

United States District Court
For the Northern District of California

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E-FILED on 9/29/2008

IN THE UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF CALIFORNIA
SAN JOSE DIVISION

In re LEAPFROG ENTERPRISES, INC.
SECURITIES LITIGATION,

No. C-03-05421 RMW

ORDER GRANTING LEAD PLAINTIFF'S
APPLICATION FOR AWARD OF
ATTORNEY'S FEES AND
REIMBURSEMENT OF EXPENSES

This Document Relates To:

ALL ACTIONS.

Lead plaintiff Parnassus Fund and Parnassus Equity Income Fund ("The Parnassus Fund" or "Fund") apply for an award of attorney's fees and reimbursement of expenses following the settlement of this class-action securities fraud litigation. The court has received objections to the request for attorney's fees from G. Norman, Natasha L. Engan and the National Automatic Sprinkler Industry Pension Fund, and the Parnassus Fund has responded to these objections. The court has reviewed these papers and considered the arguments of counsel. For the following reasons, the court approves a reimbursement of expenses of \$82,343.23 and an award of attorney's fees of \$443,531.35.

I. BACKGROUND

ORDER GRANTING LEAD PLAINTIFF'S APPLICATION FOR AWARD OF ATTORNEY'S FEES AND REIMBURSEMENT OF EXPENSES
No. C-03-05421 RMW
TSF

1 **A. Procedural History Prior to Settlement**

2 The first of these four consolidated cases was filed on December 2, 2003. *See* C-05-05421-
3 RMW, Docket No. 1 (N.D. Cal. Dec. 2, 2003). The court held a hearing to select a lead plaintiff and
4 lead counsel and to decide whether to consolidate the various actions. *See* Docket No. 79 (Mar. 19,
5 2004). Complications ensued, and the court ended up appointing a different lead plaintiff and lead
6 counsel than it intended at the initial hearing. *See* Docket No. 106 (Mar. 31, 2005). Additional
7 jockeying for lead plaintiff and lead counsel status followed, delaying the litigation. *See* Docket No.
8 141 (July 27, 2005). Nevertheless, by the end of 2005, the court had selected the Parnassus Fund as
9 lead plaintiff and approved its counsel as lead counsel. *See In re Leapfrog Enterprises, Inc. Sec.*
10 *Litig.*, 2005 WL 3801587 (N.D. Cal. Nov. 23, 2005). The Parnassus Fund then filed an amended,
11 consolidated class action complaint on January 27, 2006. *See* Docket No. 191.

12 The defendants promptly moved to dismiss, *see* Docket Nos. 194, 195 (Mar. 27, 2006), and
13 the court granted the motions. *In re Leapfrog Enterprises, Inc. Sec. Litig.*, 2006 WL 2192116 (N.D.
14 Cal. Aug. 1, 2006). The Parnassus Fund amended its complaint, the defendants moved to dismiss,
15 and the court again granted the motions. *In re Leapfrog Enterprises, Inc. Sec. Litig.*, 527 F. Supp.
16 2d 1033 (N.D. Cal. Sept. 30, 2007). The Parnassus Fund filed a Third Amended Consolidated
17 Complaint on November 21, 2007. *See* Docket No. 267.

18 **B. The Settlement Filings**

19 The parties then reached a settlement and sought preliminary approval. *See* Docket No. 274
20 (Apr. 18, 2008). After reviewing the terms, the proposed notice form, and the other pertinent
21 details, the court granted preliminary approval and scheduled a fairness hearing for July 18, 2008.
22 *See* Docket No. 276 (May 1, 2008).

23 The court received no objections to the terms of the settlement and at the hearing remarked
24 that the settlement appeared fair, reasonable and adequate. *See* Docket No. 288 (Jun. 18, 2008)
25 (civil minutes). To accommodate objections to the attorney's fee request, however, the court
26 continued the final approval hearing to September 19, 2008. *See* Docket Nos. 289 (Jun. 25, 2008)
27 (scheduling order), 300 (Aug. 21, 2008) (stipulation continuing hearing).

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II. ANALYSIS

The Parnassus Fund negotiated a settlement of \$2,300,000 in cash. The Parnassus Fund's counsel now requests 20% of this gross recovery (\$460,000), plus reimbursement of \$82,343.23 in expenses.

A. The Effect of the Fund's Agreement With Counsel

1. The Fund's Retention of its Attorneys

When the court appointed the Parnassus Fund as lead plaintiff, it noted that the Fund claimed to have suffered approximately \$10 million in damages. *Leapfrog*, 2005 WL 3801587 at *2. The Parnassus Fund therefore retained its attorneys (Cohen, Milstead, Hausfeld & Toll and Berman Devalerio Pease Tabacco Burt & Pucillo), and those attorneys were then selected as lead counsel.

See id.

In support of the attorney's fee application, Matthew K. Handley (one of the Fund's attorneys from Cohen, Milstead) declares that his firm "seeks a fee award that results from a negotiated agreement with the Lead Plaintiff." Docket No. 285 ¶ 54 (Jun. 11, 2008) ("Handley Decl."). Mr. Handley also states that "Lead Plaintiff has worked with Lead Counsel throughout the prosecution and settlement of the litigation, is familiar with the work done by Lead Counsel, and supports the fee request presently before the Court." *Id.* The declaration does not, however, include a copy of the retainer agreement between the Fund and its attorneys.

In further support of the application, Jerome L. Dodson has filed a declaration. Docket No. 301 (Sept. 11, 2008). Mr. Dodson is the founder and president of Parnassus Investments and the portfolio manager for the Parnassus Fund. *Id.* ¶ 2. Mr. Dodson states that:

I also decided it best to await the results of the litigation before deciding what was a fair and reasonable fee as I believed the outcome of the case and the time spent by class counsel litigating the case would be factors that I would need to assess. . . . Given all of the circumstances , including the diligent and excellent work of class counsel, I believe a fee of 20% of the Settlement Fund is fair and reasonable to the class, *which is why I agreed to that percentage after the recovery was obtained* and before class counsel submitted their fee petition.

Id. ¶ 6 (emphasis added). Based on this, it appears that the Parnassus Fund agreed to retain its counsel, but that it did not agree to any amount of attorney's fees until after the case had settled.

1 plaintiff's counsel's fee request is reasonable depends on lead plaintiff and lead counsel negotiating
2 such a fee *ex ante*, any such presumption would not apply in this case.

3 Indeed, the Seventh Circuit has incorporated this *ex ante* perspective into the requirement
4 that any award of attorney's fees correspond to a "reasonable percentage" of the damages paid to the
5 class. *Sutton v. Bernard*, 504 F.3d 688, 692 (7th Cir. 2007). The court explained that where
6 "attorneys' fee had not been determined up front," the court must consider "the terms to which the
7 private plaintiffs and their attorneys would have contracted at the outset of the litigation when the
8 risk of loss still existed." *Id.* To that end, courts in the Seventh Circuit look to "(1) actual fee
9 agreements; (2) data from large common fund cases where the parties negotiated the fees privately,
10 and (3) bids and results from class counsel auction cases for insight into the fee levels attorneys in
11 competition were willing to accept." *Id.* at 692 & fn.2.

12 Despite the appeal of the Seventh Circuit's reasoning, the Ninth Circuit does not appear
13 likely to embrace a rule that fees must be determined on an *ex ante* (or hypothetical *ex ante*) basis.
14 In reversing a trial court's selection of lead plaintiff on the basis that plaintiff had negotiated the
15 lowest percentage contingent fee for his attorney's services as opposed to being the plaintiff with the
16 largest stake in the litigation, the Ninth Circuit explained that the statute requires that the "actual
17 fees paid will be subject to close judicial scrutiny based on counsel's actual work done and results
18 achieved." *In re Cavanaugh*, 306 F.3d 726, 733 (9th Cir. 2002). It was therefore unreasonable for
19 the trial court to rely on the plaintiff's having negotiated a low fee because "negotiations with
20 counsel before lead plaintiff has even been appointed have an inherently hypothetical and contingent
21 quality, making them a relatively poor indicator of plaintiff's adequacy to serve as lead." *Id.* In
22 further explaining the district court's role in approving a request for attorney's fees, the court noted
23 that "at best, such an agreement serves as a cap, because the court will seldom approve a fee award
24 that exceeds the terms of the retainer agreement, but the court has wide latitude to go below the
25 agreed amount in actually awarding fees." *Id.* at 733, fn. 13.

26 The only other Ninth Circuit case addressing the reasonableness of fees paid to attorneys
27 under the PSLRA is in accord. *Powers v. Eichen*, 229 F.3d 1249, 1258 (9th Cir. 2000). In *Powers*,

1 the court remarked that the PSLRA "simply requires that the fees and expenses ultimately awarded
 2 be reasonable in relation to what the plaintiffs recovered." *Id.* It bears noting, however, that the
 3 *Powers* court also held that "[a]lthough the new provision requires reasonable fees and expenses, it
 4 does not mandate a particular approach to determining fees." Thus, it is unclear whether
 5 *Cavanaugh's* dictum regarding using retention agreements as a cap on recoveries can be reconciled
 6 with *Powers*. Nonetheless, the two cases are harmonious with respect to their emphasis on
 7 considering reasonableness *ex post*, i.e., based on what the class recovered. The Ninth Circuit's
 8 interpretation of the PSLRA thus seems to require the court to scrutinize attorney's fees requests
 9 even if the lead plaintiff and lead counsel have engaged in arms-length negotiations (regardless of
 10 when they occurred). Accordingly, the court cannot accept Mr. Dodson's judgment for the court.²
 11 Whether the 20% fee request is reasonable must be determined based on the work counsel has done
 12 and the results they have achieved.

13 **B. The Work Performed & Counsel's Lodestar**

14 The Handley Declaration states that the Fund's counsel devoted 3,945.60 hours, which works
 15 out to \$1,685,394.00 when applied to the rates of those who worked on the case. Handley Decl. ¶
 16 50. To substantiate that figure, Mr. Handley includes two exhibits compiling tables of the work
 17 performed by the Fund's two law firms, reproduced below in full:

NAME (STATUS)	TOTAL HOURS	CURRENT RATE	TOTAL LODESTAR
<u>Partners</u>			
S. Toll	454.00	\$710.00	\$322,340.00
A. Friedman	0.25	\$575.00	\$143.75
D. Sommers	5.75	\$575.00	\$3,306.25
<u>Of Counsel</u>			
E. Berney	1,554.00	\$485.00	\$748,840.00
C. Torrell	55.25	\$485.00	\$26,796.25

26 _____
 27 ² Of the 3,945.60 hours counsel purportedly spent on this case, 7.00 hours were spent in
 28 "discussions with lead plaintiff and class members regarding case." This suggests that, even under
 the PSLRA, the lead plaintiff may not have meaningfully controlled this litigation

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<u>Associates</u>			
M. Handley	462.00	\$335.00	\$154,770.00
B. Lehman	57.75	\$295.00	\$17,036.25
J. Leviton	43.25	\$315.00	\$13,623.75
<u>Law Clerks</u>			
J.D. Burns	0.25	\$180.00	\$45.00
<u>Paralegals</u>			
G. Buck	15.75	\$200.00	\$3,150.00
D. Choi	2.00	\$175.00	\$350.00
S. Evans	78.75	\$200.00	\$15,750.00
M. A-Fallon	80.00	\$175.00	\$14,000.00
K. Fiore	71.25	[blank in filing]	\$14,250.00
D. Frusco	14.75	\$140.00	\$2,065.00
P. Macker	1.00	\$200.00	\$200.00
E. Schulz	24.75	\$200.00	\$4,950.00
R. Smits	2.00	\$200.00	\$400.00
E. Takas	0.50	\$200.00	\$100.00
<u>Paralegals Assts.</u>			
K. Brenner	14.50	\$155.00	\$2,247.50
C. Sherman	11.50	\$155.00	\$1,782.50
TOTAL LODESTAR	2,939.25		\$1,346,146.25

NAME (STATUS)	TOTAL HOURS	CURRENT RATE	TOTAL LODESTAR
<u>Partners</u>			
Joseph J. Tabacco, Jr.	27.40	\$690.00	\$18,906.00
Christopher T. Heffelfinger	21.50	\$610.00	\$13,115.00
Nicole Lavallee	227.60	\$610.00	\$138,836.00
Leslie Stern	2.00	\$460.00	\$920.00
<u>Of Counsel</u>			
Stacey Dana	0.40	\$420.00	\$168.00

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<u>Associates</u>			
Jay Eng	1.50	\$345.00	\$517.50
Deborah Evans	12.00	\$315.00	\$3,780.00
Julie Bai	281.80	\$265.00	\$74,677.00
Matthew Pearson	2.50	\$235.00	\$587.50
James Magid	10.75	\$235.00	\$2,526.25
Kristin Madigan	3.00	\$200.00	\$600.00
<u>Paralegals</u>			
Deborah Vanore	104.00	\$210.00	\$21,840.00
Jeannine Scarsciotti	9.75	\$210.00	\$2,047.50
Jeffrey Gates	51.00	\$180.00	\$9,180.00
Melroy Atkins	1.00	\$180.00	\$180.00
Gracynthia Claw	37.00	\$170.00	\$6,290.00
Anna Hale	20.00	\$165.00	\$3,300.00
Jacob Strom	12.50	\$160.00	\$2,000.00
Yelena Soboleva	79.15	\$80.00	\$6,332.00
<u>Investigators</u>			
Christopher Szechenyi	100.50	\$330.00	\$33,165.00
Robin Estrin	1.00	\$280.00	\$280.00
TOTAL LODESTAR	1,006.35		\$339,247.75

Id., Exs. 2 & 3. Based on these billing records, counsel submits that their request amounts to a "negative multiplier." Putting aside nomenclature, counsel's requested fee is purportedly 27% of their "billing."

This lodestar calculation is a helpful "cross-check" on the reasonableness of the requested attorney's fees. *In re Chiron Corp. Secs. Litig.*, 2007 WL 4249902 (Nov. 30, 2007) (Walker, C.J.). But a lodestar calculation is only as reasonable as the numbers that go into it, and a non-exhaustive review of the submissions suggests that this lodestar is inflated.

To begin, counsel's initial submissions do not reveal what the attorneys *did* to justify the large number of hours they billed. This want of information makes it impossible for the court to

1 gauge the reasonableness of the figures submitted above. The supplemental submissions of Joseph
2 Tabacco and Matthew Handley (docket nos. 295 and 296, filed August 15, 2008) break down each
3 attorney's hours, though into somewhat vague categories. Yet as opaque as the categories are, what
4 they reveal is telling. The Cohen firm alone spent 554.00 hours on "research for and drafting of
5 opposition to motion to dismiss first amended complaint."³ While the opposition was fifty pages
6 long, this suggests that counsel billed more than 11 hours *per page* of that opposition. The Cohen
7 firm then spent 424.50 hours on "research for and drafting of the opposition to motion to dismiss
8 second amended complaint." While the opposition again totaled fifty pages, it addressed the same
9 issues as the first opposition (whether the statements were actionable, whether a strong inference of
10 scienter had been alleged, and whether loss causation had been alleged). It is difficult to imagine the
11 second opposition required as much research as the first, yet the Cohen firm billed almost as much
12 time on it.

13 Yet more questionable is that the Cohen firm then spent 257.00 hours on "oral argument of
14 motion to dismiss first amended complaint and preparation for argument." Mr. Toll (who argued the
15 motion) claims to have spent 63.75 hours in preparation for oral argument, while Ms. Berney (who
16 did not argue the motion) claims to have spent another 168.00 hours preparing for the argument.
17 Assuming Ms. Berney can bill 12 hours a day, her records suggest that she spent 14 *days* preparing
18 for an oral argument she did not make. It would have been unreasonable to have spent that much
19 time preparing for argument (especially after the time spent preparing the opposition), leading the
20 court to believe that these time records have been substantially padded.

21 In addition to inflating the number of hours worked, the "rates" for that work are not
22 reasonable. For example, the Cohen firm's paralegals bill at between \$160 and \$210 per hour (with
23 one exception). But the prevailing market rate for paralegals in Washington D.C. was about \$125
24 per hour. *Chiron*, 2007 WL 4249902 at *6. Even in New York, the prevailing market rate was only
25 \$131.25. *Id.* Nothing in the record explains why, for example, Deborah Vanore's paralegal work

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27 ³ The Berman firm did not allocate its time by task, but instead reported lumped categories
28 like "pleadings, briefs and pretrial motions (includes legal research)."

1 justifies a billing rate 68% above the market rate.

2 The court sympathizes with the objectors' concerns in light of the issues discussed above.
3 Nevertheless, the court cannot agree with the objectors that this fee request is unreasonable. Even
4 after slashing the number of hours billed and rate charged, the multiplier does not substantially
5 exceed 1, let alone the multiplier of 2 to 3 often deemed reasonable in this type of case. *See Chiron*,
6 2007 WL 4249902 at *8-*9. The contingent nature of the case created a substantial risk that the
7 Fund's attorneys would recover nothing given the difficulties posed by this case. The relatively
8 small recovery also does not raise concerns that the attorneys have struck a bonanza at the expense
9 of the class. *See id.* In light of these difficulties, a 20% contingency fee "does not exceed a
10 reasonable percentage of the amount of any damages and prejudgment interest actually paid to the
11 class." Accordingly, the court approves a 20% contingency fee in this case.

12 Though the court agrees with the Fund's counsel's proposed contingency fee, the court cannot
13 agree that the attorneys should recover their fee from the \$2,300,000 gross recovery. The court has
14 the discretion to award a reasonable fee based on either a net or gross calculation. *Powers*, 229 F.3d
15 at 1258. While the Ninth Circuit has held that the PSLRA does not *require* the attorney's fee award
16 to be based on the class' net recovery, the court believes this to be the best practice because it bases
17 the attorney's fee on what the class actually receives. It also encourages the counsel to carefully
18 monitor the costs incurred.

19 The court has reviewed the \$82,343.23 in expenses reported by the Fund's counsel, and
20 agrees that they were reasonably incurred in pursuing this case. The court therefore authorizes a
21 reimbursement of \$82,343.23 to counsel for their expenses. This results in a net recovery for the
22 class of \$2,217,656.77. Applying the 20% contingency fee, the court authorizes an award of
23 attorney's fees of \$443,531.35.

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III. ORDER

For the foregoing reasons, the court approves a reimbursement of expenses of \$82,343.23 and an award of attorney's fees of \$443,531.35.

DATED: 9/29/2008



RONALD M. WHYTE
United States District Judge

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19 Counsel are responsible for distributing copies of this document to co-counsel that have not
20 registered for e-filing under the court's CM/ECF program.

22 **Dated:** 9/29/2008

TSF
Chambers of Judge Whyte