EFiled: Aug 20 2010 5:13PM EDT
Transaction ID 32791454
Case No. 3940-VCN

IN THE COURT OF CHANCERY OF THE STATE OF DELAWARE

SHELDON DUBROFF and MERVYN KLEIN on behalf of themselves and all others similarly situated,	:	
Plaintiffs,	:	
v.	:	**C.A. No. 3940-VCN**
WREN HOLDINGS, LLC, JAVVA PARTNERS, LLC, CAMERON FAMILY PARTNERSHIP, L.P., CATALYST INVESTORS, L.P., CHRISTOPHER SHIPMAN, ANDREW T. DWYER, DORT A. CAMERON, III, HOWARD KATZ, TROY SNYDER and NINE SYSTEMS CORPORATION,	:	
Defendants.	:	

MEMORANDUM OPINION

Date Submitted: May 4, 2010
Date Decided: August 20, 2010

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William P. Bowden, Esquire, Richard D. Heins, Esquire, Andrew D. Cordo, Esquire, and Peter Faben, Esquire of Ashby & Geddes, Wilmington, Delaware, Attorneys for Defendants, and Richard G. Haddad, Esquire and Stanley L. Lane, Jr., Esquire of Otterbourg, Steindler, Houston & Rosen, P.C., New York, New York, Attorneys for Defendants Wren Holdings, LLC, Cameron Family Partnership, L.P., Dort A. Cameron, III, Howard Katz, and Troy Snyder.

NOBLE, Vice Chancellor

I. INTRODUCTION

Plaintiffs, former minority shareholders, seek class certification for this action which has only one remaining claim—one alleging inadequate disclosure of a corporate action approved by written consent of less than all of the shareholders under 8 *Del. C.* § 228. The defendants assert that class certification should be denied for many reasons, ranging from the absence of numerosity, to the inadequacy of the plaintiffs as class representatives. Although most of the requirements of Court of Chancery Rule 23 are satisfied—even if only marginally—the nature of the remaining disclosure claim precludes certification. Because no shareholder approval was sought through the challenged disclosure, Delaware requires that reliance and causation be alleged and proven. The highly individualized nature of these elements demonstrates that the potential class members do not share common claims.

II. BACKGROUND

A. *Parties*

Plaintiffs Sheldon Dubroff and Mervyn Klein are former shareholders of Defendant Nine Systems Corporation ("Nine Systems" or the "Company"), a now-privately held Delaware corporation that was once known as Streaming Media Corporation. They purport to bring this action on behalf of themselves and other

similarly situated former shareholders. They are represented by The Rosen Law Firm, P.A. (the "Rosen Firm"), which aspires to be class counsel.

Defendants Wren Holdings, LLC ("Wren"), Cameron Family Partnership, L.P. ("CFP"), and Catalyst Investors, L.P. ("Catalyst") were Nine Systems shareholders and debtholders (collectively, the "Entity Defendants"). Defendant Dort A. Cameron, III, a former member of the Company's board (the "Board"), is the managing member and principal owner of CFP and a 50% owner of Wren.[1] Defendant Howard Katz is the sole equity owner of now-dismissed Defendant Javva Partners, LLC ("Javva") and was also a member of the Board. Defendant Christopher Shipman is the managing partner of Catalyst and is also a former member of the Board. Defendant Troy Snyder is, and at all relevant times was, the Company's President, Chief Executive Officer, and a member of the Board.

B. *The Recapitalization*

The Plaintiffs' remaining claim relates to an August 2002 recapitalization transaction (the "Recapitalization") that allowed the Entity Defendants to convert preferred debt of Nine Systems that each held into preferred stock, resulting in an increase in their collective equity holdings from 56% of the Company's stock to nearly 80%, thereby diluting the minority shareholders' equity from approximately 44% to 22%. The Board—including the interested directors—voted in favor of the

[1] The other 50% is owned by now-dismissed Defendant Andrew T. Dwyer.

Recapitalization, which then was approved by written consents executed by the Entity Defendants pursuant to 8 *Del. C.* § 228. In accordance with the statutory requirement for shareholder action by written consent, Nine Systems thereafter sent a notice to the minority shareholders disclosing that an exchange of subordinated debt for preferred shares had occurred, along with a 1-for-20 reverse stock split. The notice did not disclose the identity of the debt holders, their connections to the Board, or the price at which the debt was exchanged.[2] Not until November 2006, upon receiving a proxy statement in connection with a proposed acquisition of the Company by Akamai Technologies ("Akamai") that listed the Company's shareholders and the number of shares that each possessed, did the minority shareholders discover that the Entity Defendants had materially increased their equity interest in the Company by way of the Recapitalization.

C. *Procedural History*

In February 2007, the Plaintiffs filed suit in California for claims related to the Recapitalization. In September 2007, that action was dismissed for lack of personal jurisdiction and on forum non conveniens grounds. In October 2007, the Plaintiffs re-filed their complaint in New York but thereafter moved to have it voluntarily dismissed in order to permit suit to be re-filed in Delaware; Plaintiffs were assessed $30,000 for Defendants' attorneys' fees. A separate New York

[2] For more complete background on the Recapitalization and the underlying disclosure claim, see *Dubroff v. Wren Holdings, LLC*, 2009 WL 1478697, at *1 (Del. Ch. May 22, 2009).

action was brought by Morris Friedman and sixty-eight of Nine Systems' other former shareholders (the "Friedman Action") shortly after the Plaintiffs filed in California. The Friedman Action was eventually settled and, as part of the settlement, the shareholders agreed to the dismissal of their claims with prejudice, and all but three of the individual plaintiffs (along with four other former shareholders who had connections to the Friedman Action plaintiffs but who were not parties to the suit) signed a written general release that also specifically provided that each would not be a class member in this action.[3] This action was filed in August 2008. By a May 22, 2009, Memorandum Opinion and Order,[4] the Court dismissed the Plaintiffs' claims, but for their claim for breach of fiduciary duty of disclosure. Plaintiffs now seek certification of a class action as the platform for resolving the disclosure claim.

D. *Class Certification*

> The Plaintiffs propose a plaintiff class to be defined as:
>
> > All persons who owned the common stock and Series A preferred stock of the Company as of the date of the initiation of the Self-Dealing Transactions, which is believed to be August 1, 2002 (the "Class").

[3] Transmittal Affidavit of Andrew D. Cordo, Esq. Submitted in Connection with the Defs.' Answering Br. in Opp'n to Pls.' Mot. for Class Certification, Appointment of Class Representatives and Appointment of Class Counsel ("Cordo Aff.") Exs. I & J.

[4] *See supra* note 2.

Excluded from the Class are the Defendants, the current and former officers and directors of Nine Systems, their affiliates, and related individuals and entities.[5]

E. *Defendants' Opposition to Class Certification*

The Defendants argue class certification is inappropriate because the requirements of Court of Chancery Rule 23(a) have not been met: the Class is not sufficiently numerous; individual issues of law and fact preclude commonality; the Plaintiffs' claims are not typical of those of the Class; and the Plaintiffs have not demonstrated by their actions that they are willing or able to adequately and fairly protect the interests of the Class at large; the Defendants also assert that there are no grounds to certify a class under Rule 23(b). In addition, the Defendants oppose the designation of the Rosen Firm as class counsel.

III. RULE 23(a) STANDARDS

In order to obtain class certification, the Plaintiffs must satisfy the criteria of Court of Chancery Rule 23(a):

> (1) the class is so numerous that joinder of all members is impracticable, (2) there are questions of law or fact common to the class, (3) the claims or defenses of the representative parties are typical of the claims or defenses of the class, and (4) the representative parties will fairly and adequately protect the interests of the class.[6]

[5] Compl. ¶ 40.
[6] Ct. Ch. R. 23(a).

The first two prerequisites focus on the characteristics of the proposed class, while the latter two prerequisites focus on the characteristics of the proposed class representatives.[7] Each element of Rule 23(a) will be discussed seriatim.

A. *Numerosity*

The Defendants challenge nearly all of the "approximately 125-130 potential class members"[8] put forward by the Plaintiffs on grounds including release, consent, and knowledge of and/or participation in the Recapitalization. Should the Class be reduced to the handful of former Nine Systems shareholders that have not been contested by Defendants, the Class clearly would not be sufficiently numerous to make joinder of eligible plaintiffs impracticable under Rule 23(a)(1). Moreover, even if the Court determines that only those shareholders who released their claims with the termination of the Friedman Action should be excluded—a majority of the proposed class—the remaining potential class members would be fewer in number than the number of plaintiffs who individually participated in the Friedman Action. Accordingly, the Defendants suggest that joinder of those remaining would, likewise, not be impracticable. The Plaintiffs counter that there is insufficient evidence to dismiss at this stage any of the groups to which the Defendants object.

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[7] *Leon N. Weiner & Assocs., Inc. v. Krapf*, 584 A.2d 1220, 1225 (Del. 1991).

[8] Pls.' Opening Br. in Support of Mot. for Class Certification, Appointment of Class Representatives, and Appointment of Class Counsel at 2. This number is down from the "approximately 175 members" alleged in the Complaint. Compl. ¶ 43.

1. The Friedman Action Plaintiffs

The Defendants argue that the proposed class members who signed releases or were otherwise affected by the dismissal with prejudice of the Friedman Action are prohibited from being included as part of the Class as a result of this release and should not be counted when considering whether the numerosity requirement is met. The Plaintiffs respond that these releases will ultimately prove to be ineffective as an affirmative defense and that it would be an abuse of discretion for this Court to exclude any potential class member from the putative class on grounds of release at this stage because the Defendants have not yet provided any "admissible, authenticated, non-hearsay evidence" that each of the releases was properly obtained, *i.e.*, with consideration, under proper guidance by counsel, and not under coercion.

Nevertheless, all available evidence suggests that these potential class members should be excluded from the Class.[9] Moreover, outstanding questions of release would seem to raise additional questions with respect to commonality and typicality since those potential class members who signed releases or otherwise had their claims dismissed with prejudice would appear to face distinct legal and

[9] *See, e.g.*, Cordo Aff. Exs. I & J. The circumstances in this case are very different than those the Court faced in *Turner v. Bernstein*, 768 A.2d 24 (Del. Ch. 2000), where the plaintiffs signed away their rights "based on an unsupervised, potentially one-sided presentation of the facts made in advance of their receipt of any court-approved notice." *Id.* at 27. Here, the releases were apparently signed under the advice of counsel in connection with that action's final settlement and were the product of intense negotiations and delivered in exchange for substantial consideration. In addition, the dismissal with prejudice was overseen by the courts of New York.

factual issues not faced by the Class as a whole or by the Plaintiffs. As such, the Court will not count the seventy-three potential class members whose claims were dismissed with prejudice and/or separately released in connection with the settlement and discontinuance of the New York action when considering whether the proposed class is sufficiently numerous.

Disqualifying those former shareholders would leave a potential class of no more than fifty-seven—twelve fewer than the number of shareholders who joined as individually named plaintiffs in the Friedman Action. The Defendants contend that the fact that the Friedman Action—which was based on the same underlying facts and same offending transactions as this one and included not only the disclosure claim remaining in this action but also the additional claims that were previously dismissed—was managed to conclusion with sixty-nine individual plaintiffs participating shows that joinder of the remaining class members in this case would not be impracticable.

2. Other Challenged Plaintiff Groups

The Defendants also raise issue with other potential class members who allegedly consented to, or participated in, the Recapitalization, or else had direct connections to certain Nine Systems directors and, the Defendants contend, thereby knew or had access to additional information that would have undone any

harm from the allegedly insufficient disclosure.[10] They assert that after subtracting out all of the former shareholders who should be disqualified for one of various reasons the Class would have fewer than ten eligible members, a number far too small to satisfy Rule 23(a)(1).

Specifically, the Defendants argue that more than forty potential class members should be disqualified on the ground that their investments in Nine Systems were solicited by Abraham Biderman or through Lipper & Company, where Biderman worked as Chief Financial Officer (the "Biderman Plaintiffs").[11] Defendants assert that this granted those holders a "designee on Nine Systems' Board" in Biderman, and that this "pipeline to their own Board representative" should disqualify any claim based on inadequate disclosures by the Board, since they did or could have received the undisclosed information from Biderman.[12] Moreover, the Defendants suggest that, as Manager for Streaming Media Investment Group, LLC—the entity through which the Biderman Plaintiffs bought their Nine Systems stock, Biderman may have owed distinct fiduciary duties to

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[10] This group would include former Defendant Javva and former director Abraham Biderman, who has not been named as a defendant but who voted to approve the Recapitalization resolutions, both of whom are included in the shareholder list submitted by Plaintiffs. Transmittal Declaration of Brian D. Long in Support of Pls.' Mot. for Class Certification, Appointment of Class Representatives, and Appointment of Class Counsel Ex. 3.

[11] It is perhaps worth emphasizing that Nine Systems was not a publicly traded corporation, which meant that its stockholders acquired their interests from private sources and none received her shares, so to speak, in the market.

[12] Defs.' Answering Br. in Opp'n to Pls.' Mot. for Class Certification, Appointment of Class Representatives and Appointment of Class Counsel at 22.

these individuals. Nevertheless, because there is no evidence that Biderman actually functioned as a fiduciary to those individuals whose purchase of Nine Systems shares he facilitated, or that he separately informed any or all them of any prior Board decision, the Court may not exclude shareholders simply based on the source of their shares.[13]

However, fifteen of the Biderman Plaintiffs entered into a "Stockholders Agreement" on August 12, 2002, that specifically referenced the Recapitalization and was executed contemporaneously with the adoption of the formal Recapitalization resolutions.[14] The Defendants argue that these proposed class members should be disqualified because, in signing the agreement, they directly consented to the transaction at issue. With respect to this smaller group, the Court agrees.

Finally, the Defendants seek to preclude a group of investors who held debt positions—either as convertible notes or senior debt—who, the Defendants assert, either affirmatively consented to or participated in the Recapitalization, since one condition of and basis for the Recapitalization was the elimination of debt from the Company's balance sheet. Because there is an open question as to which, if any, of these potential class members knew of the nature of the Recapitalization, they

[13] Likewise, the Court does not exclude potential class members on similar grounds suggested by the Defendants, including shareholders who were merely employees of Nine Systems, or were Nine Systems Founders or Founder Consultants or purchasers from those Founders or Founder Consultants. *See* Affidavit of Andrew Dwyer in Opp'n to Mot. for Class Certification Ex. B.
[14] Cordo Aff. Ex. M.

cannot be excluded at this stage.[15] That they may have benefited from the Recapitalization is not a reason to exclude them from a class seeking a remedy for incomplete or inaccurate disclosures with respect to the Recapitalization.

Despite the fact that excluding those involved in the Friedman Action and those who signed the Stockholders Agreement reduces the Class to roughly forty-five members,[16] the Court cannot conclude that a forty-five-member class is, nonetheless, not "so numerous that joinder of all members is impracticable." The test is not impossibility of joinder, but practicability.[17] "A showing of strong litigational inconvenience in the prosecution of claims separately or jointly by the proposed class members is sufficient."[18] Numbers in a proposed class in excess of forty have sustained the numerosity requirement,[19] and classes with a few as twenty-three members have been upheld.[20] Moreover, "[t]he number of potential

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[15] The Entity Defendants are, of course, not part of the Class.
[16] Some potential members of the Class belonged to both groups.
[17] *Garcia v. Gloor*, 618 F.2d 264, 267 (5th Cir.), *cert. denied*, 449 U.S. 1113 (1981).
[18] *Weiner & Assocs.*, 584 A.2d at 1225 (quoting *Esler v. Northrop Corp.*, 86 F.R.D. 20, 34 (W.D. Mo. 1979)).
[19] 3B J. Moore & J. Kennedy, Moore's Federal Practice ¶ 23.05[1] at 23-144, 23-145 (2d ed. 1990); *In re Itel Sec. Litig.*, 89 F.R.D. 104, 111 (N.D. Cal. 1981) ("Where the number of class members exceeds forty . . . the numerosity requirement will generally be found to be met.").
[20] *See, e.g.*, *Meeker v. Bryant*, 1981 WL 7633 (Del. Ch. Nov. 30, 1981) (class comprised of twenty-three members); *In re Kirschner Med. Corp. Sec. Litig.*, 139 F.R.D. 74 (D. Md. 1991) (class of twenty-five to thirty members creates presumption of impracticability of joinder). *But see Erickson v. Centennial Beauregard Cellular, L.L.C.*, 2003 WL 1878583, at *3 (Del. Ch. Apr. 11, 2003) ("[C]lass sizes of fewer than twenty-five members are generally not permitted unless there are special circumstances in favor of certifying the class.").

class members is not, in itself, determinative of this analysis,"[21] and Delaware courts have held that the question of whether joinder of members would be impracticable depends on the circumstances surrounding the case and not merely the number of class members.[22]

Candidly, the Plaintiffs' assertion that it would be impracticable to pursue this litigation as individually-named plaintiffs is undermined by the number of similarly situated individual plaintiffs who chose to litigate in the Friedman Action. Nevertheless, the Court is reluctant to deny certification on grounds of numerosity where the plaintiff class is within the size typically certified by our courts. As such, the Court is unwilling to invoke the numerosity requirement to deny class certification.

B. *Commonality*

Commonality is satisfied under Rule 23(a)(2) where the Plaintiffs share questions of law or fact in common with other class members,[23] "even though the individuals are not identically situated."[24] Here, common questions include, inter

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[21] *Smith v. Hercules, Inc.*, 2003 WL 1580603, at *4 (Del. Super. Jan. 31, 2003) (quoting *Liberty Lincoln Mercury, Inc. v. Ford Marketing Corp.,* 149 F.R.D. 65, 73 (D. N. J. 1993)).
[22] *See, e.g.*, *Mentis v. Delaware Am. Life Ins. Co.*, 2000 WL 973299, at *3 (Del. Super. May 30, 2000). *See also Christiana Mortgage Corp. v. Delaware Mortgage Bankers Ass'n.*, 136 F.R.D. 372, 377 (D. Del. 1991).
[23] *CME Group, Inc. v. Chicago Bd. Options Exch., Inc.*, 2009 WL 1547510, at *4 (Del. Ch. June 3, 2009).
[24] *Weiner & Assocs.*, 584 A.2d at 1225 (quoting *Gordon v. Forsyth County Hosp. Auth., Inc.*, 409 F. Supp. 708, 718 (M.D.N.C. 1976), *aff'd in part, vacated in part*, 544 F.2d 748 (4th Cir. 1976)).

alia, whether the Board breached its fiduciary duties to the minority shareholders, whether the notice provided to the minority shareholders following the Recapitalization contained inadequate disclosures or omitted material facts, whether the Class has sustained damages, as well as the proper measure of those damages, and whether any disclosure failures led to those damages. Additionally, because the Plaintiffs' claims all stem from the allegedly inadequate or misleading disclosure by the Board, they finally arose out of the same operative facts and are based on a common legal theory. Moreover, remedies that the Plaintiffs seek, such as rescission, will affect the entire Class.

The Defendants argue that the Class should, nevertheless, not be certified because the one claim remaining—breach of a duty to disclose outside of a request for shareholder action—requires individualized proof of certain elements, including reliance, loss causation, and damages, which would seemingly overrun the issues of law and fact common to the Class.[25]

[25] *See, e.g.*, *A.R. DeMarco Enters., Inc. v. Ocean Spray Cranberries, Inc.*, 2002 WL 31820970, at *4 n.10 (Del. Ch. Dec. 4, 2002) ("When stockholder action is absent, plaintiff must show reliance, causation, and damages."); *O'Reilly v. Transworld Healthcare, Inc.*, 745 A.2d 902, 917 (Del. Ch. 1999) (holding that, for "a disclosure claim arising out of a communication that does not contemplate shareholder action," plaintiffs must plead "causation and identify actual quantifiable damages in order to plead sufficiently this category of disclosure violation."); John C. Coffee, Jr., *Disclosure Duties: New Law & Issues*, 1/21/99 N.Y.L.J. 5, col. 1 at p. 2-3 ("[W]hen shareholder action is not sought, reliance, causation and damages must be shown. Because Delaware does not recognize the 'fraud on the market' doctrine, the reliance requirement effectively prevents a class action from being maintained.").

The notion that a disclosure violation occurring in the absence of shareholder action may not be remedied through a class action stems from *Malone v. Brincat*.[26] In *Malone*, our Supreme Court first confirmed that directors must be candid in their communications with stockholders "even in the absence of a request for shareholder action."[27] This is because fiduciary duties, including the duty to be candid, "[do] not operate intermittently but [are] the constant compass by which all director actions for the corporation and interactions with its shareholders must be guided."[28] Nevertheless, the Court noted that "[a]n action for a breach of fiduciary duty arising out of disclosure violations in connection with a request for stockholder action does not include the elements of reliance, causation and actual quantifiable monetary damages. Instead, such actions require the challenged disclosure to have a connection to the request for shareholder action."[29]

Courts and commentators have inferred from the Court's language that, in disclosure suits not involving a request for shareholder action, each plaintiff must make an individualized showing of reliance, causation, and damages.[30] By

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[26] 722 A.2d 5 (Del. 1998).
[27] *Id.* at 14.
[28] *Id.* at 10.
[29] *Id.* at 12.
[30] *See, e.g.*, *supra* note 25; *In re Oracle Corp. Deriv. Litig.*, 867 A.2d 904, 931 n.118 (Del. Ch. 2004) ("Arguably, the case of *Malone v. Brincat* already represents an expansion of the Delaware carve-out, because it theoretically permits recovery by stockholders against directors who make knowingly false disclosures that are not in connection with a request for stockholder action. . . . As a practical matter, this state's unusual approach to the certification of class actions in disclosure cases, *see Gaffin v. Teledyne* (holding that because individual reliance predominates

establishing separate state law disclosure claims based upon whether or not shareholder approval was sought, the Supreme Court avoided creating significantly enhanced liability for directors and prevented a complete overlap of state and federal causes of action for disclosure.

The Plaintiffs contend that *Malone* need not be read as mandating that these additional elements be established in the absence of shareholder action, and that the commentary suggesting otherwise is either incorrect or else mischaracterized by the Defendants. Furthermore, argue the Plaintiffs, the *Malone* Court expressly allowed for the re-pleading of this very type of disclosure claim as a class action.

The Plaintiffs are correct that *Malone* does not expressly forbid bringing a class action for disclosure claims that are unrelated to a request for shareholder action, and the Court appears to leave hypothetical room for them, if properly

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over other issues, no class may be certified in a common law fraud claim involving the stockholders of a corporation as a proposed class), serves to limit the utility of *Malone* to plaintiffs' lawyers.") (citations omitted); *Metro Commc'n Corp. BVI v. Advance Mobilecomm Techs., Inc.*, 854 A.2d 121, 158 (Del. Ch. 2004) ("Later cases have logically read *Malone* as also contemplating a requirement of reasonable reliance in the non-vote and non-tender context. The decision by the Supreme Court to set a high bar for *Malone*-type claims was not, I think, inadvertent and represented an effort on its part to ensure that our law was not discordant with federal standards and that our law did not encourage a proliferation of disclosure claims outside the discretionary vote or tender context by exposing corporate directors to an additional host of disclosure claims that did not involve the need to show reliance or scienter. That policy choice is one that commands the respect of this court and necessarily influences my decision. . . .") (citations omitted); *Torch Liquidating Trust ex rel. Bridge Assocs. L.L.C. v. Stockstill*, 561 F.3d 377, 389 (5th Cir. 2009) ("The elements of a claim for misrepresentation of a corporation's financial condition where no shareholder action is requested are: (1) deliberate misinformation either directly or through public statement; (2) reliance; (3) causation; and (4) actual, quantifiable damages.") (citing *Malone*, 722 A.2d at 12, 14; *Metro Commc'n*, 854 A.2d at 157; *A.R. DeMarco*, 2002 WL 31820970, at *4 n.10; *O'Reilly*, 745 A.2d at 917, 920).

plead. Specifically, the Court held that plaintiffs would be able to bring such disclosure claims "on behalf of the corporation," as an "individual cause of action," or as "a properly recognizable class consistent with Court of Chancery Rule 23, and our decision in *Gaffin*."[31] Nevertheless, the Court's invocation of *Gaffin* suggests that a plaintiff's ability to pursue disclosure claims through the mechanism of a class action, while technically possible, is limited as a practical matter.

The Court's reference to *Gaffin* is footnoted and cited for the principle that "[a] class action may not be maintained in a purely common law or equitable fraud case since individual questions of law or fact, particularly as to the element of justifiable reliance, will inevitably predominate over common questions of law or fact."[32] Moreover, the footnote lists a series of cases which rejected the treatment of claims on a class-wide basis because of a need to demonstrate individual reliance, causation, or damages.[33] Thus, although *Malone* leaves open the possibility of certifying a class for this subset of disclosure claims, its language is consistent with a requirement of individual proof of reliance, causation, and

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[31] *Malone*, 722 A.2d at 14.

[32] *Id.* at 14 n.47 (citing *Gaffin v. Teledyne, Inc.*, 611 A.2d 467, 474 (Del. 1992)). *Gaffin* is also commonly cited for its refusal to adopt the fraud-on-the-market presumption of reliance. *Gaffin*, 611 A.2d at 474.

[33] *Barnes v. Am. Tobacco Co.*, 161 F.3d 127 (3d Cir. 1998); *Broussard v. Meineke Discount Muffler Shops, Inc.*, 155 F.3d 331 (4th Cir. 1998); *Cimino v. Raymark Indus., Inc.*, 151 F.3d 297 (5th Cir. 1998); *Amchem Prods., Inc. v. Windsor*, 521 U.S. 591 (1997).

damages.[34] This necessarily limits the types of disclosure actions that can be brought by a plaintiff class.[35]

The Plaintiffs' claims are subject to the broader requirements set forth in *Malone*.[36] Because the elements of reliance, causation, and damages will need to be individually established, it cannot be said that the relevant questions of law or fact are commonly shared by the proposed Class, since, for example, the Company's former stockholders obtained and held their shares in ways that made

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[34] Jennifer O'Hare, *Director Communications and the Uneasy Relationship Between the Fiduciary Duty of Disclosure and the Anti-Fraud Provisions of the Federal Securities Laws*, 70 U. Cin. L. Rev. 475, 513 (2002) ("By referencing *Gaffin*, the court indicated that reliance is an element of an action for breach of the duty of disclosure when shareholder action has not been requested and that plaintiffs are not entitled to the fraud-on-the-market presumption. Without this presumption, it will be difficult for plaintiffs to bring a class action suit to recover for a breach of fiduciary duty for false market disclosures. . . .").

[35] *See* Michael H. Barr, et al., *Recent Developments in Class Action Law*, Practicing Law Inst., 1590 PLI/Corp 85 (2007) ("[U]nder the rubric of predominance, courts tend to consider whether individualized issues relating to affirmative defenses, reliance, [and] damages . . . render the class device inappropriate. While not all courts are consistent in denying class certification on these bases, as a general matter, the existence of individualized defenses should defeat class certification."). *But see* Coffee, *supra* note 25, at 5 ("In the case of false statements not intended to secure or induce shareholder action, the plaintiff would need to prove reliance, causation, and damages in addition to materiality. But it is possible to imagine a consortium of large investors, particularly including angry institutional investors, who might file such actions on a consolidated basis, possibly sharing a common counsel.").

[36] Perhaps one could argue that actions by written consent necessarily fall within the exception for disclosure violations made "in connection with a request for shareholder action," with the notice requirement of 8 *Del. C.* § 228 functioning as the final phase of securing stockholder approval. However, this would seem to get the exception entirely backwards; the § 228 notice does not relate to a "request" for shareholder action, but merely functions to inform shareholders of action that has already taken place. Proving individual reliance in the former case is unnecessary because shareholders vote on proposed corporate action, at least in part, on the information made available to them, and incomplete or misleading information provided before the vote may very well have affected the ultimate outcome. No such harm to the shareholder franchise rights of those who have not been called on to consent occurs in the context of an incomplete or misleading notice following shareholder action by consent; instead, any harm experienced stems from delayed (or precluded) access to judicial remedies.

them more or less reliant on the information generally disseminated by the Board.[37] Thus, the commonality requirement has not been met.

C. *Typicality*

The Defendants also argue that the claims and defenses of Dubroff and Klein are not typical of the proposed Class and, thus, that they cannot appropriately represent its claims. At base, this is because Dubroff purchased his shares from Biderman,[38] while Klein has testified that he never received the notice of the Recapitalization.[39] These facts, assert the Defendants, raise material issues as to reliance by the Plaintiffs on the disclosures at issue, and thereby provide the Defendants additional defenses against the Plaintiffs that are not available against certain other members of the Class. The Defendants also assert that, because Dubroff realized a taxable gain on his investment in Nine Systems, he would not be able to prove damages attributable to his reliance on the Company's allegedly incomplete and/or misleading disclosures.

The test of typicality is that "the legal and factual position of the class representative must not be markedly different from that of the members of the class."[40] This ensures that the class representative claim fairly presents the issues

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[37] *Cf. In re Countrywide Corp. S'holders Litig.*, 2009 WL 846019, at *12-*13 (Del. Ch. Mar. 31, 2009).
[38] Dubroff was an employee of Lipper & Company.
[39] Cordo Aff. Ex. A ("Klein Dep. Tr.") at 91.
[40] *Singer v. The Magnavox Co.*, 1978 WL 4651, at *2 (Del. Ch. Dec. 14, 1978).

on behalf of the representative class. A representative's claim will suffice if it "arises from the same event or course of conduct that gives rise to the claims of other class members and is based on the same legal theory."[41] Although Dubroff's alleged connection to Biderman and arguably questionable damages are not sufficiently material to make his claim atypical of the Class, Klein's testimony that he did not receive the notice of the Recapitalization—because it raises a more glaring issue as to his reliance—operates to defeat typicality as to him.

D. *Adequacy*

The Defendants also allege that Dubroff and Klein have not demonstrated that they are capable of "fairly and adequately" protecting the interests of the Class, as required under Rule 23(a)(4). Typically, the adequacy prong focuses on whether the Plaintiffs have any serious conflicts of interest with other class members and whether they are represented by qualified, experienced counsel.[42] Both of these factors appear to be met here, as the Plaintiffs held Nine Systems shares during all of the relevant periods and do not appear to have any conflicts with the other class members, and the Rosen Firm has already demonstrated its commitment and capability in this case in successfully opposing the Defendants' dismissal motion as to the surviving claim.

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[41] *Zeffiro v. First Pa. Banking & Trust Co.*, 96 F.R.D. 567, 569 (E.D. Pa. 1983) (quoted in *Weiner & Assocs.*, 584 A.2d at 1226).

[42] *See, e.g.*, *Emerald Partners v. Berlin*, 564 A.2d 670, 673-74 (Del. Ch. 1989).

Dubroff and Klein are alleged to be inadequate representatives because, according to the Defendants, neither has shown "sufficient diligence" in the action.[43] The Defendants seem to suggest that Dubroff and Klein ought to be held to a higher standard than representative plaintiffs are normally held since this is the third action involving these facts where Dubroff and Klein were the representative plaintiffs, and since they have had access to the critical facts since the action was first filed in California in February 2007.

The Defendants contend that, in their depositions, neither Dubroff nor Klein "was able to identify the relationships between the various defendants, or display any specific knowledge about the claims and transactions that are the subject of the litigation. . . ."[44] Further, the Defendants assert that neither of them has done "anything at all to verify the truth or accuracy of the claims asserted," and they express concern that the Plaintiffs may not have read the Complaint prior to signing the verification that its allegations were "true and accurate."[45] They also point out that the Plaintiffs have not been closely involved with the progress of the

[43] Defs.' Answering Br. in Opp'n to Pls.' Mot. for Class Certification, Appointment of Class Representatives, and Appointment of Class Counsel at 28.
[44] *Id.* at 29 (citing Klein Dep. Tr. at 28-45; 75; Cordo Aff. Ex. B ("Dubroff Dep. Tr.") at 48-51, 83-92, 125).
[45] *Id.*

litigation and did not understand the reasoning behind some of the developments in the case.[46]

Nevertheless, our law only requires that a named plaintiff demonstrate a "knowledge of the underlying facts"[47] or a "keen interest in the progress of the litigation."[48] Dubroff and Klein have met this standard.[49] Their deposition testimony establishes that each understands the issues in the case and has a general sense of the progress of the litigation.[50] They are likewise entitled to rely on their attorneys for the prosecution of the matter[51] and have properly done so here.

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[46] Specifically, the Defendants contend that the Plaintiffs had not sought nor been provided copies of the decisions by the California and New York courts dismissing their prior actions, that they were not immediately informed of the decision awarding the Defendants $30,000 in attorneys fees, that neither could explain how or why these separate actions have been filed and that they did not receive many of the Defendants' pleadings in this case. The Defendants also assert that the Plaintiffs did not fully understand their role as named plaintiffs and did not realize that they could be called to testify at trial.

[47] *In re Daimler-Chrysler AG Sec. Litig.*, 216 F.R.D. 291, 299 (D. Del. 2003). *See also In re ML-Lee Acquisition Fund II, L.P.*, 848 F. Supp. 527, 559-60 (holding that plaintiffs are held to a "very minimal requirement of knowledge about the litigation and the facts upon which it is based").

[48] *In re Goldchip Funding Co.*, 61 F.R.D. 592, 595 (M.D. Pa. 1974).

[49] *See, e.g.*, Dubroff Dep. Tr. 87, 93; Klein Dep. Tr. 16-17.

[50] *See, e.g.*, *In re College Bound Consol. Litig.*, 1994 WL 236163, at *4 (S.D.N.Y. May 31, 1994); *Klein v. A.G. Becker Paribas Inc.*, 109 F.R.D. 646, 651 (S.D.N.Y. 1986); *Robbins v. Moore Med. Corp.*, 1992 WL 396423, at *2 (S.D.N.Y. Dec. 21, 1992).

[51] *See, e.g.*, *In re Fuqua Indus., Inc. S'holder Litig.*, 752 A.2d 126, 135 (Del. Ch. 1999) ("Our legal system has long recognized that lawyers take a dominant role in prosecuting litigation on behalf of clients. A conscientious lawyer should indeed take a leadership role and thrust herself to the fore of a lawsuit. This maxim is particularly relevant in case involving fairly abstruse issues of corporate governance and fiduciary duties.").

IV. DOES THE PROPOSED CLASS SATISFY RULE 23(b)?

Class certification has also been opposed on grounds that the requirements of Court of Chancery Rule 23(b) have not been met. Rule 23(b) sets up the "second step" for class certification, providing that an action may be maintained as a class action where the prerequisites of paragraph (a) are satisfied and where, in relevant part:

> (1) The prosecution of separate actions by or against individual members of the class would create a risk of:
> (A) Inconsistent or varying adjudications with respect to individual members of the class which would establish incompatible standards of conduct for the party opposing the class, or
> . . .
> (3) The Court finds that the questions of law or fact common to the members of the class predominate over any questions affecting only individual members, and that a class action is superior to other available methods for the fair and efficient adjudication of the controversy. The matter pertinent to the findings include:
> (A) The interest of members of the class in individually controlling the prosecution or defense of separate actions.
> (B) The extent and nature of any litigation concerning the controversy already commenced by or against members of the class;
> (C) The desirability or undesirability of concentrating the litigation of the claims in the particular forum;
> (D) The difficulties likely to be encountered in the management of a class action.

The Plaintiffs assert that certification is available under Rule 23(b)(1)(A) and under Rule 23(b)(3). The Court will consider each in turn.

A. *Class Certification Under Rule 23(b)(1)(A)*

Class actions are appropriate for certification under Rule 23(b)(1)(A) when a determination of the rights of all parties is necessary to avoid inconsistent or varying adjudications.[52] To qualify under Rule 23(b)(1)(A) "there must be a total absence of individual issues."[53]

However, as determined above, individual issues remain, including issues of reliance, causation, and actual damages. Because these individual issues will need to be established for Plaintiffs to succeed on their disclosure claim, class certification is unavailable under Rule 23(b)(1)(A).

B. *Class Certification Under Rule 23(b)(3)*

To meet the requirements for certification under Rule 23(b)(3), common questions of fact and law must predominate over individual questions ("predominance"), and a class action must be superior to other available methods for the fair and efficient adjudication of the controversy ("superiority").[54]

Claims for breach of fiduciary duty are regularly certified under Rule 23(b)(3).[55] However, it is far from clear that the common questions of law

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[52] *See* 3B Moore's Federal Practice ¶ 23.35[1] at 23-242.
[53] *Joseph v. Shell Oil Co.*, 1985 WL 21125, at *4 (Del. Ch. Feb. 8, 1995) (citing *Tober v. Charnita, Inc.*, 58 F.R.D. 74 (M.D. Pa. 1973)).
[54] Ct. Ch. R. 23(b)(3).
[55] *See, e.g.*, *J.L. Schiffman and Co., Inc. Profit Sharing Trust v. Standard Indus., Inc.*, 1993 WL 271441, at *2 (Del. Ch. July 19, 1993); *Zirn v. VLI Corp.*, 1991 WL 20378, at *6 (Del. Ch. Feb. 15, 1991).

and fact that persist in this case necessarily predominate over the individual questions of reliance, causation, and damages. Similarly, because of the complications that will undoubtedly arise in establishing these elements on an individual basis, it is not apparent that a class action is a superior method for the former shareholders to have their claims heard or the most efficient means of litigating these claims. Consequently, the Class also may not be certified under Rule 23(b)(3).

V. CONCLUSION

Although the Plaintiffs are unable to satisfy several of the discrete requirements of Court of Chancery Rule 23, class certification ultimately fails on this Court's reading of *Malone* as imposing individual requirements for establishing a disclosure claim outside of the context of a request for shareholder action. Absent the implications of *Malone*, there would appear to be no grounds for refusing to certify the Class. Accordingly, for the foregoing reasons, the Plaintiffs' motion to certify the Class will be denied.[56] An implementing order will be entered.

[56] With this conclusion, the application to designate the Rosen Firm as class counsel is moot.