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Seventh Circuit Pans Pursuit of Mootness Fees, Urges Further Judicial Scrutiny of "Problematic" Merger Objection Cases

On April 15, 2024, the Seventh Circuit issued an opinion written by Judge Frank H. Easterbrook in *Alcarez* v. *Akorn, Inc.*, criticizing the plaintiffs' bar for pursuing "mootness fees" in merger objection cases, and outlining potential mechanisms by which courts can scrutinize mootness fees even following the voluntary dismissal of such cases.[1]

Background

The announcement of a public company merger almost inevitably invites dozens of shareholder litigations challenging the target company's disclosures under Section 14(a) of the Securities Exchange Act of 1934, or challenging the board's approval of the deal as a breach of fiduciary duty. Following the Delaware Court of Chancery's decision in *In re Trulia, Inc. Stockholder Litigation*, 129 A.3d 884 (Del. Ch. 2016), these cases are rarely litigated; instead, companies typically resolve the actions by issuing supplemental disclosures and then agreeing to pay a "mootness fee" to plaintiffs' counsel. Plaintiffs' firms often bring these cases as individual actions rather than class actions to evade the requirements of the Private Securities Litigation Reform Act of 1995 ("PSLRA"). Many other plaintiffs' firms bring their allegations in the form of demand letters, to avoid having to file a case and risk judicial scrutiny altogether.[2]

In recent years, federal courts have criticized merger objection cases as "no better than a racket" that "must end,"[3] and have in some cases rejected plaintiffs' firms' efforts to extract attorneys' fees from companies after they have issued supplemental disclosures.[4] The Seventh Circuit's decision in *Akorn* highlights tools that courts can use to apply further scrutiny to mootness fees in such cases.

Procedural History

The *Akorn* case involved attorney and Akorn shareholder Theodore Frank, who was concerned about the rampant proliferation of merger objection lawsuits and mootness fees taking money from corporate treasuries.

[1] *Alcarez* v. *Akorn, Inc.*, Nos. 18-2220, 18-2221, 18-2225, 19-2401, 19-2408, --- F.4th ----, 2024 WL 1617389 (7th Cir. Apr. 15, 2024).

[2] *See generally* Matthew D. Cain, et. al., *Mootness Fees*, 72 VAND. L. REV. 1777 (2019).

[3] *In re Walgreen Co. S'holder Litig.*, 832 F.3d 718, 724 (7th Cir. 2016).

[4] *See, e.g., Serion* v. *Nuance Commc'ns, Inc.*, 2022 WL 356695, at *3 (S.D.N.Y. Feb. 7, 2022).

In 2017, after Akorn announced its proposed merger with Fresenius Kabi AG, six Akorn shareholders filed lawsuits challenging the adequacy of the disclosures.[5] Five of these were filed as class actions, which many plaintiffs' firms have stopped doing. Akorn subsequently revised its proxy statement to include additional disclosures, and plaintiffs voluntarily dismissed their suits, asserting that the additional disclosures mooted their complaints.[6] Counsel informed the court that their claim to attorneys' fees and costs had been resolved by Akorn's payment of $322,500 in "mootness fees."[7]

Frank moved to intervene, and sought to require plaintiffs' counsel to disgorge the mootness fees back to Akorn and to enjoin them from filing future "strike suits," pursued "for the sole purpose of obtaining fees for the plaintiffs' counsel."[8] The district court denied Frank's motion, finding that he had not identified an interest in the case justifying his intervention.[9] However, mindful of the Seventh Circuit's previous admonition in *Walgreen* that disclosure litigation is a "racket" that "must end,"[10] and "concerned with the plaintiffs' apparent success in evading the requirements of Rule 23," the district court invited Frank to file a motion for reconsideration.[11] Although the district court again denied his motion to intervene, it determined to "exercise its inherent powers to police potential abuse of the judicial process—and abuse of the class mechanism in particular—and require plaintiffs' counsel to demonstrate" that the disclosures they sought corrected a "plainly material" misrepresentation or omission.[12]

The district court ultimately held that the disclosures were not plainly material and instead "were worthless to the shareholders."[13] In an "exercise [of] its inherent authority to rectify the injustice that occurred," the district court abrogated the settlement agreements and ordered plaintiffs' counsel to return the mootness fees to Akorn.[14] Plaintiffs' counsel appealed.

The Seventh Circuit's Decision

On appeal, plaintiffs challenged the district court's assertion of its "inherent authority" to review the mootness fees after they had voluntarily dismissed their cases.

The Seventh Circuit agreed that the district court had erred in reopening the cases without a motion under Rule 60(b).[15] Nevertheless, it noted that the PSLRA, "affect[s] the proper treatment of suits filed in quest of mootness fees."[16] Specifically, the PSLRA dictates that upon "final adjudication" of a securities class action brought under the Exchange Act, courts must "include in the record specific findings" as to whether the parties complied with Rule 11(b) of the Federal Rules of Civil Procedure—including that the lawsuit was not filed "for any improper purpose" and the claims are supported by the law.[17]

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[5] Five of the six cases were filed as class actions, but all were dismissed before plaintiffs sought class certification. *Alcarez*, 2024 WL 1617389, at *1.

[6] *Id.*

[7] *Id.*

[8] *House* v. *Akorn, Inc.*, 2018 WL 4579781, at *1 (N.D. Ill. Sept. 25, 2018) ("*House I*").

[9] *Id.*

[10] *In re Walgreen Co. S'holder Litig.*, 832 F.3d 718, 724 (7th Cir. 2016).

[11] *House I*, 2018 WL 4579781, at *1.

[12] *Id.* at *3.

[13] *House* v. *Akorn, Inc.*, 385 F. Supp. 3d 616, 623 (N.D. Ill. 2019) ("*House II*").

[14] *Id.*

[15] *Akorn*, 2024 WL 1617389, at *2, *6.

[16] *Id.* at *4.

[17] *Id.* at *5; 15 U.S.C. § 78u-4(c)(1).

Applying the PSLRA to the dispute at hand, the Seventh Circuit reasoned that the voluntary dismissal of each suit was a "final adjudication of the action," and therefore, the district court was obligated to "determine whether each suit was proper" under Rule 11(b) "at the moment it was filed."[18] Despite the district court's invocation of its "inherent authority" rather than the PSLRA and Rule 11(b), the Seventh Circuit "agree[d] with the district judge's analysis," which in substance had found that the complaints violated Rule 11(b).[19] The Seventh Circuit also noted that Rule 11(c)(4) "gives the district judge discretion over the choice of sanction," and therefore the court was "entitled to direct counsel who should not have sued at all to surrender the money they extracted from Akorn."[20]

The Seventh Circuit thus remanded with instructions to treat Frank as an intervenor, allow him to move under Rule 60(b) to reopen the cases, and determine the appropriate relief, if any, under the PSLRA and Rule 11(b).

Implications

The Seventh Circuit's opinion once again takes issue with "problematic" merger objection cases and the "racket" mootness fee practices by the plaintiffs' bar.[21] The decision sends a strong message that courts should consider being more proactive in policing these suits.

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[18] *Akorn*, 2024 WL 1617389, at *5.

[19] *Id.* at *5–6.

[20] *Id.* at *6.

[21] *Id.* at *2.

This memorandum is not intended to provide legal advice, and no legal or business decision should be based on its content. Questions concerning issues addressed in this memorandum should be directed to:

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