UNITED STATES DISTRICT COURT
DISTRICT OF MINNESOTA

MICHAEL TATE, JOSEPH SHUSTER, LYLE EVANSON and JOHN AYERS, individually and on behalf of all others similarly situated, Plaintiff v. RESTAURANT TECHNOLOGIES, INC., PARTHENON CAPITAL LLC, JEFFREY R. KIESEL, JOHN C. RUTHERFORD, JONATHAN O. GRAD, ZACHARY F. SADEK, PHILIP A. CLOUGH and ROBERT E. WEIL, Defendants	Civil File No. 09-cv-02076 (MJD/JJG) **OBJECTION OF GEMINI INVESTORS III, L.P. TO CLASS CERTIFICATION AND CLASS ACTION SETTLEMENT**

This Court conditionally certified a class consisting of certain common and preferred stockholders in Defendant Restaurant Technologies, Inc. ("RTI") as of May 13, 2009. Because of an irreconcilable conflict of interest between the common and preferred stockholders, the Court should reject the proposed settlement and decertify the class so that subclasses can be created with separate lead plaintiffs and counsel.

Gemini Investors III, L.P. ("Gemini") does not object to the amount of the proposed settlement. Gemini's objection is based on the unavoidable conflict of interest between the common and preferred shareholders in the proposed class and the resulting proposed Plan of Allocation of the settlement proceeds among these differing interests. In drafting the proposed settlement allocation, there was no

separate and distinct representation, as specifically required by the Supreme Court in its interpretation of Federal Rule of Procedure 23, of the differing interests within the Plaintiff Class. As a result, the proposed Plan of Allocation imposes an unjustifiable allocation of settlement proceeds between preferred and common shareholders, by inappropriately treating preferred shares as having little more value than common shares.

Under these circumstances, and based on controlling Supreme Court precedent, the Court cannot as a matter of law certify a class consisting of both preferred and common shareholders, because the class representatives cannot fairly and adequately represent the interest of the entire class. Similarly, the proposed settlement allocation is inequitable because the conflict of interest led to a settlement that unjustly favored common shareholders over preferred shareholders.

I. Summary of Facts

In a series of transactions from 2001 through 2008, Gemini invested over $5.2 million in RTI, for which Gemini was issued primarily preferred stock, plus a small amount of common stock. Declaration of Mehran Ahmed ("Ahmed Decl.") ¶¶ 4-5, filed herewith. Gemini was never a controlling shareholder of RTI. Id. ¶ 7. Gemini's preferred stock carried with it two valuable benefits. In the event of a sale or liquidation, Gemini's shares would be satisfied in full prior to the common stock. Id. ¶ 6. In addition, Gemini's shares carried annual accretion percentages such that Gemini would be repaid more than it had invested. Id.

Plaintiffs filed a class action lawsuit alleging that Defendants took control of

RTI and used that control to the detriment of both common and certain preferred shareholders, including Gemini, by diverting RTI's equity to themselves. Notice of Proposed Settlement of Class Action and Hearing Regarding Settlement (Document 150-1) at 7. Plaintiffs allege that this misconduct culminated in a 2009 recapitalization which harmed both common and preferred shareholders. Id.

The three original named plaintiffs held only common shares prior to the 2009 recapitalization. Complaint ¶¶ 1-3 (Document 1-1). It was not until eight days before the filing of a motion for class certification that they added a named plaintiff who held some preferred shares, though he still held more common shares than preferred. First Amended Complaint ¶¶ 1-4 (Document 58). The vast majority of the named plaintiffs' shares were common (171,423) as opposed to preferred (6,228). Ahmed Decl. Ex. B, p. 2.

The class which Plaintiffs purport to represent consists of all common and Series A preferred shareholders prior to the 2009 recapitalization, but excluding the Defendants and related parties. Notice of Proposed Settlement of Class Action and Hearing Regarding Settlement (Document 150-1) at 3 ¶ 2. If that class were certified, it would consist of the holders of 1,251,015 common shares and 329,455 preferred shares. Gemini held 68.3% of those preferred shares. Ahmed Decl. Ex. B, p. 2.

II. Legal Argument

A. The Class Representatives Cannot Fairly and Adequately Represent the Class Because the Class Consists of Preferred and Common Shareholders Who Have Conflicting Interests.

1. Controlling Supreme Court precedent prevents class certification where distinct groups within the class have conflicting interests.

The Court cannot certify a class unless "the representative parties will fairly and adequately protect the interests of the class." Fed. R. Civ. P. 23(a)(4). "The focus of Rule 23(a)(4) is whether: (1) the class representatives have common interests with the members of the class, and (2) whether the class representatives will vigorously prosecute the interests of the class through qualified counsel." Burch v. Qwest Commc'ns Intern., Inc., 677 F. Supp. 2d 1101, 1127–28 (D. Minn. 2009). The party seeking class certification bears the burden of establishing that it has satisfied each of Rule 23's class certification requirements. Lockwood Motors, Inc. v. GM Corp., 162 F.R.D. 569, 573 (D. Minn. 1995).

The Supreme Court has warned that Rule 23's protections "demand undiluted, even heightened, attention in the settlement context. Such attention is of vital importance, for a court asked to certify a settlement class will lack the opportunity, present when a case is litigated, to adjust the class, informed by the proceedings as they unfold." AmChem Prods., Inc. v. Windsor, 521 U.S. 591, 620 (1997).[1] "The adequacy inquiry under Rule 23(a)(4) serves to uncover conflicts of

[1] Accord Vervaecke v. Chiles, Heider & Co., 578 F.2d 713, 719 (8th Cir. 1978) ("'[T]he adequacy of the representation issue is now of critical importance in all class actions and the court is under an obligation to pay careful attention to the Rule

interest between named parties and the class they seek to represent." Id. at 625.

In AmChem, the Supreme Court denied certification of a class of asbestos victims because the proposed class contained individuals who had already manifested asbestos-related diseases as well as individuals who had only been exposed to asbestos. Id. at 625-28. The interests of these discrete subgroups were in conflict because currently-injured plaintiffs would favor generous immediate payments, while exposure-only plaintiffs would favor an inflation-protected fund for the future. Id. at 626.

The Court reasoned that "the terms of the settlement reflect essential allocation decisions designed to confine compensation and to limit defendants' liability. For example, . . . the settlement includes no adjustment for inflation; only a few claimants per year can opt out at the back end; and loss-of-consortium claims are extinguished with no compensation." Id. at 627. "The settling parties, in sum, achieved a global compromise with no structural assurance of fair and adequate representation for the diverse groups and individuals affected. Although the named parties alleged a range of complaints, each served generally as representative for the whole, not for a separate constituency." Id.

The Court quoted with approval language particularly instructive here from a prior Circuit Court opinion. In that case, the Second Circuit had rejected class certification due to conflicting interests among class members even where the class

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23(a) (4) prerequisite in every case.'") (quoting Wright & Miller, *Federal Practice and Procedure* § 1765, at 616-17 (1972)).

representatives as a whole included both groups of plaintiffs. As quoted by the Supreme Court:

> Where differences among members of a class are such that subclasses must be established, **we know of no authority that permits a court to approve a settlement without creating subclasses on the basis of consents by members of a unitary class, some of whom happen to be members of the distinct subgroups**. The class representatives may well have thought that the Settlement serves the aggregate interests of the entire class. But the adversity among subgroups requires that the **members of each subgroup cannot be bound to a settlement except by consents given by those who understand that their role is to represent solely the members of their respective subgroups**. (Id. at 627, quoting In re Joint Eastern and Southern Dist. Asbestos Litigation, 982 F.2d 721, 742-743 (2nd Cir. 1992), modified on reh'g sub nom. In re Joint E. & S. Dist. Asbestos Litig., 993 F.2d 7 (2nd Cir. 1993) (emphasis added)).[2]

2. The Court cannot certify a class containing both preferred and common shareholders without creating subclasses and appointing separate class representatives for each subclass.

The lessons of AmChem apply squarely to this case, because the common and preferred shareholders are in direct conflict over the structure and allocation of the settlement proceeds. The class representatives have advanced a Plan of Allocation valuing the preferred shares at $2.92 per share and the common shares at $2.14 per share. Notice of Proposed Settlement of Class Action and Hearing Regarding Settlement (Document 150-1) at 14-15. As stated in the Supreme Court's reversal of class certification in AmChem, "the terms of the settlement reflect essential

[2] The Manual for Complex Litigation similarly requires the creation of subclasses in cases like ours. "Subclasses must be created when differences in the positions of class members require separate representatives and separate counsel. Those differences may arise from a variety of sources." II *Manual for Complex Litigation (Fourth)* § 21.23 (Matthew Bender & Co. 2010).

allocation decisions . . . ." 521 U.S. at 627. As in AmChem, the conflicting interests of the preferred and common shareholders prevent class certification.

Similarly, in Broussard v. Meineke Discount Muffler Shops, 155 F.3d 331, 338-39 (4th Cir. 1998), the Fourth Circuit reversed a $390 million judgment in a class action lawsuit and held that the District Court erred by certifying a class in which the purported members had divergent interests in the requested remedy. Former franchisees had an interest in pursuing strictly backward-looking monetary damages, while current franchisees had an interest in a forward-looking remedy involving reinstatement to a weekly advertising account benefitting franchisees. Id. at 338. The court followed AmChem and held that these conflicting interests prevented the class representatives from fairly and adequately representing the class. Id. at 338-39.

A similar intra-class dispute over valuation methodology prevented class certification in Duchart v. Midland Nat'l Life Ins. Co., 265 F.R.D. 436 (S.D. Iowa 2009). Because the choice of damages valuation methodology would invariably have benefited some class members but harmed others, the court held that there could be no fair and adequate representation of all class members without forming subclasses. Id. at 449-51.

a. The class representatives' explanation of the Plan of Allocation itself shows the conflict.

The conflicting interests between preferred and common shareholders in the allocation of settlement proceeds cannot be seriously disputed. Indeed, the class

representatives' explanation of the Plan of Allocation shows on its face the inherent conflict. Their only explanation is as follows:

> Plaintiffs' proposed Plan of Allocation of the settlement proceeds for the RTI preferred and common shareholders is based on **an analysis** which considered investment amounts, **Plaintiffs' argument that the 2009 recapitalization was not a liquidation event and gave no preference rights to RTI preferred shareholders**, the amounts actually received in the 2009 recapitalization, the types of equitable relief that a court could administer and the respective strengths and weaknesses of the legal position of the RTI preferred shareholders and the RTI common shareholders. (Memorandum in Support of Plaintiffs' Motion for Preliminary Approval of Class Action Settlement (Document 145) at 23 (emphasis added)).

This justification exposes the conflict within the proposed class, and the way in which the class representatives have ignored that conflict and sided with the common shareholders. No weight is given to the preferences given by the Articles of Incorporation to the preferred shareholders or, as discussed in detail below, the fact that under any scenario, the preferred shareholders would have received substantially more than provided in the Plan of Allocation.

Also, by "argu[ing] that the 2009 recapitalization was not a liquidation event," the class representatives have advocated against the interests of the preferred shareholders. Since the preferred shareholders would receive most of the settlement proceeds in the event of a different characterization, the class representatives are arguing against the interests of those they purport to represent, the preferred shareholders.

In addition, the explanation refers to "an analysis," but makes no attempt to share with the Court the methodology or factual basis of that analysis, which makes

it impossible for the Court to assess any purported justification for the extremely high valuation of the common shares. Nowhere is the Court told that the Plan of Allocation accords with none of the operative documents defining the rights of the respective preferred and common shareholders.

The undisclosed "analysis" is also based on errors of fact favoring the common shareholders. In the Notice of Proposed Settlement of Class Action (Document 150-1) at 14, the class representatives claim that the settlement allocation "analysis" considered "the amounts actually received by RTI preferred shareholders in the 2009 recapitalization." Yet the preferred shareholders, and specifically Gemini, received no cash in the 2009 recapitalization. Ahmed Decl. ¶ 20. Gemini has received no money in repayment for its purchase of shares in RTI.

b. The conflict is inherent in the right of the shareholders under the operative corporate documents.

Under the Articles of Incorporation of RTI, the preferred shareholders are given substantial preferential rights over common shareholders – which is why they are called "preferred shares." The bundle of preference rights allocated to the preferred shares over the common shares have substantial value. Preferred shares enjoyed priority over common shares in the event of a sale or liquidation, such that the common shareholders could not receive any return on their investment until the preferred shareholders were satisfied in full. Ahmed Decl. ¶ 6.; Eighth Amended and Restated Certificate of Incorporation of Restaurant Technologies, Inc., Art. IV, § 3(d)(i) & (ii) (Document 11-4, pages 6 of 66 to 10 of 66. In addition, the preferred

shares came with rights of accretion, whereby they would not merely be repaid the amount they had invested, but also an additional annual accretion percentage over and above their investment. Id.

Prior to the 2009 recapitalization, the total investment in the preferred shares was $92.2 million, and with accretion it would have taken $234.4 million in order satisfy those preferred shares in full. Ahmed Decl. Ex. A. Under at least one valuation, RTI's pre-recapitalization value was only $143 million, and after deducting RTI's funded debt (which had priority over all equity holders), that would have left only $31.1 million available to equity holders. Id. Even disregarding the accretion, the full $31.1 million would not have been enough to pay the face value amounts due to the preferred shareholders. Id. So, prior to the recapitalization, the common shareholders could not have reasonably expected to receive any return in the event of a sale or liquidation. Id. By allocating 74% of the net settlement proceeds to common shareholders who would have received $0.00 in a sale of RTI, the Plan of Allocation only underscores the conflict and shows how the class representatives benefited the common shareholders at the expense of the preferred.

In addition, although the proposed settlement allocation contemplates an increased settlement payment in the event that RTI is sold for more than $190 million by June 2013, the settlement only makes the preferred shares slightly more valuable in the event of a sale ($3.73 per preferred share versus $2.72 per common share in the event of a sale for $190 million, or $4.17 per preferred share versus $3.01 per common share in the event of a sale for $200 million). Notice of Proposed

Settlement of Class Action and Hearing Regarding Settlement (Document 150-1) at 15. This allocation ignores the preference rights that Gemini and the other preferred shareholders bargained for when they bought preferred shares. By disregarding these preferred rights in the event of a sale, the class representatives again elevated common shareholders' interests above those of preferred shareholders, and have not adequately protected the class.

c. Adding one class representative with common and preferred shares does not solve the conflict.

Favoring the common shareholders should not be surprising considering the makeup of the class representatives. This case was originally filed with only three named Plaintiffs, all of whom held only common shares. Complaint (Document 1-1) ¶¶ 1-3. Plaintiffs did not add a named plaintiff who held any preferred shares until eight days before they moved for class certification, when they amended their complaint and added Mr. Evanson. First Amended Complaint (Document 58) ¶¶ 1-3. But even Mr. Evanson held more common shares than preferred shares, and when taken together, the four named Plaintiffs held 171,423 common shares, but only 6,228 preferred shares. Ahmed Decl. Ex. B, p. 2. The class representatives therefore had a powerful incentive to favor common shareholders over preferred.

In any event, under the Supreme Court's AmChem decision, Mr. Evanson's presence cannot solve the conflict. As the Supreme Court warned, certification of a class is not appropriate with conflicting interests within a unitary class even if "some of whom happen to be members of the distinct subgroups." 521 U.S. at 627. As

explained in AmChem, members of each subgroup cannot be bound to a settlement except by consents given by those who understand that their role is to represent solely the members of their respective subgroups. Id. In light of the foregoing, the class representatives have not and cannot fairly and adequately represent the interest of the entire class, and the Court cannot certify the class as currently composed.

B. The Proposed Settlement Allocation Is Inequitable to Preferred Shareholders.

The proposed Plan of Allocation constitutes a huge transfer of value from the preferred shareholders to the common shareholders and harms preferred shareholders.[3] Under any conceivable scenario here, the preferred shareholders are due substantially more than they would receive under the proposed Plan of Allocation.

Under any realistic scenario under the documents applicable here, the preferred shareholders should receive the bulk of the settlement proceeds. The Ahmed Declaration lays out three different ways to allocate the proposed settlement. Ahmed Decl. ¶¶ 14-17& Ex. B. One scenario (labeled "Legal Settlement Economics") breaks down the allocation of the proposed settlement that the class representatives have proposed. Ahmed Decl. Ex. B.

The second scenario (labeled "Pre-Recap Economics") breaks down the allocation of the settlement based on the corporate documents of RTI as things stood

[3] Gemini is by far the largest preferred shareholder in the proposed class, because prior to the recapitalization it held 68.3% of the preferred shares that had not been excluded from the class. Ahmed Decl. ¶ 5.

prior to the 2009 recapitalization. Id. In a liquidation, which is what various affidavits before the Court indicate would have occurred,[4] all of the proceeds would have gone to the preferred shareholders, or at least they would have been paid in full prior to the common shareholders. While the class representatives dispute that the only alternative was a liquidation, even a sale of RTI would again have resulted in the payment of the preferred shareholders in full. Thus, under either scenario involving the pre-recapitalization period, whether it be the sale or liquidation of RTI, the preferred shareholders receive the entire settlement and the common shareholders receive nothing, or at least the preferred get paid in full before the common see anything. Id.

The third scenario ("labeled Post-Recap Economics") analyzes how the settlement would be distributed based on the corporate documents of RTI taking into consideration the capital structure post-2009, when most preferred stock had been converted into common stock. Id. Roughly 40% of a settlement in the post-recapitalization scenario would go to Gemini, since at that point Gemini held roughly 40% of the common stock. Id.

[4] RTI Proxy Statement Offering Memorandum dated May 13, 2009 (Document 11-1)at i-ii; Affidavit of Robert E. Weil (Document 7) ¶¶ 9, 11.

The following chart summarizes the amounts that the preferred and common shareholders would receive under these three scenarios:

	Pre-Recap Scenario	Post-Recap Scenario[5]	Proposed Settlement Scenario
Pre-Recap Preferred Shareholders	$3,645,000	$1,479,221	$962,009
Pre-Recap Common Shareholders	$0	$1,489,576	$2,677,172

Similarly, the following chart summarizes the amounts that Gemini and the class representatives would receive under these three scenarios:

	Pre-Recap Scenario	Post-Recap Scenario	Proposed Settlement Scenario
Gemini	$2,484,127	$1,476,066	$683,911
Class Representatives	$68,905	$22,580	$385,031

These comparisons show the significant transfer of funds to the common shareholders and away from the preferred shareholders. In light of the available

[5] This column is based on estimates of how the pre-recapitalization preferred shares (other than those excluded from the proposed class) converted into post-recapitalization common shares. Gemini held 68.3% of the pre-recapitalization preferred shares that were not excluded from the proposed class (Ahmed Decl. ¶ 5), so Gemini's 1,344,707 post-recapitalization common shares (Ahmed Decl. Ex. D) constituted 68.3% of the post-recapitalization common shares that had been converted from preferred shares. Accordingly, the total number of excluded pre-recapitalization preferred shares converted into post-recapitalization common shares was approximately 1,966,561 (1,344,707 / 68.3%). And the remaining portion of the 3,320,721 post-recapitalization common shares (Ahmed Decl. Ex. D) represented the approximate number of pre-recapitalization common shares. The per-share values for purposes of allocating the proposed settlement payment are drawn from Exhibit B to the Ahmed Declaration (Post-Recap Economics column).

measures, and the lack of any explanation from the class representatives as to how they arrived at an allocation so favorable the common shareholders, the Court should not approve the settlement.

Neither Class Counsel nor the Class Representatives can justify this wholesale transfer of assets to the common shareholders simply because Gemini did not fund the litigation. First, their fiduciary duties are to all shareholders. They do not have the right to modify the corporate documents to the detriment of any particular shareholders. Nor do they have the right to pick and choose in favor of certain classes.

Second, the proposed settlement already contains incentive payments to reward those who funded the litigation. Notice of Proposed Settlement of Class Action and Hearing Regarding Settlement (Document 150-1) at 12. Nor can the highly favorable treatment properly be considered an incentive payment for the class representatives, because the proposed allocation benefits many, many more common shareholders than the four class representatives, and in any case the class representatives have already requested $35,000 in incentive payments for themselves. Id. at 12-13.

In sum, the class representatives have proposed allocating to themselves far more return than they would receive under objective measures of RTI's pre-recapitalization and post-recapitalization value. The proposed allocation is inequitable and violates the class representatives' fiduciary duties to preferred shareholders in the class. The Court should reject the proposed settlement.

III. Conclusion

For the foregoing reasons, the Court should reject the proposed settlement and decertify the class pending a motion to create subclasses and appoint separate representative plaintiffs and lead counsel for each subclass.

Respectfully submitted,

LAW OFFICE OF SHAUN SPENCER, P.C.

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