDIX

VOLUME I

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EIGHTH JUDICIAL DISTRICT COURT

CLARK COUNTY, NEVADA

CHARLES JESSEPH AND CHARLES CHURCHWELL, Plaintiffs, v. DIGITAL ALLY, INC., Defendants.	Case No.: A-18-781874-C Dept. No.: Department 14 **COMPLAINT FOR ATTORNEYS' FEES AND EXPENSES**

Plaintiffs Charles Jesseph ("Jesseph") and Charles Churchwell ("Churchwell," and with Jesseph, "Plaintiffs"), by their undersigned counsel, allege upon information and belief, except for their own acts, which are alleged upon personal knowledge, as follows:

1. Plaintiffs bring this action against Digital Ally, Inc. ("Digital Ally" or the "Company") to obtain payment of attorneys' fees and expenses as compensation for causing the Company's Board of Directors (the "Board") to correct material flaws in Digital Ally's capital structure resulting from the Board's prior misconduct in improperly instructing stockholders and tabulating stockholder votes on Board proposals.

2. The Board had previously amended the Company's Articles of Incorporation (the "Articles of Incorporation") to increase the number of authorized shares of common stock by 15,625,000 and to create a new class of 10,000,000 shares blank check preferred stock. Plaintiffs informed the Board that these actions were not properly approved by the Company's stockholders, as required by Nevada law and the rules of the New York Stock Exchange (the "NYSE"), and demanded that the Board remediate this issue. In response to Plaintiffs' efforts, the Board procured proper stockholder approval of the common stock share increase and rescinded the class of blank check preferred stock.

3. Had Plaintiffs not caused the Board to take remedial actions, Digital Ally's capital structure would be fundamentally defective and unstable, and the Board would have proceeded to issue up to 25,000,000 shares of common stock and 10,000,000 shares of "blank check" preferred stock, actions that are required to be – but were not – validly approved by stockholders. The issuance of these invalid shares would dwarf the 9,375,000 shares that of common stock that were in fact authorized by stockholders.

4. Accordingly, Plaintiffs seek attorneys' fees and expenses in connection with the substantial benefits they have conferred on the Company and its stockholders[1]. When Plaintiffs attempted to resolve this matter without commencing litigation, Digital Ally refused to negotiate.

PARTIES

5. Jesseph owned Digital Ally common stock from January 2015 until November 2017.

6. Churchwell is a stockholder of Digital Ally and has owned Digital Ally common stock since July 2015.

7. Digital Ally is a Nevada corporation that maintains its principal offices at 9705 Loiret Boulevard in Lenexa, Kansas. As described in its most recent Annual Report, the Company

[1] Individual stockholders and their counsel are entitled to reasonable attorneys' fees and expenses when they have acted in a representative capacity and produced a material benefit that inures to stockholders as a group. *Mills v. Electric Auto-Lite Co.*, 396 U.S. 375, 396 (1970); *Thomas v. City of N. Las Vegas*, 127 P.3d 1057, 1059 (Nev. 2006).

"produces digital video imaging and storage products for use in law enforcement, security and commercial applications."

SUBSTANTIVE ALLEGATIONS

A. The Preferred Stock Amendment and the 2016 Proxy

8. On March 21, 2016, Digital Ally filed a Schedule 14A Definitive Proxy Statement (the "2016 Proxy") with the U.S. Securities and Exchange Commission (the "SEC") in connection with its 2016 Annual Meeting of Stockholders on May 12, 2016 (the "2016 Annual Meeting"). In the 2016 Proxy, the Board sought stockholder approval of five proposals, including: (1) re-election of four of its then-current directors and the election of one new director; (2) an amendment to the Company's 2015 Stock Option and Restricted Stock Plan; (3) ratification of the appointment of RSM US LLP ("RSM") as the Company's independent registered public accounting firm; and (4) the compensation package of the Company's named executive officers[2].

9. In another proposal, which was "Proposal 2" in the 2016 Proxy, the Board sought stockholder approval of an amendment to the Articles of Incorporation increasing the number of authorized shares of capital stock that the Company could issue by 10,000,000 shares (from 25,000,000 to 35,000,000 shares), all of which would be classified as blank check preferred stock (the "Preferred Stock Amendment"). As stated in the 2016 Proxy, "Proposal 2 seeks your approval of an amendment to our Articles of Incorporation … to increase the number of authorized shares of capital stock that we may issue from 25,000,000 to 35,000,000, of which 25,000,000 shares shall be classified as common stock and 10,000,000 shares shall be classified as blank check preferred stock. The Articles Amendment has the effect of creating a new class of stock: blank check preferred."

10. According to the 2016 Proxy, the Board sought to add 10,000,000 shares of blank check preferred stock because it would allow the Board to issue the preferred stock "for, among other things, possible issuances in connection with such activities as public or private offerings of

[2] The last of these four proposals was non-binding and sought stockholder approval on advisory basis only.

shares for cash, acquisitions of other companies, pursuit of financing opportunities and other corporate purposes."

11. Pursuant to Section 78.390 of the Nevada Revised Statutes ("NRS"), approval of the Preferred Stock Amendment required the affirmative vote of a majority of the Company's stock. As stated in the 2016 Proxy: "The affirmative vote of a majority of the issued and outstanding common stock will be required to approve the [Preferred Stock] Amendment."

12. According to the 2016 Proxy, there were 5,311,999 outstanding shares of common stock entitled to vote at the 2016 Annual Meeting. Proposal 2 therefore required the affirmative vote of at least 2,656,000 shares to garner approval.

13. The 2016 Proxy explained that, with respect to the election of directors, a stockholder could either vote "For" a given director or "Withhold" their vote. With respect to each of the other proposals, a stockholder could vote "For" that proposal, "Against" that proposal, or "Abstain" from voting on that proposal. With respect to shares held in an account at a broker or similar organization, the owner of the shares is considered the beneficial owner, with the shares being held by the brokerage in "street name." The organization holding the account is considered the stockholder of record for purposes of voting. A beneficial owner is entitled to instruct that organization on how to vote shares in the beneficial owner's account.

14. The 2016 Proxy informed stockholders what would happen if a stockholder failed to provide their broker with specific voting instructions. As stated in the 2016 Proxy, in such a case, brokers would not have authority to cast a vote on Proposals 1 through 3, which included the Preferred Stock Amendment, and would only have authority to cast a vote on Proposals 4 and 5. As stated in the 2016 Proxy: "If you beneficially own your shares in street name and you do not instruct your bank or broker how to vote on Proposals 1 through 3, no votes will be cast on your behalf at the annual meeting as to these proposals. Your bank or broker will, however, have discretion to vote any uninstructed shares on Proposals 4 and 5." The 2016 Proxy further represented to stockholders as follows:

> **Abstentions and Broker Non-Votes:** If your shares are held by your broker as your nominee (that is, in "street name"), you will need to obtain a proxy form

> from the institution that holds your shares and follow the instructions included on that form regarding how to instruct your broker to vote your shares. If you do not give instructions to your broker, your broker can vote your shares with respect to "discretionary" items, but not with respect to "non-discretionary" items. Discretionary items are proposals considered routine under the rules of the New York Stock Exchange ("NYSE") on which your broker may vote shares held in street name without your voting instructions. **On non-discretionary items for which you do not give your broker instructions, the shares will be treated as broker non-votes.** Under NYSE rules, any election of a member of the Board of Directors, whether contested or uncontested, is considered "non-discretionary" and therefore brokers are not permitted to vote your shares held in street name for the election of directors in the absence of instructions from you. **Each of Proposals 1, 2 and 3 are "non-discretionary." Therefore, if you hold your shares through a broker, nominee, fiduciary or other custodian, your shares will not be voted on those proposals unless you provide voting instructions to the record holder.**
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> A "broker non-vote" occurs when a broker expressly instructs on a proxy card that it is not voting on a matter, whether routine or non-routine. Broker non-votes are counted for the purpose of determining the presence or absence of a quorum, but are not counted for determining the number of votes cast for or against a proposal. **Your broker will have discretionary authority to vote your shares on Proposals 4 and 5 only.** [(emphasis added).]

15. Thus, according to the Company's representations in the 2016 Proxy, if a stockholder did not provide a broker with voting instructions, that broker would not have the authority to vote the stockholder's shares in favor of Proposal 2, the Preferred Stock Amendment, resulting in a so-called "broker non-vote" for that proposal. Because Proposal 2 needed the affirmative vote of a majority of the Company's outstanding shares to be validly approved, not voting effectively constituted a vote **against** Proposal 2. Accordingly, stockholders who wished to vote against Proposal 2 were told that they could do that by withholding voting instructions from their broker.

16. On May 13, 2016, the Company filed an 8-K with the SEC disclosing the results of the 2016 Annual Meeting. According to the 8-K, the results were as follows:

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Proposal One: ***Election of Five Directors of the Company.***

Name	Votes For	Votes Against/ Withheld	Abstain	Broker Non-Votes
Stanton E. Ross	1,313,408	96,017		2,612,390
Leroy C. Richie	1,223,414	186,011		2,612,390
Daniel F. Hutchins	1,225,638	183,787		2,612,390
Elliot M. Kaplan	1,227,814	181,611		2,612,390
Michael J. Caulfield	1,328,859	80,566		2,612,390

All nominees were duly elected.

Proposal Two: ***Amendment to Articles of Incorporation***. To approve an amendment to the Company's Articles of Incorporation to increase the number of authorized shares of its capital stock that the Company may issue from 25,000,000 to 35,000,000, of which 25,000,000 shares shall be classified as common stock and 10,000,000 will be classified as blank check preferred stock.

Votes For	Votes Against/ Withheld	Abstain	Broker Non-Votes
3,100,087	869,712	51,888	—

The proposal was approved.

Proposal Three: ***Approval of an Amendment to the 2015 Stock Option Plan and Restricted Stock Plan***. To approve an amendment to the 2015 Stock Option and Restricted Stock Plan to increase the number of shares reserved for issuance under such Plan by 450,000 shares.

Votes For	Votes Against/ Withheld	Abstain	Broker Non-Votes
1,118,017	270,534	20,824	2,612,440

The proposal was approved.

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Proposal Four: ***Provide an Advisory (non-binding) vote on the Compensation of the Company's Named Executive Officers***. To provide an advisory (non-binding) vote on the compensation of the Company's named executive officers, as disclosed pursuant to Item 402 of Regulation S-K, including the compensation tables and narrative discussion in the definitive proxy statement.

Votes For	Votes Against/ Withheld	Abstain	Broker Non-Votes
1,231,941	148,369	29,190	2,612,315

The compensation of the named executive officers was approved.

Proposal Five: ***Ratification of RSM US LLP Appointment.*** Ratification of the appointment of RSM US LLP as the independent registered accounting firm of Digital Ally, Inc. for the year ending December 31, 2016.

Votes For	Votes Against/ Withheld	Abstain
3,644,711	262,364	114,740

The selection of RSM US LLP as the independent registered accounting firm was ratified.

17. According to these results, Proposal 2, the Preferred Stock Amendment, purportedly received 3,100,087 "votes for" approval, and the Board deemed the proposal approved on the basis of its having purportedly surpassed the 2,656,000 affirmative votes needed for approval.

18. However, the Company was able to garner sufficient votes in favor of Proposal 2 only by counting votes cast by brokers for shares owned by beneficial stockholders who declined to submit voting instructions to their brokers. The counting of such votes as "For" votes directly contravened the voting instructions the Board provided to stockholders in the 2016 Proxy.

19. As shown in the voting results above, stockholders holding approximately 1,409,000 shares cast their votes "For," "Against," or in "Abstention" for each of the proposals (or "For" or "Withheld" for each director)[3]. Additionally, more than 2,612,000 shares were beneficially owned by stockholders who failed to provide their brokers with voting instructions. This is evidenced by

[3] Specifically, 1,409,425 votes were cast for/withheld for each director, 1,409,375 votes were cast for/against/in abstention of Proposal 3, and 1,409,500 votes were cast for/against/in abstention of Proposal 4.

the "2,612,390," "2,612,440," and "2,612,315" figures that appear in the "Broker Non-Votes" columns for Proposals 1, 3, and 4, respectively.

20. Consistent with the representations in the 2016 Proxy, these uninstructed shares were voted by brokers on Proposal 5, the vote seeking appointment of RSM as the Company's independent registered public accounting firm, as evidenced by the lack of broker non-votes for that proposal.[4]

21. Contrary to the express representations to stockholders in the 2016 Proxy, more than 2,612,000 uninstructed shares were also voted in favor Proposal 2, as evidenced by the lack of broker non-votes recorded for that proposal.

22. In other words, stockholders who thought they were effectively voting against Proposal 2 by not submitting voting instructions to their broker instead had their broker "non-votes" treated as affirmative votes for Proposal 2.

23. Additionally, regardless of the Board's failure to adhere to the voting instructions for Proposal 2 described in the 2016 Proxy, NYSE Rule 452 expressly prohibits NYSE member organizations such as brokers from voting uninstructed stock beneficially owned by a client on a matter that "authorizes or creates a preferred stock or increases the authorized amount of an existing preferred stock." The Preferred Stock Amendment does just that, and broker votes on uninstructed stock concerning Proposal 2 therefore were not authorized and should not have counted.

24. Had broker votes on uninstructed shares not been counted in favor of Proposal 2, consistent with the representations in the 2016 Proxy and in accordance with NYSE Rule 452, Proposal 2 would have had fewer than 500,000 affirmative votes – not remotely close to the 2,656,000 shares necessary to garner approval – and would have easily failed.

B. The Share Increase Amendment and the 2015 Proxy

25. On April 28, 2015, the Company filed a Schedule 14A Proxy Statement with the SEC (the "2015 Proxy") in connection with the Company's 2015 Annual Meeting of Stockholders

[4] With respect to Proposal 4, although the 2016 Proxy stated that brokers would have discretion to vote uninstructed shares, pursuant to NYSE Rule 452 brokers did not actually have such discretion, and accordingly there were 2,612,315 broker non-votes with respect to that proposal.

on June 9, 2015 (the "2015 Annual Meeting"). In the 2015 Proxy, the Board sought stockholder approval of four proposals, including (1) the election of four directors; (2) the Company's 2015 Stock Option and Restricted Stock Plan; and (3) ratification of the appointment of McGladrey LLP as the Company's independent registered public accounting firm.

26. In another proposal, which was "Proposal 2" in the 2015 Proxy, the Board sought stockholder approval of an amendment to the Articles of Incorporation to increase the number of authorized shares of common stock from 9,375,000 to 25,000,000 shares, of which all 25,000,000 shares would be classified as common stock (the "Share Increase Amendment").

27. In the 2015 Proxy, the Board explained its purpose in seeking approval of this amendment by stating in the 2015 Proxy:

> We believe that an increase in the number of our authorized capital stock is prudent in order to assure that a sufficient number of shares of our capital stock is available for issuance in the future if our Board of Directors deems it to be in the best interests of our stockholders and us. Our Board of Directors has determined that a total of 25,000,000 shares of common stock to be a reasonable estimate of what might be required in this regard for the foreseeable future to (i) issue common stock in acquisitions or strategic transactions and other proper corporate purpose that may be identified by our Board in the future; (ii) issue common stock to augment our capital and increase the ownership of our capital stock; and (iii) provide incentives through the grant of stock options and restricted stock to employees, directors, officers, independent contractors, and others important to our business under our stock option plans. Immediately following this increase, the Company will have approximately 20,978,931 shares of common stock authorized but unissued and available for issuance. At present, we have 4,021,069 shares of common stock issued and outstanding, 369,898 shares issuable upon exercise of options granted under the Plans, and 56,386 shares issuable upon exercise of outstanding warrants to purchase common stock.

28. As with the Preferred Stock Amendment, the Share Increase Amendment required an affirmative vote of a majority of the Company's stock in accordance with NRS Section 78.390. This requirement is reflected in the 2015 Proxy, which states: "The affirmative vote of a majority of the issued and outstanding common stock will be required to approve the [Share Increase] Amendment."

29. According to the 2015 Proxy, there were 4,021,069 outstanding shares of common stock entitled to vote at the 2015 Annual Meeting. Proposal 2 therefore required the affirmative vote of at least 2,010,535 shares to garner approval.

30. The 2015 Proxy instructed beneficial owners that: "If you do not provide instructions for voting the shares that you beneficially own, the organization holding your shares ***cannot*** vote them for you for Proposals 1 through 3." The 2015 Proxy reiterated that brokers could not vote shares without instruction from beneficial owners on Proposals 1 through 3, and provided the following directions:

> **Beneficial Owner: Shares Registered in the Name of Broker or Bank.** If you are a beneficial owner of shares registered in the name of your broker, bank, or other agent, you should have received instructions for granting proxies with these proxy materials from that organization rather than from us. A number of brokers and banks enable beneficial holders to give voting instructions via telephone or the internet. Please refer to the voting instructions provided by your bank or broker. To vote in person at the annual meeting, you must provide a valid proxy from your broker, bank, or other custodian. Follow the instructions from your broker or bank included with these proxy materials, or contact your broker or bank to request a proxy form.
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> ***If you return a signed and dated proxy card without marking any voting selections, your shares will only be voted for Proposal 4, and not for Proposals 1, 2 or 3.*** Thus, if you are not a record holder and hold your shares through a bank or broker, you must provide voting instructions to the record holder of the shares in accordance with its requirements in order for your shares to be properly voted for the following proposals: Proposal 1, the election of directors; Proposal 2, to approve an amendment of our Articles of Incorporation to increase the number of authorized shares of our common stock from 9,375,000 to 25,000,000; and Proposal 3, to approve the 2015 Digital Ally, Inc. Stock Option and Restricted Stock Plan and to reserve 300,000 shares for issuance under the Plan. If any other matter is properly presented at the meeting, your proxy (one of the individuals named on your proxy card) will vote your shares using his or her best judgment.
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> ***If you beneficially own your shares in street name and you do not instruct your bank or broker how to vote on Proposals 1 through 3, no votes will be cast on your behalf at the annual meeting as to these proposals.*** Your bank or broker will, however, have discretion to vote any uninstructed shares on Proposal 4. [(emphasis added).]

31. In other words, any stockholder who opposed Proposal 2, *i.e.*, the Share Increase Amendment, was told they could vote against it simply by withholding voting instructions from their broker.

32. On June 12, 2015, the Company filed a Form 8-K with the SEC, disclosing the following results of the 2015 Annual Meeting:

Proposal One: *Election of Four Directors of the Company*.

Name	Votes For	Votes Against/ Withheld	Abstain	Broker Non-Votes
Stanton E. Ross	721,553	35,625		2,241,259
Leroy C. Richie	712,984	44,194		2,241,259
Daniel F. Hutchins	720,911	36,267		2,241,259
Elliot M. Kaplan	716,594	40,584		2,241,259

All nominees were duly elected.

Proposal Two: *Amendment to Articles of Incorporation*. To approve an amendment to the Company's Articles of Incorporation to increase the number of authorized shares of its capital stock that the Company may issue from 9,375,000 to 25,000,000, of which all 25,000,000 shares shall be classified as common stock.

Votes For	Votes Against/ Withheld	Abstain	Broker Non-Votes
2,140,495	800,058	57,883	--

The proposal was approved.

Proposal Three: *Approval of the 2015 Stock Option Plan and Restricted Stock Plan*. To approve the 2015 Stock Option and Restricted Stock Plan and reserve 300,000 shares for issuance under the Plan.

Votes For	Votes Against/ Withheld	Abstain	Broker Non-Votes
625,527	118,581	13,070	2,241,259

The proposal was approved.

Proposal Four: ***Ratification of McGladrey LLP Appointment.*** Ratification of the appointment of McGladrey LLP as the independent registered accounting firm of Digital Ally, Inc. for the year ending December 31, 2015.

Votes For	Votes Against/ Withheld	Abstain
2,819,507	103,789	75,141

The selection of McGladrey LLP as the independent registered accounting firm was ratified.

33. As set forth above, there were purportedly 2,140,495 votes "for" Proposal 2, surpassing the threshold requirement of 2,010,535 affirmative votes, and the Board deemed this amendment to have been passed.

34. However, as with the Preferred Stock Amendment in the 2016 Proxy, the Company apparently was able to garner enough votes in favor of the Share Increase Amendment only by counting votes cast by brokers for shares owned by beneficial stockholders who did not submit voting instructions. Counting such votes directly contravened the voting instructions provided to stockholders in the 2015 Proxy.

35. The improper counting of uninstructed broker votes is reflected in the reported voting results on Proposals 1 and 3, which reported 2,241,259 broker non-votes for each of these proposals, while Proposal 2 had zero broker non-votes.

36. Like the Preferred Stock Amendment in 2016, the Share Increase Amendment would have failed if not for uninstructed broker votes being counted in favor of the proposal.

37. Although the applicable NYSE rules did allow brokers to vote on Proposal 2, the 2015 Proxy was materially misleading in that it instructed stockholders that Proposal 2 was "non-discretionary" and thus could not be voted on by brokers.

C. On behalf of the Company and its stockholders, Plaintiffs prompted the Board to take corrective actions

38. After becoming aware of the irregularities described above, on May 18, 2017, Plaintiffs served a written demand on the Board (the "Demand").

39. In the Demand, Plaintiffs explained the issues respecting the purported approval of the Preferred Stock Amendment and the Share Increase Amendment. Plaintiffs demanded that the Board immediately deem both amendments ineffective, and further demanded that the Board disclose the invalidity of the amendments and seek a proper stockholder approval of these changes to Digital Ally's capital structure.

40. In response to the Demand, the Company filed a Form 8-K with the SEC on June 30, 2017 (the "Form 8-K"), announcing that the Company would rescind the Preferred Stock Amendment. As stated in the Form 8-K:

> The Company has determined that there is a problem with the vote taken respecting the Blank Check Preferred Amendment. It relates to the authority of brokers to vote in favor of the Blank Check Preferred Amendment without instructions from the beneficial owners of certain of the outstanding shares in accordance with the rules of the NYSE that govern how the brokers may cast such votes and instructions in the Voting Instruction Form transmitted to such beneficial owners. Based on information the Company has recently received, the instructions in the Voting Instruction Form sent to beneficial owners stating that the brokers could vote in their discretion on the Blank Check Preferred Amendment were erroneous, and the brokers' votes in favor should not have been counted. Accordingly, the Company will make appropriate filings with the Nevada Secretary of State to rescind the Blank Check Preferred Amendment. It is important to note in this connection that the Company has not issued, or committed to issue, any shares of the Blank Check Preferred.

Sometime shortly thereafter, the Company made the appropriate filings with the Nevada Secretary of State rescinding the Preferred Stock Amendment.

41. The Company also announced in the Form 8-K that it planned to hold a Special Meeting of its stockholders on August 14, 2017 to conduct a new vote on the Share Increase Amendment. The Form 8-K informed stockholders that the reason for the special meeting was due to concerns regarding the validity of votes taken on the Share Increase Amendment. Specifically, the Form 8-K explained to stockholders that:

> A question has been raised recently regarding the validity of the votes taken on both proposals at these Annual Meetings. In this connection and to eliminate any uncertainty that may exist related to the effectiveness of the Share Increase Amendment, the Company will hold a Special Meeting on August 14, 2017 to ratify the filing and effectiveness of the Share Increase Amendment in accordance with certain provisions of the Nevada Revised Statutes that govern such a matter.

> It is important to note that the Company has not issued, or reserved for issuance, any shares of its Common Stock in excess of 9,375,000, the pre-Share Increase Amendment number. Further, it will not issue, or reserve for issuance, any shares of its Common Stock in excess of 9,375,000 unless the vote at the Special Meeting is in favor of the ratification of the Share Increase Amendment.

42. Also on June 30, 2017, the Company filed a Schedule 14A Definitive Proxy Statement (the "2017 Proxy") with the SEC in connection with the Special Meeting of Stockholders (the "Special Meeting") described in the Form 8-K. The 2017 Proxy contained extensive disclosures concerning the background of the proposed vote to ratify the effectiveness of the Share Increase Amendment. The 2017 Proxy explained:

> Our Board, in consultation with counsel, has determined that the conflicting descriptions in the Proxy Statement for 2015 Annual Meeting of the Share Increase Amendment proposal as "non-discretionary" and in the Voting Instruction Form sent to the clients/beneficial owners by the brokers/nominees as "discretionary" may create some uncertainty as to the effect of the vote obtained at the 2015 Annual Meeting. Thus, our Board has determined that it is in the best interests of our stockholders and us to ratify the filing and effectiveness of the Share Increase Amendment pursuant to Section 78.0296 of the NVR to eliminate any uncertainty that may exist related to the effectiveness of this corporate act.

43. On August 14, 2017, the stockholders voted and ratified the Share Increase Amendment at the Special Meeting.

44. After rescinding the Preferred Stock Amendment, the Board attempted for a second time to create blank check preferred stock. At the Company's 2018 Annual Meeting of Stockholders, which was held on July 5, 2018, the Board submitted a new proposal to amend the Articles of Incorporation to increase the number of authorized shares of capital stock by 10,000,000 shares and classify those shares as blank check preferred stock. As the Company later reported in an 8-K filed with the SEC on July 10, 2018, the proposal was not approved by stockholders at the meeting.

CAUSE OF ACTION
PLAINTIFFS' CLAIM FOR ATTORNEYS' FEES

45. Plaintiffs' Demand raised meritorious legal claims with respect to the effectiveness of the Share Increase Amendment and the Preferred Stock Amendment.

46. In response to the Demand, Digital Ally remediated serious defects in the Company's capital structure. If left unresolved, Digital Ally would have issued up to 15,625,000 shares of common stock and 10,000,000 share of preferred stock, all of which would have been unauthorized.

47. The correction of these defects and corresponding disclosures directly conferred a fundamental and substantial benefit on the Company's stockholders, which in turn entitles Plaintiffs to receive an award of reasonable attorneys' fees and expenses. Plaintiffs' counsel attempted to obtain a reasonable attorneys' fee from the Company without resort to litigation. The Company refused to negotiate.

48. Plaintiffs' counsel has expended time and expense, completely at risk of loss and without remuneration, in connection with its successful remediation of the issues described in the Demand, which permitted stockholders to make an informed decision about whether to ratify the Share Increase Amendment and which resulted in the Company rescinding the unauthorized Preferred Stock Amendment.

49. Plaintiffs and their counsel are a direct and proximate cause of this common benefit, and it would be unjust and inequitable not to compensate Plaintiffs' counsel for achieving it.

WHEREFORE, for the foregoing reasons, Plaintiffs requests an order:

A. Awarding attorneys' fees and expenses commensurate with the benefit that has been conferred as a result of the efforts undertaken by Plaintiffs and their counsel, including attorneys' fees and expenses and incentive awards for the prosecution of the Demand and this action; and

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B. Granting such other relief as the Court may deem just and proper.

Dated this 28th day of September, 2018.

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EIGHTH JUDICIAL DISTRICT COURT FOR THE STATE OF NEVADA
CLARK COUNTY, STATE OF NEVADA

Dept no. XIV

CHARLES JESSEPH AND CHARLES CHURCHWELL,

Plaintiff(s)

v.

DIGITAL ALLY, INC.,

Defendant(s)

Case No.:A-18-781874-C
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Client File# 884-003

I, Tonya Malone, being sworn, states: That I am a licensed process server registered in Nevada. I received a copy of the Summons; Complaint for Attorneys' Fees and Costs, from ALDRICH LAW FIRM, LTD

That on 10/8/2018 at 2:57 PM I served the above listed documents to Digital Ally, Inc. - c/o Registered Agent, Inc., Registered Agent by personally delivering and leaving a copy at 769 Basque Way, Suite 300, Carson City, NV 89706-7934 with Amanda Crill - Receptionist, a person of suitable age and discretion, authorized by Registered Agent to accept service of process at the above address shown on the current certificate of designation filed with the Secretary of State.

That the description of the person actually served is as follows:
Gender: Female, Race: Latino, Age: 20's, Height: 5'8", Weight: 300 lbs., Hair: Brown, Eyes:N/A

I being duly sworn, states: that all times herein, Affiant was and is over 18 years of age, not a party to or interested in the proceedings in which this Affidavit is made. I declare under perjury that the foregoing is true and correct.

Date: October 15, 2018

Tonya Malone
Registered Work Card# R-100246
State of Nevada

(No Notary Per NRS 53.045)

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DISTRICT COURT

CLARK COUNTY, NEVADA

CHARLES JESSEPH AND CHARLES CHURCHWELL,

Plaintiffs,

v.

DIGITAL ALLY, INC.,

Defendant.

A-18-781874-B

Case No. ~~A-18-781874-C~~

Dept. No.: ~~Department 14~~ XI

BUSINESS COURT REQUESTED PURSUANT TO EDCR 1.61(a) and (c)

DEFENDANT DIGITAL ALLY'S MOTION TO DISMISS PLAINTIFF'S COMPLAINT PURSUANT TO NRCP 12(b)(5)

Defendant Digital Ally, Inc., by and through its undersigned counsel, hereby moves to dismiss the Complaint under Nevada Rule of Civil Procedure 12(b)(5) for failure to state a claim

upon which relief can be granted. This Motion is made upon the attached points and authorities, the papers and pleadings on file, and any argument permitted by the Court in this matter.

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Attorneys for Defendant

NOTICE OF MOTION

TO: Plaintiffs Charles Jesseph and Charles Churchwell; and

TO: Their Counsel of Record and all other interested parties.

Please take notice that Defendant Digital Ally, Inc.'s MOTION TO DISMISS PURSUANT TO NRCP 12(b)(5) is scheduled for hearing in Department XI of the above entitled court on the 17 December 9:00 am day of ~~November~~, 2018, at the hour of ___, or as soon thereafter as counsel can be heard.

DATED this 13th day of November, 2018.

MEMORANDUM OF POINTS AND AUTHORITIES
IN SUPPORT OF DEFENDANT'S MOTION TO DISMISS

I. INTRODUCTION

Plaintiffs demand that this court award $250,000 in attorney's fees from a Nevada corporation for writing a letter. Before the Court is Charles Jesseph and Charles Churchwell ("Plaintiffs") Complaint for Attorneys' Fees and Expenses ("Complaint") against Digital Ally, Inc. ("Defendant" or the "Company"). Plaintiffs' request is based on their claim that they conferred a substantial benefit on the Company and its stockholders when they served a demand letter on the Company that allegedly caused Defendant's Board of Directors (the "Board") to "correct material flaws in Digital Ally's capital structure". *See, e.g.*, Compl. ¶¶ 1, 4, Cause of Action.

Under Nevada law, the substantial benefit doctrine governs the award of attorney's fees for a benefit conferred, and requires that the benefit be conferred through litigation. Consequently, despite 15 pages of allegations detailing the purported effect of the demand letter, the Complaint fails as a matter of law to state a claim for which relief can be granted. Accordingly, Defendant respectfully requests that this Court dismiss the Complaint under Rule 12(b)(5) of the Nevada Rules of Civil Procedure.

II. BACKGROUND

On May 18, 2017, Plaintiffs served a written demand (the "Demand") on the Company's Board of Directors (the "Board"). Compl. ¶ 38. Their Demand raised perceived issues with the voting instructions in two proxy statements. First, the Demand stated that the Board's April 28, 2015 Schedule 14A Proxy Statement invalidated shareholder approval of the increase in the number of authorized shares of common stock (the "Share Increase Amendment"). Compl. ¶¶ 26, 39. The Demand also stated that the voting instructions in the March 21, 2016 Schedule 14A Definitive Proxy Statement were flawed, allegedly invalidating the creation of a new class of preferred stock (the "Preferred Stock Amendment"). Compl. ¶¶ 9, 39. Specifically, Plaintiffs requested (a) that

the approval of the Preferred Stock Amendment and the Share Increase Amendment be deemed ineffective, and that the ineffectiveness be publicly disclosed, and (b) that the Board seek stockholder approval of changes to Defendant's capital structure. Compl. ¶ 39.

Thereafter—but before any shares in connection with the Share Increase Amendment and the Preferred Stock Amendment were issued or committed to issue—Defendant rescinded the Preferred Stock Amendment and conducted new shareholder votes on both the Share Increase Amendment and the Preferred Amendments. Compl. ¶¶ 40-44. Defendant publicly disclosed all of these events. *Id.* On September 28, 2018, Plaintiffs sued for attorney's fees and expenses in connection with the alleged substantial benefit purportedly conferred by their Demand. Compl. ¶¶ 45-49.

III. ARGUMENT

A. Legal Standard

Rule 12(b)(5) of the Nevada Rules of Civil Procedure authorizes this Court to dismiss a complaint that fails to state a claim upon which relief can be granted. NRCP 12(b)(5). To survive dismissal, the complaint "must contain some 'set of facts, which, if true, would entitle [the plaintiff] to relief.'" *Weise v. Admin. Office of Courts*, No. 60148, 2013 WL 785098, at *1 (Nev. Feb. 28, 2013) (quoting *In re Amerco Deriv. Litig.*, 127 Nev. 196, 210, 252 P.3d 681, 692 (2011)). Although this Court must accept Plaintiffs' factual allegations as true when reviewing a motion to dismiss, the allegations must be "legally sufficient to constitute the elements of the claim asserted." *Sanchez ex rel. Sanchez v. Wal-Mart Stores, Inc.*, 125 Nev. 818, 823, 221 P.3d 1276, 1280 (2009). Where, as here, Plaintiffs fail to allege one of the essential elements of the claim, Defendant's motion to dismiss should be granted. *Dezzani v. Kern & Associates, Ltd.*, 134 Nev. Adv. Op. 9, 412 P.3d 56, 63 (2018) (affirming Rule 12(b)(5) dismissal where the complaint failed to allege one of the statutory elements); *Felden v. Shapiro*, 126 Nev. 766, 367 P.3d 831 (2010) (dismissing

complaint for failure to allege several of the key elements entitling him to relief).

B. Plaintiffs Cannot Plead a Substantial Benefit Conferred Through Litigation to Support an Award for Attorney's Fees

Nevada follows the American rule that a party cannot recover attorney's fees absent a statute, rule, or contract authorizing the award. *See Thomas v. City of N. Las Vegas*, 122 Nev. 82, 90, 127 P.3d 1057, 1063 (2006). Understanding this barrier to their claim, Plaintiffs try to invoke the substantial benefit doctrine, which is a judge-created exception that allows fee recovery "where a plaintiff has *successfully maintained a suit*, usually on behalf of a class, that benefits a group of others in the same manner as himself." *Mills v. Electric Auto-Lite Co.*, 396 U.S. 375, 392 (1970) (allowing a shareholder to recover attorney's fees where the corporation received a substantial benefit from a derivative suit) (emphasis added). But Nevada law is clear—for this narrow exception to apply, "the prevailing party must show that the losing party has received a benefit *from the litigation*" and that "the class of beneficiaries is *before the court* in fact or in some representative form." *Thomas*, 122 Nev. at 90 (emphasis added).[1]

In this case, Plaintiffs claim that they are entitled to attorney's fees under the substantial benefit doctrine based on their demand letter that allegedly caused the Board to take remedial actions. Compl. ¶ 4, n.1 (citing *Mills*, 396 U.S. at 396; *Thomas*, 122 Nev. at 84). But their complaint is fatally flawed because it fails to plead a key element of the doctrine: that the alleged benefit was conferred through litigation.

Indeed, under Nevada's caselaw and statutory framework, the substantial benefit doctrine applies only to plaintiffs who have prevailed in *litigation*. *Thomas*, 122 Nev. at 90-91; *see also,*

[1] To recover fees under the substantial benefit doctrine, the prevailing party must demonstrate that "(1) the class of beneficiaries [is] 'small in number and easily identifiable'; (2) 'the benefit [can] be traced with some accuracy'; and (3) 'the costs [can] . . . be shifted with some exactitude to those benefiting.'" *Thomas*, 122 Nev. 91 (citing *Kinney v. Int'l Bhd. of Elec. Workers*, 939 F.2d 690, 692 n. 1 (9th Cir. 1991)).

e.g., *Wagner v. City of N. Las Vegas*, No. 60482, 2013 WL 7155945, at *1 (Nev. Dec. 18, 2013) (concluding that the substantial benefit doctrine applied where plaintiff's lawsuit brought a benefit to all taxpayers in the municipality); *Guild, Hagen & Clark, Ltd. v. First Nat. Bank of Nevada*, 95 Nev. 621, 623, 600 P.2d 238, 240 (1979) ("The 'substantial benefit' doctrine applies when the defendant in a class action or corporate derivative suit receives some benefit as a result of the action."); *Cf. Schulz Partners, LLC v. Zephyr Cove Prop. Owners Ass'n, Inc.*, Nos. 55006, 55557, 2011 WL 2652321, at *2 (Nev. July 5, 2011) (denying party's request for attorney's fees under the substantial benefit doctrine because he was neither the successful nor prevailing party in the litigation).

Moreover, Plaintiffs' claim for attorney's fees based solely on a demand letter has no support under the relevant Nevada statutes; the rule providing for shareholder derivative suits expressly requires a shareholder demand on the corporation as a prerequisite for filing suit, but does not provide for attorney's fees following the demand. NRCP 23.1 (requiring plaintiffs filing a shareholder derivative suit to "allege with particularity the efforts, if any, made by the plaintiff to obtain the action the plaintiff desires" from the corporation). Indeed, even the general attorney's fee statute has also been uniformly interpreted to require litigation. Nev. Rev. Stat. 18.01(2) (in relevant part, the court may award attorneys' fees where provided for by statute or agreement or to a "prevailing party" meeting certain requirements); *see also Thomas*, 122 Nev. at 93-94, ("This court has always interpreted [NRS 18.010(2)(a)] as requiring a money judgment as a prerequisite to recovering attorney fees"); *N. Nev. Homes, LLC v. GL Constr., Inc*., 134 Nev. Adv. Op. 60, 422 P.3d 1234, 1237 (2018) ("A party to an action cannot be considered a prevailing party within the contemplation of NRS 18.010, where the action has not proceeded to judgment.") (citation omitted). Plaintiffs filed no such lawsuit here. Thus, because Nevada courts and statutes require litigation to support a claim for attorney's fees, their claim must fail as a matter of law.

A court in the Eastern District of Michigan was recently presented with this exact issue. In *Willner v. Syntel*, the plaintiff filed a demand letter with the corporation, after which the corporation amended its proxy statement. 256 F. Supp. 3d 684, 685-86 (E.D. Mich. 2017). The plaintiff subsequently filed suit, claiming his counsel was entitled to attorney's fees for the substantial benefit conferred on the corporation. *Id.* at 686. In granting the defendant's motion to dismiss, the court found that the plaintiff was "not entitled an award of attorney fees because the benefit that he claims to have conferred did not result from litigation." *Id.* at 696. The court reasoned that because it could not find any cases in the state holding or even suggesting that the doctrine applied outside of the litigation context, or any state statutes to support such an extension of the limited doctrine, it would decline to apply the doctrine to benefits conferred without litigation. *Id.* at 693 (exceptions to the American rule requiring parties to bear their own costs must be construed "narrowly").[2] Although this case is not controlling, its well-reasoned holding is grounded in the interpretation of *Mills* and substantially similar caselaw applied to strongly analogous facts, and Defendant respectfully submits that this Court should use the decision as a roadmap for confirming here that the extension of the substantial benefit doctrine outside the litigation context is not permitted under Nevada law.

Accordingly, Plaintiffs fail to plead any facts, even if all are taken as true, entitling them to relief under the substantial benefit doctrine because they did not confer a benefit through litigation. Instead, they seek fees based solely on a demand letter. This is plainly insufficient, and the

[2] The court in *Willner* noted that the Delaware Chancery court has suggested a plaintiff *may* be able to recover attorneys' fees based on a benefit conferred through a demand letter (though noting the Delaware Supreme Court has never adopted this rule). *Willner*, 256 F. Supp. 3d at 688, 690 n.4. However, the *Willner* court rejected the plaintiff's invitation to apply the Delaware Chancery court's interpretation because (i) Michigan statutory law is not silent on the issue, but in fact requires litigation, and (ii) Michigan common law is inconsistent with the common law of the Delaware Chancery court. *Id.* at 688. Any invitation for this Nevada court to apply Delaware Chancery rulings should be rejected for the same reasons.

Complaint should accordingly be dismissed with prejudice.

IV. CONCLUSION

Given Plaintiffs' inability to plead any facts supporting an essential element of their claim for attorney's fees under the substantial benefit doctrine—namely, the requisite benefit conferred through litigation—their Complaint fails as a matter of law to state a claim for relief. Because there was no lawsuit conferring the alleged benefit, there is no set of facts under which Plaintiffs can recover their fees here, and Defendant asks that this court dismiss the action against it with prejudice.

Dated: November 13, 2018

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Attorneys for Defendant

CERTIFICATE OF SERVICE

I hereby certify that on the 13th day of November, 2018, I served a true and correct copy of Defendant Digital Ally, Inc.'s MOTION TO DISMISS PURSUANT TO NRCP 12(b)(5) as follows:

_X_ By electronic case filing and service through the Court's e-filing service (Odyssey)

___ By U.S. mail, first class postage prepaid to the address below

___ By electronic mail to the e-mail address(es) listed below

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EIGHTH JUDICIAL DISTRICT COURT

CLARK COUNTY, NEVADA

CHARLES JESSEPH AND CHARLES CHURCHWELL, Plaintiffs, v. DIGITAL ALLY, INC., Defendants.	Case No.: A-18-781874-B Dept. No.: XI **PLAINTIFFS' OPPOSITION TO DEFENDANT'S MOTION TO DISMISS COMPLAINT UNDER NRCP 12(b)(5)**

Plaintiffs Charles Jesseph and Charles Churchwell oppose Defendant Digital Ally, Inc.'s, ("Digital Ally" or the "Company") motion to dismiss the Verified Complaint (the "Complaint") under Nevada Rule of Civil Procedure 12(b)(5).

PRELIMINARY STATEMENT

As a result of Plaintiffs' pre-suit litigation demand (the "Demand"), Digital Ally became aware of serious problems with its capital structure and took extraordinary steps that benefited its stockholders and saved the Company from a potential disaster. First, the Company sought and

obtained stockholder ratification of an amendment to its articles of incorporation (the "Articles of Incorporation") that nearly tripled its authorized stock. The amendment had originally been approved based on a proxy statement that falsely told stockholders they could oppose the amendment simply by not voting at all, when in reality, by not voting stockholders had unwittingly authorized their brokerage firms to vote their shares instead. Second, an amendment to the Articles of Incorporation authorizing stockholder-unfriendly "blank check preferred stock" was withdrawn entirely because it had been approved through unauthorized votes cast by brokers. Third, stockholders voted down the blank check preferred stock amendment when it was resubmitted to them in 2018.

Because of the Plaintiffs, deep faults in the Company's capital structure were repaired before any further damage could be done. Had the unauthorized shares issued, the Company would not know which stockholders were voting invalid shares (contaminating all future votes), which stockholders were entitled to dividends, and whether to respect the special rights of preferred stock that was never authorized in the first place. The Company would have been open to claims of damages on all fronts. Because Plaintiffs acted early, the Company's capital structure was saved.

Plaintiffs seek payment of their attorneys' fees for these efforts under the substantial benefit doctrine that has been recognized in Nevada as an equitable means of spreading the costs of a benefit created by one stockholder to all stockholders as a group. Plaintiffs easily satisfy all three elements established by the Supreme Court for a fee award – *a fact that Digital Ally does not contest*.

Instead, the Company urges the Court to add another element to the Supreme Court's test, asserting that it is entitled to freeride on Plaintiffs' efforts simply because the benefit was conferred outside of formal litigation. Digital Ally relies on inapplicable statutes – the substantial benefit doctrine is purely common law in Nevada – and cases which do not even mention the issue of

whether fees are payable under these circumstances. Taking forum shopping to the extreme, for no other reason than that a Michigan court applying Michigan law reached the result Digital Ally wants here, the Company asks the Court to adopt Michigan law. But the substantial benefit doctrine is far narrower in Michigan than in Nevada, in part because the Michigan legislature has expressly limited fee awards in stockholder derivative matters to litigated cases. Nevada has no comparable statute or rule, and the Demand did not assert derivative claims in any event. Without explanation, the Company dismisses Delaware precedent authorizing fees following litigation demands even though the Nevada Supreme Court routinely adopts Delaware law concerning stockholder litigation as well-reasoned and appropriate for Nevada.

Denying stockholders the ability to recover their attorneys' fees for successful litigation demands is not only contrary to existing law: it would establish bad policy for Nevada. Dismissal will not lead to free legal services for Nevada corporations. Rather, it would lead to more, expensive, and unnecessary stockholder litigation, as matters that could have been resolved by demands will be driven into courts so that stockholders and their counsel are eligible for fee awards. And stockholders collectively would enjoy less value-creating monitoring efforts, meaning that misconduct would go undetected and serious problems such as those identified in the Demand would proliferate. Because that result would be highly detrimental to Nevada corporations and their stockholders, the Defendant's motion to dismiss should be denied.

STATEMENT OF FACTS

A. The Parties

Jesseph owned Digital Ally's common stock from January 2015 until November 2015 and Churchwell has owned the Company's common stock continuously since July 2015. (¶¶ 5-6).[1]

[1] All ¶ references are to the Complaint.

Defendant is a Nevada corporation and producer of digital video imaging and storage products. (¶ 7).

B. The Company effects unauthorized changes to its capital structure

Section 78.390 of the Nevada Revised Statutes ("NRS") sets forth the requirements for making amendments to a corporation's articles of incorporation. Among other things, amending the articles of incorporation requires the approval of a majority of the company's outstanding stock in a stockholder vote. (¶¶ 11, 28). In addition, when matters are submitted for a stockholder vote, brokerage firms that are New York Stock Exchange ("NYSE") member organizations are subject to rules concerning their ability to vote the shares that they hold on behalf of beneficial holders. Beneficial holders are stockholders who hold their shares in accounts at brokerages such as JPMorgan Chase or E*Trade. Under NYSE Rule 452, a beneficial owner is entitled to instruct the broker how to vote shares held in the beneficial owner's account. In the absence of such instructions, brokers are allowed to vote the shares owned by beneficial owners only for "routine" matters, such as the ratification of the company's auditor. NYSE Rule 452 expressly prohibits brokers from voting uninstructed stock beneficially owned by a client on a matter that "authorizes or creates a preferred stock or increases the authorized amount of an existing preferred stock." (¶ 23).

In 2015 and 2016, Digital Ally proposed two amendments to its Articles of Incorporation that would affect the Company's capital structure. On April 28, 2015, Digital Ally filed its Schedule 14A Definitive Proxy Statement with the U.S. Securities and Exchange Commission (the "SEC") in connection with the Company's 2015 Annual Meeting of Stockholders. (¶ 25). The 2015 Proxy sought stockholder approval of four proposals, including an amendment to the Articles of Incorporation increasing the amount of common stock from 9,375,000 to 25,000,000 shares (the "Share Increase Amendment"). And on March 21, 2016, Digital Ally filed its Schedule 14A

Definitive Proxy Statement with the SEC (the "2016 Proxy," and collectively with the 2015 Proxy, the "Proxies") in connection with the Company's 2016 Annual Meeting of Stockholders. (¶ 8). The 2016 Proxy sought stockholder approval of five proposals, including a proposed amendment to the Articles of Incorporation creating 10,000,000 shares of a new class of stock known as blank check preferred stock (the "Preferred Stock Amendment," and collectively with the Share Increase Amendment, the "Amendments"). (¶ 9). Unlike common stock which has fixed rights under the Articles of Incorporation, with respect to blank check preferred stock, the Company's board of directors (the "Board") would have very broad authority to determine voting, dividend, conversion and other rights for this new class of stock.[2]

The Proxies disclosed the majority vote requirement applicable under NRS 78.390 and explained to stockholders how failing to vote would impact the results. (¶¶14, 30). Specifically, with respect to the Amendments, beneficial holders of Digital Ally stock were expressly told that if they did not affirmatively submit voting instructions to their brokers (*i.e.*, voting "for", "against", or "abstain") the brokers themselves would not have discretionary authority to vote on the Amendments, resulting in a so-called broker non-vote. (¶¶ 15, 31). Accordingly, stockholders were told that they could effectively vote against the Amendments by choosing the simplest option available to them: not voting at all. (¶¶ 15, 31).

Following its 2015 Annual Meeting, the Company filed a Form 8-K with the SEC, disclosing the voting results on the Share Increase Amendment proposal. (¶ 32). According to the 8-K, the Share Increase Amendment received the affirmative vote of a majority of the Company's outstanding stock, and Digital Ally's common stock reserve was increased from 9,375,000 to 25,000,000 shares. (¶ 32). After the 2016 Annual Meeting, the Company filed a Form 8-K with the

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[2] "While [such stock] can be used to enable a company to meet changing financial needs, its most important use is to implement poison pills or to prevent takeovers by placement of this stock with friendly investors." *See* https://www.nasdaq.com/investing/glossary/b/blank-check-preferred-stock.

SEC, disclosing the results of the stockholders' vote on the Preferred Stock Amendment proposal. (¶ 16). According to the 8-K, the Preferred Stock Amendment received the affirmative vote of a majority of the outstanding stock, and the Company created 10,000,000 shares of a new class of stock on that basis. (¶ 16).

However, read carefully, the voting results announced in the 8-K filings suggested that the Company had improperly permitted brokers to vote uninstructed shares in favor of the Amendments. (¶¶ 18, 34). Allowing brokers to do so was in direct contravention of the representations made to stockholders in the Proxies, and with respect to the Preferred Stock Amendment, was also a violation of the NYSE rules. The improper broker votes were outcome-determinative in both cases, as without those broker votes neither of the Amendments received the necessary votes for approval. (¶¶ 24, 36).

C. Plaintiffs serve the Demand and the Board takes corrective action

On May 18, 2017, Plaintiffs served their Demand on the Board. (¶ 38). In their letter, the Plaintiffs explained that the Amendments were never validly approved by stockholders, and demanded that the Board deem both Amendments ineffective unless and until the Company resubmitted the proposals and obtained valid stockholder approval. In response, Defendant acknowledged that the Demand had identified legitimate issues "regarding the validity" of the vote on the Share Increase Amendment. (¶ 41). To address the problematic vote, the Company resubmitted the Share Increase proposal for another vote at a Special Meeting of Stockholders on August 14, 2017, and a majority of stockholders ratified the Share Increase Amendment. (¶ 41). With regard to the Preferred Stock Amendment, the Company did not seek a ratification vote and instead announced that the amendment needed to be rescinded. (¶ 40). The Board then resubmitted it to stockholders for approval at the Company's 2018 Annual Meeting of Stockholders. (¶ 44). This

time, after the votes were counted properly, it was revealed that stockholders had rejected the Preferred Stock Amendment and the proposal to create a new class of stock failed. (¶ 44).

Plaintiffs sought to recover their attorneys' fees and expenses from the Company out of court. Without any explanation, the Company refused to negotiate. Accordingly, Plaintiffs filed their Complaint on September 28, 2018. Defendant moved to dismiss on November 13, 2018.

ARGUMENT

The Complaint adequately pleads all three elements established by the Supreme Court for an award of attorneys' fees under the substantial benefit doctrine. The Company does not even argue otherwise. Relying on the law of the state of Michigan, Digital Ally instead attempts to impose a new element, which would limit fee awards to filed litigation. As explained below, Digital Ally's argument has no basis under Nevada law and represents unsound policy that would harm stockholders of Nevada companies.

A. The Complaint adequately pleads the elements of the substantial benefit doctrine

While parties ordinarily are expected to bear their own attorneys' fees under the so-called "American rule," Nevada recognizes a common law exception to this rule: the substantial benefit doctrine. The doctrine "allows recovery of attorney fees when a successful party confers 'a substantial benefit on the members of an ascertainable class, and where the court's jurisdiction over the subject matter of the suit makes possible an award that will operate to spread the costs proportionately among them.'" *Thomas v. City of N. Las Vegas*, 122 Nev. 82, 90-91, 127 P.3d 1057, 1063 (2006) (quoting *Mills v. Electric Auto-Lite Co.*, 396 U.S. 375, 393-94 (1970)). Citing federal precedent, the Supreme Court of Nevada laid out a three-element test for recovering attorneys' fees under the substantial benefit doctrine. "To recover fees under the substantial benefit doctrine, a successful party must demonstrate that: (1) the class of beneficiaries is small in number and easily identifiable; (2) the benefit can be traced with some accuracy; and (3) the costs can be shifted with

some exactitude to those benefiting." *Id.* at 91 (ultimately quoting *Alyeska Pipeline Co. v. Wilderness Society*, 421 U.S. 240, 265 n.39 (1975)) (internal quotations and alteration indications omitted). The Complaint sufficiently pleads all three elements and therefore states a claim under the substantial benefit doctrine.

1. The class of beneficiaries is small and easily identifiable

Digital Ally's stockholders are a sufficiently small and easily identifiable group. Indeed, *Thomas* specifically identified stockholder litigation as the archetype for applying the substantial benefit doctrine. 122 Nev. at 91 ("Typically, the substantial benefit exception is applied in cases involving shareholders or unions."). While Plaintiffs cannot specify the precise number of Digital Ally stockholders, it is surely smaller than the taxpaying population of North Las Vegas (a city of more than 200,000 people), the group found to meet this element in *Thomas*. *See id*.

2. The benefit can be traced with some accuracy

Plaintiffs' efforts created a benefit for the Company and its stockholders. If not for those efforts, the Company's capital structure would have become highly destabilized by the existence and potential issuance of 15,625,000 unauthorized shares of common stock and 10,000,000 shares of a new, unauthorized class of preferred stock. The issuance of those shares would ultimately threaten to unravel the Company altogether, as no one would know whether the unauthorized shares could vote or receive dividends (contaminating all future votes and dividend distributions), nor would anyone know whether the special, typically pro-management rights granted to new preferred shares were enforceable or whether any resulting actions were valid. Holders of the new stock and the old stock could have sued the Company for damages, and its creditors could attempt to declare defaults on outstanding loans. Because of the Plaintiffs, none of this came to pass. Instead, the

15,625,000 shares of common stock have been validly created, and the 10,000,000 shares of preferred stock that the Company's stockholders never wanted were eliminated. [3]

A recent Delaware Court of Chancery case, *In re Galena Biopharma, Inc*., recognized the same type of benefit and awarded attorneys' fees to the responsible stockholder. C.A. No. 0423-JTL (Del. Ch. June 14, 2018) (TRANSCRIPT) ("*Galena*") (attached as Exhibit A), As here, *Galena* involved false proxy representations that brokers could not vote uninstructed shares concerning a vote to authorize more common stock, followed by brokers voting such shares. The case was resolved after the parties agreed that the company would have the court validate the articles of incorporation, thus eliminating uncertainty about the company's capital structure.[4] In approving the settlement, the court recognized that the stockholder had "fixed deep faults in the company's capital structure[.]" *Galena*, p. 80. The court held that the benefit obtained "easily supports a fee of $250,000[,]" which was the maximum allowable by the parties' settlement agreement, and noted it "could support a much larger award" based on precedent. *Id*. The court explained that "giving meaningful awards where plaintiffs raise issues that result in companies taking validative action has

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[3] The repeated lack of support for the Preferred Stock Amendment is not surprising – blank check preferred stock "has been derided by shareholder rights advocates given its potential use as an anti-takeover tactic[.]" *See Greenlight Capital, L.P. v. Apple, Inc.*, 2013 U.S. Dist. LEXIS 24716, at *5 (S.D.N.Y. Feb. 22, 2013); *see also A Voice in the Boardroom*, CORNERSTONE CAPITAL GROUP (July 2016) ("Many shareholders oppose [blank check preferred stock] as failing to align with shareholder interests."), https://cornerstonecapinc.com/wp-content/uploads/2017/04/A-Voice-in-the-Boardroom_July-2016.pdf.

[4] Delaware courts can validate otherwise defective corporate acts and documents under 8 Del. C. § 205. Highlighting the sorts of problems that were avoided here because Plaintiffs acted promptly, in *Galena* the company had intended to have stockholders ratify the articles of incorporation amendments at a special meeting of stockholders, but was unable to do so because unauthorized shares had already been issued and contaminated a potential ratification vote. Because of this, the settlement also included a payment to certain stockholders, which was subject to a separately calculated fee award.

important incentive effects" even where "companies can, with a relatively straightforward procedure, take steps to fix things." *Id.*[5]

The *Galena* ruling was not novel. As recognized by the United States Supreme Court in *Mills*, correcting misleading proxy disclosures has been recognized as "furnish[ing] a benefit to all shareholders" and deserving of payment of attorneys' fees. 396 U.S. at 396-97. Courts have routinely awarded fees for obtaining corrective proxy disclosures. *In re Sauer-Danfoss Inc. S'holders Litig.,* 65 A.3d 1116, 1136-37 (Del. Ch. 2011) (collecting cases). In the same vein, preserving stockholder voting rights is a benefit that has typically resulted in the payment of the responsible stockholder's attorneys' fees. *E.g. EMAK Worldwide, Inc. v. Kurz*, 50 A.3d 429, 433 (Del. 2012); *San Antonio Fire & Police Pension Fund v. Bradbury*, 2010 Del. Ch. LEXIS 218, at *48 (Del. Ch. Oct. 28, 2010) (awarding attorneys' fees for "protect[ion] [of] the stockholder franchise"). And correcting a company's capital structure where a question was raised over the authorization of shares due to alleged errors in vote counting has likewise led courts to award attorneys' fees. *E.g. In re Cheniere Energy, Inc.*, C.A. No. 9710, p. 104 (Del. Ch. Mar. 16, 2015) (TRANSCRIPT) (attached as Exhibit B) (citing *Olson v. ev3*, 2011 Del. Ch. LEXIS 34 (Del. Ch. Feb 21, 2011)).

3. The costs can be shifted be to those benefiting

Plaintiffs also satisfy the final requirement. As *Thomas* explains, when a stockholder successfully confers a benefit for all of the company's stockholders, attorneys' fees "assessed against the corporation . . . are easily and equitably spread among the shareholders . . . who are the beneficiaries of the litigation." 122 Nev. at 91.

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[5] The court also rejected the company's argument that "this was a problem that the plaintiffs created[,]" a position the court described as reflecting "a profound lack of awareness" as the problem would have been avoided altogether if the company's disclosures had been accurate. *Galena*, pp. 69-70.

B. Because Plaintiffs' claim is based on common law, Defendant's arguments based on NRS 18.010 and NRCP 23.1 are unavailing

Despite the fact that the substantial benefit doctrine is, as expressly described by the Supreme Court in *Thomas*, a "judicially created exception" rooted in the common law, the Company argues that "Plaintiffs' claim for attorney's fees based solely on a demand letter has no support under the relevant Nevada statutes[.]" This argument is a *non sequitur* because the substantial benefit doctrine provides an independent non-statutory basis for attorneys' fee awards. The requirements of NRS 18.010 are entirely inapplicable to the substantial benefit doctrine. *Thomas* makes this clear by analyzing the two separately. Indeed, Digital Ally implicitly recognizes this by relying on *Wagner v. City of N. Las Vegas*, in which the Supreme Court remanded a plaintiff's claim for fees to enable the lower court to apply the substantial benefit doctrine. 2013 Nev. Unpub. LEXIS 1947, at *3 (Nev. Dec. 18, 2013). Under the holding of *Thomas*, the plaintiff in *Wagner* could not have obtained a fee under NRS 18.010 because no monetary recovery had been obtained. *See Thomas*, 122 Nev. at 94 (affirming denial of attorneys' fees under NRS 18.010(2)(a) because plaintiffs "did not recover a monetary judgment"). NRS 18.010 is plainly irrelevant to this case.

In a similar attempt to invoke inapplicable law, the Company claims that NRCP 23.1 "does not provide for attorneys' fees following [a] demand." True, but NRCP 23.1 has nothing to do with attorneys' fees at all, and instead concerns the requirements a stockholder must meet before filing a derivative action. This is not a derivative action, nor would it be one even if Plaintiffs had filed a complaint at the outset instead of making the Demand. As in *Galena*, the underlying claims are direct, not derivative.[6]

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[6] The Company also incorrectly asserts that Rule 23.1 requires a demand prior to filing a derivative action, when it does not. NRCP 23.1 (stockholder may state a derivative claim by pleading its reasons for not "making the effort" of a demand); *Shoen v. SAC Holding Corp.*, 122 Nev. 621, 137 P.3d 1171 (2006) (addressing situations where stockholders do not have to make pre-suit demand).

C. The Court should reject the Defendant's request to adopt Michigan law

Digital Ally's argument that Nevada precedent requires a benefit to have been generated in filed litigation is unsupported by any of the cases cited for that proposition. In *Thomas*, what the court found "determinative" is that the plaintiffs could not meet the substantial benefit doctrine's "third factor required for relief because they ha[d] not demonstrated that the costs will be shifted to those benefiting." 122 Nev. at 92. In *Guild, Hagen & Clark, Ltd. v. First Nat'l Bank*, attorneys' fees were denied because the benefit inured to a non-party, and was generated incidentally to counsel's failed efforts to obtain relief for his client. 95 Nev. 621, 624-25, 600 P.2d 238, 240 (1979). In *Wagner* the Supreme Court remanded the case because the district court failed to apply the *Thomas* factors when it denied an award of attorneys' fees. 2013 Nev. Unpub. LEXIS 1947, at *3. And in *Schulz Partners, LLC v. Zephyr Cove Prop. Owners Ass'n, Inc.*, the Supreme Court found that the plaintiff "had failed to prove its substantial benefit argument" because plaintiff was neither "successful" nor "prevailing." 2011 Nev. Unpub. LEXIS 1047, at *8 (Nev. July 5, 2011). None of these cases even mentions an application for fees outside of formal litigation, much less establishes a bar to fees for benefits conferred through a pre-suit demand. Instead, these cases simply use the word "litigation" for the unremarkable reason that the substantial benefit doctrine was invoked following litigation in those cases.

Recognizing as much, the Company asks the Court to adopt the law of Michigan, a state with no connection to this dispute whatsoever. Specifically, the Company relies on the Michigan decision in *Willner v. Syntel*, 256 F. Supp. 3d 684 (E.D. Mich. 2017), which Digital Ally calls a "roadmap for confirming here that the extension of the substantial benefit doctrine outside the litigation context is not permitted under Nevada law." *Syntel* relies on Michigan law that is contrary to Nevada law, and is therefore not instructive here.

The *Syntel* ruling was predicated on Michigan statutes that the court interpreted as representing an express legislative decision to limit the availability of attorneys' fees in derivative actions to cases involving actually litigated claims. 256 F. Supp. at 694 ("[T]o the extent the Michigan Legislature has recognized the common or substantial benefit exception, it has limited that exception to benefits conferred through litigation."). The court explained that Michigan statutes authorize the court to "award attorney fees *only* where a shareholder has prosecuted a derivative '*proceeding* [that] has resulted in a substantial benefit to the corporation,' and the statutes further define a 'proceeding' as 'a *civil* suit.'" *Id*. at 693-94 (citing Mich. Comp L. § 450.1497(b) (emphasis and alterations in original). There is no analogous statute in Nevada, where the substantial benefit doctrine remains purely common law.

Moreover, Nevada's substantial benefit doctrine bears little resemblance to Michigan's version. Unlike in Nevada, "Michigan courts construe all exceptions to the American [r]ule 'narrowly[.]'" *Syntel*, 256 F. Supp. 3d at 693. A half century of Michigan precedent holds that "a court may not order a corporation to pay a shareholder's attorney fees unless the legal work that generated the fees resulted in a direct benefit to the corporation" as opposed to the shareholders' themselves. *Id*. at 692-93. Contrary to Defendant's assertion that *Syntel* is "grounded" in the reasoning of *Mills*, the *Syntel* court acknowledged that Michigan law is "not consistent with the federal rule." *Id*. at 695. *Thomas* of course adopted *Mills*, and states the precise opposite rule from *Syntel*. *Thomas*, 122 Nev. at 91 (where substantial benefit doctrine applies, "attorney fees *assessed against the corporation* . . . are easily and equitably spread among the shareholders . . . who are the beneficiaries of the litigation") (emphasis added).

Lastly, the *Syntel* court acknowledged that plaintiff had "advanced many reasonable arguments as to why it may be both sensible and fair to permit a fee award" following a successful litigation demand. 256 F. Supp. 3d at 696. But the sensible and fair result could not obtain in that

case without overruling Michigan's express statutory and common law limitations, which the court could not do. *See id*. As the *Syntel* Court concluded: "While there may be sound policy reasons that may at some point convince the Michigan Supreme Court and/or the Michigan Legislature to permit a fee award for a benefit conferred without litigation … the current state of Michigan law does not permit such an award." *Id*.

While Michigan law is demonstrably inapposite here, the Supreme Court of Nevada has routinely looked to Delaware precedent to shape Nevada's rules governing stockholder litigation.[7] Operating under a rule materially identical to NRCP 23.1,[8] Delaware judges have concluded that the policy underlying the substantial benefit doctrine applies with equal force to litigation and pre-litigation demand resolutions of meritorious claims. *Bird v. Lida*, 681 A.2d 399 (Del. Ch. 1996); *Raul v. Astoria Fin. Corp.*, 2014 Del. Ch. LEXIS 103, at *16-17 (Del. Ch. 2014). In so holding, Delaware courts have rejected the same arguments Digital Ally makes here. Specifically, the Delaware Court of Chancery rejected the argument that attorneys' fees must be unavailable for a litigation demand on the ground that precedent required claims to be meritorious "when filed" – an

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[7] *E.g.*, *Parametric Sound Corp. v. Eighth Judicial Dist. Court*, 401 P.3d 1100, 1102 (Nev. 2017) (noting past reliance on Delaware corporate law and abandoning established Nevada precedent to adopt Delaware's test for distinguishing between direct and derivative stockholder claims) (citing *Tooley v. Donaldson, Lufkin & Jenrette, Inc.*, 845 A.2d 1031, 1033 (Del. 2004)); *Kahn v. Dodds* (*In re AMERCO Derivative Litig.*), 127 Nev. 196, 218, 252 P.3d 681, 697 (2011) ("To determine whether demand upon the board is excused, we apply standards articulated by the Delaware Supreme Court"; citing six Court of Chancery decisions) (citations omitted); *Shoen v. SAC Holding Corp.,* 122 Nev. 621 at 641 (finding "[t]he Delaware court's approach is a well-reasoned method for analyzing demand futility and is highly applicable in the context of Nevada's corporations law").

[8] *Compare* NRCP 23.1 ("The complaint shall also allege with particularity the efforts, if any, made by the plaintiff to obtain the action the plaintiff desires from the directors or comparable authority and, if necessary, from the shareholders or members, and the reasons for the plaintiff's failure to obtain the action or for not making the effort.") *to* Del. Ch. R. 23.1(a) ("The complaint shall also allege with particularity the efforts, if any, made by the plaintiff to obtain the action the plaintiff desires from the directors or comparable authority and the reasons for the plaintiff's failure to obtain the action or for not making the effort.").

argument the court dismissed as "stunted literalism" not "grounded in theory or practice[.]" *Bird,* 681 A.2d at 404-05.

The policy underlying Delaware's rule is that public corporations and their stockholders face an insurmountable collective action problem because, although expenditures on monitoring public companies and enforcing directors' fiduciary duties benefits stockholders collectively, each individual stockholder owns only a fraction of the corporation and therefore has "little incentive to incur those costs himself in pursuit of a collective good[.]" *Bird,* 681 A.2d at 403. The law solves this problem by "awarding to successful shareholder champions and their attorney's risk-adjusted reimbursement payments (i.e., contingency based attorneys fees)." *Id*. (citation omitted). However, racing into court is not the only way to remediate corporate wrongdoing. Nor is it the most efficient in a situation in which, as here, a stockholder can prompt the correction of discrete wrongdoing by demanding that a company address the issue or face litigation should it refuse. "Substantially the same benefit accrues to the corporation whether it be as a result of the demand or of successful litigation." *Id.* at 404 (citation omitted). Granting a fee for a successful litigation demand serves many positive purposes, not the least of which is discouraging unnecessary litigation and avoiding costs while encouraging stockholder vigilance and careful management. *See id*. (citation omitted).

This case exemplifies why sound policy supports providing compensation for successful litigation demands. Attorneys' fees are awarded not to promote litigation, but to provide incentives to encourage appropriate corporate monitoring and ultimately produce positive outcomes for companies and stockholders. *See In re Activision Blizzard, Inc. S'holder Litig.*, 86 A.3d 531, 548 (Del. Ch. 2014) ("'In [incentivizing counsel with contingent fees], corporations are safeguarded from fiduciary breaches and shareholders thereby benefit.' Understood from this perspective, well-founded stockholder litigation becomes 'a cornerstone of sound corporate governance.'") (citations omitted). Here, very impactful (and potentially catastrophic) defects in Defendant's capital structure

were detected and remedied as a result of Plaintiffs' Demand. Although a demand was not legally required before filing suit, counsel concluded that it made sense for stockholders and the Company to attempt to fix the defects efficiently through a litigation demand. Counsel was correct. Contrast that situation to *Galena*, where a similar remedy was obtained only after a fire-drill of expensive, expedited litigation. The result obtained here was superior to the result in *Galena*, and less costly and disruptive to the corporation. As aptly asked by the court in *Bird*:

> If we appreciate the collective action problem of shareholders and the neat solution to the collective action problem that paying a bounty to successful shareholders lawyers represents, why should the law care whether Mr. Bird conferred a benefit through a meritorious legal claim or through stimulating the board simply to act in a way he correctly thought was advantageous? In either event the collective action problem of shareholders was overcome and a substantial financial benefit was realized by the corporate collectivity.

Id. at 407. Awarding counsel in *Galena* $250,000 and counsel here $0 would promote a rule that incentivizes litigation for its own sake, rather than the efficient and successful outcomes that stockholders and courts care about. The message sent would be clear: either clutter the courts with unnecessary litigation or forego collectively wealth-creating monitoring efforts.

CONCLUSION

Digital Ally does not deny that Plaintiffs' Demand substantially benefitted the Company's stockholders. Nevertheless, the Company asks the Court to allow it to freeride on Plaintiffs' efforts and deny them any fee – all because Plaintiffs did what was best and most efficient for stockholders. That outcome is neither required by Nevada law nor consistent with it. Accordingly,

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the court should deny the Defendant's motion to dismiss.

Dated: December 21, 2018

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CERTIFICATE OF SERVICE

I hereby certify that on the 21st day of December, 2018, I served a true and correct copy of **PLAINTIFFS' OPPOSITION TO DEFENDANT'S MOTION TO DISMISS COMPLAINT UNDER NRCP 12(b)(5)** as follows:

X By electronic case filing and service through the Court's e-filing service (Odyssey)

___ By U.S. mail, first class postage prepaid to the address below

___ By electronic mail to the e-mail address(es) listed below

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EXHIBIT 1

EXHIBIT 1

IN THE COURT OF CHANCERY OF THE STATE OF DELAWARE

IN RE GALENA BIOPHARMA, INC. : Civil Action
: No. 2017-0423-JTL

- - -

Chancery Courtroom No. 12B
Leonard L. Williams Justice Center
500 North King Street
Wilmington, Delaware
Thursday, June 14, 2018
9:59 a.m.

- - -

BEFORE: HON. J. TRAVIS LASTER, Vice Chancellor.

- - -

CONTINUED SETTLEMENT HEARING AND RULINGS OF THE COURT

- - -

CHANCERY COURT REPORTERS
Leonard L. Williams Justice Center
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- - -

THE COURT: Good morning, everyone.

COUNSEL: Good morning, Your Honor.

MR. DAVENPORT: Your Honor, Kevin Davenport, Prickett, Jones & Elliott on behalf of plaintiff. With me at counsel table is Eric Juray and Paul Fioravanti from my office.

THE COURT: Great. Welcome. Thank you for being here.

MR. DAVENPORT: We're here today for the Galena Biopharma settlement hearing.

I'll jump right in with class certification. The class here consists of holders on the record date for the 2016 annual meeting, 2016 special meeting, and/or 2017 special meeting. We've set forth the elements for class certification in our opening brief. Class certification is unopposed by defendants, and we respectfully request the Court certify the class.

As described in the settlement administrator's affidavit of mailing, notice has been sent to the class in accordance with the scheduling order. Over 45,500 copies of the notice have been provided. The settlement administrator's affidavit of mailing stated that 44,216 copies were mailed on

February 25, 2016, and noted in a footnote that an additional 4,890 requests had come in the prior three days. Turned out about 4,000 of those requests were duplicates. So -- and then there were another 300 copies that went out after the first settlement hearing. And the way the duplicates were determined by the settlement administrator, it had to be the same number and the same address. If it was the same name and a different address, two copies went out. If it was different names and the same address, two copies went out.

As to the notice itself, Your Honor, we informed the Court that there was a discrepancy in the deadline for the objections between the scheduling order and the notice. I apologize again for that error.

There were no objections to the settlement. No one contacted us to ask for more time, and stockholders have now had another 90 days, and no objections have been made.

Turning to the settlement, the consideration here is $50,000 in cash and $1.25 million in stock. Given the particular circumstances of this case and this company, we agreed

to take stock and will sell that stock for cash and distribute it to class members. The stock sales will be handled by Huntington Bank, which maintains the settlement fund.

The stipulation limits the amount of stock that can be sold daily, and the plan of allocation provides for the stock to be sold as soon as reasonably practical within the limits of the stipulation. Huntington requires a stock sale instruction letter from the settlement administrator which will state that Huntington is directed to sell X number of shares which we will know when we get the maximum number of shares they can sell each day. That's based off the average volume of the 10 days leading up to it. And there will be no minimum or maximum price in the stock sale, and the instruction letter plans to sell the stock as promptly as reasonable possible after it goes into the fund.

If the Court approves the settlement, we can provide Your Honor with the instruction letter as part of an administrative order before any stock is sold, if Your Honor would like, or we can just proceed as I just described.

The plan of allocation provides for

the settlement proceeds to be distributed pro rata to class members that held as of the record date for the 2016 special meeting, which we believe is a fair and reasonable allocation plan.

Regarding the merits of the claims themselves, the allegations of the original complaint were that votes were incorrectly counted, which was the only logical conclusion that you could draw from looking at the proxy statement and the disclosed voting results. The defendants subsequently told us the disclosures were false. They produced an e-mail from the New York Stock Exchange that said the certificate amendment votes at issue in the case were routine matters. So brokers were allowed to vote in their discretion.

We still had a disclosure claim, and we uncovered evidence that the polls for the certificate amendment were left open overnight at the 2016 annual meeting, but we would still need to prove a nonexculpated breach and damages, which would have been difficult here. On balance, obtaining value directly for the class for these claims is a good result and one that we may not have been able to achieve through a trial.

Also counseling in favor of approving the settlement is, the release here is more narrow than releases in other actions. The release does not include unknown claims. It specifically carves out federal claims, existing federal lawsuits, and the release does not extend to defendants' agents, advisors, or affiliates.

So for those reasons and the reasons explained in our brief, we'd respectfully request the Court approve the settlement.

Turning to attorneys' fees. Attorneys' fees for the creation of the settlement fund, we're seeking 15 percent and asking that the percentage be applied after the settlement stock is sold so it's net of any costs in selling the stock, which we're told will be 2 cents per share plus a transaction fee for the bulk stock sales. So that would be 15 percent of the $50,000 plus the cash proceeds from the stock sales less the cost to sell the stock.

The primary factor --

THE COURT: Say that formula again.

MR. DAVENPORT: Sure. So it's 15 percent of the $50,000 in cash proceeds plus the

cash proceeds that are generated from selling the stock, which will be net of Huntington Bank's costs, which will be 2 cents per share to sell it. So the idea was to try to replicate a cash fund as best that we could. And this way, you know, whatever percent -- whatever actual amount of attorneys' fees would get paid are proportionate to what the class will ultimately get.

Now, the primary factor to consider in awarding attorneys' fees under *Sugarland* is the benefit conferred. The benefit here of recovering value that will be paid directly to stockholders for disclosure claims on certificate amendments supports the full fee request.

The settlement was reached several days before depositions were scheduled to start, but the litigation was expedited and trial was only a month away. The parties had completed document discovery and written discovery.

As we explained in our brief, the other *Sugarland* factors support the request as well. There's been no objection or opposition to this request, and we respectfully request the Court award the full amount.

We are also seeking an award to plaintiff Mr. Patel $13,000, which will come out of any attorneys' fee award from the settlement fund. We've explained the basis for this request in our briefs. We've also explained the reasons for why defendants should not be heard on their arguments against any award and why those arguments should be rejected. Mr. Patel was actively involved in analyzing the case, including discovery and negotiation of the settlement, and we ask that he be awarded the full amount.

THE COURT: How did you come up with that number?

MR. DAVENPORT: Your Honor, I don't think there was any sort of magic or algorithm to it. It's a number that we discussed with Mr. Patel and agreed to seek.

THE COURT: Yeah. I mean, from my standpoint, if you're going to pick one, it's an odd one to pick. And I say "it's an odd one to pick" because it's definitely more than I've been awarding in these situations where people really haven't done a lot, but then it's also just an odd number. I mean, 13 isn't a number that in our Western culture people

naturally cling to or are drawn to. In fact, if anything, superstition drives people to avoid 13. Also, in our culture, at least the human culture, because we have, you know, five fingers on each hand and five toes on each foot, we tend to think in, like, base 10 and, hence, increments of 5.

So it struck me as just an odd number to pick out. Now, there are some cultures where 13 is lucky. But -- and I didn't know if it translated to some sense of how much time Mr. Patel had put in. It struck me as something where you look at it, you say well, how did these guys get this one?

MR. DAVENPORT: Understand. I don't know that Mr. Patel is an especially superstitious person. This is -- I don't know ... what more I can say other than this is just the number that we discussed with Mr. Patel and sought to seek. It isn't based on, you know, a specific time or stock or anything like that.

THE COURT: You didn't do some back-of-the-envelope time-value calculation.

MR. DAVENPORT: No. No, Your Honor, we didn't do that. This is just the number that we agreed to request the Court to award.

THE COURT: And let's see. If I give you-all everything you request, you'll get basically 400,000; right?

MR. DAVENPORT: Something right around that, yes, Your Honor.

THE COURT: Something right around there. So it's not even an easy multiple of that. If I were to think about it, okay, maybe they're thinking 1 percent of what -- or, you know, 2 percent, 3 percent. It's not even a multiple there. Like, it doesn't seem to correspond to anything.

MR. DAVENPORT: It's 1 percent of what the total settlement fund would be, but that -- obviously, Your Honor, that wasn't the reason we picked it. So I don't have a specific reason why it was 13,000 instead of, you know, 12 or 14 or 10 or a different number. That's just the number that we discussed and --

THE COURT: Well, I guess that's a good one. You actually made a good point. It's so obvious, I'm embarrassed I didn't think about it. But you're right. If you add the cash component, basically you're saying that he ought to get 1 percent of the total fund is what it would work out to.

MR. DAVENPORT: That's what the number works out to, yes, Your Honor.

THE COURT: Yeah. As I say, I'm sort of embarrassed that didn't jump right out at me. I was so fixated on the superstitiousness of 13, it didn't occur to you. Is that how you got to it?

MR. DAVENPORT: It's not. I can't say that that's how we got to it. It's actually something that I didn't realize until we, you know, went to brief it. But, you know, that's just the number that we discussed and agreed to seek. It also happens to be 1 percent of what the settlement fund is.

THE COURT: And it's part of what I had to wrestle with in that *Chen* case, because I had a named plaintiff there claiming that he was a real part of the litigation team and, hence, rather than doing a fee, an incentive fee, the way I think we've traditionally done, which is not very scientifically or even with any type of discernible thought process, here -- there, he -- what he was arguing for was you should essentially view the incentive fee and the contingent compensation of the attorneys as a total package of incentive compensation for those people who are working as part of the team to get the result.

And then what the Court should be doing is allocating among those members of the team how much each should get.

And there, his pitch was that -- and I forget whether he said he was equally responsible or a third responsible or what. But his view of the world was that he had been such an active component and part of the team, that he really should get some substantial portion of the total fee at 30 percent or 50 percent, if my memory fades. And he did do a lot of work.

I personally found that way of thinking about these things fairly principled and comprehensible in terms of a way to go about it. Like, from a theoretical standpoint, it had the virtue of actually being transparent, understandable, a reasonable alternative to doing some type of hourly calculation based on some perceived time value. But it's nothing that I think ever has been written down as a viable way of approaching these things or anything like that.

MR. DAVENPORT: I think that's very helpful guidance to have in --

THE COURT: I'm not guiding anybody.

I'm having a discussion with you. What do you think? Is -- in terms of the -- if you had to think about who did the work for getting this result, would it be fair to say that of the amount of the fees that are being allocated to the team, that Mr. Patel did what would work out to essentially between 3 and 4 percent, that his contribution was 3 to 4 percent that have?

MR. DAVENPORT: I think that's a reasonable -- and I think that's a reasonable approach. I think what we really did was looked at what everything Mr. Patel did in the case and trying to arrive at the 13,000, and that's what we agreed to seek in believing that that was reasonable. We didn't do the math that Your Honor just went through. I think that's a reasonable way of thinking about it. And I would agree that when you look at it on that basis here, 3 to 4 percent is a fair and reasonable number.

THE COURT: So what did he do? Because in terms of things that were transparent to the defendants and which, at least, you know, from docket entries and things are transparent to me, frankly, doesn't seem to have done that much. But part of what Mr. Chen came in in the *Occam* case and

showed there, he did do more of the transparent things. He had been vigorously attacked by the defendants, deposed, you know, dragged through the mud in terms of accusations and that type of thing. But what he was able to show was behind the scenes he was providing a very sophisticated level of input to counsel in terms of analyzing theories, doing valuation work. I mean, the guy really did an amazing amount.

So I would -- there's no way -- it would not be credible to me that Mr. Patel did anything like Mr. Chen did, only because Mr. Chen seemed so exceptional in that regard. Maybe he did. I don't know.

What types of things did Mr. Patel do with you guys?

MR. DAVENPORT: Well, Mr. Patel -- that was involved really at every stage, both in analyzing the SEC filings before we filed any complaint, before we spoke with him. And then at each stage, both when we amended the complaint and when we went through discovery and looking at the documents and analyzing the documents, each step in the settlement process, really on a, you know,

move-for-move basis Mr. Patel was, you know -- we were actively engaged in discussing with him. He did produce us documents.

He did produce -- we did serve interrogatory responses. He was prepared to be deposed, but we reached a settlement shortly before that. And sort of -- you know, in the nature of a highly expedited case that was headed to trial in a month, you know, the fact that we settled it before anyone was deposed I don't think should be held against us both as the attorneys and against Mr. Patel for having sat for a deposition simply because we were able to obtain a settlement before we got to that point.

THE COURT: Were you talking to him? I mean, in the old days, the old model was, you know, Mr. Lerach saying he didn't even have clients, and the idea that the belief used to be that you would get your named plaintiff, and then the great thing was you never had to talk to him again. And part of the difficulty of actually getting the affidavits required for submitting a settlement was you had to go back and find the person you were ostensibly suing on behalf of because they might have moved, they might even have

left the country. And so sometimes people just -- they couldn't even find their named plaintiff. And so you'd get these requests to substitute in someone at the end for purposes of settlement because nobody had talked to this person in years.

So what was going on in terms of your communications with Mr. Patel?

MR. DAVENPORT: That was definitely not Mr. Patel. What Your Honor just described was definitely not Mr. Patel. I don't have the exact number of communications that we had with him, but it was easily over 150, you know, back and forth communications with him.

THE COURT: It was regular. 150 is a lot. I don't know if I talk to my wife 150 times.

MR. DAVENPORT: Well, I would say start to finish the case from then to now. I didn't sort of separate it, but I did try to look back at the communications we had with Mr. Patel and also numerous, numerous telephone conversations. I can't estimate exactly how much time I spent and that, you know, others at my firm spent speaking with Mr. Patel and communicating with him. But the communications, they were extensive, and he was actively involved at

each stage.

THE COURT: All right. Thank you.

MR. DAVENPORT: Next, Your Honor, we're seeking a fee of $250,000 for the benefits under Section 204 and 205. Again, under *Sugarland*, the primary consideration is the benefit conferred. The litigation caused defendants to hold the 2017 special meeting. This provided stockholders with disclosures and the Court with the benefit of the voting results on the 205 petition. And the litigation also caused entry of the validity order that validated five certificate amendments and hundreds of millions of shares.

Finally, the litigation stopped defendants from continuing to make the same false disclosure every single time they sought to amend the certificate. And as we explained in our brief, this benefit has already paid off in connection with the reverse split and the SELLAS merger.

Now, in our opening brief we cited *Cheniere*, *Colfax*, and *Xencor*, which were cases involving validity orders under 205. And *ev3*, which predated 205, but it's been cited in 205 cases for comparable benefits. We've explained in our briefs

how the benefits and the fees awarded in those cases, which were between 375,000 and 1 million, compared to the benefits here and fully support the $250,000 fee request.

Defendants, they didn't cite, let alone distinguish, any of these cases in arguing that no fee should be awarded. Their position that no fee should be awarded is a default. Their failure to distinguish the cases that we cited is a concession that those cases are reasonable benchmarks and apply and support the full fee request.

The defendants also make arguments that were specifically rejected in the cases that we cite. Their argument that there are no benefits here because Galena was returned to the same position as before the litigation, that's wrong. And that's been rejected repeatedly in the context of 205 validity orders.

Defendants' argument that the litigation didn't cause the benefits is both legally and factually unsupported. Defendants admit the litigation caused them to recognize the disclosure was false. They argue that because they filed the 205 petition, they get all the credit for the correction,

but that's exactly what the corporations in *Colfax* and *Xencor* and *Cheniere* did. The defendants in those cases weren't given any causation credit. The defendants here especially can't take credit because they were told by a stockholder after the 2016 annual meeting that their disclosures and voting results couldn't be reconciled. Defendants called the stockholder annoying, dismissed his e-mail and then made the same false disclosure several months later at the 2016 special meeting.

Defendants made several other arguments about double-dipping, challenging our time and expense and seeking to shift fees. We've addressed those on our reply papers. So I won't repeat those responses to the arguments, unless the Court has any questions.

So, Your Honor, we respectfully request that the full $250,000 be awarded.

Thank you.

MR. ROHRBACHER: Good morning, Your Honor.

THE COURT: Good morning.

MR. ROHRBACHER: Blake Rohrbacher, Richards, Layton & Finger, for the defendants. With

me from my office is John O'Toole.

THE COURT: Great. Thank you all for being here as well.

MR. ROHRBACHER: So the big question for today was whether we would get the no-action letter. I'm happy to report that the answer is yes and really, actually, in spite of plaintiff's counsel. As things got down to the wire with our resubmission, we were asked by the SEC for a factual basis for a statement that plaintiffs had made in a letter to this court. The SEC set a call on short notice to discuss those questions, and one of them involved the statement by plaintiff's counsel. The SEC believed the statement was false and demanded that we confirm the facts. So we reached out.

The response I got was startling, Your Honor. Mr. Brown --

THE COURT: What was the statement?

MR. ROHRBACHER: The statement was that -- the quote from Mr. Davenport's February 28 letter on page 2, the quote is: "As Plaintiff's Counsel has already explained to Defendants, Settlement Stock cannot be distributed directly to Class Members for numerous reasons, including that

nominees will not accept stock on behalf of their numerous beneficial holders."

THE COURT: Okay. So that was the statement. What I hear you saying is the SEC believed that that was an inaccurate statement.

MR. ROHRBACHER: Because they've seen other situations where nominees did accept stock. So they said, you know, "What's going on here? We need to have a call in an hour or two to discuss this."

THE COURT: All right. So then you were about to tell me about being startled.

MR. ROHRBACHER: So Mr. Brown called me back. He was, first of all, furious at me for letting the SEC know about the statement, a public statement that the Court -- in a letter to the Court. He threatened to come after me, I believe for sanctions, if I ever did it again. He was furious that we had acted as a, quote, middleman with the SEC and demanded that any other inquiry from the SEC should be directed to him and him alone so that he could refuse to answer the SEC's questions because he thought they were silly and did not deserve an answer.

So after getting that helpful response, we had the call with the SEC, with nothing

to report on that point.

To be fair, I called Mr. Davenport the next day to explain how unhelpful Mr. Brown had been. And he did offer to provide the information we'd sought the day before, but the call was over by that time. Nevertheless, we did get the no-action letter.

So as Your Honor may recall, Mr. Patel sued Galena and certain officers and directors for breach of fiduciary duties and to invalidate the results of three votes to amend the company's charter. His original claim was that the votes approving those amendments were invalid because the brokers have improperly exercised discretionary authority to vote shares regarding which they had not received voting instructions.

He then recognized that these claims were wrong as a matter of law and fact. So he now essentially challenges the company's disclosures months and years after those disclosures were made.

So I understand that our position is unusual in that Patel's counsel is not entitled to any fees for that, the 204 and 205 issues. They are, of course, getting the fee on the class action award. But let me explain why we are taking that position.

Essentially, this relief was obtained by Galena through Galena's efforts and in spite of plaintiff's efforts. So as Galena said in its public filings, Mr. Patel's litigation placed a cloud on the company and its capital structure. The litigation constrained its business. We disclosed that it prevented certain strategic transactions and threatened the company's survival.

So Galena sought to mitigate the effects of the litigation by publicly validating the amendments even though the amendments were valid and were valid under Delaware law. We asked early on if Mr. Patel would join us in removing the cloud that this litigation had caused by agreeing to a 205 order so the parties could focus on the fiduciary claims. He refused, obviously because he wanted the litigation leverage and didn't care about what the uncertainty of the stock meant for the other stockholders.

So we set out on our own under Section 204. Galena's board approved the ratification of the charter amendments and sought approval from its stockholders. And Your Honor will recall that Mr. Patel sought to enjoin that vote. His attempt was rejected, and this court ordered the parties to agree

to a trial schedule.

We held a special meeting to approve the ratification, and each ratification proposal passed. After expedited written discovery, the parties began discussing settlement. We weren't worried about the fiduciary claims, but we needed to get rid of the doubts that the company was facing because of the litigation.

So we negotiated a settlement agreement that would have allowed us to obtain a Section 205 order. Because of the financial status, which had been made clear, we didn't fund it with cash. We had to fund it with stock. We entered into a binding term sheet. Mr. Patel refused to proceed with the settlement. We had to come to Your Honor to get enforcement. Your Honor granted enforcement. We filed the stipulation, got the no action -- well, we all ended up here a couple months ago without the no-action letter. Mr. Patel asked the Court to reject the settlement at that time. But Your Honor adjourned it so that we could get the no-action letter, which we, as I said, ultimately did.

So I'll move to the fee and correct a few of the statements that Mr. Patel made. So we saw

references in the -- in their briefs to the motion to expedite teleconference that we had with Your Honor where Mr. Patel challenged the 204 vote and we had no opportunity to fully address the merits of those arguments. The message from that side is that the 204 vote was invalid and that he was correct in trying to stop it. We see that page 46 of his opening brief is a good example. It's a bit inconsistent with the demand for fees and causing a benefit that you say is invalid, but, you know, that's just one of the fun parts of their argument.

The 204 vote was the opposite of what he wanted because he didn't care about what -- the invalidity of the stock would mean for his fellow stockholders. He wanted to keep the litigation leverage. So he should not get any credit for the curbs of the 204 vote.

And here's the fact missing in Mr. Patel's briefs. This court ruled, paragraph 1 of the validity order on December 11, that "The 204 Ratification is hereby validated and declared effective." Footnote 2 of Mr. Patel's reply brief says that the 204 ratification was "ineffective for purposes of ratifying the certificate amendments ...."

So that is just wrong and inconsistent with this Court's ruling. So Mr. Patel should get no credit for the 204 ratification, given that his entire litigation efforts were devoted to stopping it.

THE COURT: Can you unpack, though, the question of the inclusion of putative stock on the vote, like what the positions were and where that came out?

MR. ROHRBACHER: Well -- so, again, it came up in a motion to expedite. He said, "Oh, you can't do it, there's just no way." We were -- at that stage I don't think we -- we didn't engage on the merits because of the stage. We eventually, in our brief on December 8 supporting the 205 validity order, went through the two primary arguments. And those are on pages 21 and 22 -- or 23, 4, and 5, I guess, actually, of the brief.

One is -- there were two. One is that all the shares were valid. So it was good. And the reason is that the board of directors set the date of the record date for the ratification vote and, by definition, those shares would all have been in the pot that he challenged. So the board effectively had to conclude that those were valid shares. And

Section 204(h) says in the absence of actual fraud, the judgment of the board that shares are valid is conclusive unless this court decides otherwise.

So they're either all valid because the board's decision would have been illogical otherwise, or if everything was putative, because of Mr. Patel's position that you couldn't separate the putative from the valid, 204 gives you another fix, which is if it's not valid, it's putative, and if it's all putative, there's no stockholders to vote, so you don't need a vote at all and you can do it just through the board.

So those were the two arguments. It's either all valid because the board necessarily determined that they were valid, or if some were putative but you can't distinguish the two, then they're all putative and you don't need the vote.

And I will note that the statute is being clarified this year to confirm that what we said was exactly the way that 204 is supposed to work.

THE COURT: Wonderfully expansive verb, "clarify."

MR. ROHRBACHER: So I still think we were right, but the statute merely confirms it.

So the 204 was something that we got in spite of Mr. Patel. His No. B. of his prayer for relief of his amended complaint was enjoining the 204 meeting. So we wrested it away from him, and now he takes credit for it.

The 205 order, Mr. Patel suggests that was required under the stipulation. It's in both of his briefs. That wasn't something he got in the settlement. It is something we got. We required him to consent to a validity order. That's fairly clear in paragraph 19. We weren't required to seek the order. That was something he had been seeking from the beginning. But, again, the 205 petition only became necessary, first of all, because the litigation put a cloud on the company, but because he was actively opposing the 204 ratification. We never would have needed the 205 if the 204 hadn't been challenged.

So the one thing that he says is a great benefit, the 204, he was against; the other thing he said was a great benefit, we only had to get because of his opposition.

Now, *Orchard* at *4 says, a plaintiff's counsel, quote, only should receive fees for the

portion of the benefit to which they causally contributed. Here, Mr. Patel actively opposed the benefit. So looking at the amended complaint, I mentioned prayer for relief B. was stopping the 204. C. was declaring one amendment not valid. And D. was declaring the other one not valid.

So this is not like a case where you ask for disclosures and get some of the disclosures. This is a case where he had to lose for us to win. And the 204 petition, as we have said, did little more than erase the stain that the litigation had already caused. So the notion he's claiming credit for it is, you know, received was an unnecessary expense and effort caused by hi own refusal to let Galena clean up the issues.

Now, Mr. Davenport, and then in his briefs, mention the *Cheniere*, *Colfax*, *Xencor*, *ev3*, which was pre-205. But in each of those cases there was some statutory validity that was cured as a result of plaintiff's litigation. That is not the case here. Here, it's just a reversal of the uncertainty created by the litigation. The votes were validly counted. The charter was validly amended. Were there disclosure issues? Yes, some of them several years

old. Mr. Patel didn't even challenge them, and they're outside the bounds of what the class would even apply to.

But to the extent we connected the disclosures long after the votes were already taken, no fee, we submit, should be awarded for such an illusory benefit. Plus, any fee that is awarded should be reduced to account for Mr. Patel's breach of the term sheet. That breach cost Galena time and money. I quantified the amount of costs in an affidavit with our papers. Galena deserves to be made whole for that. It shouldn't have to pay double.

The reason that the settlement was structured this way was because we didn't have much cash. That hasn't changed. Mr. Patel's argument, "Well, you didn't ask for fees back then." Well, it wasn't like a contempt motion. But Your Honor found that Mr. Patel beached the term sheet. The term sheet is a contract. We were damaged by the breach in having to enforce it. Those are contract damages. And we submit it makes no sense to invite a formal counterclaim for contract damages, but it would be cleaner just to set it off against any fee. And Your Honor can certainly consider the issue in the

discretion to award a fee.

So I'll turn now to Mr. Patel's $13,000 payment for himself. Now, as an initial matter, we did not give up standing to oppose. Mr. Patel argues that the *Activision* case controls, and he's wrong for a couple reasons. First, in that case, the defendants agreed not to oppose the application for a fee award, which is why this court held that defendants' objection would not be considered. We did not have the same agreements here.

And, second, in that case the plaintiffs specifically included in the stipulation a provision that they expected to seek a special incentive award. Here, they did the opposite. Paragraph 18 of the stipulation provides: "Plaintiff's Counsel warrant that no portion of the Fee and Expense Award shall be paid to Plaintiff or any Class Member ...." Now, it says, "... except as approved by [this] court." So there is the little out there. But if they're going to get credit for that little out, they do say in the notice that they intend to seek 13,000; but in the notice we said we may oppose.

And so if they get the -- if they get

to sneak around what the stipulation says through the subject of the approval of the court language, then we should not be bound by any agreement that was in there and we should certainly have standing to oppose.

THE COURT: But first there's a bigger question, though, of how you're harmed if allocation comes from the total award.

MR. ROHRBACHER: So we are not harmed because this -- well, because it doesn't come from the total award. It doesn't come out of the amount that we pay. It comes out of the class award. And so there's no actual harm to Galena. But -- so we are making this argument, you know, based on the integrity of the process and --

THE COURT: You're championing --

MR. ROHRBACHER: -- standing up for the -- championing --

THE COURT: Who are you championing? You're championing -- I mean, who do you view yourself as championing in this instance?

MR. ROHRBACHER: Well, in this instance, we had to go through this litigation. We had to deal with a --

THE COURT: No; I understand that.

But in -- and I also understand that, you know, there's a general long-term reason for people who are positioned institutionally to more often resist stockholder representative litigation to seek developments in the law that make it less attractive for people to bring stockholder litigation and, hence, that there may be institutional reasons as a player in the litigation environment not to want there to be, you know, any type of remuneration, or at least that to be restricted.

But in terms of the actual people involved in this case, you guys, class, counsel, Mr. Patel, like, who are you helping out?

MR. ROHRBACHER: So the way that they structured it, to follow Your Honor's argument to its logical conclusion, nobody would have a chance to object because it doesn't harm the stockholders, either. The -- counsel is going to get a fee and that fee is X. Well, if Mr. Davenport decides to take less than X and give that share to Mr. Patel, it's still X. So Your Honor could say the same thing -- if every member of the class came in and was lined up behind me saying "We don't think Mr. Patel should get $13,000," if Your Honor says, "Well, how are you harmed, madam?

How are you harmed, sir?" They all have the same answer: "Well, no, it doesn't come out of my pocket," Your Honor, because the way they've done it, it's already an amount that's coming out, whether Mr. Patel gets it or not. And so --

THE COURT: Yeah. I think the distinction to be drawn there -- and you can correct me if I'm misunderstanding this -- but the class wouldn't have agreed not to oppose a total fee amount. And so the class could make the argument of pay them less. And if that comes out of, you know, their 15 percent, if that means that they don't want to pay Mr. Patel 13 and they, you know, really only want to pay him 8 or 5 or whatever, like, great. Or they could even say back them down. Give them, you know, 15 minus whatever the deduction you give -- 15 percent minus whatever deduction you give for Patel. But didn't you guys agree not to oppose?

MR. ROHRBACHER: We did not, Your Honor.

THE COURT: Oh, you did not agree to oppose.

MR. ROHRBACHER: No.

THE COURT: Then that's the answer.

MR. ROHRBACHER: And the other thing is if that is true, then Your Honor's given us standing the other way because we're trying not to give them the 250.

THE COURT: I know you're trying to --

MR. ROHRBACHER: And so --

THE COURT: -- not give them the 250.

MR. ROHRBACHER: -- if Mr. Davenport gets our 250, then it's easier for him to be generous with the 13. So it's the same analysis as, you know, how much -- if standing is based on how much does Mr. Davenport take home, then we have standing under that because we're part of his take-home, you know, argument.

THE COURT: So would you -- if I whittle away or eliminate his 13, is your pitch that you want the 13?

MR. ROHRBACHER: No. No. We're not -- we're not trying to get the 13 back that. 13, the way that that fee is structured, that 13 comes out of the class. And so we're not saying that it should be -- that it should be lower or higher. And we could have --

THE COURT: So I guess maybe that's --

so that's the distinction; right? I mean, it seems to me, then, that's the answer to how the class is different from you-all, is you-all have agreed to the amount that will go to the class. And so there's no opportunity for you to get more, whereas a class objector would have the opportunity to get more.

MR. ROHRBACHER: So --

THE COURT: Your pushback, I guess, is on the 250,000.

MR. ROHRBACHER: So it's primarily the 250. And I guess I misspoke a little bit. We have not agreed to not oppose the 15. But we have not -- I think we mention it in our papers, but we've not pushed it hard because whether it's 10 or whether it's 15, yes, we think it should be lower; but -- so if -- if the 13 is part of that fight, then yes, we will join that fight. But we made the decision not to -- not to add a whole nother section to the brief to yell and scream about the 15. We did not agree to not oppose it. And if we knew that making that argument was the difference between having the ability to say 13 shouldn't go, then yes, we will say that Mr. Davenport should take 13,000 less because that should go to the class. And we're happy to make that

argument. We did not brief up the 15 percent because, you know, we figured that Your Honor would probably give them the 15 percent, given --

THE COURT: Just an irony in -- or at least -- I mean, you can again correct me. At least there's a surface irony in you-all not deciding not to oppose an aspect of the fee analysis that could potentially generate a bigger change in the outcome and choosing to oppose a portion of the analysis where we're dealing with $13,000.

MR. ROHRBACHER: Well, one, the 10 -- I mean, essentially the analysis is is it 10 or 15. And the fight on the class award I think is probably -- we probably -- most of us would agree that it's 10 to 15 because there was an actual quantifiable benefit created for the class. And so that's different from the 204, 205. That's a thing that created -- you know, a fund will be created. And so is it 10, is it 15, okay. So that's -- you know, that is some quantum of money.

But the -- you know, to fight that out, we would have to, you know --

THE COURT: But that's a $50,000 swing; right?

MR. ROHRBACHER: It is.

THE COURT: So what you guys sat down and said was $50,000, not worth fighting over. $13,000, man, we're going after this.

MR. ROHRBACHER: Well --

THE COURT: That's where I'm at least sensing some irony.

MR. ROHRBACHER: I would put it a slightly different way. $50,000 was an uphill -- a, you know, strong uphill battle to show why, in the middle of an expedited case, when document discovery had gone, had been expedited, we are about to start depositions, why it should be 10 as opposed to a situation where the Delaware law presumption is strongly against awarding a fee, where this particular person who breached a settlement agreement in the middle of the case and had to be brought to this court to enforce it, where the support is nonexistent for this kind of fee. There's no "I spent this many hours." There's nothing like Mr. Chen had, where -- and Mr. Davenport said that since we didn't cite *ev3*, we conceded that they're correct. Well, nor did they cite or distinguish any of the cases where we said, "Look, here are plaintiffs who did real work." They

came in with affidavits saying 50 hours. I think one guy was 90 hours. Here's a lot of work they did. No fee was awarded. Now, they did not cite those, so I guess by his logic that means that they're correct.

So if Mr. Patel gets a fee in this context there is no logic that would deny a fee to every other plaintiff in the class context who signs a verification for a complaint, signs a verification for an amended complaint, and signs a verification for interrogatory responses and documents. Those are four things we heard. Yes, there were a number of e-mails, but there's no basis -- there's no substantiation for that in the record.

So what Your Honor has --

THE COURT: I have Mr. Davenport. And, I mean, if we're still in a world where we believe Delaware lawyers, which I hope we're still in the world and I think you should want us to still be in that world -- I at least have Mr. Davenport telling me that, you know, he made 150 calls with this guy and he was instrumental in identifying the original disclosure violation and that type of thing and that would distinguish this from a case where some future Delaware lawyer could not stand up and legitimately

make those representations.

MR. ROHRBACHER: No. Okay. So that is fair. Now, this complaint, I think -- and Mr. Davenport can speak for himself. I think he meant the 150 was kind of global, was beginning to end.

THE COURT: Yeah, I think did, too, because that's what result I was thinking of. That was during the expedited discovery phase. As I say, that would be, like, five calls a day or five conversations a day. That's what prompted my sarcastic comment I'm not sure I even had that many conversations with my wife during the course of a month.

MR. ROHRBACHER: And so their complaint was filed in April -- late April of last year. So obviously they had conversations before the complaint. There are a couple for the verification, sending back some drafts. They had to produce documents. They had to get verifications for the interrogatories. They had to amend the complaint, schedule depositions. Then, you know, then he breached the settlement agreement.

So, you know, I don't know if it's 150 just in that stretch, but that doesn't seem crazy, and

we're now a year and change after that.

But not to forget these cases that they refused to talk about, but these are people who came in and quantified, "I spent 40 to 50 hours," "I spent 90-some hours." And they were denied fees because the presumption of Delaware law is that you don't give fees to class plaintiffs. Now, certainly people have gotten fees and they have done a ton of work. And I -- you know, that is what it is. But this particular situation, particularly where you have a breach in the middle, is not, we submit, one of those cases.

And so that is the reason why, standing up here getting grilled on the 10 versus 15 percent seemed a lot less attractive than going with the prevailing Delaware law on plaintiff fee awards. So a cost/benefit analysis, a going with the presumption on 13 is probably a better economic return than a very low percentage of 50.

THE COURT: I don't know. We'd have to do the math on that one. Are you a thousand-dollars-an-hour guy now?

MR. ROHRBACHER: Oh, no. I'm --

THE COURT: I keep seeing --

MR. ROHRBACHER: -- a simple country lawyer, Your Honor.

THE COURT: I don't ask -- seriously. I ask only because I see these -- I've been getting these fee petitions now with some regularity because we're doing a lot of contract cases that have prevailing party provisions. And so now, instead of the old fee petitions that I used to get from Mr. Fioravanti and his colleagues, I now get them from these -- you know, these big large firms. And it does seem like, if you are a big-city lawyer in New York, Chicago, you know, San Francisco and you're not billing a thousand dollars an hour, like, you're just -- you're sort of behind the times.

And the reason I ask is not to put you on the spot, but only it does figure into the cost/benefit analysis. If you're -- even if you're a 750 guy or something like that, you put four hours into a section of a brief, you're starting to get to a decent chunk of the potential swing.

MR. ROHRBACHER: As part of the -- that's just part of the -- that's just part --

THE COURT: That's just how the math works.

MR. ROHRBACHER: That is how the math works, but that, fortunately, is --

THE COURT: And I think --

MR. ROHRBACH: -- unavoidable.

THE COURT: I think you should be a thousand dollars an hour.

MR. ROHRBACHER: I will let the fee committee know.

THE COURT: I think you should. If you can get it, you should charge it.

MR. DAVENPORT: I'll be brief, Your Honor. And I want to clarify something.

The 150 estimate wasn't just phone calls. I was including any types of communications, e-mails. And I didn't want to suggest that I had 150 phones calls with Mr. Patel. That's not accurate. But we did have extensive communications with him on the phone and through e-mails.

Mr. Rohrbacher is wrong. Defendants have waived the right to attack Mr. Patel on the fee that we seek. The stipulation states: "The Defendants and the Released Defendant Persons shall have no input into or responsibility or liability for the allocation by Plaintiff's Counsel of any Fee and

Expense Awards." They've waived that.

And, you know, the personal attacks on Mr. Patel and us continue, Your Honor. I don't know how many times I heard today and saw in the briefs that Mr. Patel and my firm created a mess and put a black cloud over the company's head. To state the obvious, I didn't write their proxy statements. I didn't file the wrong certificate amendment that wasn't voted on at the meeting. The defendants did. The defendants created this mess.

And if Mr. Rohrbacher or other folks at the company want to get $13,000 back, they should go talk to TroyGould, the law firm that Sanford Hillsberg was a director at and was paid over $2 million to screw up their proxy statements.

I want to address another point. Mr. Rohrbacher said that the *Colfax*, *Cheniere*, and *Xencor* cases all dealt with statutory violations. First, they didn't address those cases, so he can't speak to them now. That's also not true. *Cheniere* dealt with the treatment of abstentions on a vote for an increase in an incentive plan under the New York Stock Exchange rules versus the bylaw rules. So that wasn't a pure statutory claim there.

This concept that they approached us and tried to get us to agree to a 205 early on and we refused. Well, what actually happened is we told them that we're not just going to settle the case and give them a release for 205. And if they want to, you know, pursue that route, they can go ahead and pursue the 205 route, but they weren't, you know, going to settle the case on that basis.

And I specifically told Mr. Rohrbacher before they tried to do the 204 vote, that the 204 vote didn't work and the explanations that were given today on putative stock they just don't hold up. 204 and 205 they don't require a board to admit that they screwed things up; but when you try to get a 204 vote to ratify things, you are acknowledging that the stock is invalid and that stock is then putative stock which can't be voted.

I don't want to hit on every point, but I do want to come back to the point that Mr. Rohrbacher started, which I think is completely irrelevant in describing a conversation that Mr. Brown and I had with him. What actually happened was after not hearing from the defendants and not being involved in any of the communications with the SEC for months,

I got a phone call out of the blue that said they have a call with the SEC in an hour and they want to know information about a statement I made in a letter three months earlier. And the statement that was in there was that it's going to be difficult, if not impossible, to get brokers, which is who -- you know, that's the -- the information that we have to pay the settlement proceeds on, is at the broker level. To get the brokers to take stock is going to be next to impossible. It can be difficult to get the brokers to take cash that they then have to distribute to their beneficial owners. It's next to impossible. It's going to be impossible to get them to take stock.

And, you know, the cases -- or the instances in which that may happen, what our settlement administrator told us if you have a claims-made process or some other instance where, you know, the ultimate beneficial holders are giving you account information, maybe you can pay it to them that way; but the way that we have this set up, it just doesn't work.

So initially, you know, after I kind of got the third degree on the phone trying to recollect conversations I had with the settlement

administrator from long ago, we resisted having further discussions and said the SEC can contact us if they have questions.

The settlement that we negotiated requires that we sell the stock. But then the very next day we called and offered them the opportunity to speak with the settlement administrator and they refused. So they just shouldn't be heard to complain about it today.

I just felt the need to address it because I thought it was irrelevant and I didn't agree with the description.

That's all I have, Your Honor, unless you have any further questions.

THE COURT: I don't.

MR. DAVENPORT: Thank you.

THE COURT: I appreciate you-all being here today. I'm grateful for your presentations. It was a healthy stack of documents that this settlement produced, a healthier stack of documents than perhaps the ordinary settlement, which is a good, maybe nine inches, ten inches as opposed to the perhaps two or three inches' worth of filings that used to be common in the old days where we would get to consider and

approve one or two settlements each month. I don't want to sound like I'm hankering for the old days. I'm using it for comparison purposes, not because I think that there was anything in any way redeeming about the era of nonlitigation litigation.

So we're here for the settlement in Galena Biopharma. I'm approving it. I'm granting the full amount of the fee award, and I'm authorizing payment of an incentive award, but I'm going to reduce that amount to $5,000.

The underlying complaint alleged that the defendants breached their fiduciary duties by improperly counting broker nonvotes as votes in favor of a charter amendment to increase shares of the 2016 annual meeting, and also in favor of a charter amendment to effect a reverse stock split at the 2016 annual meeting.

When the plaintiffs raised these issues, the defendants changed course and said, "We didn't really do what we said we were going to do in the proxy statement." As a result, from the defendants' standpoint, they treated the votes accurately and simply misdescribed them. The defendants figured out that they'd made the same

problem for disclosures for other charter amendments in 2011, 2013, and 2015.

It was asserted frequently in the papers and reiterated today that this was a problem that the plaintiffs created and that resulted in a stain on the company from the litigation, put a cloud over the company, created uncertainty that the company had to fix, et cetera. I think these statements reflect a profound lack of awareness by the defendants. This is a problem that they created by having inaccurate disclosures and initially creating the impression that they had actually done the votes improperly and then, when they decided to take the position that they hadn't done what they had said they'd done in the proxy statements, resulted in the unavoidable fact that the proxy statements were inaccurate.

That is a problem, to reiterate, that the defendants themselves created. They created the cloud over the company. They created the fissure in the capital structure. They created the stain. The plaintiffs were here to try to fix the situation.

The dynamic here is the same as a company that is guilty of fraud or other type of

wrongdoing, blaming the whistleblower for actually bringing to light the fraud and asking that it be fixed, then claiming that rather than the wrongdoers causing the problem, it's, in fact, the party that seeks to bring the problem to light and fix it that is at fault. As I said, I think that reflects a profound lack of self-awareness, as well as a desire to be free from any type of accountability. Most importantly, self-responsibility for doing what you're supposed to do, which is actually to put out accurate proxy statements that say how you're handling things and not to have direct conflicts between your proxy statement and what you actually did.

We then get to the next phase where the company sought to validate the actions under Section 204. The plaintiffs challenged the ability of the company to do that, resulting in a shift to a petition under Section 205. I think there were litigable issues over whether 204 could be used under these circumstances. I think the plaintiffs were justified and within their rights to want a valid validation rather than a potentially invalid validation. It wouldn't be very helpful to have an invalid validation. It has the effect of patching

over a crack in your foundation with plaster of Paris. You may be able to hide it, and if you're the type of person that says one thing in your proxy statement when you did another, maybe it will hide it long enough so that you can sell the property to somebody else. Maybe they won't see it for purposes of the inspection, but when it ultimately comes out that what you've done is try to plaster-Paris over something, you're not better off.

During expedited discovery relating to the validation efforts, the parties reached a settlement. That, I think, was the right answer. I commend people for finally coming to grips from the company's side with the fact that they had a problem, and for the plaintiffs for insisting on real consideration.

Lest the problem be demeaned as merely a disclosure violation, this is a disclosure violation that I think logically could have had some effect on the vote. If you just believe that people don't really think about these things, then you can discount voting generally. But in a world where *Corwin* is the law, I think we in Delaware have to believe that voting matters and that how people approach votes

matter.

If you say something is nonroutine, then if you oppose it, you don't have to do anything. You don't have to go in and vote. If you say it's routine, then the brokers can vote. And so by not acting, you basically allow your broker to vote in favor. The opposite is true as well.

So these disclosures, they're not mere formalities that don't matter. They affect whether someone thinks that they actually have to take action to vote or whether inaction has a consequence. So I think that even if this matter was limited to a disclosure issue, it still was something significant that was prudently settled.

The settlement involved two major components. The first was consideration ultimately for the stockholders, consisting of $50,000 in cash and $1.25 million in Galena common stock. The second aspect was a stipulation to a Section 205 validation order.

In terms of the requirements for class certification, all are met. Numerosity is satisfied. There were approximately 181 million shares entitled to vote in the 2016 annual meeting, approximately

214 million shares entitled to vote at the 2016 special meeting, and approximately 37 million shares outstanding for purposes of the 2017 special meeting. This is a set of big numbers that's sufficient to satisfy numerosity.

Commonality is also satisfied. The common questions include the validity of the votes, whether defendants breached their fiduciary duties by making inaccurate disclosures and issues such as the validation and whether it was going to be a valid validation.

Typicality is satisfied. All of the allegations of the complaint were brought by a stockholder who was not differently situated than anyone else and who suffered the same injury as everyone else.

I specifically find that adequacy of representation was satisfied. This case was litigated that resulted in a settlement that I approve. It would be somewhat odd to find that the settlement is reasonable and a proper outcome and yet somehow the representation was inadequate.

In terms of evaluating the adequacy of representation, as well as for other aspects of my

consideration today, I discount the kerfuffle over the validity of the settlement in light of the SELLAS merger. I think those also were issues that people could litigate in good faith. Compared to many of the other arguments that I see, that perhaps had more of a basis than those others.

In short, the class meets all the requirements for certification under Rule 23(a). It also is properly certified under Court of Chancery Rules 23(b)(1) and 23(b)(2) for reasons stated in cases such as the *Celera* decision and the *Cox Radio* decision.

Now, the record reflects that notice was adequately delivered. I won't go through -- well, actually, I will go through because it was slightly different. It was mailed to all recordholders for the 2016 special meeting and the 2017 special meeting. It was also mailed to banks and brokers that held at the record dates for the 2016 special meeting and the 2017 special meeting.

It wasn't mailed for purposes of the 2016 annual meeting because that was in relative close proximity, let's say six months. Given the other mailings, there was a view that that type of notice

was excessive. I think given the structure of our securities market in which most folks hold through banks and brokers, notice was reasonable under the circumstances.

In another case choosing not to mail for one of the meetings that gives rise to validation might have been problematic, but given the clumped meetings in this case, I think notice was adequately delivered.

In terms of the merits, I think the settlement falls within a range of reasonableness. In evaluating a settlement, my task is to consider the nature of the claim, the possible defenses, the legal and factual circumstances of the case, and then to apply my own judgment in deciding whether the settlement is reasonable. That's a paraphrase of the *Polk v Good* case.

I think that the settlement fund in this matter, which has resulted in a total of $1.3 million in consideration to the class, with some fluctuation depending upon what the actual sale dates are for the shares, is reasonable in light of the value of the plaintiffs' claims, particularly in a world where Section 205 validation is available.

I've taken into account the dynamics that the plaintiffs explained in their briefs, including the availability of exculpation; the possible effect of advancement and indemnification in terms of the cost of the suit that Galena would bear and stockholders ultimately would bear; the potential nonavailability of insurance; Galena's capital profile and cash availability, which led to the structuring of the settlement payment to include stock; and also there was a helpful discussion of other possible ways settlement could have been structured.

I say this because plaintiffs' counsel usually don't take the time to give that type of meaningful analysis of why the path chosen was reasonable. I think that's a lacuna in most plaintiffs' counsel's briefs that causes me to ask questions at the hearing. So the fact that you-all went through that in terms of talking about alternatives that you thought about and why, on the facts of this case, this structure made sense was very helpful and I appreciate it.

The plan of allocation, in my view, makes sense. It contemplates paying the settlement fund to holders as of the record date of the 2016

special meeting. That's easy and straightforward. It's imperfect because there's necessarily trading, but I think, on balance, it is a reasonable approach that is cost effective and particularly warranted given the relatively small size of the settlement payment compared to what fees might accrue for a full-bore administration process on a claims-made basis.

I've also taken into account the fact that the settlement provided for filing a validity order. This order lifted the problems that were hanging over Galena's head in terms of a potentially defective capital structure. The validity order, instead of patching over those problems, actually fixes them. It solves the problems. And I do believe that the validity order was causally related to the litigation. It resulted from the plaintiffs' efforts and addressed a problem that, to reiterate, the defendants created, not one that the plaintiffs created.

In evaluating the settlement, I've also taken into account that the release is narrow and does not include unknown claims. That is also, in terms of weighing the give and the get, something that

is warranted and supports approval.

Moving on to the fee, I think 15 percent of the settlement fund is reasonable in light of the stage of the litigation. I agree with the defendants that really this is a question as to whether it's a 10 percent case or a 15 percent case in terms of how I look at it. The plaintiffs filed the amended complaint and obtained an expedited schedule that would result in a three-day trial two days later. Expedited discovery ensued. The settlement resulted about halfway through the schedule. Document production was complete, but depositions hadn't yet started. I think, on balance, I can be comfortable with 15 percent under the circumstances.

I also take into account that this is a small issuer. I personally have a concern about the risk of undercompensation of contingently compensated plaintiffs' counsel for small issuers and, hence, the risk of underenforcement. A reality in this world, or at least a perceived reality by me, is that Fortune 500 companies with big capitalizations usually hire really top lawyers and often retain fine Delaware counsel like Richards Layton and generally do things right. So it may be that for plaintiffs' counsel,

those big issuers is where the money is, but that's often not where the problem is. Small companies, by contrast, often have problems. They often don't have the money to do things right from the outset. They may bypass steps in the interest of getting things done. They don't have the legal support staff to make them aware of issues that they need to fix. They often don't have the same type of blue-chip boards or blue-chip advisors. And so, really, it's the smaller issuers where we need a higher degree of oversight from plaintiffs' counsel. But these are also the most difficult cases for plaintiffs to bring on a contingent basis because you're not working any less, and yet if you're paid based on a percentage of the benefit, it can simply be noneconomic to act in the settings where action is most needed.

So if I had any doubt about whether I was going to fall on the 10 percent range or the 15 percent range, that puts me decidedly on the 15 percent range.

I do believe that the validity order is a compensable part of the settlement. I've already explained why I believe that it's appropriately considered as a part of the settlement and the relief

that the plaintiff causally generated. I think it easily supports a fee of $250,000. It validated five certificate amendments through which hundreds of millions of shares were issued that theoretically could support a much larger award by comparison to cases such as *Cheniere*, *ev3*, Colfax, and Xencor. It fixed deep faults in the company's capital structure. And I think giving meaningful awards where plaintiffs raise issues that result in companies taking validative action has important incentive effects, particularly now that Section 204 and 205 are on the books, and that companies can, with a relatively straightforward procedure, take steps to fix things. The problem with that is that it can lead companies and corporate counsel in real time to adopt a more cavalier attitude, with the belief that they can simplify things later merely for the cost of a few corporate documents from a fine firm like Richards Layton.

I think that counsel and issuers should not have a cavalier attitude toward statutory compliance or fiduciary compliance and that they should be upholding their obligations under Delaware law. As a result, I think that when a plaintiff

identifies a problem, even if it is one that the company can fix by pursuing action through 204 or 205, the plaintiff should get credit for identifying that issue. And I think that this is part of what ideally will induce companies to continue to do things right in the first place rather than to risk being cavalier and only turning to things later after the fact.

All the secondary factors support the requested award. The case was not overly complex, but it was also not cookie-cutter litigation. The plaintiffs got a real result that will put money into the stockholders' pockets. The time and effort that the plaintiffs' counsel invested is reasonable, and the ability and reputation of counsel is consistent with the award.

This lastly leads me to whether there should be an incentive award for plaintiffs. One of the things that has resulted from the real reduction in the sue-on-every-deal industry where Delaware lawyers got to devote some of their time to nonlitigation litigation is that lawyers have found time to do other things. I think most of that reinvestment has happened in terms of devoting time productively to real litigation and real disputes.

But at least two less salutary cottage industries have developed.

I think one cottage industry is a new interest in motions for reargument, which all of us on the Court are sensing. They are already running this year at slightly more than double historical rates. The reargument motions don't seem to be any more meritorious than they were in the past. They don't seem to be raising any different issues. Perhaps I've gotten dumber -- age does that to you -- but I don't think my colleagues are any worse this year than they were last year, and yet people seem to have more time now to file reargument motions. I don't think people have a lot of time. I think this is just time on the margin.

The second thing is a cottage industry of defendants challenging relatively innocuous incentive awards. I really do question whether the defendants have standing to challenge in most of these settings. Nevertheless, I can't fault the idea that it's helpful for the defendants to bring awards to the Court's attention when they seem out of step or out of line. But it's really not the defendants' cross to bear. It's the same type of scenario as when

defendants will seek to vindicate the rights of the class or vindicate the rights of the represented party by challenging adequacy of representation at either the class certification stage or 23.1. There's a little bit of a sense of the fox being very concerned about whether there's adequate fencing for the chickens.

In terms of this matter, though, I do think the 13,000 is a step up from the ranges of 1,000 to 5,000 that I've been awarding for service as a named plaintiff. I think those types of nominal awards are understandable and appropriate, given the current litigation environment in which there's significant downside to serving as a named plaintiff. You can expect to be targeted by the defense side. You can certainly expect to have to have your deposition taken, to gather documents, all those types of things.

And I also think that the Court's expectations have changed as well. We want and expect named plaintiffs to be involved. That's the theory behind most of *the Hirt* factors or at least the plaintiff-directed *Hirt* factors in our selection process. If we want plaintiffs to be involved and if

we want them to engage in adequate supervision of counsel, we have to recognize that they're doing more than just being passive participants.

I am concerned about fee creep. I do countenance and recognize that both sides have valid arguments on the amount in this case. I am going to authorize an award up to $5,000 because I think that is more consistent with the awards that I've historically approved, given the type of showing that was made here and the arguments that were put forth here in the briefing.

Do you have an order with you?

MR. DAVENPORT: I do, Your Honor. I just want to clarify one thing on the notice. We did provide the notice to the recordholders for all three meetings and used the DTC list for the 2016 special meeting --

THE COURT: It was the mailing you didn't do, though; right?

MR. DAVENPORT: It was mailed to the recordholders for all three meetings. The DTC list that we sent out to the brokers, that was based on the 2016 special meeting and 2017 special meeting. We put a letter in on this. I should have mentioned it in my

opening presentation.

THE COURT: That's all right. What you just described is more reasonable than what I had understood to be reasonable. So that works in your favor.

MR. DAVENPORT: Okay. May I approach?

MR. ROHRBACHER: And I'll mention, Your Honor, the only complication with this is that because the fee from the class portion of the award is a percentage, I guess we'll need to draft -- right now it's a dollar sign and a blank.

THE COURT: You know what I want you-all to do, then? I want you to draft up some nifty language and send me over a revised form of order that gets this done --

MR. DAVENPORT: Absolutely.

THE COURT: -- so that I can enter that. And I want you guys to be nice to each other when you're talking about this. If Mr. Rohrbacher calls up Mr. Davenport or anybody else at Prickett Jones, I want you guys to sound happy to hear from him and not angry or anything. And I'm sure -- and, Mr. Rohrbacher, I want you to be similarly appreciative and not dismissive. You obviously can

disagree with my views about what the plaintiffs contributed to this litigation, but just for the sake of collegiality, when you're dealing with this one, let's all be happy and friendly and get this one done.

Fair enough?

MR. DAVENPORT: Thank you, Your Honor.

THE COURT: Excellent. All right. Well, thank you all for your time today.

We stand in recess.

(Recess was taken from 11:20 a.m.)

CERTIFICATE

I, NEITH D. ECKER, Chief Realtime Court Reporter for the Court of Chancery of the State of Delaware, Registered Diplomate Reporter, Certified Realtime Reporter, do hereby certify that the foregoing pages numbered 22 through 86 contain a true and correct transcription of the continued proceedings as stenographically reported by me at the hearing in the above cause before the Vice Chancellor of the State of Delaware, on the date therein indicated, except for the rulings at pages 67 through 86, which were revised by the Vice Chancellor.

IN WITNESS WHEREOF I have hereunto set my hand at Wilmington, this 21st day of June 2018.

/s/ Neith D. Ecker

Chief Realtime Court Reporter
Registered Diplomate Reporter
Certified Realtime Reporter

EXHIBIT 2

EXHIBIT 2

IN THE COURT OF CHANCERY OF THE STATE OF DELAWARE

IN RE CHENIERE ENERGY, INC. stockholders litigation	:	CONSOLIDATED C.A. No. 9710-VCL
IN RE CHENIERE ENERGY, INC.	:	C.A. No. 9766-VCL

- - -

Chancery Courtroom No. 12C
New Castle County Courthouse
500 North King Street
Wilmington, Delaware
Monday, March 16, 2015
10:00 a.m.

- - -

BEFORE: HON. J. TRAVIS LASTER, Vice Chancellor.

- - -

SETTLEMENT HEARING and RULINGS OF THE COURT

CHANCERY COURT REPORTERS
New Castle County Courthouse
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Wilmington, Delaware 19801
(302) 255-0523

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Appearances Cont'd ...

... Appearances Cont'd

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THE COURT: Welcome, everyone.

ALL COUNSEL: Good morning, Your Honor. Mr. Andrews, how are you, sir?

MR. ANDREWS: Good morning, Your Honor. How are you today?

THE COURT: Great.

MR. ANDREWS: We are here today for the final approval in Cheniere, plus a motion for an award of attorneys' fees. To my left, Mr. Jeffrey Golan from Barrack Rodos.

MR. GOLAN: Good morning, Your Honor.

THE COURT: Good to see you.

MR. ANDREWS: He will be making the presentation today, with Your Honor's permission. To his left, obviously, Ms. Calder, Grant & Eisenhofer. Mr. Arnold Gershon from Barrack Rodos.

THE COURT: Welcome.

MR. ANDREWS: To the back table, Mr. Craig Springer from Andrews & Springer.

THE COURT: Mr. Springer, good to see you.

MR. ANDREWS: Mr. Mike Toomey from Barrack Rodos, Julie Palley from Barrack Rodos, and David Wales from Bernstein Litowitz.

MR. WALES: Good morning, Your Honor.
THE COURT: Thank you all for coming.
MR. WELCH: Good morning, Your Honor.
THE COURT: Good morning, Mr. Welch. How are you doing?
MR. WELCH: I'm very well, thank you for asking. Your Honor, a couple of quick introductions. My partner and friend Susan Saltzstein from our New York office.
MS. SALTZSTEIN: Good morning, Your Honor.
THE COURT: Nice to see you again.
MR. WELCH: And also Jeff Geier from our New York office.
MR. GEIER: Hello.
THE COURT: Welcome.
MR. WELCH: Thank you, Your Honor.
THE COURT: All right. You may proceed.
MR. GOLAN: Thank you, Your Honor.
THE COURT: So my first question is a nitpicking one. Why did we not get your brief until -- well, we never got the paper copy, and the reply brief wasn't filed until 3:48 on Friday. So

why, in a nonexpedited case, where there should have been ample time for everybody to get these things in, do I have to read something over the weekend to get ready? Look, it's the same thing for attorneys, right? In nonexpedited matters, you really shouldn't be putting your associates in the position where they have to work all night or all weekend to get things done. So what did I miss?

MR. ANDREWS: Your Honor, I can explain the --

THE COURT: Why don't you come over and explain. And we've never gotten a paper copy.

MR. ANDREWS: Your Honor, I was -- I actually contacted your chambers --

THE COURT: I know. That's why we were able to get it online.

MR. ANDREWS: -- and I was assured that the runner had gotten it there by 4:30. And I apologize --

THE COURT: What about the Friday? Like, you know, I would have happily read this thing on Friday, you know, rather than on championship tournament weekend. Look, I'm sure I speak for a lot of people in this room. We have family stuff. I have

kids' activities; right?

MR. ANDREWS: Your Honor, I don't disagree.

THE COURT: My son had two championship basketball games. You know, he is playing sixth grade basketball, this isn't like world-beating stuff but, you know, sitting reading your brief was not -- and I'm happy to do it in expedited cases. It's my job, all right? Happy to do it. Part of my job, it's what I signed up for. But in nonexpedited cases, what's up with that?

MR. ANDREWS: Your Honor, it's my understanding one of the reasons was the defendants' brief got filed on Monday and there were expert reports making the rounds. And that was the primary reason for the delay, that the rebuttal expert reports, we had less than four days to prepare such. Otherwise, we would have endeavored to get it sooner.

THE COURT: Let's try to plan these things in the future, and hopefully this will be -- hopefully you will remember this unpleasant time we've just had together, and the next time the defendants are talking about a schedule that makes you think you will have to endure more unpleasantness, you will be

able to say, you know, that was not fun for me and I really don't care about Laster's son's basketball games, and so give me enough of a schedule that lets me not have to endure that unpleasantness.

MR. ANDREWS: Your Honor, I apologize again, and I'm always willing to take your unpleasantness.

THE COURT: All right.

Mr. Welch.

MR. WELCH: Your Honor, if I might, I heard the defendants mentioned, and I would simply say, without trying to aggravate things any further, which I don't want to do, we did talk about a schedule early on. We tried to work something out. The proposal was, I think, ultimately that they were going to take about two months and we were going to get about two weeks, but that didn't work. Ultimately, we did try to pursue -- my colleague Sarah Martin did try to call them, made a number of calls to try to get a schedule in place. When we got the brief, as my friend Peter says, it did have -- they had a couple of expert reports. We had to get it done. I think we got -- they got two months, we got it in in three weeks. So to the extent that --

MR. GOLAN: Four weeks.

MR. WELCH: -- we could have been quicker, I wish we had, but I think we had less than half the time they did. I do --

THE COURT: Well, look. I've vented. I've gotten it off my chest. You guys have been forced to endure me getting it off my chest. But the bigger issue is, in these nonexpedited matters, you know, let me be the voice of your associates and staff.

MR. WELCH: Yes, sir. Agreed.

THE COURT: And let's try to plan these things so that people aren't put in this position. Again, I get it in expedited cases. Totally get it. Or, you know, when a trial is coming up, you have this situation, you're jammed for time. I understand when it's necessary. This did not strike me as one of those times.

MR. WELCH: It struck us the same way. We would have hoped to have had the stuff sooner than we did. And so --

THE COURT: All right. Let's just take it as a learning experience move on.

MR. WELCH: Yes, sir.

THE COURT: All right.

Mr. Golan.

MR. GOLAN: Good morning, Your Honor. Jeffrey Golan on behalf of the plaintiffs, who are both the putative class representatives and derivative plaintiffs. And again, my apologies as well, Your Honor, for the tardiness of the reply papers.

We're here to present to the Court for final approval the settlement reached between the parties for a consolidated class and derivative action brought on behalf of stockholders of Cheniere Energy and a subsequent application filed by the defendants under Section 205 of the Delaware Code. And the class includes purchasers of Cheniere stock from March 2011 to the present and, on behalf of the derivative plaintiffs, the current holders of Cheniere stock. The Court granted preliminary approval to the settlement on January 5 for purposes of providing notice.

THE COURT: As you say, I hope I preliminarily certified it. I hope I didn't preliminarily approve it.

MR. GOLAN: Yes, Your Honor. I'm sorry. Conditionally certified the case as a class

action. Notices were issued to more than 200,000 potential class members and current Cheniere stockholders. Out of this group, we -- we received calls from probably 70 to 80 either members of the class or current shareholders. And after receipt of the notice, we were asked questions about it. We answered those questions, primarily Mr. Andrews and I. And out of the entire group, no objections were filed, either by the February 24 deadline or to the present, either to the settlement or to the fee and expense application. Thus, at present there are no objections to the settlement, which is supported by both sides, and the only objection to the fee and expense application comes from the defendants.

Respectfully, Your Honor, this is precisely the type of case that this Court has said should be encouraged. After noting the incredible compensation that Cheniere had paid to its senior executives -- and particularly its chief executive Mr. Souki -- in 2013, and using our knowledge of Delaware law, plaintiffs' counsel investigated the circumstances surrounding the stock awards that had been the bulk of the insiders' compensation in 2013. And after analyzing the company's incentive plans, the

proxies that had been issued, the company's bylaws, both in effect at the time and as later amended in April 2014, and the proposals that Cheniere had made to its stockholders in April 2014 to add another 30 million shares to the plan reserve and to institute a 2014 to 2018 LTIP, we determined that the vote at the February 2013 proposal to add 25 million shares at that time had not, in fact, passed.

Your Honor, we're not talking about small sums here. The stock awarded in 2013 to Mr. Souki made him the highest-paid executive in the country, by more than $50 million. It paid the company's next-highest executives, next-most-senior executives, the same amounts or more than CEOs of companies like Exxon. And these grants, especially on top of earlier grants of restricted stock that were still in effect, provided company executives with hundreds of millions of dollars in yet-to-vest restricted stock which was set to vest -- excuse me, Your Honor -- in 2015, 2016, 2017, and 2018.

And it also became clear to us by viewing the history of this company and its proposals, both prior and made in April 2014, it became clear to us that Cheniere's board fully intended that it would

continue to make these same kinds of payments to the company's senior executives and keep within the pattern that the company had paid in the years 2011 to 2013. Basically, the compensation philosophy had not changed from the prior period to what the company was proposing in April 2014. And in fact, Your Honor, the 2014 plan and the Amendment No. 2 that they were presenting for stockholder approval through the April 2014 proxy, the board was seeking more shares at that time, at a greater value, than it had ever previously done before.

In June of 2011 it had proposed and obtained stockholder approval for 10 million shares into the plan. Those shares were completely used up, other than about 100,000 of them, by December 2012, when the board had proposed for stockholder approval another 25 million. And on top of that, they were seeking, in April 2014, another 30 million, at a far greater price per share than the company stock was then trading at.

We investigated this case, Your Honor, and found that under the bylaws, at least in our view, under the bylaws in place at the time of the February 2013 vote, the company's stockholder proposal for 25

million shares had not in fact passed. While there were more votes for than against -- approximately 87 million to 58 million -- when you added in the abstentions which, under the bylaws at the time and the Delaware code, the standard provision under Delaware law, in fact, it appeared to us that the yes votes, the for votes, constituted only 45 percent, and the no and abstention -- the no votes and abstention constituted 55 percent. So in our view, the 17 million shares that had been granted pursuant to that, as well as this approximately 7.8 million shares that had yet been allocated, were not validly within the board's right to grant.

THE COURT: So why didn't you get back any of the existing awards, particularly those that went to the senior guys and the board? I understand the employees, but the folks who actually were involved in this decision, it seemed to me that they would have been a fair place for you to look. And that seems to me the settlement, part of the settlement, you wouldn't have gotten all of them, like you would have had you went forward on the merits, or tried to if you had gone forward on the merits. But you didn't get any.

MR. GOLAN: Your Honor, it was a -- there were a number of considerations, in terms of the settlement positions that were taken. The --

THE COURT: But it just seems to me -- you came into this with righteous indignation about the amount of compensation that these fellows had been given. And, look, you know, it goes beyond eyebrow-raising. It's sort of jaw-dropping. These are the guys, apparently their parents didn't pay them for A's, they paid them millions of dollars for A's when they were in school. These are the guys, at least according to the affidavits, they can't work for the satisfaction of doing a good job and the feeling that they've accomplished something and done well. They have to, you know, receive dynastic wealth, the potential for dynastic wealth. So you came in with that level of righteous indignation and then, you know, essentially walked away from it. I mean, I know you got stuff going forward.

MR. GOLAN: Your Honor, there were a number of things that entered into that. First of all, the -- both in the briefing and at the hearing on August 26 last year, the defendants had made a number of equitable arguments why stock that was issued at

the time to the executives could not be or should not be clawed back or invalidated, seeking -- arguing either that it had been validly issued pursuant to the vote or that it should be ratified by this Court pursuant to Section 205 of the Delaware Code. And that was a point that we discussed extensively internally.

The 7.8 million shares that were left over, we took the position -- which is 30 percent of the 25 million -- we took the position that there was no way that the defendants could continue to claim to have the absolute right to issue that, and one of the key settlement provisions is that for those shares, those are barred from being distributed inside without a revote being taken sometime after -- assuming the Court approves the settlement, and that the revote on that will be under the present-and-entitled-to-vote standard which was --

THE COURT: I get that.

MR. GOLAN: Okay. So --

THE COURT: I guess what I'm focusing on is, again, I think that when you think back to the stock option backdating cases, there was a sense that one would differentiate between line employees,

lower-level employees, even mid-level employees, who received grants as part of a compensation package and rely on those grants, and one would not seek to impose penalties or do things that would harm ordinary folks who were working at the company. But that there could be consequences when people violated plan documents, or did other types of things, for the actual people involved. And so I'm -- I remember when we were all together -- and I haven't gone back and reread that transcript, I probably should have -- that type of distinction was in my mind as to the 205 issues.

And so again, I get that you got stuff going forward, but it almost seems to me that, you know -- I don't want to say you picked up the easy stuff, but you took the far less difficult stuff, rather than essentially banging a drum at least for some -- I'm not saying you get everything. You didn't get anything. I mean, you came in with an argument that these shares were invalid because they didn't get the vote.

MR. GOLAN: Your Honor, what we -- what we contemplated through the settlement is that we actually -- and it wasn't in any sense an unwillingness to litigate this case or to do the work

that was necessary. What we -- the settlement that we reached, we reached taking our -- taking our status as fiduciary seriously. And quite frankly, what we achieved through the settlement, we think, is -- is more than what we could have achieved through the litigation. Had we gone forward with the litigation, it is possible that the Court could have invalidated some or all of the 17 million shares that had been granted. At that point, the company would have been free to go right back to its shareholders to seek a re-approval of those shares and even more shares, up to the 30 million.

What we got instead of that, Your Honor, is that, first of all, the company can't use the 7.8 shares without a revote. The company can't seek any further compensation, stock-based compensation, essentially going dry in 2014, 2015, and 2016, or any variant of stock-based compensation. And we got the other things.

Now, it seemed to us that we would not have been able to enjoin the company from presenting for approval future stock-based awards until 2017. We could not have forced the company to take future votes under the present-and-entitled-to-vote standard. We

could not have forced them to limit Mr. Souki's take from the available 7.8 million shares, even if that had passed. And we could not have forced the company to have a fully independent compensation committee.

And our view was that what we did instead was we -- we used the company's -- I don't want to go into the settlement negotiations, but the refusal to consider clawbacks, we used that in terms of negotiating what we felt would be extraordinarily valuable forward-looking -- forward-looking terms of the settlement, without -- without keeping the cloud over the company's prior grants.

THE COURT: Remind me how the compensation committee structure differs from what it was before.

MR. GOLAN: Your Honor, there were people on the compensation -- to my understanding, there were people on the compensation committee that had been former employees of the company. But --

THE COURT: Were they former employees who, because of the look-back period, met the --

MR. GOLAN: I'm not sure if there's a difference, Your Honor.

THE COURT: That looked to me like

gilding the lily. I mean, I didn't see what you got there.

MR. GOLAN: But clearly the other things, we could not have gotten through a litigation in this case; we could have only gotten through a settlement of this case. And having retained experts who looked at the provisions of the settlement as we were looking at them, we recognized -- and I obviously will go into this more during this discussion, Your Honor, but we recognized that making the company revote the 7.8 million shares has a very, very significant value to the shareholders, in terms of the dilution. Whereas before the company claimed the absolute right to -- to allocate those shares, today they can't allocate them without a positive approval of the stockholders. And that, to us, taking the 7.8 million shares times the market price of those shares, to us constitutes a value of approximately $565 million.

The other key provision that we believe is quantifiable is the provision that, going forward, the company cannot either pay to its executives or seek stockholder approval for any further stock-based compensation until at least 2017.

And that was obviously an intensely negotiated point. And our view of that was that in terms of the stock that was as yet unvested -- the unvested stock awards that had been made, there was no need for this company to dilute further stockholders' interests in the company, at least until 2017. Because what the executives and employees have, based on their current holdings, and what they have, based on their as-yet-vested restricted stock, are hundreds of millions of dollars of value. And forcing the company not to further dilute and not to seek further stock-based compensation until at least 2017, we believe, has a value in excess of $1 billion, as Mr. Root put forward both under a Monte Carlo analysis in his initial report and under a burn rate analysis.

And, in fact -- I'm sorry that Your Honor got the papers late. Truly, we -- we thought that we were getting them to you earlier than we did. Mr. Root's supplemental report points out very specifically, chapter and verse, why the Monte Carlo analysis is an appropriate method to value these -- this provision of the -- the bar provision of the settlement, why the burn rate analysis is an appropriate method to value the bar provision of the

settlement, and why the defenses that have been raised, primarily the net economic benefit defense, is not viable here, because there is so much -- there is so much yet value that the company executives, employees, have from their stockholdings and from their to-be-vested stock that there is no need for an alternative incentive plan to be brought forward.

And as Mr. Root also pointed out, and as we try to point out in our reply brief, there was no -- other than the overall claim that this is an unquantifiable benefit, and other than the unsupported claim that you have to look at the net economic benefit, which I think Mr. Root really did take care of in the supplemental affidavit, neither of the defendants' experts nor the defendants themselves take any issue whatsoever with the underlying assumptions that Mr. Root made with respect to his Monte Carlo analysis or with respect to his burn rate analysis.

THE COURT: So I'm looking for the reference, I'm not finding it, but what did you think about the response that seemed to be telegraphing that the easy way around this is to put in place a phantom stock plan, so that nominally has cash payouts equivalent to stock. And once we get beyond the 2017,

we'll replace the phantom stock plan with a regular stock plan so as to save the company the cash expense. And we will have, you know, circumvented any type of restriction that Mr. Golan thinks he got.

MR. GOLAN: Your Honor, the phantom stock really is a phantom alternative. When the stock -- the phantom stock, of course, is that you will pay cash upon the -- at the appreciated rate of what a stock grant would have been. So it is a cash payment.

THE COURT: No, I understand that.

MR. GOLAN: It is --

THE COURT: And that's how you get to put it in place now. Because your settlement doesn't restrict cash. And then, once you get beyond 2017, is there anything that would stop the board and its compensation committee from saying, "We put in place this phantom stock plan. We realize now that it's a major cash expense. Because the company has numerous net present value positive projects for which the company could better use its cash, we are going to replace the cash plan with a stock plan, an equity-based plan, so that we don't have to spend the cash. And it will have the equivalent incentive

effect, because we designed the original phantom stock plan to the equivalent of stock."

Is there anything in the settlement that would block that type of work-around?

MR. GOLAN: There is nothing in the settlement that blocks the company, in 2017, from going forward and seeking approval of another stock-based plan. However, in Mr. Root's supplemental affidavit, he shows very clearly that this would be -- first of all, this is a company that only had 200 -- it's a cash-strapped company.

THE COURT: Oh, I get it. But --

MR. GOLAN: It has only 270 million of --

THE COURT: That's why you're going to replace it with a stock plan on --

MR. GOLAN: In the meantime, Your Honor, it's a very -- it's very expensive in terms of the financial statements, and it's -- and it's -- and it's subject -- it subjects the company to incredible fluctuations, depending on the price of the stock, which -- which is the reason that most companies stay away from these kinds of plans.

And Mr. Root explains that under the

FASB rules, it would have to take -- it would be a liability that would be potentially significant in years when this company has net operating losses and has cash flow constraints and has only a -- for this past year, only had 270 million of stock.

It's also, Your Honor, respectfully to the defendants -- they make the argument that our analysis is speculative, but now they're talking about developing a plan -- first of all, we filed our lawsuit in May of 2014. They say they're working on an alternative plan, but it's now March of 2015 and there's not one in place. Mr. Root and Mr. Taxin both show that a cash-based alternative would be far inferior to the kind of stock-based plan that's prohibited by the settlement.

And in addition to that, it is -- the savings that have already occurred -- in fact, in Mr. Root's analysis, had the 2014 to 2018 LTIP been put in place, they already would have paid $800 million worth of stock to company executives and employees in 2014, which have not been paid because of this case and because of this settlement. So that there is tangible benefits that have already accrued, both in terms of the 7.8 million shares that have not

been allocated and the bar provision that bars them from putting forth or paying any stock-based compensation in 2014, 2015, and 2016.

And I don't think that Your Honor -- there is a hint in the defendants' papers that this might be a plan that the company might put in place in 2017, but they clearly haven't done anything concrete on that yet. And it will be subject to stockholder approval if they ever seek it.

THE COURT: I definitely agree with that. If they were going to do some type of replacement, it would be subject to stockholder approval. But, you know, you'd be in the position of being able to tell your stockholders, you know, if you don't approve it, they're going to have to make these big payouts.

MR. GOLAN: Well, and there is a whole other set of -- I mean, I'm not trying to enlarge the scope of this case, but there are a whole other set of claims that may be made. I mean, it's akin to putting in provisions in debt instruments that if you vote the board out, you know, they're immediately punitive and payable. And quite frankly, if this company now were to put in these kinds of phantom stock awards and

basically seek to blackmail their own public shareholders in two years, that if you don't allow us to put the stock in because of what we've done when we were cash-strapped, we're going to have to make these huge payments. That's -- first of all, this is a company that says in its proxy statements that they're trying to meet concerns of stockholders and meet concerns raised by ISS and Glass Lewis. And that kind of cash-based plan, Your Honor, respectfully, would be something that we believe would be very difficult for this company to put into place.

THE COURT: So help me resolve a tension in my mind that perhaps may not exist, maybe I'm imagining it. It seems to me that part of the reason you're able to put a big value on the -- I forget your defined term -- the available shares is because you believe that the available shares actually aren't going to be available for exercise because, effectively, the stockholders won't give them the vote. And so it's not just a matter where you've saved time value of those shares. You've actually saved the shares.

But then, in terms of the deferral of additional grants, you claim the benefit of those,

although by the same reasoning, it would seem to me that the stockholders wouldn't have given them any additional shares to grant. And so essentially, just by getting the voting standard, there would be a deferral anyway. And in fact, you know, as long as stockholder ire remains raised, the deferrals would continue.

So I'm sensing this tension where, for the first part of your valuation of the benefit, you're playing up the idea that the stockholders are going to vote it down. But for the second half of the benefit you want to ignore the fact that the stockholders otherwise would be likely not to give them any more. So help me -- help me understand whether I'm -- I am incorrect in perceiving that tension, or am -- or how I should resolve it if I'm correct that it's there.

MR. GOLAN: I'd be happy to, Your Honor. For the 7.8 million shares -- and I'm sorry if I'm repeating myself, but I think a little context might -- might help in the overall response. Before April 2014, this company claimed, both in this litigation and in its proxy statement, that it had the absolute right to give those shares as they saw fit,

without any prior -- without any further stockholder input. And those 7.8 million shares, at today's value, have a value of approximately 600 million today.

And the litigation stops them from doing that. It puts that decision, whenever the company may choose to present it, it puts that decision back into the shareholders' hands. And it does so under a much more favorable standard than had been in place after the board amended its bylaws. And so we say that that is an immediate 600 million benefit.

And, in fact -- and under this Court's Del Monte decision, having presented that, you don't look -- you don't need to look at what might eventuate from that vote. The fact that you provided that opportunity for the stockholders is a benefit in and of itself.

THE COURT: Let me push back on you on that so we're on the same page in terms of my question. So, you know, look, I follow you as to that. But it seems to me that if one -- so there's certainly a benefit from the vote. The question is valuing the benefit. If stockholders -- to say that

you have prevented these shares from being used, what has to happen is stockholders have to vote it down. Because if they voted in favor, these shares can be used. If they vote in favor, then you really haven't achieved the full value of the available shares. What you have achieved is the time value of delaying the issuance of the available shares from the time when they originally would have been granted under the company's previous position until the future time when, having been approved by stockholders, they can be used.

So if the stockholders vote up, you can't claim the full 600 million. You can only claim the time value of that. So looking at that, I think, okay -- and I think I remember seeing something like this, maybe I was hallucinating -- to claim the full value of that, you have to combine that with an idea that because the stockholders are irritated about these guys' compensation practices, they are not going to vote in favor of this. Therefore, we can plan to have delivered the full 600 million to the stockholders, because those things are never going to be available. That's how I understand your argument on the first chunk to work.

MR. GOLAN: It's -- it's nearly what our argument is. Our argument is that it's not just time value. It's that we have put into the hands of the shareholders the ability to control what happens to those shares. And if the stockholders decide that the 3.3 percent dilution is worth it, in terms of whatever incentive value there might be, they can have that -- they, the stockholders, have that decision to make. And that is the benefit all by itself.

But --

THE COURT: But what's the value of that benefit? What's the value of the up or down vote? And it sounds like --

MR. GOLAN: Well -- I'm sorry, Your Honor.

THE COURT: No, I was going to say, again, I have trouble -- unless the stockholders vote it down, I have trouble getting to the idea that the benefit is the full value of those shares.

MR. GOLAN: And that's why we asked Mr. Taxin to do -- to use his -- that's why we asked Mr. Taxin to look at that second question in his report. And what he did was he looked at the votes that had been taken in June of 2011, February of 2013,

and the say-on-pay vote in 2013. In both of those, Your Honor, if I may, in both of those, when you didn't take into account abstentions, the for votes were 57 percent and the against votes were 43 percent. Both -- both -- in both instances.

Then, when you get to 2014, ISS and Glass Lewis make the same recommendations against the proposals. They say that the -- that the proposals do better aligning public stockholders with executives under this plan, rather than the older -- the Amendment No. 1, but they still come out against it.

Then we filed our lawsuit. The company immediately postpones the annual meeting because of the filing of the lawsuit, because of the filing of the motion to expedite. There is significant press on June 4, when the company does that. The Wall Street Journal covers it, the Houston Chronicle covers it. There were a series of articles that we've put into my declaration. And two weeks later -- and as Mr. Taxin pointed out in his report, initial indications by the time of the vote were that there were -- there was stronger stockholder sentiment against it. And, in fact, when Mr. Kilpatrick puts in his affidavit, he said that even though the vote had

been postponed, the last figures they got on June 11 were showing that now, instead of 57 percent in favor and 43 percent against, it was now 67 percent against, 33 percent in favor.

So this lawsuit by itself had an impact on that shareholder coalescing against this company's compensation practices.

THE COURT: And what you've just described is what I boiled down in simplistic terms to say you don't think the company's going to get the vote.

MR. GOLAN: And, in fact, when you look at the 2014 say-on-pay vote in September of last year, it goes against the company. And as we put into the reply papers, both ISS and Glass Lewis had extensive discussions about this lawsuit as additional background and reasons for their --

THE COURT: Now take the next step with me.

MR. GOLAN: Okay. Now --

THE COURT: If we assume that they're not going to get the vote, why does it matter that you got the deferral until 2017? Because they weren't going to get the vote anyway.

MR. GOLAN: Well, but two things, Your Honor: First of all, just if I could, just finishing up on the 7.8 million share question that Your Honor asked, we had Mr. Taxin go forward with that second line and say, how likely is it that they'll get the vote when they ask for it? And his looking at all the history of this and the ISS metrics and the Glass Lewis metrics, his view, opinion, was that it is highly unlikely that they will get the vote in favor. Especially with the standard that we've put in place through the settlement.

THE COURT: That's what I simplified as ain't going to get it.

MR. GOLAN: Right. And neither of the defendants' experts nor the defendants themselves take any issue with that. Everybody agrees that the 7.8 million shares is not quantified into a percentage, but it is highly unlikely that they are going to get that approval. So on the basis of that, we do say that the 560 or 600 million, at today's price of value, has been presented through this settlement.

Now, in terms of the other, first of all, notwithstanding Mr. Kilpatrick's affidavit, we view that the pulling of the proposals had -- at least

in some way, that this lawsuit had an impact. If nothing else, the vote would have already taken place. Had we not filed this case, they would have presented that vote to stockholders on June 12. They would have made an effort -- and this is in Mr. Root's supplement. Companies often have votes where proxies are put in, and then they do a shareholder outreach program and they try to change the view. And in this case, they didn't even have to change the view. They could have just tried to get somebody to vote -- to abstain, rather than vote for. And Mr. Root, in his supplement, includes a set of statistics showing that while ISS recommended against about 23 percent of pay proposals from 2007 to 2012, only about 1.4 percent of those actually failed. And that's because companies can do something about ISS recommendations.

So here, the litigation itself has something to do with the pulling of that proposal and the stockholder coalition against this company's compensation philosophy. And in addition, through the settlement, we've gotten the postponement, the deferral, the prohibition against any stock-based until 2017. And at that point the company will be in a very different position. It won't have all these

unvested shares still outstanding. It will have a few; it will have some. Enough, we say, to give the incentive to these executives that maybe they should continue working -- doing their fiduciary duties, rather than insisting, as Mr. Kilpatrick and the defendants' experts say, they need all this extra incentive to do what they're supposed to do.

But it is --

THE COURT: I was going to say, it's very hard for me to get up and come into work in the morning just getting a salary. It's very hard.

MR. GOLAN: But it is getting the company to 2017, when these projects will be much further along and when there may need to be, in -- whether there is -- may at that point be a reasoned basis for another stock-based plan is a significant achievement. And it's more than just deferring this, because --

THE COURT: If they had proposed a stock-based plan under the bylaws standard in 2016 or 2015, this year or next year, would they have gotten the vote?

MR. GOLAN: Your Honor, we didn't -- we didn't -- I don't think we could say that, and I

don't think --

THE COURT: Isn't it fair to say that if your experts believe that it's highly unlikely that they would get the vote on the available shares, that it's also highly unlikely that they would get a vote on a new plan? I mean, that's the -- that's the tension that I am sensing. And again, I feel like the -- you're not going to get -- the vote benefits you on the one prong, but I think it hurts you on the other prong, because it suggests that while there are certainly benefits causally conferred by the litigation and your settlement, the magnitude of them -- and again, to my mind, it uses this sort of conflicting assumption.

MR. GOLAN: So even, Your Honor, assuming that -- first of all, I don't think that we would necessarily agree that it was just confirming what was already preordained. For one thing, the preordination is in part because of this lawsuit, because of the publicity it got and the claims that were made. But also, by 2016, this company may have been able to provide a better rationale for needing more stock-based compensation at that point.

But even if you just look at 2014 --

and this is what Mr. Root did in his initial report and again in his supplement -- given the way the stock appreciated from -- and I don't know if -- again, Your Honor, I'm sorry for the lateness of the papers, but in his papers he showed that the way this plan was formulated, the 2014 plan was formulated, by the time they went to the stockholders for approval, they already had 210 million in the money. Because they had done the plan as of January 30, 2014, they had used a November 1 or November 30 stock price as the reference price, and then they discounted that another 20 percent.

So they already had 210 million in the money when they went to the shareholders for approval. And had the plan been put into place, they would have paid 800 million just for 2014's benefits under the plan. So even if Your Honor thinks that the 2015, 2016, may be -- may not be shown with the certainty it needs, you still have not only the 565 million from the 7.8 million shares, but you have another 800 million of value just from foregoing the stock awards that were planned to be made in 2014.

And there's absolutely no -- there's not one piece -- every piece of evidence, Your Honor,

in this case is that this company intended to make those awards. There's not one piece of evidence that says that they wouldn't. And in fact, the -- having the 7.8 million shares available clearly was not enough for this company, because they were seeking another 30 million at the time. And they still say -- Mr. Kilpatrick, in his affidavit, still says that, you know, even with everything that happened, all the votes in 2013, the say-on-pay vote in 2014, Mr. Kilpatrick still says in his testimony that he doesn't believe these executives were overpaid. And he still says that he believes that they should be paid on this equity -- private equity model whereby the company executives get at least 10 percent of any stock appreciation.

So given all that, Your Honor, there should be no question that these shares, both in the LTIP for 2014 to 2018 and the 7.8 million available shares, were going to be granted and were intended to be granted. And there's not one piece of evidence against that. And Mr. Kilpatrick doesn't say that in his affidavit that he has put in for the purpose of this hearing.

Your Honor, I could go through --

obviously, we believe that the class should be certified finally.

THE COURT: You don't need to dwell on all that.

MR. GOLAN: And I think I've probably said enough, because our view -- obviously, we think that the settlement provides the kinds of benefits that warrant approval by this Court. We think that it provides extensive quantifiable benefits, as well as therapeutic benefits.

We think that those items also fully, fully justify the fee request that's been made in this case. And in fact, even if Your Honor only -- I'm not suggesting that this is the case, but even looking only at the 7.8 million available shares and the 565 million of value that we've placed on them -- that Mr. Taxin has placed on them -- the fee request is still 7.5 percent of that, is only 7.5 percent of that. It's obviously a much lower percentage of the 800 million or the 1.7 billion that we claim to have as fully -- the full quantifiable benefit. But we think that under the Court's American Minings decision and under Your Honor's decision in Orchard Enterprises, and even under the Simon Property, where

there was a Monte Carlo analysis done of before and after and the defendants' expert showed that the -- that the adjusted figure should be used and came out with a valuation of 6.3 million, and there was a 20 percent value given to that, in terms of the fee.

So we think that the Delaware jurisprudence, given this -- given the quantifiable, as well as the therapeutic, benefits from the settlement, fully justify the fee that we've requested.

THE COURT: Thank you.

MR. GOLAN: Thank you, Your Honor.

MR. WELCH: Your Honor, good morning again.

THE COURT: Good morning, Mr. Welch.

MR. WELCH: Your Honor, I'd like to talk a little bit about the settlement, if that's okay. But before I do that, I want to touch on a couple of the points, really, that focus upon what the overall picture in terms of what the board did here.

I think it's probably fair to say that what we've seen here is an extraordinary performance, in terms of what has and can happen in American industry. This was a company that was $2 stock --

THE COURT: Look. You guys -- they've definitely created a lot of value. I mean, the irony, to me, is that when things are bad, when there's a bad situation and plaintiffs come in and sue over a bad situation, what CEOs and top executives do is they sit in that chair and they say, "We're not responsible for everything that happens in the company. Stock price doesn't automatically reflect what happened in the company. CEO can't know everything. CEO can't be accountable for everything." Senior executives say that.

Now, again, there is a tension in my mind between saying that when bad things happen and when good things happen saying, "We are responsible for all this value creation and we ought to get it." I mean, there's been a lot of other stuff going on, and I'm all in favor of people being well paid. Mr. Welch, I think you ought to get paid more. I think you're worth it.

MR. WELCH: Your Honor, I appreciate it. And that's obviously mutual.

THE COURT: But I also think that, you know, you get up and you go into work and you do a good job because part of what you believe you need to

do is do a good job. And you take pride in your work and you do a good job for your clients because you're representing your clients. And part of what they expect you to do is do your job, even if you're not going to get some, you know, nine-figure payout at the end of the case.

And I think that people have -- certainly it would be not unfounded to have some skepticism about fiduciaries who claim that the only reason they can get up in the morning is because they're getting 20 percent total, or I guess 10 percent here, of the gains that they're creating. It's just -- it's a stretch. And again, I'm not saying that you got a waste claim here. I'm not saying that you've got a breach of fiduciary duty claim. What I'm saying is that these are big numbers.

MR. WELCH: Well, Your Honor, with -- with the position of the Court, I'll probably ask the court reporter to excerpt your comments about me. There have been others mentioned at other times that aren't entirely consistent with that, and so I'm obviously happy with that response.

THE COURT: No, Mr. Welch, I'm always in favor of the good job that you do and the

preparation you bring.

MR. WELCH: Thank you, Your Honor. And I'll ask her to add that to the excerpt. Thank you so much. Your Honor, I appreciate it.

If I might, I understand Your Honor's view. I understand the hypothetical executives that would try to wash their hands of problems as they arise. And, in fact, those executives, I suppose, the hypothetical executives with other firms may well be -- or not be, depending upon the facts -- justified in that.

The way -- I think one way to look at this, Your Honor, from our perspective, is this: This was a $2 stock. It's now pushing an $80 stock. It was a market cap not that long ago of $150 million. It's now a market cap of $18 billion. Now, the peer group didn't do anywhere near as well. I mean, Mr. Dages points out in his affidavit that if he invested $100 in Cheniere stock not that long ago, and you look at it today, it would be worth $1400.

Now, as to the peer group, plaintiffs say well, it's all coincidence, because the market rode up. That's just not so. You look at the peer group which Mr. Dages talks about, and if you invested

$100, you'd have a profit today, and the profit would be about 50-some dollars. The stock would be worth about $158. This is really -- what they did is extraordinary.

But the other thing, I think, that I try to keep in mind in thinking about these issues is that when these shares were granted, they weren't at the high levels that they're at now, the 70 to $80 price. I mean, when this process started, the stock was at about $18 a share.

So when you get incentive-based comp, and that 18 -- which was up a little bit from where it was before at 2, obviously. These people were working hard. But when you get it at 18 and you produce the value that obviously does, in turn, benefit you as well -- but it's extraordinary. It's like this. I mean, this is almost unparalleled. I certainly can't -- maybe there's other examples of it, but I certainly couldn't identify any examples of things like this happening.

THE COURT: No. It would be interesting to chart this relative to the growth of Skadden, from a smallish firm in the late '70s, early '80s, to the international colossus that you are now.

I hear what you're saying, Mr. Welch. I'm not pooh-poohing it. But I am also of the view that, you know, you can understand why the defendant -- why the plaintiffs say that the stockholders might have objections to some of it.

MR. WELCH: Well, and they certainly didn't have objections for a while. But have there been some objections voiced under the say-on-pay vote? Of course. You know, what's the role of the board under those circumstances? I think the role of the board is to do exactly what I think we've indicated to Your Honor this board is doing. What is it doing? It's looking at its alternatives. It's agreeing to the settlement and will stick with its agreement to that effect. At the same time, it's looking over its options.

Why? Because incentive comp at this point, as Mr. Kilpatrick points out, only goes through Trains 1 through 4. Again, I know Your Honor is aware of this. The liquidated -- the LNG business was going to be an important business. It didn't exactly work out. These folks are the ones who came up with this idea to create these liquefaction trains which, in turn, compress the natural gas into liquid gas so it

can be transported on purchase in vehicles to other countries. And it's working. It's working extraordinarily well.

Now, is there competition out there? You bet. There certainly is, Your Honor. Mr. Kilpatrick points that out too. They only have an incentive-based comp plan in place up through Trains 1 through 4. They want to do not only in Sabine Pass, but in Corpus Christi, Trains 5 through 9. There are really powerful reasons to do that.

Now, plaintiffs also make a very large point of the five top officers, and I understand that. Again, five top officers started not with stock what it's worth today, but started at shares when the shares were $18 a share. And they were the ones built it up. They built it up to pushing 80 bucks a share. All right?

So the fact of the matter is, they have further plans in the works. They want to build Trains 5 through 9, including at Corpus Christi. They have competition coming at them from a variety of directions. So there is good reason to be considering the alternative plan.

Now, when you consider the alternative

plan, which is not in place yet, what's one of the things that you look at? Number one, all of these things we're talking about now, including the competitive environment, including the fact that there may be efforts made by competitors to grab some of these employees, take their vested shares, and go. You want to keep them working, incentivized, and to repeat the success that you've already had here. So there are very powerful reasons to do what they're doing.

What's another factor they might consider? Well, among other things, the say-on-pay vote. Among other things, Your Honor's settlement hearing, Your Honor's -- Your Honor's comments here. So, of course, I think our clients will take into account all of the important things that they're supposed to do, which is what business judgment's about, which is what dealing with alternatives is about, which is what dealing with risk is about. So I think those are some important things that I try to keep in mind about this.

Perhaps, with the Court's permission, I might just take a minute and talk about the terms of the settlement, particularly those that are most

important to us. Your Honor, as I know the Court is aware, the settlement provides that the parties will jointly request an order pursuant to Section 205 that would validate the stock issued, the so-called existing grants. That was issued pursuant to the 2011 plan. And the concept would be that those existing awards would be validated.

Now, obviously, as to the available shares, again, a defined term that refers to the 7.8 million, they would need to send it to a vote. The advantage of that, the beauty of that, is that it would remove the uncertainty with respect to the validity of that stock that caused the jump from 18 to -- to pushing 80. It would remove the possibility that the compensation to Cheniere's officers, directors, and employees would be invalidated.

And, Your Honor, on that score, just a slight diversion. I am mindful that it's not just the directors who are getting this, not just the officers who are getting this. The reality is the 600 employees of this company now -- it's up from -- that's a very large increase in jobs. They expect it to be a whole lot higher than that if they can get Trains 5 through 9 put together. But these shares

went to everybody. They went to all the employees. It wasn't just the senior group. And the senior group might have ridden the price up, but so did everybody else. An important fact. And this 205 order, Your Honor, I think would -- would be very important in terms of validating those shares.

Now, obviously, before 205 was passed, there were cases that created problems for something like this. 205 empowers Your Honor in a number of ways, a number of really important ways. Number one, you can determine the validity of any defective act. Your Honor has the power to determine the validity of any stock. You can declare the shares of putative stock -- that is, shares purportedly issued and voted on -- are shares of valid stock and make such orders as the Court deems to be appropriate.

205 lists the factors that Your Honor can take into account. They're -- again, they're fairly clear and fairly broad. You can consider whether a defective corporate act was effectuated with the belief that it was in compliance. And I'm going to talk about that for just a moment, whether the corporation and the board has treated the act as a valid act. We think, obviously, they have. We talked

about that at the last hearing, I think, when we were before Your Honor; whether any person would be harmed by the validation. I think the answer to that would be no; and whether any person would be harmed by the failure to validate. And I think the answer to that would be decisively yes.

I want to quickly, without burdening the Court, identify a number of things that I think that upsides to doing this. In other words, things that warrant the granting the relief under 205 that's been requested and negotiated with our colleagues on the plaintiffs' side.

Number one, was there a good -- the fact that there was a good-faith basis for the company's application of the votes-cast standard. We talk about the NYSE market rules. Rule 7.10 does have a votes-cast standard. We know that, under the Licht case, that a votes-cast standard, as compared with a majority of the quorum, is in fact a legitimate standard under the Delaware law that was applied in that case.

We also know on the good faith side of things that Cheniere sought the advice of two law firms, one Delaware and one from -- from another

jurisdiction. But they went and sought legal advice before they did it, and looked at Rule 7.10 of the NYSE market rules, and they did all those things.

Second, 17 months passed between the original proxy statement, which set forth that abstentions and broker non-votes wouldn't be taken into account in this action. A lot of time passed. 15 months passed between Cheniere's public announcement of the vote counts and that the stockholders had approved the amendment. So people have known about this for a very, very long time. Nothing happened.

The fact that, again, Cheniere acted in good faith. Well, it filed appropriate disclosures, it notified the NYSE market, it got the shares listed on the NYSE market and, of course, told the NYSE market about the vote count. So we think that's important.

The shares, in addition, have been at all times treated as valid by Cheniere, by their stockholders. The shares, Your Honor, have done the job. They've done the job that they were intended to do, and that -- at least where a majority of those voting presumably intended to achieve that result.

On the good faith, again, side of things, stockholders were told in the proxy statement that abstaining stockholders would -- would not be treated as no votes. Now, we understand, obviously, the different result that goes under the alternative standard. But Cheniere, as I think I said to Your Honor before, and I firmly believe it, was transparent about the whole thing. Cheniere was aboveboard.

In addition to that, Cheniere has awarded more than 17 million shares of stock. That's upon Amendment No. 1. The recipients have relied upon that. Stockholders, those recipients, employees and others, stockholders who purchased the shares in the market, perhaps, but certainly the employees, again, have relied upon the -- the validity of those shares and could and would, I think, be hurt by -- by the absence of an appropriate validation under 205.

Two other points that I think are really important. Number one, stockholders have been given notice of what's going on in this hearing today. Stockholders have been told what the plans are. Stockholders -- no one has objected. And of course, the plaintiffs, who are supporting the settlement, are

fiduciaries for that class and, of course, they support it as well.

Now, the other thing I would say about the 205 order, Your Honor, is that it strikes a balance. It avoids harm by validating the existing awards. Employees, stockholders, get the benefit of that validation. But at the same time, as to the available shares -- and I know Your Honor is sensitive to this based upon the questions you asked my colleague Mr. Golan -- they get a right to vote on those which have not yet been awarded. It's a balanced -- very much a balanced award.

So we would respectfully request that the 205 order be entered and that the shares be validated. We think that that's an appropriate part of the settlement and very respectfully, Your Honor, request that that be done. I think, you know, it's been said that 205 is aimed at mistakes, or maybe even goofs, or something to that effect. And this is a situation that seems to call out for the kind of remedy that 205 allows.

Now, there are other elements to the settlement. Your Honor, we negotiated those. We negotiated hard. We didn't always agree, but we did

reach an agreement, and we support that settlement as well.

THE COURT: What's your view on the compensation committee part? Again, what is the difference, the before and after difference, in that part?

MR. WELCH: Well, Your Honor, I think our view was that we thought our committee was independent. A contractual agreement that -- that requires that it be independent going forward provides value. There's a lot of things that the company is doing which, again, provide value. We thought our comp committee was doing a good job. But that said, I mean, to the extent you have a court-ordered agreement that says that that's how it will be and how it should be going forward, I think that provides value. I don't question that.

And indeed, Your Honor, I would echo that with respect to all of the elements of the settlement. Again, they were all hard-fought. We worked hard on them. But I do think that they do -- they do have value. So I would respectfully request that not just the 205 order, of course, but indeed, that the entire order approving the settlement be

entered.

So --

THE COURT: Do you want to talk about the fee?

MR. WELCH: I'm happy to do that if now is a good time for that, Your Honor.

THE COURT: Sure.

MR. WELCH: Your Honor, I guess a couple things. First, with respect to the 7.8 million revote, that -- we think that's a voting issue. So we looked at the voting cases. We looked at EMAK, we looked at Bradbury. We think that the benefit here was the vote. Those cases are different than this case here.

But ultimately, shareholders are not getting the 7.8 million shares. And indeed, we don't know whether the vote is going to go up or down, but depending upon where it goes, the shareholders aren't necessarily going to get those. What they're going to get here is the right to vote. And the right to vote is important. It's really important. We don't have any doubt about that. It's important to Cheniere, it's important to its board, it's important to the comp committee. And Cheniere respects the voting

rights of its stockholders. So that is, in our judgment, an important benefit. But that's the benefit. It's not $565 million. It's -- it's the right to vote yes or no. Again, a valuable -- a valuable right, and one that we think plaintiffs deserve a fee for. No doubt about it.

That said, our instinct is, in looking at EMAK -- now EMAK involved, I think the Court pointed out, the Supreme Court, evidence of serious loyalty breaches. That's not the case here. Number two, in Bradbury, that case went a whole lot longer than this one. And I am not denigrating for one minute what plaintiffs have done here. But we did reach a settlement after, I think it was, a scheduling hearing and then a hearing on the 205 application that we made. So it did conclude relatively promptly. It didn't go to trial, as did Bradbury. So our thought was that $1 million for that 7.8 million share vote was -- was a good number.

Now, the second item that -- and obviously, that's Mr. Taxin's -- and I do want to talk about their view of that in a minute. But as to the prohibition on any equity comp until January 1 of 2017, on that one, Your Honor, we looked at the Citrix

case. Now, plaintiffs didn't site the Citrix case in their opening brief. They didn't touch it until their reply brief. And that's okay, but one thing that the Chancellor says in Citrix is when you're looking at a cancellation of a stock option plan or, in this case, an incentive stock comp plan, you have to look at not just the cancellation. You can't just do a simple mathematical exercise and multiply the number of shares times the -- times the stock price. You have to consider the benefit that you'd be losing out on. In other words, the Chancellor said, look --

THE COURT: So let me ask you this, though. So here's where I wonder about that. And I reread Citrix. You know, I always remember Citrix because it's the one that I thought said we could do interim fees. So Citrix, I remember Citrix; right? It's one I thought we were supposed to do.

Regardless, leaving that aside, if you-all had put in place and had in place some type of alternative plan and you were saying, hey, look, we really had to compensate these guys, we couldn't leave them hanging in the wind, you know, I would take that as something of a measure of this alternative thing you had to do. That's what happened in Simon

Property.

MR. WELCH: It is, Your Honor. I agree.

THE COURT: And so I am a little bit at sea, because you haven't done that. You haven't come in and said, hey, we looked at this, we saw that this was going to be taken off the table. And because we were worried that, you know, our five top guys were just going to walk out the door, we had to put in place something to keep them. And so we did, and so it's really a net benefit.

What do I do where you haven't given me that? You've told me you're thinking about it, but you haven't given me anything to hang my hat on in terms of figuring it out.

MR. WELCH: Well, Your Honor, I would respectfully suggest that we have. Because if you look at what the Chancellor did in Citrix, the argument was made that when the plan was invalidated, that it produced an $180 million benefit. And he said no, you can't do that. You can't just ignore the benefits that you lost out on because you're not issuing incentive comp. So what he did was to order -- or to award a fee of $140,000, which I think,

if memory serves, was very close to the -- to the -- to the lodestar.

So I think -- what do you do in a situation like that, Your Honor? I think the best I can say -- and I'm mindful and respectful of the fact that this is a judgmental issue that Your Honor has to think about, but you look at the lodestar, which is important, and --

THE COURT: And that's where I am struggling. Because again, if we're having a candid discussion in front of all of our good friends --

MR. WELCH: Sure.

THE COURT: -- it seems to me that Citrix undercompensates. Because Citrix sort of seems to assume that none of these options otherwise would go out or be exercised. And I think, look, we all know that when people grant options, it's true, some people leave before they vest. Sometimes the stock doesn't hit the strike price. There's reasons why full dilution is not necessarily representative. It's why you do other calculations; Black-Scholes, et cetera.

But when a company has a practice of granting a certain amount of equity year in, year out,

it seems to me that there's a pretty good indication that there's some savings there if you can stop them from doing that for a period of time. And I have trouble with the Citrix approach, because it seems to me to ignore that, or underprice that real impact of that type of savings.

I also, though, agree with Citrix that to do a basic calculation of number of shares in the plan times stock price, or even just to do some Black-Scholes calculation, is probably excessive. So I'm left with two poles, neither of which do I find analytically satisfying. And I am trying to think of how I do it in a way that, I guess, seems more fair to me in a case where you guys were pumping out a lot of stock to your folks and there is now going to be a hiatus.

And so, you know, I was thinking in my mind, is there a time value that I put on this? Is there a time value that I put on this of the delta between what you would have done and what the replacement plan would be? But that gets me back to the fact that I don't know what the replacement plan would be.

So I do feel like I'm a little bit

hanging in the wind on this deferral calculation. And I'm looking for help, what a wise gentleman like yourself would do in a situation where Citrix underprices, but 1.7 billion is -- that's amazing money. I mean, what? It probably puts you in the top 200 wealthiest citizens in America. But that's a lot of money.

MR. WELCH: Well, in our judgment, the notion that, you know, that that benefit was conferred just -- it may be a lot of money, but it doesn't make a lot of sense.

THE COURT: Yeah. So what do I do in the -- there's got to be some middle ground. And I'm not saying I'm going to split the baby, but there's got to be some other way of thinking about it that --

MR. WELCH: I hope not, Your Honor.

THE COURT: There's got to be some other way of thinking about it that grapples better with the pros and cons of this situation than those two extremes.

MR. WELCH: All right. I guess I would say this: Citrix is, I want to say, ten years old now? Eleven years old? So we're not suggesting in any sense that the $140,000 is necessarily the

right number. I mean, what we did say about the 7.8 was there's a couple of metrics that you can look at. You can look at the case law --

THE COURT: What if I took 148 times the compound annual growth rate in your stock?

MR. WELCH: Your Honor --

THE COURT: I'm teasing you, Mr. Welch. I --

MR. WELCH: Not the first time you've had me, Your Honor. So I'm mindful, and I always enjoy it. It's okay.

I do think that there's been -- obviously some time has passed since Citrix. But there's also some wisdom, some serious wisdom from the Chancellor in Citrix. I mean, he said, look, when you're valuing this stuff, you can't ignore what's been cut out. You can't ignore the benefit that you're not going to get.

Now here, we've also said, looked at the other side of the equation, and we've also said not only do you not get the benefit, but we are looking, as we are entitled to do, as plaintiffs agreed we were entitled to do, look at stock-based compensation on the other end of the equation. So I

think we have to look at that.

The other piece of wisdom, though, that I think comes out of the Chancellor's opinion in Citrix is that, really, the benefit -- it's not 1.7. I mean, that's just over the top. The truth is, it isn't quantifiable. It just isn't. And I can't tell Your Honor that there is some technique that -- when the Chancellor tells me in that case that it's not quantifiable -- and I think he's right. I think he makes perfect sense.

THE COURT: You got Dages; right? Dages is a smart guy.

MR. WELCH: That's correct, Your Honor. We do. And Dages is a smart guy, and he'll be happy to read the transcript, as indeed I will, Your Honor. So I think Kevin will be happy to hear that --

THE COURT: And the plaintiffs' experts are smart people too. I don't want to denigrate them.

MR. WELCH: And no doubt Your Honor intends that. I understand and agree with that.

THE COURT: Why couldn't Dages come in and give me a middle ground?

MR. WELCH: Well, Dages came in and, I

think, gave you the right ground. What he said was, you know, that this guy -- essentially, Dages says the same thing that the Chancellor says.

THE COURT: Yeah.

MR. WELCH: Which is that -- and that's not bad authority to look to. In other words, if you're Dages looking at what the Chancellor said, this is not a quantifiable benefit. It's just not. But Dages also says what the Chancellor says, which is you got to take into account what you're losing out on when you cut out a stock-based comp plan. But you also, Dages says, have to take into account what you -- that there's an unquantifiable piece on the other end in the form of the alternative plan, which -- which we don't have to give you.

THE COURT: Why should --

MR. WELCH: It's not illogical, Your Honor, if I could --

THE COURT: Go ahead.

MR. WELCH: It's not illogical for the company to think about and to reflect upon Your Honor's views on this before you engage in something different.

THE COURT: Yeah. I guess I'm

wondering why I don't make you guys bear the burden of not coming forward with a plan. Sort of essentially make it your cross to bear, that you didn't come forward with some alternative measure that I can hang my hat on. And then, rather than stepping into that vacuum, I'm going to leave you in the bed you made. And had the board sort of made some decision about what the alternative plan had to be, well, then I'd have some metric to use, I could figure this out. But here, sort of left it open.

MR. WELCH: Well, you shouldn't -- I would submit -- and again, I haven't seen minutes on this, or anything like that, but I would submit that you don't put in place an alternative prematurely. You take into account, as a diligent comp committee member or diligent board member, you know, a variety of factors. But -- and one of them is, you know, what happens with this settlement. And again, our position is the settlement absolutely ought to be approved. We feel very strongly about that. And that would help guide the committee in terms of what they're doing.

But to get ahead of themselves and to try to put something on the table, you know, at this point, is just not what they chose to do. They

haven't done that.

THE COURT: Yeah. I guess it may be that because I had the experience with Simon Property where that was done, and I had the two things to look at --

MR. WELCH: Sure. Of course.

THE COURT: -- it did seem to be a lacuna, to use then-Vice Chancellor, then-Justice, now Retired Justice Jacobs' famous word.

MR. WELCH: Understood, Your Honor.

THE COURT: Yeah.

MR. WELCH: Well, Simon Property is a very different case. You had one award being given, I think, to the CEO, if my memory serves on that. And then ultimately, that was pulled, it was mooted. It did another award. And so did it make sense to say that --

THE COURT: Yeah. That's why I was saying. I was able to look and see, okay, they did have to have some retention expense.

MR. WELCH: Right.

THE COURT: And so there was a delta there.

MR. WELCH: Right. Well, here,

though, I mean, if you look at the before and after analysis, you know, the 7.8, that was never awarded. Hasn't been awarded. Might never be. It's the vote. That's what --

THE COURT: I'm with you on that. I understand that. I'm focusing --

MR. WELCH: No I'm asking -- pardon me, Your Honor.

THE COURT: I was going to say, I'm really struggling with the 1.7.

MR. WELCH: Well, when you look at that and you do a Simon Property type analysis, and I say to myself, well, before all this happened we had a stock plan, we had world-class, record-setting benefits from that stock plan. Now we don't. We -- but on the other hand, they're looking at an alternative, as permitted by the -- by the settlement, and none of those factors, to go back to Citrix, none of those factors can be, you know, quantified. They simply can't.

Now, what does one do in a situation like that? The metrics that I can offer Your Honor are simply these: Number one, that you can look at the case law that's out there and look at the numbers that

were awarded, and we've talked about a little bit of that. And you can look at the lodestar -- at the lodestar that has been approved, or that has been submitted for Your Honor's approval.

And I think -- you know, and just turning to the other factor, the correction of the capital structure issue, did they play a role in that? Sure. Yeah. They did. They brought the issue to the attention of Your Honor and to us. So they certainly did that. On the other hand, are they really the ones that are making this happen? We would suggest no, that they're not. We filed the 205 case and did what the statute seems to contemplate.

Now, a huge fee on the -- you know, in a 205 context just doesn't seem to make a lot of sense. Doesn't seem to be consistent with the statute. A reasonable fee certainly does. We suggested half a million dollars. Aggregating with the three positions, the 7.8, the January 1, '17 30 million -- the no equity comp restriction, and the correction of the capital structure, 2 1/2 would seemingly make sense. That's how we looked at it.

Now, if I could take a moment and look at plaintiffs' position on fees -- and I wish I could

give you something from the case law to assist in the process, but I think it comes down to the fact that this is a unique circumstance. This is the first -- Trupanion was out there, Numoda was out there. This is the first one that comes along that presents these issues, and I don't know that there's something I can point to other than the key facts that, number one, it isn't quantifiable, and we know that from the Chancellor's viewpoint and common sense. They say they invented something, the Chancellor invented something. He invented common sense. That's all he did. And so that was powerful.

Now, with respect to the plaintiffs' position on fees, I will -- and I'll be brief on this, but I think I would say the following: They -- Mr. Root, you know, says that the restriction on the ability to approve additional incentive-based comp until January 1 of '17 is this enormous value. I mean, the interesting thing about that is, as we said in our brief, it's a little bit like saying if stockholders think that the track record of this management is stunning, is extraordinary, that they've benefitted hugely from it, they nevertheless can't vote for additional incentive compensation. Now, from

their standpoint, we have respect for the fact that that's a benefit. Very much so. At the same time, we don't think, you know, stockholders not being able to choose to do that for a period of time is necessarily a huge benefit. We don't think it is.

Now, there's several other points with respect to the assumptions that Mr. Root makes. Number one, he seems to say, you know, incentives can be abolished without cost. We think that doesn't make any sense. We think Citrix completely rejects that. It doesn't make sense. There's a powerful need for additional incentives here. The fact of the matter is, Trains 5 through 9 have yet to be built, and they need to be.

The second assumption we think that they're wrong about is that because there's no equity-based comp, there won't be any comp. Well, certainly the -- any incentive comp, rather. Certainly the settlement agreement says to the contrary, that that's -- that's not the case. Indeed, we're allowed to do that. Which also makes sense. And, of course, Mr. Kilpatrick has said that they're doing it.

Number three, in order to run a burn

rate or a Monte Carlo simulation, I think Mr. Dages and the Hay Group point out, you got to have a plan. You got to have shares and you got to have a plan.

Now, at this point in time, the company has pulled the 2014 to 2018 plan. It wasn't submitted to a stockholder vote. Other than the 7.8, which have not yet -- has not yet been approved, we don't have shares, and we don't have a plan. So for them to run this -- this -- this Excel spreadsheet and come out with these numbers, we think just doesn't make sense at all.

Now, the next assumption that we think that they're off on is this: They seem to -- they're assuming that all the elements, you know, of the past compensation awards remain the same, even after the negative say-on-pay vote, even after the developments, the other developments that have occurred in this situation. It's like saying the board -- this board's not capable of adjusting and making different business judgments under different circumstances. Of course they are. And that's why, I think, the stipulation of settlement provides for the adoption and approval of an alternative which is cash-based, which is what they're looking at. But this notion that it all stays

the same just doesn't compute.

Now, obviously there was some discussion in our brief about our perception that they seem to think $1 of -- it's a dollar-for-dollar detriment in incentive comp. We don't think that's the case at all. Why do we say that? Well, because they're claiming a dollar-for-dollar benefit with this mathematical exercise that they do. We don't think that's right. The event study that Mr. Dages submitted supports that. Citrix, of course, looked at an event study as well. So that -- I don't think that analysis is particularly helpful.

Bottom line is we don't think, with respect, that the Root analysis is particularly helpful. We simply don't. Now, and that's why we said to Your Honor at the outset, in our brief, and in our affidavits, this is not quantifiable. It's not possible to come up with a mathematical exercise that would be anything other than artificial to try to -- and Dages doesn't do that, and neither does -- does Hay. They simply don't.

But they have said to Your Honor, and what we have said to Your Honor, is that, in fact, this is a situation where you can't quantify it, and

it's going to be a judgmental exercise. We -- we obviously do look at the suggestion of lodestar. We do look at the case law that was identified to Your Honor earlier. But we also are mindful that keeping in mind, as you look at Root and Taxin -- Taxin is subject to the same problems. He ignores the benefits of the 7.8; right? And he ignores the potential back-end cash-based compensation as well. Both are critical points. So we think his submission is no more persuasive than -- than is Root's.

Your Honor, I would -- I've been up here a while, and I don't want to, particularly in light of Your Honor's comments earlier, wear out my welcome. I would take a minute, or perhaps two, and no more, and touch upon some of the points they raised in their reply brief.

THE COURT: Sure.

MR. WELCH: Unless Your Honor would find that not helpful.

THE COURT: First let's check with our court reporter. How are you doing? Can you make another 15?

THE REPORTER: Absolutely.

THE COURT: Why don't you take five,

and I'll give Mr. Golan ten minutes for his reply, and we'll see where we are.

MR. WELCH: As we went through the brief, Your Honor, I had the following reactions. Number one, Simon Property. They say consider the situation today versus the situation that existed before. I think we've talked about that. As to the 7.8, never was awarded, may never be. Vote is the benefit. As to the 30 million shares, the plan was pulled. We have no stock-based comp plan. We have no benefits from that plan. But we might have an alternative, but that's not out there yet. It can't be quantified.

Secondly, they make the criticism that the Citrix case invented something. And I -- I think I've spoken to that. They invented -- the Court invented common sense.

Your Honor picked up on the next point, which was that, you know, Taxin's view of the shareholders would not approve the incentive plan 7.8 million, I think that does apply to the 30 million shares as well. It won't happen because the plan was pulled. There are no shares and there is no plan at the moment. Hopefully there will be in the future,

because this has been a great success story, but there isn't anything at the moment.

They claim at page 18 that, look, their experts are right, Dages and Hay are wrong. I would suggest that, you know, their experts don't know the business. The Kilpatrick affidavit is the only submission Your Honor has from somebody that does know the business. His history in oil and gas and history with this company and history with other companies in the business is extraordinary. That affidavit is effectively ignored. They know, I think, nothing about, and didn't even mention in their opening reports Trains 1 through 4 or 5 through 9. Sabine Pass, Corpus Christi, or anything else.

Their experts essentially ask Your Honor to take on the role of the board; right? But this is a board that's brought this company from a $150 million market cap to an $18 billion market cap, and the options were granted at much lower prices and everybody benefitted from it.

They say there's enough incentives, you know, at page 20 of their briefing. Just enough, you don't need any more. Again, that's usurping the role of the board and the comp committee. That's

their job to decide this, and they haven't decided it yet. However, they've put in a chart, and the chart is the five top officers. And they said this is -- they say this is the -- this is a lot of value. And it is. That said -- they ignore the fact that there were 600 employees that were getting these incentive-based comp awards. All of them rode the stock price up, all of them have benefitted, and it's been one of the most successful incentive-based comp plans in history.

Your Honor, I think, if I could just have a moment, you know, touching on just one or two other points. They claim credit for the withdrawal of Amendment No. 1, and I suppose they can say, well, there's a presumption that we complained and, therefore, you acted. I think Cheniere has rebutted that presumption with respect to Amendment No. 1, pulling the 30 million share plan. Mr. Kilpatrick attaches the Broadridge report to his affidavit as Exhibit 1. The reality is that it wasn't going to be approved by stockholders.

Now, plaintiffs might have complained about it, but the reality is it wasn't going to be approved, for that reason. It was withdrawn, and I

don't think there's any particular consequence to that. That wasn't part of the settlement anyway. We're not going to do additional incentive-based comp going forward until January 1 of 2017. But I don't think that plays a material role here, but they put it in their brief.

As to the Monte Carlo submission, Your Honor, I guess the only thought I have on that one is -- and we touched on it in our opening and -- or in our answering brief as well, that measures accounting costs. But in order to measure it, you have to have, A, shares and, B, you have to have a plan. And we've got neither. And beyond that, the Monte Carlo simulation doesn't measure the benefits to the company, to the stockholders, to the employees, that the plan would have otherwise provided. We've got no plan, so therefore, we don't have any of those benefits. Monte Carlo just doesn't make sense there. For the same reason --

THE COURT: Mr. Welch, I'm going to tell you, I think I've got where you're coming from. Let me hear from Mr. Golan on reply.

MR. WELCH: Thank you, Your Honor. I very much appreciate your time.

THE COURT: Thank you.

MR. GOLAN: Thank you, Your Honor. Your Honor, and I will try to be brief. On Monte Carlo and Simon Property, Professor Ferrell of Harvard Law School did the analysis the correct way. There was an original award, there was a subsequent replacement award. It was a pure mootness case, as I recall it. The correct delta between the original and the replacement was 6.3 million. The fee was awarded as a percentage, 20 percent of that.

The whole purpose of a Monte Carlo simulation there, and as Mr. Root did it, is to put a present value on future costs. And in Simon Property, this Court said that that was the best methodology of valuing the difference and that the correct approach is to take the situation before the litigation started compared to the situation after the litigation. Here, the Monte Carlo approach for the withdrawn plan shows that the benefits are anywhere between 1.2 and 1.7 billion. There's no dispute about the methodology underlying what Mr. Root did in the Monte Carlo system, and it would be -- it doesn't make sense what the defendants are asking you to do. What they're asking you to do is say because we haven't put a

replacement plan in place, even though Mr. Root showed that the benefit of this, net of a replacement plan, would be 1.2 to 1.7 billion, because we haven't put a replacement plan into place, you can't take the delta and, therefore, you should accord zero as the benefit.

And Your Honor is right that when you're trying to do that kind of net economic benefit analysis, as the J.C. Penney Court said -- it's a Texas Court, but it was looking at Citrix. It said --

THE COURT: They're smart people in Texas. We don't --

MR. GOLAN: But they had similar --

THE COURT: -- we don't any negative views about Texas.

MR. GOLAN: They had similar misgivings about Citrix's approach. But one thing that the Court there said was that if you're going to try to calculate this net economic benefit, it's the defendants' burden to do that. And here, Mr. Dages didn't do it, Mr. Becker didn't do it, the defendants didn't do it. And respectfully, if I can surmise a little bit, the reason they didn't do it is because they knew that that would result in too high a valuation for this Court to use as a basis for a fee

application.

And it makes no sense that they can come in and say because you can't do a before and after, because we've never provided you with the after, you have to say that the benefit of this is zero. So that's one point. And in fact, Your Honor, courts do this all the time. You value future events based on reasonable assumptions. That's what a discounted cash flow is, that's what a Monte Carlo simulation is. That's what a burn rate analysis does.

And even -- even that's what you do when somebody is injured at a workplace. You can't be sure that that person wasn't going to be hit by a bus the next day. You can't be sure that the company wasn't going to take its jobs, close the plant, and go to China. But what you do is you value based on what occurred in the past and a reasonable employment trend for that person, and you take a present value of that, of the future expected -- in that benefit -- payments, wages. In this benefit, in this context, you do it based on savings; what the company saved because we, in the settlement, A, had forced them not to award the 7.8 million shares unless voted on by the shareholders, which everybody agrees is highly

unlikely. No disagreement from the other side of the bench. And what we do on the other is say here's the value of it. This is why our experts do not believe that there's a net economic to reduce, because these incentives -- which, Your Honor, if -- they're in Charts 1, 2, and 3 to our reply brief.

THE COURT: Okay.

MR. GOLAN: There's also even a more detailed chart in the Root supplemental affidavit, in paragraph 9 at pages 6 and 7, which does include employees, a line for employees, based on what Mr. Root was able to divine from public sources.

These show that based on these unvested awards, there's plenty of incentive here, at least until 2017. So you don't need to reduce the 1.2 to 1.7 billion that Mr. Root showed in his analysis was appropriate, whether under a burn rate analysis or a Monte Carlo analysis, and there's no reason to reduce by any meaningful aspect what Mr. Taxin developed from his analysis of the 7.8 million available shares.

And just a couple other points, Your Honor, if I may. Mr. Welch cites the Bradbury case. That -- first of all, there's a 2.9 million fee for

invalidating some continuing director provisions in two debt instruments. There was a value of that. It was clearly unquantifiable, because there was nothing at issue of an economic sense. It was a straight, the plaintiffs did a nice job on this because they pointed out how this was impairing stockholders, the stockholder franchise, the voting rights of stockholders.

Here, there is a quantifiable benefit. If Your Honor, you know, wants to say it might not be 565 million because he says it's highly unlikely, but maybe there's a 10 percent chance it's going to pass, well, reduce it by 10 percent, $510 million value. That kind of thing. This Court does that all the time. The Court has obvious discretion in terms of accepting valuations and in terms of awarding fees. But there are constraints on that, respectfully, from the American Minings case and from other decisions, that say that it's the benefit achieved in a settlement that should be the primary driver of the fee that's to be awarded.

And one other point, Your Honor. I mean, we could have reached -- had Mr. Welch and his group not come up with the 205 application, which was

a -- which was, you know, a good litigation tactic. It certainly got our motion to expedite off the calendar. It made it impossible, as we pointed out in the reply brief, for this company to go forward with the proposals, because the Court was not going to hear our motion to expedite or our motion to enjoin the vote. So even that shows that the litigation had a direct impact on pulling those proposals.

It was a nice addition to the case, but we had started the case three weeks earlier. And had Mr. Welch not filed that 205 application, we could have come to the same point in the settlement. We could have come to an agreement on behalf of the plaintiffs and the non-opt-out class to say that we're asking the Court to validate or to allow those to remain -- the 17 million shares to remain, and to require the vote on the remaining 7.8. So it's really not -- it's really not necessary that that -- that doesn't create part credit on the plaintiffs' side, respectfully.

Unless Your Honor has any further questions, I think I've probably covered everything.

THE COURT: Thank you. Let's take a break until noon. We'll resume then.

(Recess taken, 11:44 to 12:00 p.m.)

THE COURT: Please be seated, everyone.

All right. Thank you very much for waiting. I am going to give you some answers now. I am going to approve the settlement, and I am going to award the plaintiffs a number that they will not be pleased with, but I am going to award them $5 1/2 million in fees. And I'm going to give you my reasons, so you can pay attention and take notes for the purposes of any appeal.

This hearing is so that I can consider the proposed settlement in In re Cheniere Energy, Inc., C.A. No. 9766, as well as In re Cheniere Energy, Inc. Stockholders Litigation, C.A. No. 9710. One is a class and derivative action, the other is a 205 proceeding to validate shares. Because the litigation settles representative litigation as well as a 205 action, I am going to go through all the steps for class certification and derivative action settlement approval, in addition to discussing 205.

The class definition set forth in the papers is "any and all record and beneficial owners of common stock of Cheniere," together with a broad list

of other folks, "at any time between and including March 2, 2011 and the Effective Date, but excluding Defendants and their immediate family members, any entity controlled by any of the Defendants and any successors in interest thereto." I.e., successors to the defendants. The class otherwise includes successors. I find that to be a reasonable and adequately cohesive unit for purposes of the litigation, and I confirm the preliminary use of that definition.

The Rule 23(a) requirements are met. Under Rule 23(a)(1), numerosity is required. In this case, as of October 16, 2014, Cheniere had 236,846,177 shares of common stock outstanding on the New York Stock Exchange. It's reasonable to assume that Cheniere's stock is held by owners across the United States, satisfying the numerosity requirement.

The second question is whether there are issues common to the class. Here, common questions of law and fact included whether Cheniere's management team and board breached their fiduciary duties towards plaintiffs and whether the same individuals breached their duties under the constituent agreements of the corporation, including

its bylaws, in connection with a vote in February 2013 on a stock option plan, the issuance of shares under that plan, a certain bylaw amendment, as well as some other events. There are also common issues of law and fact as to whether the vote that took place in February 2013 was conducted in accordance with the company's then-existing bylaws. Both for purposes of the class and derivative action and also for purposes of the 205 proceeding, there's the question of whether the shares should somehow be ratified or validated. There's also the common question of whether the class was harmed by the alleged breaches of duty. These questions are common to all class members in their capacity as stockholders, satisfying the commonality requirement.

Rule 23(a)(3) requires a showing of typicality. In this case, all class members in their capacities as stockholders faced the same injury from the same conduct, satisfying typicality.

The final Rule 23(a) requirement is adequacy of representation. There are Rule 23(e) affidavits in the record from James B. Jones, Robert Maguire, Robert Shenker, and Kayann Davidoff, all affirming that they owned Cheniere common stock at the

relevant times. There's no evidence of any divergence between the interests of the plaintiffs and the class. They retained counsel known to the Court and qualified to litigate this matter. The class representatives support the settlement and have provided the necessary affidavits. In my view, both the results obtained in the settlement as well as the conduct of the proceedings confirm the adequacy of the representation.

The next question is whether the class can be certified under one of the headings of Rule 23(b). Rule 23(b)(1) certification is appropriate if prosecution of separate actions by individual class members would risk inconsistent or varying results. In this case, adjudication with respect to one class member -- i.e., one stockholder -- would be dispositive of all the class's interests, making a non-opt-out class appropriate under Rule 23(b)(1).

The class is also appropriately certified under Rule 23(b)(2). Rule 23(b)(2) applies when the defendants have taken action that's generally applicable to the class, making non-opt-out class-wide declaratory or injunctive relief appropriate. In this case, the defendants certainly acted on a class-wide

basis. Everyone in the class felt the effects in their capacity as stockholders. They were not differentially treated as individuals, because the entire alleged injury flowed through to the plaintiffs in their capacity as holders of shares. Certification is therefore appropriate under Rule 23(b)(2) as well.

The class representatives have filed the requisite 23(e) affidavits. Consequently, I am going to certify this class as a non-opt-out class meeting the requirements of Rules 23(b)(1) and 23(b)(2).

Because the representative action also was filed as a derivative action, I must make sure that the Rule 23.1 requirements are met. Everyone has filed the necessary affidavits under Rule 23.1(c). There also were filed the necessary affidavits under Rule 23.1(b). Otherwise, the requirements for asserting a derivative action and for derivative settlement largely parallel the type of adequacy issues that I already addressed in the class action certification context, and so I won't repeat myself as to those.

The next question is whether there was adequate notice of the settlement and the settlement

hearing today. By rule, notice by mail, publication or otherwise of the proposed dismissal or compromise shall be given to shareholders or members in such manner as the Court directs. That's Rule 23(e). There's a similar rule under 23.1(c). A notice of settlement is sufficient if it contains a description of the lawsuit, the consideration for the settlement, the location and time of the settlement hearing, and informs class members where additional information can be obtained.

Here, the notice adequately described the lawsuit, including the claims asserted and the proceedings to date at pages 2 through 4. It adequately described the consideration at page 6. It adequately identified the location and time of the settlement also on page 6, and it informed class members whom to contact for further information at page 7. The affidavits of Jannette MacDonald, both an original affidavit and a supplemental affidavit that I received today, explain that notice was mailed as ordered by the Court.

My next task is to consider the merits of the settlement, which in this case requires a determination that the settlement is fair and

reasonable. In my view, the Court's task is to determine whether the settlement falls within a range of results that a client reasonably could accept. In applying that standard, the Court's job is not to determine the outcome of the claims but, rather, to consider the nature of the claims, the possible defenses thereto, the legal and factual circumstances of the case, and then to apply its own judgment in evaluating whether the settlement is reasonable in light of those factors. That's a paraphrase of the Philadelphia Stock Exchange case.

The settlement of representative litigation is unique because the fiduciary nature of the litigation requires the Court of Chancery to participate in the consummation of the settlement to the extent of determining whether the settlement meets that reasonableness requirement. That's a paraphrase of the Delaware Supreme Court in the Rome v. Archer decision.

Here, there were a variety of claims and defenses presented. The plaintiffs' central claim was that Cheniere management incorrectly applied a votes-cast methodology to find that stockholders approved Amendment No. 1 to the 2011 plan, when

Cheniere's voting bylaw at the time of the February 2013 vote was consistent with the Delaware default rule under Section 216(2), under which abstentions count as no votes unless a company's bylaws or certificate of incorporation otherwise provides.

This claim, I thought, was quite strong. One never knows what would happen in litigation, but I think there's a very high likelihood that I would have agreed with the plaintiffs and ruled in their favor on this claim. I think that there was less heft to the plaintiffs' backup claim which was, namely, Cheniere's management team and the board breached their fiduciary duties to the plaintiffs and the class in connection with these votes. I think once the bylaw issue was adjudicated, the fiduciary duty issue likely would have fallen by the wayside.

The defendants, however, also had a very strong defense. Although I thought their defense to the actual voting standard was weak, they had strong arguments in favor of validation of the shares under Section 205. Among other things, a significant amount of the shares went to employees who were not involved in the decisions to seek approval of the amount of the awards or to actually provide the

awards. There was also substantial evidence that this was an error by the board and management and not some effort to act surreptitiously or selfishly. It rather seems to have been a good-faith mistake.

Thus, I think it's highly likely that although the plaintiffs would have prevailed under their underlying legal argument, the shares, either in total or a substantial portion of them, would have been validated under Section 205. The shares that really, I think, could have been in play were the shares that were held by board members or management insiders, where there would have at least been some argument that those individuals should have borne the cost of their mistake, rather than shifting it to the company as a whole. But that would have been an issue where arguments could be made either way, and I think the outcome of how that would have turned out is difficult to predict.

So the question is, with a strong claim but also a strong validation response, does the settlement fall within a range of fairness? I think it does. The settlement consideration, as I view it, falls into three buckets. First, there was a number of shares of common stock that were available for

issuance under the 2011 plan but in fact had not yet been awarded. That number was 7,845,630 shares. The parties refer to those as "the Available Shares." Under the terms of the settlement, the company has to obtain a re-vote before using the Available Shares for compensation purposes, and that re-vote must actually comply with the company's bylaws and use the entitled-to-vote standard that the company's bylaws call for.

Notably, there were approximately 17,154,370 shares under the plan that I think, arguably, was not validity approved that have already been awarded. Some of those went to directors and senior officers. However, it appears that a significant portion of those went to line employees and others who were not involved in the decisions. Part of what this settlement will do is validate those shares so that there's no question about their validity.

The second bucket of consideration that the plaintiffs obtained is restrictions on the company's ability to seek stockholder approval to issue equity compensation until 2017. Basically, under the terms of the settlement, the company can't

do it. But what the company can do is provide some other type of compensation plan. The company is not restricted in its ability to use non-equity-based compensation, such as cash or phantom grants or similar types of things that creative compensation consultants tend to come up with.

The third bucket, that I've already touched on, is the correction of the company's capital structure. The parties have requested, and part of the settlement would involve, the validation of all existing awards -- in other words, awards that were previously granted -- and all common stock issued or to be issued in connection with existing awards, and further declare that current holders of the existing awards are entitled to ownership of such shares. If this part of the settlement is approved, that will remove uncertainty about the validity of these shares in Cheniere's capital structure and also avoid potential problems down the road figuring out who can vote, who can't vote, giving opinions as to due authorization, and all kinds of nasty consequences that would flow if these shares are not validated.

There is another piece of the settlement -- namely, a corporate governance

provision -- that says that the compensation of the committee of the board going forward will be comprised exclusively of directors who meet the independence requirements of the New York Stock Exchange. That was already true. I view that component of the settlement as gilding the lily and as having no independent value.

So what do I do with these benefits? Well, I think they are sufficient to provide consideration to settle the case. I think that there is a bargained-for exchange here. The plaintiffs and the defendants were both able to bargain at arm's length over these benefits. I've independently considered whether they're sufficient to support the type of relief that is being agreed upon. As I said, but for the fighting issue that I think was a close call over what would happen with shares owned by directors and officers at the time the mistake was made, this settlement comes very close to achieving the likely outcome that would have been obtained in the case. Namely, I think I would have validated the shares, certainly for the non-executives and non-directors. I think I also would have enforced the voting standard going forward. So in that regard the

plaintiffs essentially achieved what they could have by going to trial. On balance, I am happy to approve the settlement.

This brings me to the question of attorneys' fees, which is the most difficult aspect of the case. Delaware's policy is to ensure that even without a favorable adjudication, counsel will be compensated for the beneficial results they've produced, provided the action was meritorious when filed and produced the benefits that were conferred. That's a paraphrase of the Allied Artists case.

Plaintiffs' counsel is entitled to fees and expenses under the common fund doctrine for creating a common fund for the class. Plaintiffs' counsel is also entitled to fees and expenses under the corporate benefit doctrine for conferring other benefits on the class. Those are paraphrases of the United Vanguard case from the Delaware Supreme Court.

In setting the amount of a reasonable award, the Court considers the factors in the Sugarland case. The most important factor is the size of the benefit conferred. I will return to that one. The Court also can considers, as a cross-check, the amount of time and effort expended by counsel. I will

return to that one at the end.

In terms of the third factor, the relative complexities of the litigation, I think this was an ordinarily complex case for the Court of Chancery. It wasn't easy. It wasn't hard. It was right there in the middle. The standing and ability of counsel is unquestioned. Counsel did bring this case on a contingent basis. The litigation, in terms of the stage at which it ends, ended early, which in my mind warrants a lower range of benefit.

Let's start by focusing on the amount of benefit conferred. The parties differ substantially on the size of the benefit and, hence, the amount of fee that should be awarded. The plaintiffs believe that they conferred a benefit of $1.724 billion and, therefore, should be awarded a requested fee of $43,100,000. That would equate to approximately $14,366 per hour, based on their lodestar. The defendants respond that a fee of no more than $2,500,000 is warranted, based on nonquantifiable benefits, which would equate to $833 per hour, a result more consistent with most of this Court's precedents.

The claim of $1.724 billion is such a

staggeringly large amount of money that I tried to figure out some things that one might equate it to, my thought being that if the relief that the plaintiffs obtained is really worth this much money, one should generally be neutral as between the outcome of this settlement -- namely, a vote on the available shares and a deferral of other equity compensation -- versus the types of things that would be worth about that much money.

I don't think anything on this list is one where I would choose the relief the plaintiffs had over what's on this list. So, for example, for 1.72 billion, you could buy 93,423 new Honda Civics at the manufacturer's suggested retail price. That would be more than one for every person in Wilmington. If I had a choice between providing everyone in Wilmington with a new car and the relief the plaintiffs obtained, I would value more highly the cars, which suggests to me that the 1.724 is exaggerated.

Perhaps instead of Honda Civics, the executives in this case might be more familiar with this means of transportation. One could buy, for the 1.7 billion, 38 Gulfstream V-SP luxury private jets. One could provide, for 1.7 billion, full scholarships

to Harvard for all four years for nearly 10,000 students. One could send 24 astronauts to the International Space Station and back. One could buy 8,809 houses for homeless folks at the median sale price in Delaware. One could help out the military: One could buy 230 M1 Abrams tanks with all the latest upgrades. You could, in fact, thinking about Washington, buy the Washington D.C. NFL franchise and change its name. You could buy one of the ten Virginia-class nuclear submarines commissioned by the U.S. Navy last year. Most importantly, to my thinking, you could hire for our country 30,400 additional teachers for one year at the median salary in Delaware.

Would I be neutral as between the benefits the plaintiffs conferred or claimed to have conferred and any of these items? I would not. I think each of these items that I've identified carries significantly more worth than the benefits that the plaintiffs have claimed, which makes me think that the amount claimed is, indeed, excessive.

So why would that be so? Let's think about the first bucket. The first bucket is the vote on the available shares. When we provide votes for

stockholders in Delaware, we don't price it based on the underlying item that the stockholders are voting on. So in a deal, the value of the vote isn't measured by the value of the deal. When somebody gets disclosures to protect the vote on the deal, those disclosures aren't priced as if you obtained a $1 or $2 billion benefit, or whatever the size of the transaction is. To the contrary, the Delaware Supreme Court explained, in EMAK Worldwide v. Kurz, that the benefit to the stockholders of providing a vote doesn't vary up or down with price, because it's an intangible benefit.

Now, that's good when you're bringing a case involving a small-cap company or another small issuer, where the size of the deal is small. It means you get the amount, as in EMAK, that is suggested by the cases for the vote, even though the size of the issuer is small. But that principle works on the upside too. You don't get to claim a huge benefit for doing exactly the same work and providing the same metaphysical type of voting relief simply because the underlying thing you're voting on is big.

So at least in my view, $565 million of the $1.7 billion benefit is not well-taken.

Rather, I think to price that benefit, it's important to look at precedent cases; most notably, the $2.5 million in EMAK and the $2.9 million in Bradbury. I am going to, for that bucket, award $2 1/2 million, which is comparable to what was awarded in EMAK.

Now we get to the second bucket, which is the restriction on seeking additional shares for compensation purposes until 2017. This is the most difficult element for me, because I think it could support a relatively more substantial award. The issuer in this case was pumping out an awful lot of equity, so a deferral of that has some value. But what I don't have at present is the ability to make a responsible estimate of value. I think that one way to look at it, in terms of the value, would be the deferral of this equity opportunity. So you'd figure out the time value of the delay in the issuance.

The other way to think about this is the delta between what people are going to get now, post-settlement, and what they would have gotten before. As the Citrix case shows, you have to take into account that there's going to be some additional compensation or other plan put into place. You don't just take away incentives without recognizing that

there are trade-offs. I do think it's likely that the new plan will be less than the old plan. So an appropriate measurement of this benefit would be the delta between those two. That's how I approached things in Simon Property.

The problem that the defendants have created is that they haven't put in place the alternative plan, which doesn't let me make that type of determination. I've considered whether to essentially make the defendants lie in the bed they've made by not allowing them to make any deduction for the unknown plan, but I think that would result in an unwholesome windfall to the plaintiffs.

I think the plaintiffs might have been able to provide me, or should have been able and would know in the future to provide me, with some type of insight into what I could use for that lower bound, be that compensation at peer companies, be that ISS approval levels, or something that I could use to measure that delta instead of defaulting to the whole amount. Because of that, I'm not going to give what I think would be a windfall to the plaintiffs based on this component, which they value at basically 1.2 billion. As I've already discussed, I simply can't

equate the deferral in this case with that amount. I think the amount is likely significant. I don't know if it's 10 percent of that, 5 percent of that, 20 percent of that. I just have no way of making a responsible estimate, absent additional evidence in the record.

So what I will do for this second element is I will award $2 million, which is largely lodestar-based for lack of a better metric. Nobody should see this as a ruling for all time. I am happy to consider a better mousetrap in a future case. I think there's a need for a better mousetrap between the underpricing that I think happens under a Citrix approach and the overpricing that I think happens under the plaintiffs' approach. I don't know how to do it. I don't have a responsible estimate to do it in this case, and so I am defaulting to that $2 million number for the second bucket.

Finally, in terms of the third bucket, correcting the capital structure, I previously awarded $1 million in the Olson v. EV3 case for similar fixes. I am going to do that same thing here.

So that gets me to a total of $5 1/2 million. As a cross-check, based on the lodestar,

when I take into account these other amounts as well, it really gives the plaintiffs about $1,600 an hour. That's still a pretty good rate. I think that's an ample award. I don't feel like I'm undercompensating.

This also -- and I hate to try to give you a gut feeling -- but this has a sense of equitable appropriateness to me, because it is between the types of smaller dollar awards that we give for disclosure-based claims, in that low six figures range, and the type of larger awards that we give when people actually get cash or actually recover stuff that the defendants had. $5.5 million is in between those poles, and I view this as an in-between case. The plaintiffs got some things. They got some good things. But they really didn't take that much away from what the defendants already had.

I'm going to do this, just to make sure that we don't have any problems later. I'm going to identify some of the factors that I've considered in approving the Section 205 validation. One of the factors is whether the defective corporate act was approved or effectuated with the belief that the approval or effectuation was in compliance with law. I do think there's significant evidence here that this

was not an intentional violation or even, really, anything other than a mistake. The board consulted with advisors and just got to the wrong result; at least what in my view was very likely to be held to be the wrong result.

A second factor is whether the board of directors and the corporation have treated the defective corporate act as valid. Here, they certainly did. The corporation relied on the vote to issue additional shares. Employees, including those having no involvement in the underlying conduct, received shares and relied on them.

A third factor is whether any person would be harmed by the ratification or validation of the defective act. Here I focused predominantly on the line employees, who don't have the same ability to have the board put in place an alternative compensation plan to make up for their lost opportunity. I think they would be harmed if this act were not validated.

Then finally, any other factors or considerations that the Court deems just and equitable. Again, in my view, this is a good result to validate the shares. So in considering all those

factors, I am entering the 205 order that implements that part of the relief.

Thank you for listening through that lengthy recitation. I will go down and take care of entering the order on LexisNexis.

Before I do, Mr. Golan, do you have any questions?

MR. GOLAN: I do, Your Honor.

THE COURT: Okay.

MR. GOLAN: Would Your Honor consider keeping the record open so that plaintiffs' experts can calculate an ISS -- a replacement plan that would be meeting the maximum guidelines of ISS, since plaintiffs clearly had no opportunity to divine that it would be their burden, considering that the defendants had not put in anything as an alternative plan. Would Your Honor consider that?

THE COURT: The answer is no. I think you've had your chance. I'm not going to do a do-over. And I think, since it was your burden to support your fee claim, it was something where you had the choice to make the most credible ask you could. I think that, look, you made the choice to come in and say, you know, $1.2 billion for this, notwithstanding

the fact that Citrix was out there. Now, you could have approached it differently. You could have given me something more. But I'm not going to do a do-over at this time. Obviously, if you decide to appeal and the Delaware Supreme Court says that I have erred in doing that, I'll be happy to have you back and we can take care of it then.

MR. GOLAN: Thank you, Your Honor.

THE COURT: Mr. Welch, anything?

MR. WELCH: No, sir, Your Honor.

THE COURT: All right. Thank you, everyone, for your time. I appreciate it.

(Court adjourned at 12:31 p.m.)

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CERTIFICATE

I, JULIANNE LABADIA, Official Court Reporter for the Court of Chancery of the State of Delaware, Registered Diplomate Reporter, Certified Realtime Reporter, and Delaware Notary Public, do hereby certify that the foregoing pages numbered 4 through 108 contain a true and correct transcription of the proceedings as stenographically reported by me at the hearing in the above cause before the Vice Chancellor of the State of Delaware, on the date therein indicated, except for the rulings at pages 85 through 108, which were revised by the Vice Chancellor.

IN WITNESS WHEREOF I have hereunto set my hand at Wilmington, this 17th day of March, 2015.

/s/ Julianne LaBadia

Julianne LaBadia
Official Court Reporter
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EIGHTH JUDICIAL DISTRICT COURT
CLARK COUNTY, NEVADA

CHARLES JESSEPH AND CHARLES CHURCHWELL, Plaintiffs, v. DIGITAL ALLY, INC., Defendant.	Case No. A-18-781874-B Dept. No.: Department XI **REPLY IN SUPPORT OF DEFENDANT'S MOTION TO DISMISS COMPLAINT UNDER NRCP 12(b)(5)**

REPLY IN SUPPORT OF DEFENDANT'S MOTION TO DISMISS

I. INTRODUCTION

Before the Court is Charles Jesseph and Charles Churchwell ("Plaintiffs") Complaint for Attorney's Fees and Expenses ("Complaint") against Digital Ally, Inc. ("Defendant" or the "Company") and the Company's Motion to Dismiss the Complaint. Plaintiffs attempt to collect $250,000 in attorney's fees based on their claim that they conferred a purported substantial benefit on the Company and its stockholders when they served a demand letter on the Company that allegedly caused Defendant's Board of Directors (the "Board") to "correct material flaws in Digital Ally's capital structure." *See, e.g.*, Compl. ¶¶ 1, 4, Cause of Action. However, Nevada law—which undisputedly governs this dispute—does not recognize Plaintiffs' cause of action where, as here, the purported benefit was not conferred through litigation. Plaintiffs fail to cite a single Nevada case holding otherwise.

In a failed attempt to evade Nevada law's clear requirement that an attorney fee can only be compensated for a benefit conferred through litigation, Plaintiffs impermissibly try to amend their Complaint through their opposition brief to assert piecemeal elements from a distinct doctrine developed and applied in Delaware Chancery courts. Plaintiffs' attempts fall short. Even if Delaware Law applied, it is equally unavailing because Delaware does not award fees absent actual or potential meritorious litigation. And while Plaintiffs insist that this Court craft its own exception to the American rule that each party bears its own litigation costs simply for the reason that the result is purportedly more "efficient," they do not and cannot cite a single case to support their position. Plaintiffs thus cannot sustain a cause of action on these flawed bases and their Complaint fails as matter of law to state a claim for which relief can be granted. Accordingly, Defendant respectfully requests that this Court dismiss the Complaint under Rule 12(b)(5) of the Nevada Rules of Civil Procedure.

II. BACKGROUND

On May 18, 2017, Plaintiffs served a written demand (the "Demand") on the Company's Board of Directors (the "Board"). Compl. ¶ 38. Their Demand raised purported issues with the voting instructions in two proxy statements. First, the Demand stated that the Board's April 28, 2015 Schedule 14A Proxy Statement invalidated shareholder approval of the increase in the number of authorized shares of common stock (the "Share Increase Amendment"). Compl. ¶¶ 26, 39. The Demand also stated that the voting instructions in the March 21, 2016 Schedule 14A Definitive Proxy Statement were flawed, allegedly invalidating the creation of a new class of preferred stock (the "Preferred Stock Amendment"). Compl. ¶¶ 9, 39. Specifically, Plaintiffs requested (a) that the approval of the Preferred Stock Amendment and the Share Increase Amendment be deemed ineffective, and that the ineffectiveness be publicly disclosed, and (b) that the Board seek stockholder approval of changes to Defendant's capital structure. Compl. ¶ 39.

Thereafter—but before any shares in connection with the Share Increase Amendment and the Preferred Stock Amendment were issued or committed to issue—Defendant rescinded the Preferred Stock Amendment and conducted new shareholder votes on both the Share Increase Amendment and the Preferred Amendments. Compl. ¶¶ 40-44. Defendant publicly disclosed all of these events. *Id.* On September 28, 2018, Plaintiffs sued for attorney's fees and expenses in connection with the alleged substantial benefit purportedly conferred by their Demand, *id*. ¶¶ 45-49, but they fail to allege that the purported "corrective actions" substantially benefited a single shareholder or the Company. The Company moved to dismiss the Complaint on November 13, 2018 and Plaintiffs filed their opposition on December 21, 2018.

III. ARGUMENT

A. Legal Standard

Rule 12(b)(5) of the Nevada Rules of Civil Procedure authorizes this Court to dismiss a

complaint where, as in this case, it fails to state a claim upon which relief can be granted. NRCP 12(b)(5). To survive dismissal, the complaint "must contain some 'set of facts, which, if true, would entitle [the plaintiff] to relief.'" *Weise v. Admin. Office of Courts*, No. 60148, 2013 WL 785098, at *1 (Nev. Feb. 28, 2013) (quoting *In re Amerco Deriv. Litig.*, 127 Nev. 196, 210, 252 P.3d 681, 692 (2011)). Although this Court must accept Plaintiffs' factual allegations as true when reviewing a motion to dismiss, the allegations must be "legally sufficient to constitute the elements of the claim asserted." *Sanchez ex rel. Sanchez v. Wal-Mart Stores, Inc.*, 125 Nev. 818, 823, 221 P.3d 1276, 1280 (2009). Where, as here, Plaintiffs fail to allege each of the essential elements of the claim, Defendant's motion to dismiss should be granted. *Dezzani v. Kern & Associates, Ltd.*, 134 Nev. Adv. Op. 9, 412 P.3d 56, 63 (2018) (affirming Rule 12(b)(5) dismissal where the complaint failed to allege one of the statutory elements); *Felden v. Shapiro*, 126 Nev. 766, 367 P.3d 831 (2010) (dismissing complaint for failure to allege several of the key elements entitling him to relief).

B. Plaintiffs Fail to Plead a Substantial Benefit to Support an Award for Attorney's Fees Under Nevada Law

Plaintiffs insist that they are entitled to attorney's fees under the substantial benefit doctrine based solely on their demand letter that allegedly caused the Board to take remedial actions. Compl. ¶ 4, n.1 (citing *Mills*, 396 U.S. at 396; *Thomas*, 122 Nev. at 84). But the Complaint remains fatally flawed because Plaintiffs cannot plead key elements of the doctrine: that a *substantial* benefit was conferred *through litigation*.

Nevada follows the American rule that a party cannot recover attorney's fees absent a statute, rule, or contract authorizing the award. *See Thomas v. City of N. Las Vegas*, 122 Nev. 82, 90, 127 P.3d 1057, 1063 (2006). Understanding this barrier to their claim, Plaintiffs try to invoke the substantial benefit doctrine, which is a judge-created exception that allows fee recovery "where a plaintiff has *successfully maintained a suit*, usually on behalf of a class, that benefits a group of

others in the same manner as himself." *Mills v. Electric Auto-Lite Co.*, 396 U.S. 375, 392 (1970) (allowing a shareholder to recover attorney's fees where the corporation received a substantial benefit from a derivative suit) (emphasis added). But contrary to Plaintiffs' attempt to avoid the legal requirements of the doctrine, Nevada law is clear—for this narrow exception to apply, "the prevailing party must show that the losing party has received a benefit *from the litigation*" and that "the class of beneficiaries is *before the court* in fact or in some representative form." *Thomas*, 122 Nev. at 90 (emphasis added).[1] Far from a formality, it is "*the court's jurisdiction over the subject matter of the suit [that] makes possible* an award that will operate to spread the costs proportionately.'" *Thomas*, 122 Nev. at 90-91 (quoting *Mills v. Electric Auto-Lite Co.*, 396 U.S. 375, 393-94 (1970)) (emphasis added).

Indeed, the Company has not found—and tellingly Plaintiffs have not cited—a single case in Nevada that has extended the substantial benefit doctrine outside the litigation context. *See, e.g.*, *Wagner v. City of N. Las Vegas*, No. 60482, 2013 WL 7155945, at *1 (Nev. Dec. 18, 2013) (concluding that the substantial benefit doctrine applied where plaintiff's lawsuit brought a benefit to all taxpayers in the municipality); *Guild, Hagen & Clark, Ltd. v. First Nat. Bank of Nevada*, 95 Nev. 621, 623, 600 P.2d 238, 240 (1979) ("The 'substantial benefit' doctrine applies when the

[1] Plaintiffs suggest that Defendant's reference to the litigation requirement is an "attempt[] to impose a new element" to the substantial benefit doctrine simply because it is not one of the three separately enumerated elements of the test. Pls. Opp. at 7. Not so. Under the substantial benefit doctrine as Plaintiffs state it, "*a successful party* must demonstrate that: (1) the class of beneficiaries is small in number and easily identifiable; (2) the benefit can be traced with some accuracy; and (3) the costs can be shifted with some exactitude to those benefiting." Pls. Opp. at 7-10 (citing *Thomas*, 122 Nev. 91) (emphasis added). Indeed, Nevada courts specifically discuss the litigation requirement. *See, e.g.*, *Thomas*, 122 Nev. at 91 (the court's jurisdiction over the benefit-conferring litigation makes the fee award possible); *Schulz Partners, LLC v. Zephyr Cove Prop. Owners Ass'n, Inc.*, Nos. 55006, 55557, 2011 WL 2652321, at *2 (Nev. July 5, 2011) (same). Moreover, Plaintiffs' narrow reading of the doctrine is impermissible. Under Plaintiffs' flawed interpretation, they would not need to even plead that a substantial benefit was conferred as it is not one of the three separately enumerated elements of the test. And importantly, Plaintiffs' self-serving interpretation of the doctrine fails to account for the required predicate of a "successful party."

defendant in a class action or corporate derivative suit receives some benefit as a result of the action."); *Cf. Schulz Partners, LLC v. Zephyr Cove Prop. Owners Ass'n, Inc.*, Nos. 55006, 55557, 2011 WL 2652321, at *2 (Nev. July 5, 2011) (denying party's request for attorney's fees under the substantial benefit doctrine because he was neither the successful nor prevailing party in the litigation). Plaintiffs attempt to distinguish these cases by stating that they merely "use the word 'litigation' for the unremarkable reason that the substantial benefit doctrine was invoked following litigation." Pls. Opp. at 12. What is remarkable is that Plaintiffs are *unable to cite to a single Nevada case* in which the substantial benefit doctrine was successfully invoked following a mere letter. *See id.*

Moreover, Plaintiffs themselves demonstrate that Nevada's statutory framework does not support an attorney's fee award following a mere demand letter. Pls. Opp. at 11. Nevada's statute governing derivative suits[2] expressly requires a shareholder demand on the corporation as a prerequisite for filing suit (or particularized allegations excusing demand), but does not provide for attorney's fees following the demand. NRCP 23.1 (requiring plaintiffs filing a shareholder derivative suit to "allege with particularity the efforts, if any, made by the plaintiff to obtain the action the plaintiff desires" from the corporation or reasons for "not making the effort").[3] Indeed,

[2] It is disingenuous for Plaintiffs to claim—for the first time in their opposition brief—that "the *underlying* claims are direct, not derivative." Pls. Opp. at 11 (emphasis added). This directly contradicts their Complaint and subsequent pleadings, which claim benefits to the *corporation. See id.* at 9 (The Demand purportedly prevented the "issuance of those shares [which] would ultimately threaten to unravel the Company altogether" and "[h]olders of the new stock and the old stock could have sued the Company for damages, and its creditors could attempt to declare defaults on outstanding loans."). But regardless of the nature of the underlying claim, Nevada's substantial benefit doctrine requires successful litigation, not merely a letter.

[3] Plaintiffs mistakenly try to represent that NRCP 23.1 does not impose a demand requirement, Pls. Opp. at 11 n.6, but this is contradicted by the very case Plaintiffs cite. *See id.* (citing *Schoen v. SAC Holding Corp.*, 122 Nev. 621, 633, 137 P.3d 1171, 1179 (2006) ("[B]ecause the power to manage the corporation's affairs resides in the board of directors, a shareholder must, before filing suit, make a demand on the board, or if necessary, on the other shareholders, to obtain the action that the shareholder desires. . . . [or plead] his reasons for not making a demand")). And importantly, while the Nevada legislature clearly contemplated a demand requirement, it declined to legislate a

even Nevada's general attorney's fee statute has also been uniformly interpreted to require litigation. Nev. Rev. Stat. 18.01(2) (in relevant part, the court may award attorney's fees where provided for by statute or agreement or to a "prevailing party" meeting certain requirements); *see also Thomas*, 122 Nev. at 93-94, ("This court has always interpreted [NRS 18.010(2)(a)] as requiring a money judgment as a prerequisite to recovering attorney fees"); *N. Nev. Homes, LLC v. GL Constr., Inc*., 134 Nev. Adv. Op. 60, 422 P.3d 1234, 1237 (2018) ("A party to an action cannot be considered a prevailing party within the contemplation of NRS 18.010, where the action has not proceeded to judgment.") (citation omitted). Plaintiffs do not dispute that they fail to meet the litigation requirement—they instead ask that this Court ignore it. But because their claim finds no support in Nevada case law or statutes, their Complaint must fail as a matter of law.

Nor do Plaintiffs adequately allege that they conferred a benefit on the corporation or shareholders that can sustain a claim for attorney's fees. Defs. Mot. to Dismiss at 3. Far from alleging any financial benefit or "fundamental" voting right, Plaintiffs allege that they prompted the Company to correct "irregularities" in proxy statement disclosures, Compl. ¶ 12, and then summarily conclude that they "directly conferred a fundamental and substantial benefit on the Company's stockholders." *Id*. at ¶¶ 46-47. However, it is wholly insufficient to label something a substantial benefit without any facts to support this conclusory statement. *See, e.g.*, *Thomas*, 122 Nev. at 91 n.18; *In re Amerco Deriv. Litig.*, 127 Nev. at 232 ("[C]onclusory allegations are not considered as expressly pleaded facts or factual inferences.") (citation omitted).[4] Indeed, in each of the cases Plaintiffs cite to support the alleged benefit, the Delaware courts awarded fees where

provision for attorney's fees. *See* NRCP 23.1.

[4] Moreover, Plaintiffs misrepresent *In re Cheniere Energy, Inc.* as a case in which the court awarded fees. C.A. No. 9710, p. 104 (Del. Ch. Mar. 16, 2015) (TRANSCRIPT) (Pls. Opp. Exhibit 2). To the contrary, the court merely approved the parties' *settlement* that included fees and dismissed the entire underlying action with prejudice. Trial Order, *In re Cheniere Energy, Inc.*, Nos. 9766-VCL, 9710-VCL, 2015 WL 1206722, at *2 (Del. Ch. Mar. 16, 2015).

the stockholder created a quantifiable financial benefit, restored a fundamental shareholder right, or identified a breach of fiduciary duty. *See* Pls. Opp. at 8-10 (citing *In re Sauer-Danfoss Inc. S'holders Litig.*, 65 A.3d 1116, 1136-37 (Del. Ch. 2011) (rejecting claim for fees for 10 out of 11 corrective disclosures, awarding fees only for correction of false tender offer pricing); *EMAK Worldwide, Inc. v. Kurz*, 50 A.3d 429, 434 (fees awarded for "sizeable" benefit where litigation "was a strong challenge brought to a transaction where there was . . . real evidence of loyalty breaches"); *San Antonio Fire & Police Pension Fund v. Bradbury*, C.A. No. 4446-VCN, 2010 WL 4273171, at *8 (Del. Ch. Oct. 28, 2010) (corporation benefited where litigation caused removed barriers to shareholder's "fundamental" right to elect the board of directors).

Perhaps recognizing their paltry allegations, Plaintiffs make speculative assertions for the first time in their opposition that they protected shareholder voting rights, Pls. Opp. at 10, and if not for their efforts, the "capital structure would have become highly destabilized" and "the issuance of those shares would threaten to unravel the Company", exposing the Company to lawsuits and defaults on loans. Pls. Opp. at 8. However, not only are these new assertions wholly speculative and conclusory, Plaintiffs cannot rely on purported "benefits" articulated in their opposition brief because they cannot amend their Complaint except "by leave of court or by written consent of the adverse party." NRCP 15(a); *see also, e.g.*, *Ramani v. Chabad of S. Nev., Inc.*, No. 49341, 2011 WL 3298395, at *2 (Nev. July 29, 2011); *Woodbury Law, Ltd. v. Bank of America*, No. 2:15–CV–603 JCM (GWF), 2015 WL 3994956, at *3 (D. Nev. July 1, 2015) (declining to consider new pleadings in opposition brief because "[i]t is axiomatic that the complaint may not be amended by briefs in opposition to a motion to dismiss") (internal alterations and citation omitted). These allegations should thus be disregarded.

C. Delaware Also Prohibits Attorney's Fee Award Without an Underlying Meritorious Legal Claim.

Plaintiffs attempt to rescue their legally deficient Complaint by improperly amending it through their opposition brief to apparently rely on the corporate benefit doctrine under Delaware Law, instead of Nevada's substantial benefit doctrine as pled in their Complaint. Pls. Opp. at 14. This maneuver must fail because it is both procedurally impermissible and substantively unavailing.

First, Plaintiffs cannot amend their Complaint through subsequent pleadings. *See supra* at III.B. Plaintiffs invite this court to look to Delaware law, where courts have developed the corporate benefit doctrine—a test entirely different from the substantial benefit test advanced in Plaintiffs' Complaint and applied in Nevada.[5] This newly and improperly articulated claim cannot replace the inadequate allegations in the Complaint, and the Court should reject these revisions.[6]

Second, Plaintiffs grossly misrepresent the "policy" underlying Delaware's corporate benefit doctrine. Pls. Opp. at 14. In both cases Plaintiffs cite to support their assertion that Delaware policy justifies an attorney's fee award in Nevada, the Delaware Chancery *declined* to award attorney's fees and dismissed the stockholder's claims because the stockholders neither filed suit nor presented meritorious legal claims of director liability.[7] *See Bird v. Lida*, 681 A.2d 399

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[5] Nevada's substantial benefit doctrine, as pled in Plaintiffs' Complaint, requires "a successful party [to] demonstrate that: (1) the class of beneficiaries is small in number and easily identifiable; (2) the benefit can be traced with some accuracy; and (3) the costs can be shifted with some exactitude to those benefiting." Pls. Opp. at 7-10 (citing *Thomas*, 122 Nev. 91); *see also* Compl. ¶ 4 n.1. Contrast this test to Delaware's corporate benefit doctrine, which requires that: "(i) the underlying cause of action was meritorious when filed; (ii) the action producing benefit to the corporation was taken by the defendants before a judicial resolution was achieved; and (iii) the resulting corporate benefit was causally related to the lawsuit." *Raul v. Astoria Fin. Corp.*, 2014 WL 2795312, at *5 (Del. Ch. June 20, 2014) (internal alterations and citation omitted).

[6] Nonetheless, the Company addresses these improperly articulated claims here though they are equally unavailing.

[7] Although certain Delaware Chancery decisions have suggested that a plaintiff may recover attorney's fees under the corporate benefit doctrine even when remedial action moots a potentially meritorious legal claim, the plaintiff must plead elements distinct from those required under the

(Del. Ch. 1996); *Raul v. Astoria Fin. Corp.*, 2014 WL 2795312 (Del. Ch. June 20, 2014). In *Bird*, the stockholder sued the company for fees following a demand that allegedly caused defendant to take remedial action, creating value for the company. The court discussed in dicta that shareholder monitoring of a corporation can in some instances be valuable and efficient, even if a lawsuit was never filed. *Bird*, 681 A.2d at 407. However, the court set aside this academic discussion because, to reward a demand without a meritorious claim of legal wrong, i.e., a breach of fiduciary duty, would impermissibly "move courts from their traditional mission, including the settlement of disputed legal questions . . . to a rather different administrative task: the ex post pricing of 'volunteer' informational services to corporations." *Id.* at 407. The court accordingly dismissed the stockholder's claim for attorney's fees.

The Delaware Chancery was likewise unwilling to award attorney's fees for a mere correction to a proxy statement in *Raul v. Astoria*, where the defendant company amended its charter as requested by a stockholder's demand that the company correct a perceived violation of Section 14A of the Exchange Act. 2014 WL 2795312, at *4. In dismissing the complaint, the court reasoned that directors may, *in their discretion*, award volunteers for creating value for the corporation through a demand letter that presents a meritorious legal claim and causes the board to take corrective action. *Id.* at *7. But because it is the board—not the shareholders or the courts—that is charged with the management of the corporation under Delaware Law, the court would not require payment of such fees. *Id.* The court explained: "general allocation of the costs incurred by good Samaritans untethered to a meritorious (actual or potential) cause of action would drastically expand the jurisdiction of this Court, and usurp a core function of the board of directors." *Id.* at *6.

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substantial benefit doctrine, including in relevant part that the demand presented a *meritorious* claim of legal wrongdoing by the company's board. *Raul*, 2014 WL 2795312, *5. To be meritorious, the claim must be capable of surviving a motion to dismiss. *Id.* at *1.

Accordingly, awarding attorney's fees in the absence of a meritorious lawsuit "may appear efficient, or 'fair,' but *this Court is not a general enforcer of either of those qualities outside the context of litigation within its purview.*" *Id.* (emphasis added). Indeed, the requirement of a meritorious claim of legal wrongdoing "acts as a break on purely opportunistic behavior. Rational shareholders will weigh expected investigation costs against the possibility of recovery under the relevant legal standard." *Bird*, 681 A.2d at 405.

Therefore, even if this Court decides to take the extraordinary step of considering Delaware policy, Plaintiffs' claim still fails. In Nevada, as in Delaware, a corporation's "board of directors has full control over the affairs of the corporation." NRS 78.120(a).[8] Thus, the Court should not usurp the Board's decision making authority nor set aside the established legal precedent in Nevada merely because it may be more "efficient" for fee-seeking shareholders. *See Bird,* 681 A.2d at 405.

Nor can Plaintiffs distance themselves from the recent case from the Eastern District of Michigan because, as in Nevada, the common law substantial benefit doctrine in Michigan provide no basis for an attorney's fee award outside of litigation. Plaintiffs contend that the *Willner v. Syntel* decision was "predicated" on Michigan statues that differ from Nevada's. Pls. Opp. at 13. Not so. First, the court found that the statutory framework "contemplate[s] that shareholders may serve demand letters on corporations . . . but the statutes do not authorize an award of attorney fees for a benefit that results from a demand letter." 256 F. Supp. 3d 684, 693 (E.D. Mich. 2017) (interpreting Mi. St. 450.1493a, which provides for initiation of a derivative suit). Likewise, the

[8] Plaintiffs cite an inapposite, non-binding settlement transcript outside Nevada's jurisdiction rather than any decision or order on the merits. *See* Pls. Opp. at Ex. 1, Hearing Transcript, *In re Galena Biopharma, Inc.*, C. A. No. 2017-0423-JTLP (Del. Ch. 2017). They warn that "[a]warding counsel in *Galena* $250,000 and counsel here $0 would promote a rule that incentivizes litigation for its own sake." Pls. Opp. at 16. Even if Plaintiffs were eligible for an attorney's fee award on the basis of a mere letter—which they are not—requesting an award equal to that of the *Galena* plaintiff would be wildly disproportionate. In *Galena*, plaintiff expended the risks and costs of drafting and filing a verified class action complaint and conducting expedited discovery, compared to the Plaintiffs in this case, who merely wrote a letter.

Nevada legislature clearly contemplated a demand requirement but declined to provide for attorney's fees at all. *See* NRCP 23.1.[9] While this ground alone would have been sufficient for the court to decline to award attorney's fees, the court was *separately persuaded* by the common law, where the court found that because it could not find any cases in the state holding or even suggesting that the doctrine applied outside of the litigation context, it would decline to apply the doctrine to benefits conferred without litigation. *Id.* at 693. Like Nevada's substantial benefit doctrine, *Willner*'s well-reasoned analysis is grounded in the interpretation of the substantial benefit doctrine articulated in *Mills*[10] applied to strongly analogous facts. Defendant again respectfully submits that this Court should use the *Willner* decision as a roadmap for confirming here that the extension of the substantial benefit doctrine outside the litigation context is not permitted under Nevada law.

Citing *Raul*, the court in *Willner* noted that the Delaware Chancery court has *suggested* a plaintiff *may* be able to recover attorney's fees based on a benefit conferred through a demand letter—though noting the Delaware Supreme Court has never adopted this rule. *Willner*, 256 F. Supp. 3d at 688, 690 n.4. However, the *Willner* court rejected the plaintiff's invitation to apply the Delaware Chancery court's interpretation because (i) Michigan statutory law is not silent on the issue, but in fact requires litigation, and (ii) Michigan common law is inconsistent with the common law of the Delaware Chancery court. *Id.* at 688. Any invitation for this Nevada court to apply

[9] Although Michigan's derivative suit statute, Mich. Comp. Laws § 450.1493a, does not explicitly provide that plaintiffs can avoid the demand requirement by pleading demand futility, Michigan courts have interpreted the statute to include such an exception. *See, e.g.*, *Cyborowski v. Ennest*, No. 08–13736–BC, 2009 WL 1658181, *3 (E.D. Mich. June 11, 2009) ("Before proceeding, a shareholder must demand in writing the corporation enforce its rights or demonstrate such a request would be futile.") (citing *Thomas v. Costa*, No. 235031, 2003 WL 460222, *11 (Mich. Ct. App. Feb.21, 2003)).

[10] Plaintiffs also pluck out of context the statement that Michigan law is "not consistent with the federal rule." Pls. Opp. at 13. In fact, the court states that Michigan law differs from the federal rule only with respect to the discrete issue of whether it can assess fees against shareholders as well as the corporation, 256 F. Supp. 3d at 695, a matter which Plaintiffs have not pled here.

Plaintiffs' misguided interpretation of Delaware Chancery rulings should be rejected for the same reasons.

Accordingly, Plaintiffs fail to plead any facts, even if all are taken as true, entitling them to relief under the substantial benefit doctrine because they did not confer a substantial benefit to the Company through litigation. Instead, they seek fees based solely on a demand letter and alleged corrective action taken without any harm to the Company's shareholders. This is plainly insufficient, and the Complaint should accordingly be dismissed with prejudice.

IV. CONCLUSION

Given Plaintiffs' inability to plead any facts supporting essential elements of their claim for attorney's fees under the substantial benefit doctrine—namely, the requisite substantial benefit conferred through litigation—their Complaint fails as a matter of law to state a claim for relief. Because there was no lawsuit conferring the alleged benefit, there is no set of facts under which Plaintiffs can recover their fees here, and Defendant asks that this court dismiss the action against it with prejudice.

Dated: January 7, 2019

By: */s/Jeffrey F. Barr, Esq.*

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Attorneys for Defendant

CERTIFICATE OF SERVICE

I hereby certify that on the 7th day of January, 2019, I served a true and correct copy of REPLY IN SUPPORT OF Defendant Digital Ally, Inc.'s MOTION TO DISMISS PURSUANT TO NRCP 12(b)(5) as follows:

_X_ By electronic case filing and service through the Court's e-filing service (Odyssey)

___ By U.S. mail, first class postage prepaid to the address below

___ By electronic mail to the e-mail address(es) listed below

John P. Aldrich, Esq.
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Attorneys for Defendants

/s/ *Michelle T. Harrell*
An Employee of Ashcraft & Barr | LLP

TRAN

DISTRICT COURT
CLARK COUNTY, NEVADA
* * * * *

CHARLES JESSEPH, et al.	.	
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Plaintiffs	.	CASE NO. A-18-781874-B
	.	
vs.	.	
	.	DEPT. NO. XI
DIGITAL ALLY	.	
	.	**Transcript of**
Defendant	.	**Proceedings**
. . . . .	.	

BEFORE THE HONORABLE ELIZABETH GONZALEZ, DISTRICT COURT JUDGE

HEARING ON DEFENDANT'S MOTION TO DISMISS COMPLAINT

MONDAY, JANUARY 14, 2019

APPEARANCES:

FOR THE PLAINTIFFS:	JOHN P. ALDRICH, ESQ. DOUGLAS JULIE, ESQ.
FOR THE DEFENDANTS:	JEFFREY F. BARR, ESQ. DAVID H. KISTENBROKER, ESQ.
COURT RECORDER:	TRANSCRIPTION BY:
JILL HAWKINS District Court	FLORENCE HOYT Las Vegas, Nevada 89146

Proceedings recorded by audio-visual recording, transcript produced by transcription service.

LAS VEGAS, NEVADA, MONDAY, JANUARY 14, 2019, 10:38 A.M.

(Court was called to order)

THE COURT: Jesseph versus Ally. Can I go to the motion to associate counsel first.

MR. ALDRICH: 'Morning, Your Honor. John Aldrich on behalf of plaintiffs. With me is Doug Julie, as well.

MR. JULIE: Good morning, Your Honor.

MR. BARR: Good morning, Your Honor. Jeff Barr on behalf of defendant, Digital Ally. With me is pro hac David Kistenbroker.

MR. KISTENBROKER: Good morning, Your Honor.

THE COURT: Okay. Any objection to the pro hac motion and motion to associate?

MR. ALDRICH: No.

THE COURT: Do you agree that you will submit to the jurisdiction of this Court and appear without subpoena for any proceeding required by the Court which relates to the counsel's conduct in this matter, including motions, depositions, and evidentiary hearings?

MR. BARR: Respectfully, Your Honor, the order for Mr. Kistenbroker has already been entered. I think it's Mr. Julie.

THE COURT: Do you agree to that?

MR. JULIE: I do, Your Honor.

THE COURT: If you're bad we're going to have a

hearing, and you have to come.

MR. JULIE: I will come.

THE COURT: Okay. So --

MR. JULIE: I won't be bad. Let's start with that.

THE COURT: So now I'm up to your -- that, too. Okay.

So now we're up to the motion on substantial benefit. And I actually pulled an old case that I had done and read the Supreme Court's ODA to see what they had thought about it, but it wasn't published, so it doesn't help anybody.

MR. BARR: Was that the Wagner case?

THE COURT: Huh?

MR. BARR: The Wagner. I litigated that, Your Honor.

THE COURT: Yeah, it was that case. That was that North Las Vegas City Council [unintelligible].

MR. BARR: Yes.

THE COURT: That one.

MR. BARR: One vote, one fraudulent.

THE COURT: Okay. You're up.

MR. KISTENBROKER: Your Honor, it is our motion. I guess posturewise to dismiss the request for attorneys' fees that Mr. Julie has filed. I won't repeat the items in our brief. I think this is a case of first impression for the Court in --

THE COURT: I believe it is, in Nevada.

MR. KISTENBROKER: -- Nevada. And so the real question is the substantial benefit doctrine has three elements, and the threshold question is should it be applied in this state in a circumstance without litigation having been filed, based only upon the demand letter that was written on behalf of Mr. Julie's clients; and, secondarily, I think when you get into the element itself is it essential, as we argue it is, that the class be represented in some capacity before the Court. Which I don't see how that could ever happen in this case. There are two shareholders that have been brought forth. The Mills case from the United States Supreme Court sort of articulated the doctrine, and it has always been applied with litigation being the predicate. I will say that Counsel has attached a couple of Vice Chancellor Raster's settlement conference transcripts. I think it's important to point out, since they argue that Delaware law should be persuasive to the Court, that in Delaware the Delaware Supreme Court has not addressed nor adopted to so-called mootness settlement, substantial benefit doctrine to be applied to a demand letter only without litigation.

We cite the Court to a very recent Michigan federal case where they looked at this request and determined that the doctrine should not be applied when it has a demand letter written.

I think I'll just stop right there so I don't repeat what's in the brief. I know Your Honor has read it.

THE COURT: Thank you.

MR. JULIE: Good morning, Your Honor. And I first should say we tried to work this out before filing suit, and we never heard back from defendants notwithstanding probably half a dozen phone calls or emails.

You know, on the surface this seems like a small matter about an attorney's fee application. But it actually is a very important case that may ultimately go to [unintelligible] courts. You know, I don't think anyone here should be naive about, you know, what a negative result here would be, what a dismissal would lead to. If special shareholder attorneys can't get paid presenting a demand, they're not going to send a demand. And so --

THE COURT: Oh, yeah, they are, because they want to do the injunctive relief hearing afterwards.

MR. JULIE: Well, but there's --

THE COURT: If the demand isn't -- that's why we have demand, is so that the corporation has a chance to make some changes before we start the litigation.

MR. JULIE: In a case like this demand wouldn't be required at all. First of all, it's not a derivative case. Whether shareholders have -- were tricked in how they voted or whether the statute was -- whether the vote in question was

correctly tabulated doesn't present a corporate claim, it presents a claim that shareholders can assert directly. Even if it was a derivative claim, this -- you know, the second prong of the demand futility test would excuse any demand here. The question is -- you know, under that test is whether there's reason to doubt that the challenged corporate conduct is a -- you know, is a fair exercise of business judgment. Ignoring a vote is something that you would never have to -- that could never be a fair exercise of business judgment.

So as a practical matter we wouldn't send a demand; right? If this case cropped up again, I -- you know, given this litigation, I would sue and I would very likely, I think overwhelmingly likely survive any motion to dismiss or more likely be mooted before it ever got to -- before it ever got to court.

I agree that there's no Nevada decision that specifically speaks to whether a demand is required.

THE COURT: All of the Nevada decisions reflect litigation as being part of the substantial benefit doctrine.

MR. JULIE: All of the Nevada decisions --

THE COURT: All two of them.

MR. JULIE: -- yes, reflect -- Your Honor, they reflect that the applications were made in the context of litigation.

THE COURT: Well, and that the substantial benefit

doctrine under the common law was extended from a litigation standpoint because of the benefit that was provided. And then the Wagner case that we talk about, that was a voter's right, as opposed to a corporation. But it was a litigation when the Nevada Supreme Court extended it. And it's not a published decision, so it's not technically able to be cited.

MR. JULIE: The fact that it's only come up before in the litigation context I think is a poor reason to say that it doesn't apply outside the litigation context. Delaware law, which the Nevada Supreme Court routinely looks to for the specific purpose of coming up with the rules of the road for shareholder litigation, certainly -- there's certainly the cases we cite that recognize it. The American Law Institute Principle -- and it's not in our papers, because I was just reading it this week -- 7.17 also says that you should get paid following a demand. So I think the fact that the prior cases just haven't addressed the issue doesn't answer the issue.

If Your Honor had written a decision in a union substantial benefit case that said that parties can only get -- you know, the successful party can get paid if they meet elements X, Y, and Z, I don't think Your Honor -- well, I don't want to speak for Your Honor, but I don't think another, you know, judge in that circumstance would expect that anyone else would look at that and say, well, what the court said

there necessarily applies to, you know, the demand case. The court deciding that union case is not thinking about, you know, whether a shareholder demand is at issue. None of the four Nevada Supreme Court cases that have been cited, particularly Thomas and Wagner, none of them come up in the corporate context.

So to start saying that those cases speak to the -- you know, how far the substantial benefit doctrine should go in corporate cases, I think, you know, overreads those cases and asks those courts when they're deciding those cases to do too much. Judges tend to decide cases that are in front of them, and particularly when there isn't, you know, even dicta saying, you know, and you shouldn't get paid for a demand. I don't think those cases should be overread. I think the Michigan case that defendants rely on really should be dismissed. Michigan --

THE COURT: They have a special statutory framework there.

MR. JULIE: They have a statutory framework, and --

THE COURT: Right. I'm not worried about that. I'm looking at the Nevada common law, is what I'm concerned about.

MR. JULIE: Okay. And so can I skip the Nevada statutes that they've raised, as well?

THE COURT: Because the substantial benefit doctrine is a common law doctrine. It is not a statutory principle.

MR. JULIE: That's right. And so I think that once you get outside the reasoning that's in the Michigan statutory case, you know, the best source that the Court has to look at, and it's obviously not binding, is what Delaware is doing, particularly given the unique role that Delaware law has played in shaping Nevada law. The Court's obviously very familiar with the policy arguments made in our papers, and I don't want to -- I don't want to repeat those.

If I could just -- actually, unless the Court has any other questions --

THE COURT: I don't have any more. Thank you.

You're up.

MR. KISTENBROKER: Your Honor, the only thing I would add is the Thomas case is a reported case, and Your Honor has reviewed it. It's in the context of litigation, and it expressly states that the class of beneficiaries is before the Court, which would appear to be an essential, I think, in the common law of Nevada. I have nothing further.

THE COURT: Thank you.

MR. JULIE: Your Honor, if I could just speak to that one class of beneficiaries issue. What the Court in Thomas said concerning class of beneficiaries is that the element at issue there is the Court wanted to make sure the there was some mechanism with which to spread the fees. And so that's what that language in Thomas is getting at. And the

court said, well, if you had sued the union, then we would have the right class of beneficiaries, instead you sued the taxpayers and you've missed, because not all of the beneficiaries, you know, benefitted there. Certainly in the derivative context you would never have all of the shareholders in front of the Court, because it's not a class action.

THE COURT: Thank you.

In Nevada the substantial benefit doctrine is limited to litigation matters, at least in the currently decided cases. For that reason I'm going to go ahead and grant the motion. Thank you. Good luck on your appeals.

MR. KISTENBROKER: Thank you, Your Honor.

THE PROCEEDINGS CONCLUDED AT 10:49 A.M.

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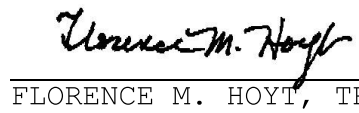
CERTIFICATION

I CERTIFY THAT THE FOREGOING IS A CORRECT TRANSCRIPT FROM THE AUDIO-VISUAL RECORDING OF THE PROCEEDINGS IN THE ABOVE-ENTITLED MATTER.

AFFIRMATION

I AFFIRM THAT THIS TRANSCRIPT DOES NOT CONTAIN THE SOCIAL SECURITY OR TAX IDENTIFICATION NUMBER OF ANY PERSON OR ENTITY.

FLORENCE HOYT
Las Vegas, Nevada 89146



FLORENCE M. HOYT, TRANSCRIBER

2/6/19

DATE