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When Is A Director's Claim For Indemnification Ripe And Appropriate?

By: Michael L. Rich

Claims for indemnification by directors facing legal actions against them can arise in unusual contexts. The Delaware Chancery Court recently addressed a particularly unusual situation in *Huff v. Longview Energy Co.*, 2013 WL 4084077 (Del. Ch. Aug. 12, 2013). There, the court dismissed as inequitable and premature a claim for indemnification by two directors.

The directors, William Huff and Richard D'Angelo, sought indemnification from the defendant, Longview Energy Company, a Delaware corporation, after a Texas court entered judgment against them. The Texas court found that they had breached their fiduciary duties by usurping a corporate opportunity from Longview. The Texas jury imposed a constructive trust in favor of Longview on profits earned by the two directors, and also awarded the company damages of $95 million. Huff and D'Angelo appealed. While the Texas appeal remained pending, the two directors asked the Delaware Chancery Court in a separate action to order indemnification of them by Longview. As things thus stood, Huff and D'Angelo were adjudicated as having breached their fiduciary duty of loyalty to Longview and the action for which they sought indemnification was not over because they themselves were appealing it.

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Under Delaware law, indemnification claims do not typically ripen until after the merits of an action have been decided and all appeals have been resolved. Nonetheless, despite suffering what on its face appears to be a devastating defeat, Huff and D'Angelo put forth the somewhat novel argument that they were "successful" within the meaning of 8 Del. C. § 145(c) because Longview had originally asserted eight counts against them, but ultimately decided at trial to present to the jury a single straightforward breach of fiduciary duty claim for usurpation of corporate opportunity. The directors analogized their claim to cases in which a corporate fiduciary sought indemnification because specific criminal counts were dismissed even though the fiduciary was found guilty on other charges.

Chancellor Leo E. Strine, Jr. granted Longview's Motion to Dismiss the claim for indemnification. The Chancellor reasoned that it was not a foregone conclusion that Longview had forever waived any right to press its other seven theories of liability because the record was not complete and the matter was pending on appeal. The Chancellor further held:

> Corporate fiduciaries who, unless they overturn a jury verdict, owed the corporation nearly $100 million and must yield to the company's substantial property rights, because they have been adjudicated to have breached their fiduciary duties, are not in an equitable position to ask this court to allow them to prematurely seek a money damages claim from the corporation to which they owed a duty of loyalty.

The Chancellor concluded that it would be inequitable to accelerate the directors' right to indemnification by expanding existing law.

This case underscores that claims for indemnification do not ripen until a matter has been finally adjudicated, including appeals. Also, as a court of equity, the Chancery Court will not lightly expand settled law to enable directors who have been adjudicated by a trial court to have breached their duties of loyalty to accelerate claims to indemnification.

When A Release May Not Be The Release You Thought It Was

By: C. John DeSimone, III

In the recent decision of *U.S. v. South Jersey Clothing Co, Inc., et al.*, Civil No. 96-3166 (JBS/AMD) (D NJ 2013), decided September 30, 2013, the United States District Court for the District of New Jersey held that non-party insurance companies who participated in a court-sponsored settlement on behalf of their insureds, contributed funds to a settlement memorialized in a consent decree, and obtained broad releases, may still be subject to suit from claims arising from the same liability previously sought released.

South Jersey allegedly discharged pollutants onto its property. Those allegations were the genesis of multiple lawsuits brought by the State of New Jersey, the United States, and others. South Jersey was not financially sound. Its insurers, who contested liability to South Jersey under applicable policies, nonetheless agreed to participate in a court-sponsored settlement process. Settlement talks resulted in a 2002 settlement of the suits in what is termed a "cash-out" settlement, i.e., South Jersey and the carriers paid into a settlement fund, and, in turn, received covenants not to sue and broad releases. Notice of the settlement was published in the Federal Register but the notice omitted mention of the carriers' involvement, contributions, and releases.

Some ten years later, adjoining landowners, Maroldas, who claimed no knowledge of the settlement and in particular, the involvement of the carriers, discovered their groundwater was allegedly contaminated from the South Jersey site. Maroldas instituted an action in the Superior Court of New Jersey and obtained a judgment against South Jersey. Finding they could not collect from South Jersey, Maroldas moved under *N.J.S.A.* 17:28-2 to collect on the judgment from South Jersey's insurers. In the interest of comity certain federal issues were directed to the District Court for resolution, with the District Court ultimately sending certain other issues back to state court. The District Court found: 1. If the state court ends up concluding that Maroldas had a protected interest in the South Jersey insurance policies at the time of the settlement consent decree, then the consent decree and releases attached to it do not preclude Maroldas from litigating their claim against the insurers. 2. If, on the other hand, the Maroldas are found not to have had a protected property interest in the insurance policies when the consent decree was approved, then the consent decree will be enforced to bar recovery against the insurers under *N.J.S.A.* 17:28-2. The issue of whether there was a contemporaneous protected property interest awaits the decision of the New Jersey state court.

A key issue in the *South Jersey* case turned on whether Maroldas had actual or constructive notice of the settlement. The court concluded Maroldas had neither. A lesson for defense counsel would be to remedy this oversight in two ways. First, publication in the Federal Register should include all participants to the settlement and the material terms of that settlement, to the extent possible. In this case the publication made no mention of the insurers or the releases.

Second, there was no evidence of direct notice of the settlement on Maroldas, even though they were an adjoining landowner. Given this decision, it may be prudent to notify all adjoining landowners in similar pollution cases going forward.

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