Fee Award Nixed After Client Abandons Case

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In a neat, short opinion, the Delaware Supreme Court dealt with a situation that the chief justice characterized as "Kafkaesque" at oral argument and "unusual" in the written opinion. In *Crothall v. Zimmerman*, No. 608, 2013 (Del. June 9, 2014), the court reversed a fee award to plaintiffs' counsel who had personally intervened in the case below solely for the purpose of seeking attorney fees for the work he had performed in the litigation after the plaintiff had abandoned the lawsuit prior to the entry of a final judgment. The court held that the plaintiff's former counsel did not create a corporate benefit and was not entitled to attorney fees because the plaintiff did not obtain an authoritative ruling of the Court of Chancery that could create a corporate benefit.

The plaintiff, Robert Zimmerman, was a common unitholder of Adhezion Biomedical LLC. Zimmerman brought a derivative action against the directors of Adhezion and two Adhezion investors challenging certain financing transactions and the issuance of additional units by Adhezion. Zimmerman alleged that the financing transactions were substantively unfair and thus violated the directors' fiduciary and contractual duties, and that the issuance of the additional units was not made in conformity with Adhezion's operating agreement because it had not been authorized by a separate vote of common unitholders as required by the agreement. After trial, the Court of Chancery rejected Zimmerman's substantive unfairness claims, but upheld Zimmerman's claim that the issuance of the units violated the operating agreement. However, because the breach of the operating agreement caused no damage, the Court of Chancery awarded only nominal damages in *Zimmerman v. Crothall*, C.A. No. 6001-VCP (Del. Ch. Oct. 14, 2013).

Before the parties could agree on the form of a final judgment, Zimmerman told his counsel that he was abandoning the lawsuit. Zimmerman subsequently sold all of his units in the company. Zimmerman's counsel filed a motion to withdraw as his counsel, but sought to intervene as an interested party in order to seek attorney fees for the work he had performed in the litigation. The defendants then moved to dismiss the litigation since Zimmerman lacked standing to continue as a derivative plaintiff and there was no other plaintiff with standing to pursue the case. The Court of Chancery granted the motion to dismiss. As a result, no final judgment from which the defendants could appeal was entered on the claim that the Court of Chancery found meritorious.

However, that did not end the matter in the Chancery Court. In a move that the Supreme Court characterized as "an odd development," the court also granted Zimmerman's counsel leave to intervene, over defendants' opposition, to seek attorney fees for creating a corporate benefit. The Court of Chancery awarded Zimmerman's former counsel $300,000 in attorney fees, finding a corporate benefit in the court's ruling that a vote of the common unitholders was required to authorize the issuance of additional units. As the Supreme Court noted, Zimmerman's former counsel was granted a nearly full recovery even though the one claim on which Zimmerman prevailed was never the subject of an appealable final judgment, Zimmerman did not prevail on most of his claims, and most of counsel's time had been spent on the claims that he lost.

The defendants appealed and sought to have the Supreme Court consider the merits of the Court of Chancery's ruling on the claim that underlay the determination that Zimmerman's former counsel had created a corporate benefit, even though that claim had been dismissed. Zimmerman's former counsel argued that the court could not review the ruling, since the claim had been dismissed, and the only issue before the court was whether the fee award was reasonable and not excessive.

The Supreme Court refused to address the merits of the Court of Chancery's mooted ruling on the dismissed claim. Instead, it held that Zimmerman's former counsel did not create a corporate benefit on which a fee award could be based. According to the court, when Zimmerman mooted the case by abandoning his claim and selling his units, causing the dismissal of his claims, he also rendered any rulings he had obtained incapable of being turned into an appealable final judgment. Thus, he did not obtain an authoritative ruling of the Court of Chancery that could create a corporate benefit. A plaintiff who generates a favorable trial court decision on a closely contested issue of corporate governance but then abandons his claim and renders the decision moot before it becomes final has not created a corporate benefit. To hold otherwise, the court said, would put the court in the untenable position of having to render a decision on a mooted issue of corporate governance merely to assure that the defendants had not been improperly asked to bear plaintiff's former counsel's fee. The court distinguished the circumstances of this case, where the plaintiff mooted the case and caused the dismissal of the claims before final judgment, from those cases where the claims were rendered moot because of actions taken by the defendants that created the corporate benefit that the plaintiffs had been seeking and for which they were entitled to have their attorney fees paid.

One other aspect of the decision is worth noting. The court went out of its way to say that nothing in its opinion should be considered as suggesting that the Court of Chancery properly granted the motion to intervene by Zimmerman's former counsel. The court referred to that motion as an "odd procedural circumstance" and an "unusual application." Rather than seeking to intervene personally in the case, the court suggested in a footnote that the more traditional remedy would have been for Zimmerman's former counsel to sue his client for his fees in accordance with his contract with the client. (At oral argument, when asked if he had sued his former client for fees, counsel said only that he had not sued his client "yet.") The court went on to say that lawyers are not permitted to sue corporate directors without a stockholder client and if the client quits the litigation and renders his claims moot, it is not obvious why the lawyer would be personally permitted to sue the corporation for having represented the former client. Permitting a lawyer in a representative action to recover from the company directly creates incentives of a troubling nature in an area of law already fraught with potential conflict.

What are the lessons to be learned from this case? First, no corporate benefit is created when a plaintiff stockholder abandons his lawsuit before a final, appealable judgment. Second, it is unlikely that a future court will permit former counsel for a plaintiff who has abandoned his lawsuit and rendered it moot to intervene personally in the lawsuit for the purpose of seeking attorney fees. Finally, counsel's remedy, if any, is to seek damages from his former client, which means making appropriate provisions for such circumstances in his engagement letter.

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