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8 JUDGE PRO TEM

9 SUPERIOR COURT OF CALIFORNIA  
10 COUNTY OF ORANGE, CENTRAL JUSTICE CENTER

11 MIKE ALEXANDROS, et al.

12 Claimants,

13 and

14 KOR ELECTRONICS, et al.

15 Respondents.  
16

JAMS Ref. No. 1200042163  
CASE NO. 06-CC-07881

**STATEMENT OF DECISION**

17  
18 Pursuant to the California Constitution and order of the Court, the undersigned appointed  
19 Temporary Judge heard the matter at issue here beginning on January 11, 2010, and the matter  
20 was submitted on January 28, 2010.

21 The Court now rules in favor of Defendants, and makes the following Statement of  
22 Decision:

23 I. BACKGROUND

24 NEA IV and Spectra made venture capital investments in KOR Electronics, a privately-  
25 held defense industry company, between 1987 and 1994, and received convertible participating  
26 preferred stock. Among other benefits, this type of stock had demand registration rights,  
27 permitting it to require KOR to undertake a public offering. From late 2004 through most of  
28

1 2005, the KOR board of directors evaluated the possibility of KOR going public, but, by  
2 November 2005, it was of the view that KOR was not ready for a public offering.

3 NEA IV had favored a public offering as a way for it to conclude its KOR investment.  
4 When that possibility faded in late 2005, NEA IV advised the board NEA IV would exercise its  
5 demand registration rights or negotiate a KOR recapitalization to buy out NEA IV.

6 To evaluate NEA IV's proposal, KOR's board appointed a Special Committee of four  
7 directors who owned no preferred stock, but held KOR common stock or options for common  
8 stock. The Special Committee negotiated with NEA IV, and considered other options.

9 In early 2006, on the recommendation of the Special Committee to KOR's board of  
10 directors, KOR recapitalized by purchasing all the shares of its preferred stock for \$40.3 million  
11 cash and \$9 million in promissory notes, and selling new preferred stock at \$40.3 million to new  
12 NEA venture capital investment groups.

13 Plaintiffs, fourteen common stockholders who are present and former KOR employees,  
14 assert the recapitalization paid an unreasonably high price for the preferred stock and, in effect,  
15 wiped out the equity value of their common stock. They claimed breach of fiduciary duty,  
16 constructive fraud, gross mismanagement, waste of corporate assets, and unjust enrichment.

## 17 II. PRELIMINARY MATTERS

18 During the trial, Plaintiffs voluntarily dismissed with prejudice their third cause of action  
19 for constructive fraud.

20 At the end of Plaintiffs' opening statement, the Court denied without prejudice defense  
21 motions to dismiss Plaintiffs' first and second causes of action.

22 At the conclusion of Plaintiff's case, the Court denied Defendants' motions for  
23 Judgment. Plaintiffs were permitted to substitute Mr. Conrad for Mr. Battaglia as the  
24 representative in the derivative causes of action, and, following that substitution, Defendants'  
25 motion to dismiss the derivative claims because of inadequate representation was denied.

26 The main basis for Plaintiffs' claims is the assertion of breach of fiduciary duty owed to  
27 them. The additional derivative theories of gross mismanagement, waste of corporate assets,  
28 and unjust enrichment embrace the same factual basis. Since liability turns on the same basic

1 facts for all the causes of action, the merits of this case will be discussed the same way the  
2 parties did in their trial presentation, under (1) the business judgment rule as it pertains to  
3 directors, and (2) the controlling shareholdings assertion as it pertains to non-directors.

4 III. BREACH OF FIDUCIARY DUTY AND THE  
5 BUSINESS JUDGMENT RULE

6 The “business judgment rule”, codified in California Corporations Code section 309,  
7 creates a presumption that directors’ decisions are made in good faith, based on sound and  
8 informed business judgment, thereby protecting directors from liability for their decisions and  
9 actions as directors. The presumption may be rebutted by a showing of conflict of interest,  
10 fraud, bad faith, or gross overreaching. The rule protects only directors, not officers or  
11 controlling shareholders.

12 Under the business judgment rule, the inquiring is not whether a director’s decision is  
13 good or bad. As recently stated in Hill v. State Farm Mutual Auto Insurance Co. (2008) 166  
14 Cal. App. 4<sup>th</sup> 1438, 1492-93, a court does not make an evaluation of a director’s judgment or  
15 whether a decision was wrong. The rule is process oriented. Whether the trier of fact believes a  
16 decision was substantively wrong provides no basis for liability so long as the process used is  
17 rational or used in a good faith effort to advance corporate interests.

18 The parties’ reference to the Heckmann and Ronald cases show that it is not necessarily  
19 improper for a company to pay what amounts to a premium for a proper business purpose to  
20 achieve an ultimate objective desirable for the company and the common shareholders.

21 The sum and substance of the business judgment rule is that directors have wide latitude  
22 in management of corporate affairs provided honest and unbiased judgment is reasonably  
23 exercised.

24 The Court finds that the evidence shows no conflict of interest, fraud, bad faith, or gross  
25 overreaching contaminated the Special Committee’s decision. On the contrary, the evidence  
26 shows the Committee members acted appropriately, using a process that was rational and used  
27 in a good faith effort to advance corporate interests.

1 Faced with NEA IV's decision to conclude its investment by exercising its demand  
2 registration rights if KOR did not take it out by recapitalization, the KOR board of directors was  
3 compelled to study the alternatives and make what then appeared to be the best business  
4 decision on what to do. This was a delicate and controversial issue because different interests  
5 would be impacted adversely, and there were different views about the best long-range plan.  
6 The board appointed an "independent" Special Committee to study the issue and advise  
7 appropriate action.

8 The board appointed disinterested directors to the Special Committee: that is, directors  
9 not having the conflict of preferred stock holdings since the preferred stock might benefit from  
10 the decision made. The Special Committee members were highly skilled and experienced. The  
11 evidence showed that use of a special committee is a beneficial precaution rarely used in a  
12 venture capital backed company.

13 Considering all factors, the evidence shows the Special Committee acted diligently and  
14 independently, and its members acted in good faith. Their testimony revealed a sincere and  
15 earnest interest in seeking to do the right thing for the long-term interests of the company and  
16 the common shareholders. At first, they disliked the NEA IV proposal. They viewed their task  
17 as a negotiation to buy NEA IV's demand registration rights and keep the company unsold and  
18 private, which they viewed as the best long range course. The evidence shows, and the Court  
19 finds, the Special Committee and its members performed their task with due care and without  
20 negligence, they made reasonable inquiry into the facts and alternatives, and they weighed the  
21 advantages and disadvantages. They rejected the Summit Partners proposal alternative for what  
22 they found to be good and sufficient reasons. The evidence did not show that alternatives were  
23 ignored or brushed aside, and there was no evidence of a purpose or plan to give a special deal  
24 to favored persons.

25 Plaintiffs, supported by their expert Mr. Purcell, contend the Special Committee should  
26 have done things differently leading to a better result. In particular, Plaintiffs criticize the  
27 involvement of Mr. Carnino and Mr. Cole in the transaction, the failure of the Special  
28 Committee to use a separate financial advisor or outside counsel, the involvement of the

1 company's counsel who had a conflict of interest, and the delivery of faulty information in the  
2 Confidential Information Statement.

3 As acknowledged by Mr. Purcell, however, the Special Committee is not expected to be  
4 perfect. As Mr. Purcell testified, the Special Committee should consider everything, including  
5 the preferred shareholders' "veto" right. He acknowledged that the decision criteria is not just  
6 the stock value but all other factors as well, the Special Committee may validly make a decision  
7 with which other reasonable minds may disagree, and a decision may be within the "range of  
8 fairness" or "range of reason".

9 Mr. Carnino was an interested party, being a preferred shareholder, but he was the person  
10 most familiar with details of the business. He was not a Special Committee member, but he was  
11 used by the Committee to look for other options, provide data, and act as Committee secretary.  
12 Although there might have been a better choice than to have him connected to the Special  
13 Committee, there is no evidence his involvement tainted the Committee's work or decision. He  
14 was the CEO with connections to possible alternatives. His stock interests would probably have  
15 benefited from any alternative that was selected, and he was not a decision-maker on the  
16 Committee. To use him was within the range of reason.

17 Mr. Cole had interests which would have disqualified him from sitting on the  
18 independent Special Committee. But, there is no evidence he improperly influenced the  
19 Committee.

20 The Special Committee decided not to hire a special financial advisor, feeling it had  
21 adequate information available and a broad range of experience reflected in the Committee  
22 itself. Although the company attorney had a potential conflict, the Committee decided it was not  
23 necessary to hire additional counsel or obtain a "fairness opinion". Although other reasonable  
24 minds might have done it differently, there is no showing these decisions compromised the  
25 Committee's work or decisions, and its decisions were within the range of reason.

26 The Confidential Information Statement (Exhibit 158) was criticized as incomplete or  
27 misleading. However, the evidence disclosed there were conflicting interpretations of the

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1 pre-money valuation of \$87 million, and the other aspects of the Statement do not establish  
2 deception, overreaching or bad faith. The Statement was a good faith attempt at analysis of the  
3 transaction.

4 Considering all the evidence, the Court finds that there was no breach of fiduciary duty,  
5 and the conduct of the directors on the Special Committee was within the business judgment  
6 rule.

7 IV. BREACH OF FIDUCIARY DUTY AND  
8 THE CONTROLLING SHAREHOLDER THEORY

9 Plaintiffs claim liability against certain preferred shareholders, asserting they were  
10 “controlling shareholders” or acting as part of a controlling shareholder group. To establish that  
11 liability, control and abuse of that control must be shown.

12 For purposes of this analysis, the Court will assume the preferred shareholders were a  
13 controlling shareholder group, in the sense that they had the power to control certain aspects of  
14 the corporation’s life. This included the lawful power to exercise “veto” power and negotiation  
15 leverage because of the preferred shareholder rights they had.

16 However, the evidence does not show they abused that power. The evidence does not  
17 support a finding that they abused their relationship with the Special Committee, tainted its  
18 work, or improperly used their corporate rights. On the contrary, the evidence shows the Special  
19 Committee made its own independent decision about what to do.

20 V. CONCLUDING FINDINGS

21 The consensus of the board and the Special Committee it appointed was that they did not  
22 want to either go public yet or sell the company. They wanted to develop more product lines  
23 and use merger and acquisitions to develop the company into what they thought it could be,  
24 which would benefit the common shareholders in the long run.

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1 They were faced with venture capital investors who did not want to do that. NEA IV  
2 was an old investment that wanted to wrap it up. It had the right to force a public offering to get  
3 its money out.

4 The alternative chosen by the Special Committee permitted it to exchange NEA IV for  
5 new NEA investors without the same demand registration rights, who were interested in  
6 pursuing and financing the growth course, while retaining the prestige of having an NEA  
7 investor. KOR paid a premium to retire NEA IV and chart its new course. That decision had an  
8 immediate stock value disadvantage to the common shareholders, but the Special Committee  
9 and full board concluded it was in the best long range interest of the company and the common  
10 shareholders. The decision making process used, and the decision that was made, were rational,  
11 in good faith, and within the range of reason.

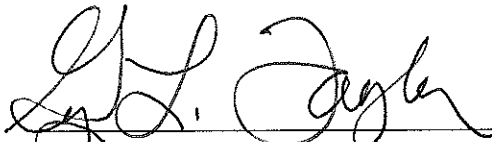
12 In addition to the rulings already made, the Court finds that, for the same reasons, the  
13 evidence does not support Plaintiffs on the theories of gross mismanagement, waste of corporate  
14 assets, or unjust enrichment.

15 Because of the rulings the Court had made, it is not necessary to reach the issues of  
16 inherent fairness, demand futility, whether Plaintiffs' claims are derivative only, standing to  
17 bring derivative claims, or damages.

18 VI. DISPOSITION

- 19 1. Defendants are entitled to a judgment against Plaintiffs that Plaintiffs have no  
20 recovery.  
21 2. Defendants shall prepare and submit a proposed JUDGMENT which includes the full  
22 names of all parties.

23  
24 DATED: February 25, 2010

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27 Hon. Gary L. Taylor (Ret.)  
28 Judge Pro Tem