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OF THE
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Re: *State of Wisconsin Investment Board v. Bartlett, et al.*
Civil Action No. 17727

Dear Counsel:

This is the Court's decision on an application for attorneys' fees in this purported class action lawsuit. The lawsuit effectively ended on February 24, 2000, when this Court denied a request to enjoin a proposed merger. After the Court's decision, stockholders approved the merger and the transaction was consummated on February 25, 2000. Stock of the acquiror company was thereafter distributed in exchange for all of the stock of the target company. Attorneys for the plaintiff, who failed to achieve their goal of stopping the merger from taking merger agreement provided a formula for the exchange ratio that included a two-sided collar, with a floor of $22.50 and a ceiling of $34. The pricing formula was calculated using a three-tiered approach. If King's average closing stock price for the twenty-day period ending three days before the merger fell between $33 and $49.87 per share, the exchange ratio would be fixed at 0.6818 shares of King for each share of Medco stock. Multiplying the twenty-day average price by the exchange ratio then yielded a range of value for Medco stock of 1) $33 x 0.68 18=$22.50 (minimum value) and 2) $49.87 x 0.68 18=$34 maximum value). On the other hand, if King's twenty-day average stock price fell below $33 or rose above $49.87, the exchange ratio would be adjusted up or down to hold the value of King stock received for each share of Medco stock at $22.50 and $34, respectively. The parties used the twenty-day average price of King's stock to calculate the exchange ratio-rather than the spot price on any given day-to smooth out variations in King's volatile stock price. For this reason, the theoretical paper value of the deal might fluctuate from day to day. On any given day, for example, if King's stock price closed above the twenty-day average, the *theoretical* value of the deal might exceed $34 per share.[3] On the other hand, if the King price

[3] It is a "theoretical" increase in value because a Medco shareholder could not have sold his or her King stock on the same day the merger closed (February 25), as the King stock was not distributed until later. King's stock price fell again after February 25.

closed below the twenty-day average on a particular day, the *theoretical* value of the deal might fall below $22.50 per share. But the intent of the parties was to cap the real upside value received by Medco shareholders at $34 per share and to protect Medco shareholders from a real downside value of less than $22.50 per share.

As a result of the fifteen-day delay, the exchange ratio, based on a recalculated twenty-day market price average, changed from 0.595 19 on February 10 to 0.67573 on February 25, a mathematical increase of 13.5% in the exchange ratio.[4] This increased the amount of King stock received by each Medco shareholder over that which they would have received if the merger had gone forward on February 10 as originally scheduled.

II. CONTENTIONS

In connection with its request for fees, G&E offers two explanations for why SWIB's lawsuit was responsible for the benefit conferred upon the class.' First, G&E argues that the fifteen-day delay in holding the shareholder vote (from February 10 to February 25) resulted in a significant increase in the exchange ratio of King stock for Medco stock. As noted earlier, the exchange ratio increased

[4] The percentage increase in the exchange ratio is calculated as follows: 0.67573-0.59519=.08054. 0.08054 ÷ 0.59519=13.5%.

[5] Actually, no class was ever certified in this litigation. Indeed, it does not appear that SWIB's counsel formally moved for class certification. No class will ever be certified in this lawsuit, as SWIB has now moved to dismiss the action without prejudice.

from 0.595 19 on February 10 to 0.67573 on February 25, yielding a 13.5% increase in the exchange ratio. Multiplying the new ratio (0.67573) times the King stock trading price at the close of trading on February 25 (King stock closed at $50.75 on the day the shareholders approved the merger and it was consummated) yields a value of $34.29. Multiplying the old ratio that would have applied on February 10 (.59519) times the February 25 King stock trading price of $50.75 yields a value of $30.21. The difference in value to Medco shareholders, according to G&E, is $4.08. In other words, G&E argues that the improved exchange ratio translated into a $4.08 per share improvement in value for Medco shareholders. The proposed class-wide benefit, according to this theory, is $48,061,755 ($4.08 x 11,757,270 Medco shares outstanding)!

Second, G&E argues that the supplemental proxy material issued to Medco shareholders was a direct result of SWIB's litigation. Thus, they contend they also conferred a benefit upon Medco shareholders in this fashion.

Before SWIB filed this lawsuit, it negotiated a fee agreement with G&E. Under the fee retainer agreement, G&E's compensation was to be determined in one of three ways, depending on the outcome of the litigation. First, if the merger

[6] G&E offer an alternative calculation of the benefit conferred by SWIB's action by multiplying the old exchange ratio by King's trading price at the time of the originally scheduled shareholder vote (February 10). Using King's trading price on February 9 and February 10, G&E claim that the minimum increase in value per Medco share would be $3.94 to a maximum increase of $5.35, yielding class-wide benefits ranging from $46,323,643 to $62,901.394.

were “restructured such that SWIB’s supports it” G&E and SWIB would petition the Court for 15% of the benefit. If insufficient fees were awarded, SWIB would guarantee that G&E received 100% of its hourly charges plus expenses. Second, if the merger were called off but no new transaction proposed, G&E and SWIB would ask the Court for a fee of 175% of hourly charges. Again, if insufficient fees were awarded, SWIB would guarantee that G&E received 100% of its hourly charges, plus expenses. Finally, if the merger were completed on its current terms (i.e., the litigation were unsuccessful), SWIB would pay G&E 50% of its hourly charges, plus expenses. In other words, as a “worst case” scenario, the terms of the retainer agreement guaranteed G&E at least half of its hourly charges, plus expenses.

G&E now rely upon the first clause of the retainer agreement that was applicable only “if the merger is restructured such that SWIB supports it”-even though SWIB has conceded that it never supported the merger and voted all of its Medco stock against it. Despite G&E’s claim that SWIB has agreed that the first clause of the retainer agreement should apply in these circumstances, SWIB’s general counsel has testified that SWIB has not determined what it will pay in the event the Court does not award fees.

G&E contends that 15% of the "benefit created" yields attorneys' fees in the amount of $7,209,263.[7] G&E points out that it invested 1,440 hours of attorney time over a six-week period, which amounts roughly to $400,000 in billable time based on customary hourly rates. A fee in excess of $7.2 million, however, would provide an enviable billing rate of over $5,000 for each hour of attorney time expended. G&E also seeks reimbursement of $180,0 18 of expert witness fees and $93,935 in litigation costs expended in the courts of the action. Finally, SWIB requests $50,000 in attorneys' fees for the efforts of its general counsel and his legal and investment staff in pursuing this litigation.

Defendants argue that SWIB and G&E are not entitled to any fees or expenses in connection with this litigation. They point out that SWIB opposed the merger and, after failing to have it enjoined, voted against it. They also point out that this Court rejected SWIB's substantive attack on the merger, concluding that the Medco Board was fully informed and acted in good faith in negotiating and recommending the merger to Medco's shareholders. Defendants further argue that no benefit was created by SWIB's litigation because the exchange ratio in the merger agreement capped Medco shareholders to an upside of $34 worth of King stock per Medco share. Because King's average closing price on both February 10

[7] The calculation is 15% x $48,061,755=$7,209,263. G&E generously notes that it will forego requesting additional compensation for the non-monetary benefits conferred by SWIB's litigation *(i.e.,* the supplemental disclosures).

and February 25 exceeded $49.87, the $34 cap applied on both dates. Thus, according to defendants, despite the change in the exchange ratio between February 10 and February 25, no real monetary benefit was conferred on Medco's shareholders as a result of the lawsuit. Finally, the defendants insist that even if one assumes a net benefit to Medco shareholders from the increase in the exchange ratio, no causal connection exists between SWIB's lawsuit and that supposed benefit. They note that the increase in the exchange ratio was the product of the terms of the merger agreement (which required, once the shareholder vote was delayed, a change in the pricing period) and the fact that market forces affected King's stock price, which went down during the fifteen-day delay, thus yielding the higher exchange ratio. Fortuitously, King's stock price rallied on February 25 (closing at $50.75) which caused a momentary "spike" in the theoretical value of the stock distributed to Medco shareholders.

III. ANALYSIS

To demonstrate that they deserve fees of any amount, SWIB must convince me that: (1) the suit was meritorious when filed; (2) the action produced a benefit to the corporation or class; and (3) the resulting benefit to the class or corporation was causally related to the suit.[8] I will now turn to a consideration of these factors.

[8] *United Vanguard, Inc. v. Takecare, Inc.*, 693 A.2d 1076, 1079 (Del. 1997).

First, I agree that the lawsuit was meritorious, if barely so, when filed Although the defendants insist that the suit was not meritorious and that this Court rejected plaintiffs request for a preliminary injunction, a ruling at the preliminary injunction stage is provisional only and cannot be considered as an adjudication on the merits. Turning to the second factor, I agree that the lawsuit provided a therapeutic benefit to the class because it prompted the defendants to make supplemental disclosures to Medco shareholders regarding the merger terms. For this therapeutic benefit, G&E is entitled to a reasonable attorneys' fee proportional to the benefit, to which I will turn in Part IV of this decision.

I do not agree with G&E's claim that SWIB's lawsuit produced a $48,000,000 benefit for Medco's shareholders. First, G&E's benefit theory, in my opinion, relies on an abstract theoretical model lacking connection to the real world. Specifically, G&E argues that the 13.5% increase in the exchange ratio between February 10 and February 25 ***automatically translated*** into a 13.5% increase in shareholder benefit. Put differently, G&E claims that the change in the exchange ratio is, in and of itself, the measure of shareholder benefit. But this completely misconceives how the exchange ratio operated in this particular case. The exchange ratio was not intended to be the contract's measure of shareholder benefit. Rather, the exchange ratio was just a mathematical formula employed by King and Medco to maintain the consideration that was being offered by King to the Medco shareholders. That formula capped the maximum value to Medco shareholders at $34 per share and created a floor of $22.50 per Medco share. On both February 10 and February 25, King's average closing price exceeded the ceiling trigger of $49.87 and, therefore, the $34 cap applied on both dates. G&E's theory ignores the $34 cap limitation and relies on an implicit assumption that Medco shareholders could (and did) sell all of their 7.2 million King shares on February 25. It so happened that on February 25 King's stock price increased to $50.75. Basing the benefit calculation on that one-day February 25 spot price, together with the assumption that *all* the shares were sold on that date, enables G&E to say "voilà": a $48,000,000 benefit to Medco shareholders.

The fact is that the King shares were not distributed to the Medco shareholders on February 25; the Medco stock was not actually exchanged for King stock until February 28. Moreover, had all 7.2 million King shares been sold on February 25, the market in King's shares was too thin to support such a massive sell off and accordingly would have depressed King's stock price.[9] These practical and real limitations on G&E's theoretical benefit analysis rob that analysis of any force. Using the twenty-day trading average of King's stock effectively means that Medco shareholders got 13.5% more of something that was worth, on ***average,***

[9] See D. Campili, Aff., ¶ 11, p. 4 (during the relevant period, the average daily trading volume of King shares was about 380,000 shares).

13.5% less. There was no $48000,000 fund created for the Medco stockholders and the Medco stockholders were not enriched to the tune of $48,000,000. That $48,000,000 "benefit" is a mathematical construct that springs from the fertile and creative imagination of those who would lay claim to a part of it, and expect someone else to pay it.

But suppose we pass through the looking glass and imagine that Medco's stockholders actually received a benefit of $48000,000. It was not a benefit, however, that was caused or produced by the efforts of SWIB and G&E. To begin with, the increase in the exchange ratio was required by the merger agreement's terms-terms that did not change one iota from the time SWIB filed its lawsuit until the merger was completed. Next, the exchange ratio increased (from 0.595 19 to 0.67573) because the average trading period was calculated differently when the shareholder vote was moved from February 10 to February 25. The resulting change in the exchange ratio was caused by the fluctuations in King's stock price over the newly calculated average trading period. SWIB was not responsible for, nor did it cause, the recalculation of the exchange ratio. SWIB's lawsuit did not cause the market value of King stock to fall during the twenty-day average trading period or to rise on February 25. King's stock price was volatile, for a host of reasons having nothing to do with SWIB. That was the very reason for using a twenty-day average trading period for purposes of calculating the exchange ratio.

SWIB admits that it could not predict whether the market price of King's stock would increase or decrease between February 10 and February 25. As luck would have it, King's stock price fell during the twenty-day average period that ended on February 22, and then rallied into the last day of the pricing period (February 25). This completely fortuitous set of circumstances resulted in an increase in the exchange ratio. It also enables G&E to argue that all of the Medco shareholders could have sold-instantly and unanimously-at the higher price on February 25 and reaped a $48,000,000 benefit. To the extent that one can even call this theoretical benefit real, for the reasons I expressed earlier it cannot be viewed as a benefit caused by SWIB's litigation or the efforts of G&E. Accordingly, with respect to this purported benefit SWIB has failed to demonstrate the second or the third factor, which are, that the action produced a benefit to the class or corporation and that the benefit was causally related to the lawsuit.

IV. CALCULATION OF THE FEE

Although no monetary benefit was created, I do agree that a therapeutic benefit was created by the supplemental disclosures. I now turn to the determination of a reasonable fee for this benefit.

This Court employs a multi-factor approach *(known* as the *Sugarland* factors) to evaluate fee requests, consisting of the following: (1) the time and effort expended by counsel; (2) the difficulty and complexity of the litigation; (3)

counsel's standing and ability; (4) the contingent nature of the fee; (5) the stage at which the litigation ended; (6) the amount of the benefit that can fairly be attributed to the efforts of the requester of the fees; and (7) the size of the benefit conferred."

First, counsel expended 1440 hours over a six-week period. But SWIB's billing records indicate that only $234,063 of G&E's fees (out of about $400,000 of fees in total time) were incurred *before* January 3 1, the date of the supplemental proxy disclosures. Thus, G&E's fees billed after January 31 related to the substantive attack on the merger, an effort that failed. G&E's post-January 3 1 fees thus do not relate to the therapeutic benefit and, consequently, do not warrant an award payable by the company. Likewise, $180,000 of expert witness fees related to valuation and pooling of interests issues involved in the substantive attack on the merger. These fees do not relate to the successful disclosure claim and do not warrant an award payable by the company. Viewed charitably, the remaining $93,935 in requested costs can be attributed to the therapeutic benefit aspect of the case and will be awarded.

Second, the litigation was not overly complex or difficult by the standards of this Court. The case was professionally managed and litigated over a six-week

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[10] *Goodrich v. E.F. Hutton Group, Inc., 68* 1 A.2d 1039 (Del. 1996); *Sugar-land **Indus.** Inc. v. **Thomas**, 420* A.2d 142 (Del. 1980).

period by counsel of recognized standing and ability in complex, corporate litigation.

Third, G&E’s fee was not fully contingent as that term is generally understood. Here, SWIB agreed, if the lawsuit failed to stop the merger or alter its terms, to pay 50% of G&E’s hourly charges in addition to all of its expenses. Thus, G&E’s compensation risk was substantially below that typically encountered in cases in which counsel seek to vindicate the rights of shareholders. There was no risk (other than the risk that SWIB might not pay) as to expenses and there was a floor equal to one-half of the fees incurred up to $400,000 to ensure a certain threshold of compensation.[11] Accordingly, because the risk was not that ordinarily associated with contingent fee cases, a reduction in the fees and expenses that otherwise would have been awarded may be appropriate or, perhaps more accurately, only those fees above SWIB’s minimum guarantee are appropriate for consideration as qualifying for an enhancement of the fee due to the risk.[12]

Fourth, as described earlier G&E did not cause the purported benefit to the shareholders from the increase in the effective exchange ratio. But the causal connection to the disclosure benefit is real. Even defendants concede, albeit

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[11] The agreement capped SWIB’s obligation to G&E at $200,000 in professional fees, exclusive of expenses, unless SWIB agreed to a greater amount.

[12] Because G&E faced a reduced “compensation risk,” the risk premium factor discussed in *Seinfeld v. Coker*, Del. Ch., C.A. No. 16964, Chandler, C. (Dec. 4, 2000) is less applicable here.

grudgingly, that the lawsuit probably resulted in the supplemental proxy disclosures.

Finally, although not specifically listed as factor in our fee analysis, the terms of a fee agreement between the law firm and its client are appropriate for the Court to consider. Fee agreements cannot absolve the Court of its duty to determine a reasonable fee; on the other hand, an arm's-length agreement, particularly with a sophisticated client, as in this instance, can provide an initial "rough cut" of a commercially reasonable fee. The fee agreement between SWIB and G&E is, beyond the $200,000 guaranteed fee aspect, unhelpful because the premium fee is based on a list of assumptions, none of which is applicable because of the manner in which the case evolved. The fee agreement established various benchmarks for the award of a premium fee. One benchmark was triggered if the merger was changed such that SWIB would support it. A second benchmark was be triggered if the King/Medco merger was called off and no new transaction emerged. The final benchmark was triggered if the merger was completed as originally proposed *(i.e.,* the lawsuit failed). In that event, the agreement provided that SWIB would pay G&E 50% of its hourly charges, plus expenses.

Only the last of these benchmarks is arguably applicable here. The litigation failed and the merger was completed as proposed and without change. SWIB is apparently obligated to reimburse G&E for 50% of its hourly charges, or roughly

$200,000, plus expenses. As SWIB billing records show that G&E billed $234,063 for hours charged before January 3 1 (when the supplemental disclosures issued), it is only fair to assess those fees against the successor corporation because those fees are directly related to, as well as proportionate to, the therapeutic benefit.[13] In similar fashion, the costs associated with the disclosure issue ($93,935) should be assessed to the successor corporation.

SWIB is responsible, under its own contract with G&E, for 50% of G&E's hourly charges, up to a maximum of $200,000. Thus, a judicial fee award of $234,063 to G&E fits precisely within the framework of the retainer agreement, leaving SWIB where it should have expected to be under its agreement---owing slightly less than $200,000 (the balance of G&E's fee after subtracting the judicial fee award). In addition, the expenses that were unrelated to the disclosure issues ($180,018) would fall to SWIB, as per the agreement in the event the merger's terms were unchanged. After reviewing the record and the arguments, I believe this to be a fair, reasonable, and proportionate award for counsel's work over the six-week period of this litigation: $234,063 in legal fees, plus $93,935 in litigation costs, for a total of $327,998.

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[13] ***See Eisenberg v. Chicago Milwaukee* Corp., Del. Ch., C.A. No. 9374, Jacobs, V.C. (Oct. 25, 1988), *aff'd*, *560* A.2d 489 (Del. 1989).**

Finally, I cannot agree to award $50,000 of attorneys' fees for the efforts of SWIB's general counsel and legal investment staff. Nothing in the record demonstrates why it would be appropriate to award fees to an institutional investor for its costs of doing business. SWIB is a sophisticated institutional investor that held 11.5% of the outstanding shares of Medco. It opposed the Medco/King merger, but it also benefited from the merger. In-house counsel for institutional investors who serve as lead plaintiffs cannot be likened to private counsel whose fees are either paid by the client according to a fee agreement or assessed by a court in the context of a fee award. One can conceive of a circumstance in which it would be appropriate to award a special fee to a representative plaintiff in a class action, but this is not such a circumstance.

V. CONCLUSION

I award SWIB's counsel (G&E) fees in the amount of $234,063, together with costs in the sum of $93,935 that were expended in the course of this litigation. I deny SWIB's request for reimbursement of its in-house counsel fees. I grant defendant's request to dismiss this action, which ended more than two years ago, with prejudice.

An Order consistent with this letter decision is attached.

Very truly yours,

William B. Chandler III

WBCIII:meg

Attachment

oc: Register in Chancery
xc: Vice Chancellors
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IN THE COURT OF CHANCERY OF THE STATE OF DELAWARE
IN AND FOR NEW CASTLE COUNTY

STATE OF WISCONSIN INVESTMENT BOARD, on behalf of itself and all others similarly situated, Plaintiff, v. WILLIAM BARTLETT, JAY N. COHN, MARK B. HIRSCH, EUGENE L. STEP, RICHARD C. WILLIAMS, and MEDCO RESEARCH, INC., Defendants.	)	Civil Action 17727-NC

ORDER

For the reasons assigned in this Court's letter decision, entered in this case on this date, it is

ORDERED:

(1) Attorneys' fees in the amount of $234,063 are awarded in favor of Grant & Eisenhofer and judgment is entered accordingly in plaintiffs favor and against defendants;

(2) Costs in the amount of $93,935 are assessed against defendants and in favor of plaintiff; and

(3) This action, upon payment of the sums of money identified in paragraphs (1) and (2) above, is DISMISSED with prejudice.

William B. Chandler III
Chancellor

Dated: April 9, 2002