

## Further Guidance on Advancing Litigation Costs to Officers, Directors

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In *Hyatt v. Al-Jazeera America Holdings II*, C.A. No. 11465-VCG (Del. Ch. Mar. 31, 2016), the Delaware Court of Chancery considered the extent to which a dispute must relate to an officer or director's corporate duties before advancement of costs is triggered. In an opinion carefully delineating when a "nexus or causal connection exists between the underlying proceedings and the defendant's official corporate capacity," Vice Chancellor Sam Glasscock III held that two former directors of Current Media LLC, which was acquired by Al-Jazeera International (USA) Inc., were entitled to advancement in connection with certain claims that required them "to defend actions taken in their official capacity," but not with respect to claims that did not "turn on" their "actions as director and officer."

In December 2012, Current entered into a merger agreement with Al-Jazeera, pursuant to which Current became a wholly owned subsidiary of Al-Jazeera. Prior to the closing in January 2013, plaintiffs Joel Hyatt and Al Gore Jr. resigned from their positions with Current. In the merger agreement, Al-Jazeera "agreed to indemnify and advance fees and expenses to Current's former officers and directors" under certain circumstances.



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In addition, the merger agreement established an escrow account to satisfy any "damages associated with Current and suffered by Al-Jazeera [after the] merger." Al-Jazeera was permitted to seek indemnification for such damages from the escrow fund by submitting a written "claim certificate" to the members' representative designated in the merger agreement: plaintiff Hyatt.

Plaintiffs Hyatt and Gore commenced litigation on Aug. 15, 2014, alleging that Al-Jazeera breached the merger agreement by submitting five improper claim certificates, which Hyatt rejected. The plaintiffs sought invalidation of the claim certificates and an award for the balance of the escrow fund, to which they otherwise would have been entitled pursuant to the merger agreement.

Al-Jazeera counterclaimed on Sept. 11, 2014, contending that rejection of the claim certificates constituted its own breach of the merger agreement. On Oct. 1, 2015, the plaintiffs filed an amended complaint seeking advancement of fees and expenses for defending against Al-Jazeera's counterclaim.

Both sides sought summary judgment on the advancement claim. Glasscock determined that the plaintiffs' entitlement to advancement under the agreement tracked Delaware General Corporation Law Section 145, which confers advancement where former officers and directors have incurred expense "by reason of the fact" that they were former officers or directors. Accordingly, Glasscock invoked the Delaware Supreme Court's decision in *Homestore v. Tafeen*, 888

A.2d 204, 214 (Del. 2005), which “held that an action is brought ‘by reason of the fact’ of a defendant’s position as an officer or director if a ‘nexus or causal connection’ exists between the underlying proceedings and the defendant’s ‘official corporate capacity.’” Glasscock also analyzed *Rizk v. Tractmanager*, C.A. No. 9073-ML (Del. Ch. May 30, 2014), in which Thomas A. Rizk, the ex-CEO of an acquired company, was sued “for breach of contract stemming from alleged misrepresentations in a merger agreement.” Then-Master of Chancery Abigail LeGrow found that Rizk was entitled to advancement because “the claim for breach of contract was ‘inextricably ... intertwined’ with the action Rizk took in his former capacity as CEO,” and “Rizk was necessarily required ‘to defend his actions as CEO, and possibly disprove the allegations that he acted improperly in that capacity.’”

With *Homestore* and *Rizk* in mind, Glasscock examined Al-Jazeera’s counterclaims “to determine whether the allegations establish sufficient ‘nexus’ to Hyatt’s and Gore’s ‘corporate powers’ such that advancement of fees and expenses was appropriate.” The counterclaims provided multiple examples of the circumstances under which that test is satisfied. For example, the first three counterclaims sought “validation of those claim certificates that allege that Current breached the merger agreement by falsely representing that Current was in compliance with its distributor agreements.” Glasscock found it “telling” that distributors allegedly “had developed a dislike for Hyatt as a result of his mismanagement of

Current.” Given that, “the underlying basis of the claim certificates create a significant likelihood that Hyatt and Gore would be forced to defend actions that they took as officers and directors in order to successfully defend the counterclaims” and, thus, the plaintiffs were entitled to advancement. Similarly, Glasscock found that the plaintiffs were entitled to advancement in connection with Al-Jazeera’s counterclaim relating to Current’s alleged representation in the merger agreement that “the resolution” of a dispute with CBS “would not result in a substantial payment to CBS.” The court held that “this claim implicated Hyatt’s and Gore’s official capacities as they would be forced to defend their negotiations with CBS as well as the characterization in the merger agreement of the resolution of those negotiations.”

Glasscock did not find plaintiffs Hyatt and Gore entitled to advancement on all of Al-Jazeera’s counterclaims, however. Specifically, the court found that Hyatt was not entitled to advancement for claims arising out of his administration of the escrow fund, which did not arise out of his official corporate responsibilities, but rather out of his individual acts as a designee under the merger agreement. Similarly, Al-Jazeera’s fourth counterclaim involved a provision of the merger agreement that “required Current’s former members to indemnify Al-Jazeera for 50 percent of the expenses that Al-Jazeera incurred to terminate its [pre-existing] distribution agreement with [a cable operator].” Hyatt and Gore were “not entitled to advancement for” this counterclaim because it

“focused solely on the terms of the merger agreement,” and not on the plaintiffs’ official duties.

The *Hyatt* decision, which, unlike *Rizk*, was decided by a vice chancellor, provides important insights into the ways that Delaware courts may view advancement litigation. Although advancement clauses are often creatures of contract, it now seems apparent that courts may seek to import the body of common law interpreting advancement statutes where the contractual provisions in question resemble them. In addition, *Hyatt* suggests that courts will carefully parse claims in considering which arise from a director or officer’s “corporate powers” and which do not. Indeed, *Hyatt* provides multiple examples of how a court might decide close issues, including where an individual has administered an indemnification fund.

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