



IN THE COURT OF CHANCERY OF THE STATE OF DELAWARE

DONALD A. KURZ and SEMS DIVERSIFIED )  
VALUE, LP, )

Plaintiffs, )

v. )

JAMES L. HOLBROOK, JR., STEPHEN P. )  
ROBECK, HOWARD D. BLAND, JEFFREY S. )  
DEUTSCHMAN, JORDAN H. REDNOR, )  
EMAK WORLDWIDE, INC., and CROWN )  
EMAK PARTNERS, LLC, )

Defendants, )

and )

JAMES L. HOLBROOK, JR., STEPHEN P. )  
ROBECK, HOWARD D. BLAND, JORDAN H. )  
REDNOR, and EMAK WORLDWIDE, INC., )

Counterclaim-Plaintiffs, )

v. )

C.A. No. 5019-VCL

DONALD A. KURZ and SEMS )  
DIVERSIFIED VALUE, LP, )

Counterclaim-Defendants, )

and )

JAMES L. HOLBROOK, JR., STEPHEN P. )  
ROBECK, HOWARD D. BLAND, JORDAN H. )  
REDNOR, and EMAK WORLDWIDE, INC., )

Third Party Plaintiffs, )

v. )

TAKE BACK EMAK, LLC, )

Third Party Defendant. )

**VERIFIED COUNTERCLAIMS AND THIRD PARTY COMPLAINT OF  
JAMES L. HOLBROOK, STEPHEN P. ROBECK, HOWARD D. BLAND,  
JORDAN H. REDNOR AND EMAK WORLDWIDE, INC.**

Counterclaim-Plaintiffs and Third Party Plaintiffs James L. Holbrook, Jr., Stephen

P. Robeck, Howard D. Bland, Jordan H. Rednor, and EMAK Worldwide, Inc., acting through its

special committee (“Company” or “EMAK”) (collectively, “Counterclaim-Plaintiffs”), by their undersigned attorneys, as and for their counterclaims and third party claims (the “Counterclaims”) herein state as follows:

### **NATURE OF ACTION**

1. These Counterclaims are for injunctive and declaratory relief with respect to Counterclaim-Defendants Donald A. Kurz’s (“Kurz”), Sems Diversified Value, LP’s (“Sems” and, together with Kurz, “Plaintiffs” or “Counterclaim-Defendants”), and Take Back EMAK, LLC’s (“TBE” or “Third Party Defendant”) participation in a consent solicitation (“Consent Solicitation”) to remove certain directors from EMAK’s Board of Directors (“Board”). As more fully described below, Kurz repeatedly has breached his fiduciary duty of disclosure by and through the dissemination of false and misleading information to EMAK stockholders in support of the Consent Solicitation. Sems and TBE have also disseminated false and misleading statements to EMAK stockholders in support of the Consent Solicitation in violation of Delaware law. Counterclaim-Plaintiffs seek (i) a declaration that Kurz has breached his fiduciary duty of disclosure; (ii) a declaration that Sems and TBE have disseminated false and misleading statements to EMAK stockholders; and (ii) an injunction requiring Kurz, Sems and TBE to make corrective disclosures relating to the Consent Solicitation.

2. On October 26, 2009, Kurz and Sems filed a Verified Complaint for Declaratory and Injunctive Relief against EMAK, Crown EMAK Partners, LLC (“Crown” or the “Preferred Stockholder”), and the other members of the Board in the Court of Chancery. Kurz and Sems alleged that the directors breached their fiduciary duties of care and loyalty in: (a) approving a transaction pursuant to which Crown’s Series AA Senior Cumulative Participating Convertible Preferred Stock was converted into New Series B Senior Convertible Preferred

Stock that carries the right to vote with the common stockholders on all matters, including the election of directors, on an as-converted basis (the “Exchange Transaction”), and (b) setting a record date for the Consent Solicitation, though it was set in accordance with the Company’s Bylaws. Kurz and Sems also alleged that Crown aided and abetted the directors in the breaches of their fiduciary duties.

3. Plaintiffs also filed motions for a preliminary injunction and expedited discovery. During a telephone conference on October 30, 2009, the Court granted Plaintiffs’ motion for expedited proceedings and scheduled a hearing on Plaintiff’s motion for a preliminary injunction for December 4, 2009. Pursuant to the expedited schedule, each of the Defendants answered the Complaint on November 3, 2009. Plaintiffs filed an amended motion for preliminary injunction on November 9, 2009. Plaintiffs filed their opening brief and supporting affidavits on November 23, 2009. Defendants filed their answering briefs on November 29, 2009.

4. On November 7, 2009, the Board’s Special Committee responsible for this litigation (the “Special Committee”) initiated a consent solicitation to ratify the Exchange Transaction (the “Ratification Solicitation”). The first written consent was delivered to the Company on November 10, 2009. On November 19, 2009, Tracy Tormey (“Tormey”), EMAK’s Chief Administrative Officer and General Counsel sent notice to the Board, including Kurz, of a special meeting to consider the written consent that had been delivered to EMAK. The Board met on November 20, 2009 and set a record date of November 24, 2009. On November 21, 2009, counsel for the Board informed counsel for Plaintiffs that the Board hoped to obtain the stockholder ratification of the Exchange Transaction.

5. A majority of the beneficial holders of EMAK common stock indicated their approval of the Exchange Transaction by returning written consents to the Company.

6. On December 3, 2009, Plaintiffs filed an Amended and Supplemental Complaint for Declaratory and Injunctive Relief (the “Amended Complaint”) in which they allege that EMAK’s CEO conspired with Crown to thwart the Consent Solicitation and that the Board committed various, unsubstantiated, allegedly false and misleading disclosures in connection with the Consent Solicitation and the Ratification Solicitation, and an Amended Motion for Preliminary Injunction seeking curative disclosures.

### **PARTIES AND JURISDICTION**

7. Counterclaim-Plaintiff EMAK is a Delaware corporation with its principal place of business in Los Angeles, California. EMAK is the parent company of a family of marketing services agencies. Its two primary businesses are Equity Marketing, which manufactures promotional products, and Upshot, a group of advertising companies. Its stock is currently traded on the pink sheets.

8. Counterclaim-Plaintiff James L. Holbrook, Jr. (“Holbrook”) is EMAK’s CEO and a director. Holbrook joined EMAK in November 2005 when he became CEO.

9. Counterclaim-Plaintiff Stephen P. Robeck (“Robeck”) has been a director of EMAK since 1989 and currently serves as the Chairman of the Board. Robeck was also Chairman and Co-CEO of the Company from September 1991 until December 31, 1998, and Counter-Defendant Kurz was President and Co-CEO during that period,

10. Counterclaim-Plaintiff Howard D. Bland (“Bland”) has been a director of EMAK since 2003. He is a retired audit engagement partner of KPMG LLP.

11. Counterclaim-Plaintiff Jordan H. Rednor (“Rednor”) has been a director of EMAK since 2008. He is the President of the Rednor Group, Ltd., an international management

consulting and merchant-banking firm. He is also a general partner of a privately held venture capital fund that invests in marketing services companies and a partner in Protagonist, a boutique creative advertising agency.

12. Counterclaim-Defendant Kurz has been a director of EMAK since June 6, 2009. He formerly served as Chairman, President co-CEO and CEO of EMAK, until he resigned effective May 13, 2005. Kurz was invited to remain on the Board after his resignation as CEO in 2005, and he did so for a few months before resigning without explanation.

13. Counterclaim-Defendant Sems, a limited partnership duly authorized under the existing laws of the State of Delaware, is a common stockholder of EMAK. Lloyd Sems

14. Third Party Defendant TBE, a limited liability company formed under the laws of the State of California, is a common stockholder of EMAK.

15. This Court has jurisdiction over TBE under 10 *Del. C.* § 3104 because TBE is transacting business in this state by soliciting the stockholders of a Delaware corporation to take action that will affect the internal corporate governance and Board representation of that corporation. In addition, one of TBE's members, Lloyd Sems, is also the managing member of the general partner of Plaintiff and Counterclaim-Defendant Sems.

### **FACTUAL BACKGROUND**

16. Kurz is a disgruntled ousted-CEO who is obsessed with regaining control of the Company that turned him out almost five years ago.

17. Kurz's communications with the Board show an ongoing pattern of hostility and vindictiveness that far exceeds the bounds of a shareholder activist and are particularly concerning because he is a current member of the Board. Kurz has made numerous, unprofessional threats to the directors, promising to "target" their personal assets.

18. Kurz has expressed repeatedly his desire to exert control over EMAK, threatened litigation against the Company and its directors, attempted to control the composition of the Board, and insisted on being reinstated as CEO of the Company.

19. On April 13, 2009, Kurz wrote a letter to the Board, threatening to remove Robeck and Holbrook and stating that he would personally carry out specific plans with the Board for a buyout, investment and recapitalization.

20. After this letter, Kurz met with a special committee, which carefully considered his business strategy but did not adopt his proposals.

21. The Special Committee then voted to invite Kurz to rejoin the Board (one of many such invitations) as a resolution to Kurz's demand.

22. Kurz rejoined the Board on June 6, 2009. The Board did this in a good faith effort to end Kurz's hostility and distractions and to respond to his demands and agitations.

23. Instead, Kurz continued to be a distraction to the Company. On September 8, 2009, Kurz proposed directly to Crown a restructuring to convert the preferred stock held by Crown (the "Preferred Stock") at full value into cash and secured debt payable over three years. Kurz did not inform the Board about this offer until after the offer was made. This offer undermined ongoing negotiations between the Board and Crown.

24. On October 12, 2009, TBE delivered to EMAK a written consent to approve and adopt resolutions removing Holbrook, Robeck, and Rednor from the Board and, in their places, electing Phillip S. Kleweno, Michael A. Konig, and Lloyd Sems to the Board. In conjunction with its Consent Solicitation, TBE launched a website, [www.TakeBackEMAK.com](http://www.TakeBackEMAK.com).

25. Prior to this consent the Board had received an August 19, 2009 letter from TBE demanding that a meeting of the shareholders be convened to vote on directors. Then,

on the eve of the September 9, 2009 board meeting, the Board received another letter threatening litigation for failing to call a shareholders meeting in response to the August 19, 2009 demand, despite the facts that the Company's Bylaws do not permit shareholders to call meetings and that the Company's annual meeting had just been held in June 2009.

26. The Board asked Kurz about the TBE letters during the September 9, 2009 Board meeting and he claimed that he was not involved in these efforts, had no prior knowledge of the TBE letters and was not acting in concert with the TBE group.

27. Disturbingly, it appears that Kurz was involved in the creation of the Consent Solicitation and was funneling confidential Board information to TBE to help it plan its consent solicitation. At a minimum, Kurz violated his duty of candor to the Board about his involvement.

### **THE DUTY OF DISCLOSURE**

28. A director of a Delaware corporation owes a fiduciary duty of disclosure, *i.e.*, "to disclose fully and fairly all material information," when issuing consent solicitation materials in contemplation of stockholder action. *Malpiede v. Townson*, 780 A.2d 1075, 1086 (Del. 2001). Similarly, parties soliciting consents from stockholders to elect them or their nominees to the board of directors must make accurate and complete disclosures.

### **FALSE AND MISLEADING DISCLOSURES IN THE CONSENT SOLICITATION**

#### **The October 19 Letter**

29. On October 19, 2009, Kurz, Sems, TBE and their other cohorts disseminated to EMAK stockholders a letter in support of the Consent Solicitation ("October 19 Letter"). The October 19 Letter contains numerous false and misleading statements.

30. For example, the October 19 Letter states that Kurz, Sems and TBE are "fully committed to an immediate and long-term return to profitability and performance." This

statement is false and misleading without disclosing that causing Kurz and his nominees to constitute a majority of the Board, and replacing Holbrook as CEO (both integral to the Kurz/TBE platform) would subject to the Company to the possibility of catastrophic payments, and in all events, would expose the Company to immediate claims which it would inevitably have to defend in litigation or settle at significant cost. Specifically, Kurz, Sems and TBE knew that there was a likelihood that Crown would take the position that TBE and Kurz, by forming a group, had already tripped the first trigger of the change of control provision in the Series AA Preferred Stock, such that, upon election of the Kurz/TBE nominees, Crown would be able to (and would) demand immediate payment of its liquidation preference of \$25 million (plus accrued dividends and premiums equal to an additional \$700,000, for a total payment of \$25.7 million). At a minimum, Crown's assertion of this claim would subject the Company to significant expense and distraction, and if Crown's construction of the Series AA Certification of Designation were found to be correct, would essentially bankrupt the Company. These facts would be highly material to any stockholder being asked to consent to the election of the Kurz/TBE slate, and the failure to disclose these facts was a material omission.

31. Similarly, Kurz, Sems and TBE also knew that the CEO has a change of control provision in his employment agreement and that terminating him after a successful Consent Solicitation (as Kurz and TBE plan to do) would trigger that provision, entitling the CEO to payment of two years' salary and benefits, an approximately \$1 million payout. This fact would be highly material to any stockholder being asked to consent to the election of the Kurz/TBE slate, and the failure to disclose this fact was a material omission. Kurz has asserted, without basis, that the CEO would be terminated for cause, voiding the severance payment, but

on information and belief, there are no grounds for such action. At a minimum, there would be further litigation about any proposed attempt to breach the CEO's contract.

32. The October 19 Letter also states that the Board "refus[ed] to consider multiple buyout overtures, including for up to \$15 per share." This statement is material to any stockholder being asked to consent to the election of the Kurz/TBE slate – that is why Kurz, Sems and TBE included it in the October 19 letter. It is also blatantly false. In fact, the \$15 "overture" referred to was nothing more than a request by a potential buyer in 2005 to conduct due diligence, with no indication of price at all. Even if there were such an offer (and there is absolutely no evidence that there was), to bring up conduct from almost five years ago as though it is a failing of the current Board is ludicrous. Stockholders have had had four years of annual meetings to throw out the Board that supposedly failed them and have chosen not to do so.

33. Similarly, the statement that the current Board is "complicit" in having "repeatedly rejected suitors willing to pay significant premiums to market" is false and materially misleading. In fact, the Company has not received any firm offers backed by financing. Moreover, such statements fail to specify who did what, when, in alleged "complicity" with whom, and thus misleadingly paint the Board in a negative light without support.

34. TBE and Kurz also omit to disclose that the interested party they refer to was not a "potential buyer" so much as a party being solicited by Kurz (contrary to specific instructions from the Board at the time) to fund a "go private" transaction or perhaps to simply redeem Crown and take over their position. One of Kurz's stated goals in this was to gain some liquidity for himself (while rolling some of his equity), likely at the expense of other common shareholders.

35. Kurz also lied to the Board about his involvement in at least one of these solicited letters of interest in the Company.

36. TBE and Kurz also fail to disclose that the Company was in disarray at the time after a dismal 2004 under Kurz' tenure, the management team was unsettled, with many of Kurz' acquisitions not integrated. One of the principal reasons the Board decided not engage in discussions was that the Board believed no such transaction would ever close but would represent another, material distraction at a time when the Company needed its CEO to address serious budgetary and operating issues.

37. In addition, the October 19 Letter misleadingly states that “[i]t is important to note that we are seeking recovery directly from the directors, and not from your company. Indeed, we are seeking a recovery for the company.” The fact is that the Company has incurred enormous expenses in defending itself in two different litigations brought by Kurz, Sems, TBE, and others. Moreover, the goal of these lawsuits, as well as the Consent Solicitation, is to restore Kurz as CEO. In addition, the October 19 Letter misstates the law, because the claims being made (as admitted in Plaintiffs' Amended Complaint), are clearly derivative claims, subject to indemnification obligations to the Defendants and with limited D&O insurance likely to be available as Mr. Kurz is a director of the Company (triggering the insured vs. insured exclusion).

38. The October 19 Letter also states that Kurz's “prior six-year tenure saw continual success, including . . . stock price over \$10.00 per share.” Again, this statement is highly misleading because the Company's thinly traded stock was artificially inflated by a stock buyback program initiated by Kurz, one effect of which was to significantly increase Kurz's percentage ownership of the Company.

39. It is also notable that some of the buyback activity went on after Kurz had been clearly instructed by the Board to suspend it. Also, the buyback program significantly reduced the "float" which caused the trading volume of the Company's stock to shrink markedly. In effect, then, Kurz's mismanagement and renegade behavior contributed greatly to the lack of liquidity for the Company. The buyback may have been part of a plot to make a go-private deal easier for Kurz.

40. Kurz's claim of "continual success" during his tenure is also blatantly false and misleading, as in 2004, the last full year of Kurz's tenure, the Company suffered a net loss of \$9.7 million – the Company's first loss since going public in 1994. Moreover, the Company's failed acquisition strategy engineered by Kurz resulted in further losses in 2005 (the year the Board forced Kurz to resign as CEO) and beyond. Under Kurz's management, by the end of 2004, the Company had burned through \$15 million of cash in 2004, and by the end of the year had only \$4.4 million of cash and over \$6 million in debt. Kurz's statement that, under his management the Company had "continual success" is blatantly false.

41. The Company's material losses in 2004 were followed by at least two years that, while profitable, fell well short of plan (and the plans were engineered by Kurz). As a result, bonus targets were missed and morale throughout the top management team at the Company suffered badly.

42. Other false and misleading statements in the October 18 Letter include the following:

- (a) "There is no coherent growth strategy";
- (b) "We may not even know the worst of it";

(c) The Board is guilty of “[f]ailure to listen to operating management”;

(d) “[O]ur CEO was fundamentally out of touch”;

(e) “Instead of actively protecting shareholder and company interests, [the Board] effectively ceded control to the chairman and the CEO, who have shown repeatedly they care only about their own self interest”;

(f) Chairman Robeck, CEO Holbrook, and director Rednor are “conflicted” and “ineffective”;

(g) “The current CEO has no experience in our core Products business . . . and has demonstrated no desire or ability to learn this critical business”;

(h) “Don [Kurz’s] prior six-year tenure saw continual success, including . . . stock price over \$10.00 per share”;

(i) “[W]e are absolutely committed to full accountability and transparency to all stockholders. We will make timely disclosures and fully comply with investor protection rules.”

### **The November 16 Letter**

43. On November 16, 2009, Kurz, Sems, TBE and their other cohorts disseminated to EMAK stockholders a second letter in support of the Consent Solicitation (“November 16 Letter”). Like the October 19 Letter, the November 16 Letter contains numerous false and misleading statements.

44. For example, the November 16 Letter states that the “current directors are doing everything they can to entrench themselves in office, and hinder EMAK’s shareholders—the owners of the company—from freely electing their board representatives,” that the “current

board shamelessly approved a self-serving exchange transaction that seeks to rob current stockholders of their right to replace directors and thereby change the direction of the company,” and that the Board has “tried to disenfranchise all of us.” The Board did not undertake the exchange transaction to entrench themselves, as evidenced by the Board’s willingness to rescind the transaction. Notably, Plaintiffs do not specify how or why any of the Defendants have attempted to “entrench” themselves (having just been duly elected by the shareholders five months previously), and fail to note also that several are significant common shareholders with voting rights of their own.

45. Kurz and TBE, of course, also fail to disclose that the most fundamentally self-serving party here is Kurz, in that he has no real interest other than to reinstate himself as CEO, and thereby increase his personal earnings and fortune, as he has stated repeatedly.

46. The November 16 Letter also states that the “board is forcing its owners to use the court system to ensure their rights are maintained. This, regrettably, drains both the company and shareholders resources and time, but is absolutely necessary.” Although the Board does not believe that Plaintiffs’ legal challenges to the exchange transaction are valid, the Board has acted to rescind the exchange transaction, the *exact relief* sought by Plaintiffs in their Complaint. Yet, Plaintiffs did not dismiss their lawsuit. Instead, they filed the Amended Complaint and are continuing to pursue litigation against the Company.

47. The November 16 Letter also falsely states that the Board “hastily” approved the exchange transaction in response to the Consent Solicitation. A recapitalization of the Preferred Stock had been under consideration by the Board for many months prior to the Consent Solicitation. In fact, Kurz himself had proposed restructurings to Crown in the months before the Consent Solicitation was initiated.

48. Indeed, as noted above, Kurz, while he was a director and without the Board's knowledge, was trying to deal with Crown at a time that he knew the Board was working to restructure the Preferred Stock.

**The Relationship Among Kurz, Sems and Take Back EMAK**

49. Kurz and Sems have never disclosed to stockholders the relationships between them concerning this litigation and the Consent Solicitation, nor have they disclosed the relationship between themselves and TBE. Discovery has shown that, contrary to express representations made to the Board of Directors of EMAK, Kurz was in discussions with TBE prior to TBE's delivery of an initial consent in this action. Discovery has also shown that Kurz is funding a significant portion of TBE's consent solicitation.

50. The relationships among Kurz, Sems and TBE are obviously material to stockholders who are being asked to execute a consent solicited by TBE to nominate directors loyal to Mr. Kurz, on a platform to restore him as CEO of EMAK. While the present solicitation is not subject to all the procedural requirement of the federal securities laws, those laws recognize the obvious materiality of such relationships, by requiring disclosure of any agreement, arrangement or understanding among a stockholder group soliciting proxies or consents, and disclosure of such agreements, arrangements or understandings among participants to a proxy or consent solicitation. Counterclaim-Defendants' and Third Party Defendant's failure to disclose this information is a material omission, as is their failure to disclose the source of Kurz's financing to wage this campaign, and personal financial relationships between Kurz and TBE's backers, the Konigs and the Konig family, who support Kurz's hedge fund.

**FIRST COUNTERCLAIM**

**(Breach of Fiduciary Duty of Disclosure against Kurz)**

51. Counterclaim-Plaintiffs repeat and reallege the statements in paragraphs 1-50 of the Counterclaims as if fully set forth herein.

52. As a director, Kurz owes the stockholders a fiduciary duty of disclosure to disclose fully and fairly all material information relating to the Consent Solicitation.

53. In breach of his duty of disclosure, Kurz has made egregiously false and misleading communications to EMAK stockholders.

54. Counterclaim-Plaintiffs have suffered and continue to suffer irreparable harm and have no adequate remedy at law.

### **SECOND COUNTERCLAIM**

#### **(Breach of Duty of Disclosure against Sems)**

55. Counterclaim-Plaintiffs repeat and reallege the statements in paragraphs 1-54 of the Counterclaims as if fully set forth herein.

56. Sems has a duty to make accurate and complete disclosures relating to the Consent Solicitation.

57. In breach of this duty, Sems has made egregiously false and misleading communications to EMAK stockholders.

58. Counterclaim-Plaintiffs have suffered and continue to suffer irreparable harm and have no adequate remedy at law.

### **FIRST THIRD PARTY CLAIM**

#### **(Breach of Duty of Disclosure against TBE)**

59. Counterclaim-Plaintiffs repeat and reallege the statements in paragraphs 1-58 of the Counterclaims as if fully set forth herein.

60. TBE has a duty to make accurate and complete disclosures relating to the Consent Solicitation.

61. In breach of this duty, TBE has made egregiously false and misleading communications to EMAK stockholders.

62. Counterclaim-Plaintiffs have suffered and continue to suffer irreparable harm and have no adequate remedy at law.

### **PRAYER FOR RELIEF**

WHEREFORE, Defendants and Counterclaim-Plaintiffs respectfully request preliminary and permanent injunctive relief and declarative relief as follows:

A. an order declaring that Kurz has breached his fiduciary duty of disclosure by disseminating false and misleading statements to EMAK stockholders;

B. an order declaring that Sems and TBE have disseminated false and misleading statements to EMAK stockholders;

C. an order requiring Counterclaim-Defendants and Third Party Defendant to make curative disclosures to correct the false and misleading statements made in communications to EMAK stockholders in support of the Consent Solicitation;

D. an award to the Counterclaim-Plaintiffs of the costs associated with bringing this action, including attorneys' fees and expenses; and

E. an award of such other relief as the Court deems just and proper.

MORRIS, NICHOLS, ARSHT & TUNNELL LLP

*/s/ Christine D. Haynes*

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December 7, 2009  
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