

Does  
the Gatekeeper  
Lawyer  
Need  
**INSURANCE?**



It's that time of year again—time to revisit your company's insurance coverage as the reminder for the renewal of the current Director & Officer (D&O) liability insurance policies just popped up on your calendar. As you pull out your files, you are impressed (or not) with the amount and degree of analysis invested in the process last year—perhaps there will be no new issues to tackle this year. Wouldn't that be nice? Just then, an email pops up on your computer screen. It's another article summarizing the charges filed against or settled with the general counsel of a Fortune 1000 company. Your initial reaction is, "That could never happen here!" Furthermore, everyone knows that in-house lawyers never get sued, right?

But then, is that still true? It seems that articles detailing claims being asserted against in-house law-

yers appear on your computer screen with increasing frequency—whether involving an indictment or criminal complaint or civil claims filed in the wake of a corporate meltdown. No matter how remote the chances of such a catastrophe may currently seem, would insurance coverage exist? Are there other contexts in which in-house lawyers are being sued? Would you or your general counsel be covered by your company's existing D&O policy? How about under its corporate Errors & Omissions (E&O) coverage? Do your company's insurers even offer coverage for in-house lawyers? One or more of the in-house lawyers at your company are officers, but are there any exclusions or exceptions in the D&O policy that eliminate coverage for some or all of the activities lawyers perform?



By John C. Tanner, Rebecca M. Lamberth, Kelly Wilcove, and Alex Reed

If you have more questions than answers, don't be surprised. You aren't alone. Employed lawyers professional liability insurance coverage is a relatively new product offered by several major insurers, but coverage for in-house lawyers is a topic many have been reluctant to pursue either within their companies or with insurance brokers. Making an informed decision on this topic, however, requires that you have accurate information concerning several questions:

- What are the liability exposures facing your corporate legal department? What specific claims might an in-house lawyer face?
- Are in-house lawyers generally given indemnification protection for acts, errors, or omissions made while serving their corporate employer? Stated another way, do most companies have a legal indemnification or advancement obligation to fund the defense or settlement of claims asserted against in-house lawyers?
- What insurance coverage is available to protect the company's indemnification obligation or the individual lawyer's assets?
- What is the scope of insurance coverage available to in-house lawyers—whether under an existing corporate D&O or E&O policy, or under a separate employed lawyers professional liability policy specifically crafted for in-house lawyers?

As you take another look at the email summarizing a recent claim asserted against a corporate general counsel, it strikes you that these questions may be worth considering.

### Will Your Corporate Client Sue You?

Everyone knows that even the best lawyers can make a professional mistake in the course of their work for a client. A legal malpractice claim is the obvious type of claim lawyers can face. Although such claims may have various labels—professional negligence, breach of fiduciary duty, breach of contract—they all constitute malpractice claims. Yet, do in-house lawyers *actually* get sued for malpractice? Do companies ever sue their in-house lawyers in the wake of a drafting mistake or other acts of possible professional negligence?



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### Just Because It's Rare, Doesn't Mean It Can't Happen

In fact, while still uncommon, malpractice claims against in-house lawyers are not unheard of. Such claims are most commonly filed when a new management team takes over or in the wake of the company's failure, when a trustee or receiver steps in. But that is not always the case. To illustrate, one private company filed a malpractice suit against its former in-house lawyer concerning several transactions he had handled

on the company's behalf.<sup>1</sup> The company complained that the lawyer defendant had "approved" and participated in the negotiation and documentation of several transactions which the company later alleged to have been closed without necessary authorizations by the principal shareholders. While the court ultimately dismissed claims asserted against the in-house lawyer, the case was litigated through summary judgment.

Because an in-house lawyer's client is the company itself, a change in corporate decisionmakers increases the chance an in-house lawyer may be sued.<sup>2</sup> So even if you are comfortable that those who hired you would never sue you, new decisionmakers might take a different view—particularly in the wake of corporate difficulties. In such a context, factors that might have restrained members of management or the board who originally hired or worked closely with the in-house lawyer may be missing from the decision-making process concerning whether to pursue a claim. Such malpractice claims may be filed by new corporate constituents or parties standing in the shoes of the corporate client. And, what such claims lack in frequency is generally made up for in the amount of the potential damages.

### A Multimillion Dollar Verdict

Consider, for example, a recent case in which claims were filed by the Chapter 7 trustee of a privately-held company, Trace International, against the company's Founder and Controlling Shareholder Marshall S. Cogan, as well as its General Counsel Philip Smith, and other former senior officers. After amassing an operating deficit of approximately \$103 million, Trace filed for bankruptcy and the court appointed a trustee. The trustee alleged that:

1. Cogan was in default on more than \$13 million worth of promissory notes to Trace;
2. Cogan had received more than \$23 million in excess compensation; and
3. all of the officer and director defendants had breached fiduciary duties of care by purportedly subordinating the company's interests to Cogan's interests.

As Trace's general counsel, Smith was charged with breaching fiduciary duties owed to the company by failing to fully advise the Trace board of directors and based upon his alleged participation in a contractual arrangement that benefited Cogan.

The trial court found Smith liable for over \$21 million based on his involvement in an arrangement by which Cogan purportedly repurchased certain Trace stock from a large shareholder and his failure to timely and adequately advise the Trace board of directors concerning company loans made to Cogan. On appeal, these findings were vacated and the case was remanded for a jury trial. The opinion of the trial court illustrates, however, the reality of potential professional liability in-house lawyers can face.

Other recent examples include findings made by court-appointed bankruptcy examiners concerning whether potential claims exist against in-house lawyers (among other corporate actors) that a company in bankruptcy may be able to pursue.<sup>9</sup> Likewise, a derivative suit recently filed against certain officers and directors of Chiquita Brands International, Inc., includes allegations against the company's former general counsel, Robert Olson. As in the Trace International litigation, the claims made against Olson focus on his role as legal counsel to the company's board of directors.<sup>10</sup> In yet another example, claims against a corporate general counsel were permitted to proceed despite defendants' motions to dismiss based in part on allegations that statements allegedly made by the CEO regarding the company's financial well-being "were bolstered by the silent acquiescence" of the company's CFO and general counsel. The court stated that silence may prove problematic in that case because those dealing with the company "allegedly trusted [them] based on their positions and specialized knowledge of [the company]'s financial health."<sup>11</sup>

### Will the Government Sue You ... or Worse?

Most common among recent examples of the growing potential liability of in-house lawyers are claims filed by the Securities and Exchange Commission (SEC), the Department of Justice (DOJ), or other government agencies.<sup>12</sup> Senior SEC enforcement officials have openly acknowledged that lawyers are now subjected to greater scrutiny as 'gatekeepers' on behalf of the companies they represent. In a March 2007 speech, Chairman Christopher Cox warned, "It's because the roles of gatekeeper and watchdog come with a great deal of responsibility that, when . . . lawyers . . . fail to live up to

## ***Pereira v. Cogan*—The Trace International Case<sup>3</sup>**

As a preliminary matter, the court found that Smith had failed to fulfill various duties as general counsel. Specifically, Smith failed to advise the board regarding:

1. corporate officers' duties;
2. the board's duty to manage the corporation;
3. the need for compliance and monitoring programs and/or an audit committee;
4. the board's responsibility for overseeing the redemption of corporate stock; and
5. the board's obligation to supervise and evaluate Cogan and to inform themselves regarding transactions between Cogan and Trace.

A central allegation against Smith concerned an agreement he had drafted under which Trace had agreed to redeem \$10 million worth of stock from one shareholder. The court found that, upon realizing that Trace could not redeem the stock without also paying certain dividend arrearages, Smith devised a plan to disguise the redemption as a stock purchase by Cogan. Pursuant to the plan, Trace lent \$3 million to Cogan, who used the funds to redeem company stock. Cogan then pledged the shares to Trace. In finding Smith liable for his role in the scheme, the court noted that "Smith's active involvement in this situation suggests that it was within his discretionary authority and that he had the ability to prevent the redemption, either at the time he and Cogan created the need for the redemption . . . or later when he came up with the subterfuge."<sup>4</sup>

In contrast, the court held that there was no evidence to suggest that the board would have challenged Cogan's allegedly excessive compensation had Smith more fully advised the Trace board. The court noted that, "the complacent board felt that Cogan was properly compensated" and found that "Smith could not have presented any legal precedent requiring the Board to take any further action."<sup>5</sup> Consequently, Smith was not liable for facilitating Cogan's excessive compensation.

Finally, the court found that Smith, upon learning that Cogan had taken personal loans from the company, "should have taken steps to advise the Board that any such loans had to be approved by them . . ."<sup>6</sup> The court noted that, while "Smith did not believe that the directors had the legal duty to determine if loans should or should not be made to Cogan or other insiders", as general counsel, "it was his responsibility to take steps to so inform himself."<sup>7</sup> For the court, the negative factor in finding Smith liable was the fact that his "advice . . . could have prevented the loans by his revelation that such loans were not permitted under Delaware law."<sup>8</sup>

their responsibility, the Commission will bring enforcement actions.”<sup>15</sup> Likewise, notable remarks were made by then SEC General Counsel Giovanni P. Prezioso at a 2005 meeting of the Association of General Counsel:

Having spent a fair amount of time trying to explain some of the elements that have not changed in the Commission’s approach to sanctioning lawyers for securities law violations, let me turn to what I think has changed—and what those changes mean for you as the chief legal officers at your companies.

What has changed—and this may seem obvious—is the law. The Sarbanes-Oxley Act, as you all know, significantly expanded the Commission’s authority to adopt professional standards governing lawyers ...

With the enactment of the Sarbanes-Oxley Act, any lingering questions about the Commission’s authority disappeared. And while the Commission cannot be expected miraculously to become [an] expert overnight in the regulation of lawyers as professionals, there is no doubt that it can—in-deed, given the mandate of Congress, really must—devote more time and resources to developing its expertise in this area.<sup>14</sup>

Proof of such increased scrutiny is not hard to find.

Within the last year and a half, the current or former general counsel of several public companies have either been charged with securities law violations by the SEC or have resolved potential charges in connection with stock option back-dating issues.<sup>15</sup> In many instances, the SEC has demanded disgorgement of funds and imposed monetary penalties, in addition to various forms of injunctive relief. For example, based on his role in connection with the company’s options backdating scheme, the general counsel of Comverse Technology, Inc., was required to pay \$1,670,915.03 in disgorgement, and to pay additionally \$817,509.07 in prejudgment interest, as well as a \$600,000 civil penalty.<sup>16</sup> As the general counsel of KLA-Tencor Corp., and later Juniper Networks, Inc., Lisa Berry is alleged to have routinely back-dated stock option grants, for which the SEC is seeking disgorgement and monetary penalties.<sup>17</sup> The DOJ has likewise filed criminal charges or reached settlements with several in-house lawyers in the context of recent option backdating issues.<sup>18</sup>

Aside from the option backdating scandal, it appears that the likelihood that in-house lawyers may be pursued based on accounting irregularities and related securities disclosure issues may be increasing.<sup>19</sup> In one example, the SEC has filed charges against the former general counsel of Tenet Healthcare Corporation for alleged securities violations. In its complaint, the SEC alleges that this former general counsel knew or was reckless in not knowing that Tenet’s public filings were misleading based on purportedly

overstated “gross charges” in order to receive larger Medicare reimbursements.<sup>20</sup> According to the SEC complaint, she had supervisory responsibility for drafting and reviewing Tenet’s Forms 10-Q and 10-K and was one of three members of the company’s disclosure committee.<sup>21</sup>

In another example of the government’s growing willingness to pursue lawyers, charges have been filed within the last few years against several in-house lawyers for alleged misconduct in responding to a government investigation.<sup>24</sup> Even when regulators or enforcement agencies ultimately decide not to pursue civil or criminal charges, in-house lawyers may be closely scrutinized during the course of a government investigation. Thus, with or without pending charges, an individual under scrutiny may decide that he or she should retain legal counsel, thereby incurring significant legal fees.

To illustrate, Chiquita Brands International became the subject of a governmental investigation based on payments made by a corporate subsidiary to a Colombian group, reportedly to ensure the safety of employees and property.<sup>25</sup>

## **United States v. Cohn—Bad Facts Always Make Bad Law**

*United States v. Cohn*<sup>22</sup> demonstrates another area of potential liability for in-house lawyers. Four Star Financial Services, LLC, and its General Counsel Mark Cohn, were convicted of multiple counts of mail fraud and wire fraud in connection with their participation in a fraudulent telemarketing scheme. The scheme allegedly originated with one of Four Star’s clients, Joel Katz, who had become heavily indebted to the company. To help Katz repay his debts, Four Star agreed to loan Katz money to start a telemarketing business which targeted consumers with impaired credit histories and promised to provide these consumers with a credit card, coupons and other discounts in exchange for a fixed payment. The product sent to consumers, however, contained items of little or no value.

Upon learning that Katz was diverting revenue from the company for personal uses, Cohn caused Four Star to assume control of the telemarketing scheme. At trial, witnesses for the government testified “that Cohn was aware that no agreements existed with companies to supply the benefits being offered in the program; that Cohn ‘micro-controlled’ the telemarketing scheme, spending 70 to 80 percent of his business day on it; and that Cohn instructed [another officer] to send out fulfillment packages, despite the fact that they lacked the promised benefits.”<sup>23</sup> In all, the telemarketing scheme defrauded more than 31,000 customers of more than \$3.6 million.

In accepting the company's plea to a single felony count of engaging in transactions with a terrorist group, the judge who presided over that proceeding acknowledged, "[i]t gives me pause that no individuals are being held accountable."<sup>26</sup> One person to whom the judge may have been referring was Chiquita Brands' former General Counsel Robert Olson. Public information concerning this matter indicates that Olson may have become aware of various facts concerning company payments made to a Colombian organization designated 'a terrorist group' by the US government in or about 2001, and that Olson communicated with and received legal advice from outside counsel for the company regarding the payments at some point before

### ***In re Chiquita Brands Int'l, Inc.***

In 1997, Chiquita's Colombian subsidiary, Banadex S.A., apparently began making payments to the United Self-Defense Forces of Colombia (AUC), a right-wing paramilitary group responsible for raping, killing and kidnapping thousands of Colombians. Public accounts indicate that the payments were made to ensure the safety of Banadex employees and property. To avoid detection, "[p]ayments were always disguised as either a check to a third party who passed the money to the AUC, or as income to a Banadex employee who paid the AUC in cash."<sup>28</sup>

Once the AUC was deemed a "specially designated foreign terrorist organization" by the US State Department in 2001, Chiquita could not legally continue to send payments to the AUC. Chiquita executives, however, claim to have been unaware of the AUC's 'terrorist' designation and purportedly continued making payments. The executives allegedly responsible for approving the payments were Chiquita's CEO, the chairman of the audit committee, and Olson, the company's general counsel.

On five separate occasions between February and March 2003, Chiquita's outside counsel reportedly warned the company that the payments were illegal and that Chiquita "must stop."<sup>29</sup> After initially replying "just let them sue us, come after us,"<sup>30</sup> Olson took outside counsel's recommendation to the board, which decided to disclose the payments to the DOJ. After the meeting with Justice Department officials proved inconclusive, however, Olson purportedly allowed the payments to continue for another 10 months, despite warnings from outside counsel that DOJ "officials have been unwilling to give assurances or guarantees of nonprosecution . . . and cannot endorse current or future payments"; and the audit committee chairman's opining that "we appear to [be] committing a felony."<sup>31</sup>

the US Attorney's Office initiated an investigation of the issue.<sup>27</sup> Following extensive negotiations among Chiquita, the US Attorney's Office and the DOJ, the government official overseeing the case decided not to charge any of the individual defendants. It appears, however, that this result was not certain during the course of the investigation.

Nevertheless, with or without the filing of formal charges, the potential for incurring substantial legal fees in the context of a governmental investigation or other governmental action—regardless of ultimate legal liability exposure—exists at a more pronounced level than in the past.

### **Potential Liability Under the Securities Laws Remains, but with Some Helpful Clarity**

Potential liability also exists for in-house lawyers in the securities class action context. Plaintiffs' counsel have asserted direct securities class action claims against in-house lawyers, as well as indirect scheme liability claims. It remains true that lawyers are seldom a principal focus of such litigation—which instead tends to target one or more senior executives and members of the board. In the past, absent either indications of personal gain or a unique role in events on which the litigation is based, in-house lawyers have generally been omitted as defendants in securities class action complaints. But the frequency with which in-house lawyers appear as defendants seems to be growing. This has certainly been true with respect to securities claims filed in the wake of the recent option backdating scandal.<sup>32</sup> Recent examples of suits naming lawyers as defendants have not been isolated to that context, however.

### **Classic Securities Fraud Claims**

Securities claims filed against Qwest Communications illustrate in-house lawyers' vulnerability to 'classic' securities fraud claims.<sup>33</sup> Securities claims were filed against the company and certain of its officers and directors, including the company's general counsel, after an internal audit led Qwest Communications to revise its revenue by \$2.5 billion. The complaint alleged that Qwest and the individual defendants made false and misleading statements regarding the company's financial performance, thereby artificially inflating Qwest's stock price. The plaintiffs claimed to have been damaged when the stock price subsequently declined after the true state of the company's finances was revealed.

Allegations made against the Qwest general counsel asserted that he—along with the other named defendants—was responsible for certain misstatements and omissions in Qwest's public filings. The named defendants asked the court to dismiss all claims at the pleadings stage, which the court refused to do. In ruling that the case could continue, the court cited: (i) the scope and magnitude of the accounting manipulations at issue; (ii) allegations of substantial insider

stock sales; and (iii) defendants' executive positions within the company and routine participation in discussions regarding the state of Qwest's finances. Qwest's general counsel was not singled out among the named defendants for specific analysis, but neither does it appear that his role as counsel to the company caused the court to consider whether he should be given any different treatment from the other named defendants.<sup>34</sup>

No one can predict the future as to whether in-house lawyers who play a role in their company's public disclosures will indeed be more frequently among the individuals named as defendants in these types of cases. However, the general trend toward more active pursuit of claims against lawyers in several other contexts makes this an issue worth considering.

### Secondary "Scheme" Liability Theory

For the last several years, plaintiffs' counsel who file securities class action complaints have pursued a scheme liability theory against secondary actors based on traditional aiding and abetting fraud claims previously rejected by the United States Supreme Court in *Central Bank, N.A. v. First Interstate Bank, N.A.*<sup>35</sup> Until very recently, there was widespread concern that if such a theory was found to have survived *Central Bank* with respect to secondary actors, in-house lawyers might routinely find themselves named as defendants in securities class action lawsuits.

One example of this potential exposure appeared in the complaint filed in *In re Enron Corp. Securities, Derivative & "ERISA" Litigation*. There, in addition to naming Enron in-house lawyers in the shareholder class action litigation, the plaintiffs alleged that the third-party bank defendants entered into partnerships and transactions that allowed Enron to temporarily remove liabilities from its books and to record revenue from the transactions when the company was, in fact, incurring debt. These third-party bank defendants allegedly engaged in a scheme to assist Enron in defrauding its investors and were thereby purportedly liable for aiding and abetting securities fraud. The lower court granted class certification based on these scheme liability allegations.<sup>36</sup>

On interlocutory appeal, the Fifth Circuit rejected this scheme liability theory,<sup>37</sup> and on January 22 of this year, the United States Supreme Court denied plaintiffs' petition for certiorari,<sup>38</sup> an outcome that was widely expected in light of the Court's ruling in *Stoneridge Investment Partners, LLC v. Scientific-Atlanta, Inc.*, just seven days earlier.<sup>39</sup>

The *Stoneridge* plaintiffs asserted a similar scheme liability theory against vendors Scientific-Atlanta and Motorola. In a 5-3 decision, the United States Supreme Court affirmed the Eighth Circuit's dismissal, finding that if the Court were to recognize the theory of scheme liability, a new class of defendants would be exposed to the threat of extorted settlements at the hands of plaintiffs asserting relatively weak claims.<sup>40</sup>

Although the *Stoneridge* decision effectively forecloses plaintiffs from bringing securities fraud claims against in-house lawyers on a theory of scheme liability, secondary actors, including in-house lawyers, "are not necessarily immune from private suit" under the securities laws as "the implied right of action in §10(b) continues to cover secondary actors who commit primary violations."<sup>41</sup> In addition, the SEC retains its authority to bring civil enforcement actions against secondary actors who violate the securities laws, and indeed has filed enforcement actions against in-house lawyers in the past.<sup>42</sup> Moreover, "some state securities laws permit state authorities to seek fines and restitution from aiders and abettors."<sup>43</sup> In-house lawyers thus continue to be vulnerable to suits brought by both governmental bodies, as well as plaintiffs via state blue-sky laws and/or other state laws, such as, common law claims for fraud or breach of fiduciary duty.

Consequently, the *Stoneridge* decision does not necessarily foreclose secondary actor liability as certain commentators have asserted. In-house lawyers should remain vigilant against exposing themselves to this liability under the various state and federal securities and common laws.

### And the List of Who May Sue You Continues

Aside from potential liabilities already discussed, in-house lawyers are also vulnerable to other third party claims. Although such claims are relatively uncommon, a recent suit asserting claims against two in-house lawyers based on their participation in their company's dealings with its banks illustrates that the potential for liability exists.

On behalf of a syndicate of commercial banks, JP Morgan Chase Bank sued various officers and directors of Global Crossing Ltd., in connection with a series of loans made to Global Crossing pursuant to a credit agreement.<sup>44</sup> The credit agreement authorized Global Crossing "to draw down funds from a credit facility, provided a GC officer certified that the company was in compliance with the covenants and other terms of the Credit Agreement at the time of each borrowing."<sup>45</sup> Global Crossing allegedly engaged in bogus 'swap' transactions to artificially inflate the company's earnings, thereby ensuring that the company would remain in compliance with its covenants. The lawsuit asserted that the swap transactions rendered Global Crossing's compliance certifications false in order to perpetrate a fraud on the banks. The suit included claims against Global Crossing's general counsel and a second in-house lawyer for aiding and abetting fraud under New York law. The lawyer defendants moved to dismiss.

To demonstrate that the lawyer defendants knew of the fraud, JP Morgan Chase alleged that its objectives and mechanics were well-known at Global Crossing, as was

the relationship between meeting revenue targets and continued access to the credit facility. As proof, JP Morgan Chase cited emails that the in-house lawyer at Global Crossing had received from the company's vice president of sales which purportedly reflected a "do whatever it takes" mentality with respect to meeting revenue targets. As for the general counsel, it was alleged that, "he knew swaps were being conducted to meet end-of-quarter revenue targets."<sup>46</sup> The general counsel also purportedly forwarded an email containing a list of potential swap transactions that would allow the company to meet those targets. In denying their motion to dismiss, the court decided that these allegations gave rise to a strong inference of knowledge on the part of the lawyer defendants.

It was also alleged that the in-house lawyer negotiated and "papered" the swaps, although it was not claimed

that she had any role in designing the transactions. The in-house lawyer argued that such activities were merely part of her routine legal duties, but the court disagreed. "The critical test is not . . . whether the alleged aiding and abetting conduct was routine, but whether it made a substantial contribution to the perpetration of the fraud,"<sup>47</sup> the court stated, explaining that the type of activity that can lead to potential liability can take many forms. Most critical was whether "there is an extraordinary motivation to aid the fraud."<sup>48</sup> JP Morgan Chase's allegations that Global Crossing's in-house lawyer was "directly involved in bringing about—including negotiating—transactions, which while not themselves necessarily fraudulent, [were] alleged to have been carried out solely for the purpose of inflating revenue"<sup>49</sup> were ruled sufficient to permit the claims to proceed past her motion to dismiss.

## Framework for Evaluating Whether Your In-house Legal Department Needs Malpractice Insurance

1. Assess the liability exposures facing your legal department.
  - o Malpractice Claims—What is the likelihood that current management or directors would cause the company to sue you for professional negligence?
  - o Malpractice Claims Following a Change in Control—What is the likelihood that current management or directors will be replaced? Is your company subject to bankruptcy exposure, potentially exposing you to claims by a court-appointed trustee, examiner, or comparable authority?
  - o Government/Regulatory Exposure—Do you appear and practice before the SEC? Does your legal work include other areas of heightened regulatory oversight?
  - o Securities Litigation Exposure/Third-Party Claims—Does your legal work include preparation of SEC filings? Do you issue legal opinions or certifications to third parties?
2. Determine the scope of your company's indemnification/advancement obligations to in-house lawyers.
  - o Review the applicable state statute governing corporate indemnification. Keep in mind that the parent company and subsidiary companies may be incorporated under the laws of different states.
  - o Review the company's indemnification grant in its Articles of Incorporation and Bylaws.
  - o Review any written indemnification agreements or policies between the company and its in-house lawyers.
3. Determine the extent to which indemnification is extended to non-officer in-house lawyers and employees generally.
4. Consider whether any such indemnification is mandatory or permissive. Is the company required to fund a defense or settlement short of a final adjudication that the attorney did not satisfy the requisite standard of conduct for permissible indemnification? Or, is the decision whether to defend and indemnify in-house lawyers left entirely to the discretion of the board of directors in place at the time of the claim?
5. Consider scenarios where the company may be legally or financially unable to fund a defense.
  - o Financial insolvency—Your indemnification protection is only as strong as your company's ability to pay.
  - o Derivative claims—Under the law in some states, a company is legally prohibited from indemnifying settlements or judgments in claims brought by or on behalf of the company.
  - o Change in Control—What happens if a new board of directors wrongly determines that the requisite standard of conduct for permissible indemnification was not met? Is the indemnification grant subject to retroactive amendment?
6. Review your existing corporate insurance policies to determine the scope of coverage already afforded to your in-house lawyers in their capacities as directors, officers, or as employees generally.
7. Identify potential gaps in coverage. Review available employed lawyers insurance policy forms and endorsements with your risk management department and outside insurance broker.

With respect to whether allegations against the general counsel sufficiently alleged “substantial assistance” to permit the suit to continue against him, the court held that the “[m]ere presence, and passive receipt of email, cannot, by definition, constitute affirmative assistance.”<sup>50</sup> Nonetheless, allegations that he “was actively involved in the negotiation, facilitation, and approval” of swaps also proved sufficient for the claim for aiding and abetting fraud to proceed.

### **What’s a Lawyer to Do?**

Now that we have convinced you that the potential for liability exists, what’s next? What should you do in order to analyze whether insurance coverage for such claims either already exists at your company, or is needed? A threshold issue is whether your company is obligated to indemnify and to advance defense costs in the event such a claim is made against you or another of your in-house lawyers.

Generally speaking, issues concerning the indemnification of corporate employees are governed by the law of the state in which the company is incorporated.<sup>51</sup> Consequently, first steps should include a review of the relevant indemnification statute.

Because a majority of the nation’s Fortune 500 companies are incorporated in Delaware, that state’s indemnification statute merits attention. Section 145 of the Delaware General Corporation Law<sup>52</sup> does not focus solely on directors and officers. Rather, Section 145 addresses indemnification in the context of employees and agents, as well as directors and officers.

One provision of Section 145, subsection (c), requires mandatory indemnification where the covered individual “has been successful on the merits or otherwise in defense of any action, suit or proceeding . . . or in defense of any claim, issue or matter therein . . . .” Significantly, however, the scope of the provision is limited to “present or former officer[s] and director[s,]”<sup>53</sup> making the statutorily required indemnification of expenses following a successful defense entirely discretionary as to non-officer employees and agents.

Several other aspects of Section 145 are noteworthy. First, the indemnitee must have acted in good faith, and he or she must have reasonably believed that such conduct was in, or at least not contrary to, the best interests of the corporation. Alternatively, in the context of a criminal proceeding, the indemnitee must not have had reasonable cause to believe that his or her conduct was unlawful. Second, unlike in other proceedings, “a Delaware corporation may indemnify an indemnitee in a shareholder derivative proceeding only for expenses (i.e., not fines, judgments, or settlement amounts)” and only so long as the party seeking indemnification is not ultimately found liable to the corporation.<sup>54</sup> Finally, a parent corporation may not be permitted

or required to indemnify employees of any direct and indirect subsidiaries, unless those individuals were serving in their respective capacities at the parent company’s request.

Of course, Section 145 and corresponding statutes in other jurisdictions simply dictate the outer parameters of what is and is not permissible with respect to indemnification. After reviewing the relevant state statute, an in-house lawyer must also consult the relevant provisions of her company’s charter and bylaws, as well as any separate indemnification agreement that may exist, in order to determine whether indemnification is available and, if so, under what circumstances.

### **Malpractice Insurance for In-house Lawyers**

In addition to any indemnity protection afforded by your corporate employer, you should carefully consider whether the current liability landscape warrants negotiating further insurance protection. Unless your company is legally required to fund the defense and settlement of claims asserted against you, there is no assurance that the decision-makers in place at the time of the claim will exercise their discretion to do so. As discussed before, a claim by or on behalf of the company may not be fully indemnifiable as a matter of law—and if your company has decided to sue you, it is highly unlikely it will offer indemnification.

In addition, even if members of your legal department are entitled to mandatory corporate indemnification, your personal financial resources will be at risk if the company files for bankruptcy or otherwise becomes insolvent. And, of course, to the extent your company is required to fund defense and indemnity to its in-house lawyers, it may benefit by shifting a portion of that risk to an insurer.

### **Assessing Coverage Under Your Existing Corporate Insurance**

At this point, you may think to yourself, “I’m sure we are covered for malpractice claims.” After all, your former law firm provided coverage for all attorneys before you went in-house. Surely your in-house legal department enjoys similar protection? You call your director of risk management and ask for a copy of the company’s current E&O and D&O liability policies. You are told that your company has considered purchasing employed lawyers professional liability insurance in the past, but has not yet done so. You send the current policies to outside coverage counsel for review. The analysis you get back may look something like this:

#### **E&O Coverage**

It is highly unlikely that your corporate E&O coverage affords protection for your legal department’s professional negligence. Corporate E&O policies often include all employees as covered insureds. However, coverage under

such policies is typically limited to claims for errors or omissions committed solely in the performance of professional services the company provides for others *for a fee*. Any coverage extended to in-house lawyers as corporate employees is intended to respond to corporate E&O exposures generally, rather than to the unique exposures facing your legal department.

The “professional services” definition, for example, is typically tied closely to the nature of the company’s business rather than the roles played by individual employees. The definition for a software developer might include the development, design, manufacturing, creating and licensing of computer software. For an investment advisor firm, “professional services” may be defined as financial advice provided

## Excerpt from the Delaware Business Code

The pertinent provisions of Section 145 are as follows:

- A corporation shall have power to indemnify any person who was or is a party or is threatened to be made a party to any threatened, pending, or completed action, suit, or proceeding, whether civil, criminal, administrative, or investigative (other than an action by or in the right of the corporation) by reason of the fact that the person is or was a director, officer, employee, or agent of the corporation, or is or was serving at the request of the corporation as a director, officer, employee, or agent of another corporation, partnership, joint venture, trust, or other enterprise, against expenses (including attorneys’ fees), judgments, fines, and amounts paid in settlement actually and reasonably incurred by the person in connection with such action, suit, or proceeding if the person acted in good faith and in a manner the person reasonably believed to be in or not opposed to the best interests of the corporation, and, with respect to any criminal action or proceeding, had no reasonable cause to believe the person’s conduct was unlawful.
- A corporation shall have power to indemnify any person who was or is a party or is threatened to be made a party to any threatened, pending, or completed action or suit by or in the right of the corporation to procure a judgment in its favor by reason of the fact that the person is or was a director, officer, employee, or agent of the corporation, or is or was serving at the request of the corporation as a director, officer, employee, or agent of another corporation, partnership, joint venture, trust, or other enterprise against expenses (including attorneys’ fees) actually and reasonably incurred by the person in connection with the defense or settlement of such action or suit if the person acted in good faith and in a manner the person reasonably believed to be in or not opposed to the best interests of the corporation and except that no indemnification shall be made in respect of any claim, issue or matter as to which such person shall have been adjudged to be liable to the corporation unless and only to the extent that the Court of Chancery or the court in which such action or suit was brought shall determine upon application that, despite the adjudication of liability but in view of all the circumstances of the case, such person is fairly and reasonably entitled to indemnity for such expenses which the Court of Chancery or such other court shall deem proper.
- To the extent that a present or former director or officer of a corporation has been successful on the merits or otherwise in defense of any action, suit, or proceeding referred to in subsections (a) and (b) of this section, or in defense of any claim, issue, or matter therein, such person shall be indemnified against expenses (including attorneys’ fees) actually and reasonably incurred by such person in connection therewith.
- The indemnification and advancement of expenses provided by, or granted pursuant to, the other subsections of this section shall not be deemed exclusive of any other rights to which those seeking indemnification or advancement of expenses may be entitled under any bylaw, agreement, vote of stockholders or disinterested directors or otherwise, both as to action in such person’s official capacity and as to action in another capacity while holding such office.
- For purposes of this section, references to “the corporation” shall include, in addition to the resulting corporation, any constituent corporation (including any constituent of a constituent) absorbed in a consolidation or merger which, if its separate existence had continued, would have had power and authority to indemnify its directors, officers, and employees or agents, so that any person who is or was a director, officer, employee, or agent of such constituent corporation, or is or was serving at the request of such constituent corporation as a director, officer, employee, or agent of another corporation, partnership, joint venture, trust, or other enterprise, shall stand in the same position under this section with respect to the resulting or surviving corporation as such person would have with respect to such constituent corporation if its separate existence had continued.

## ACC Extras on... Insurance

### ACC's 2008 Annual Meeting

Protect yourself! At ACC's 2008 Annual Meeting, October 19-22, in Seattle, WA, you can attend sessions including "702: Personal Liability Risks Facing In-house Counsel" and "907: Attacks on In-house Counsels' Ethics," both of which could help you earn CLE ethics credits! Visit <http://am.acc.com> today to register.

### ACC Alliance

Coverage Questions? Chubb is ACC's Alliance Partner for liability insurance. Chubb offers ACC members Employed Lawyers Professional Liability insurance to provide comprehensive coverage for in-house counsel. For more information, visit [www.acc.com/alliance](http://www.acc.com/alliance).

### ACC Top Ten

*Top Ten Steps to Making a Successful Transition: A Former Litigator's Guide to Going In-house* (2008). Read ACC's top ten tips on how to make a successful transition from the courtroom to an in-house operation. [www.acc.com/resource/v9284](http://www.acc.com/resource/v9284)

### ACC Docket

*Ten Issues to Consider When Negotiating Your Company's D&O Coverage* (2007). Directors and officers need to be concerned with the terms and conditions of their company's D&O liability insurance. Company heads are demanding that in-house counsel ensure that the broadest coverage available is in place, and this article will help you review the scope of protection for your company. [www.acc.com/resource/v8567](http://www.acc.com/resource/v8567)

### Program Materials

*Wearing Two Hats: Liability and Insurance Issues Facing Corporate Counsel* (2007). The aim of this paper is to assist those who maintain a foothold in each of the legal and business worlds. This paper explores the boundary between legal and business advice provided by in-house counsel, analyzes the potential liability and insurance ramifications associated with these two kinds of advice, and examines how the rules of ethics and changes in procedures may help in-house counsel in maintaining a balance. [www.acc.com/resource/v8060](http://www.acc.com/resource/v8060)

ACC has more material on this subject in our Virtual Library<sup>SM</sup>. To create your personalized search, visit [www.acc.com](http://www.acc.com), click on the "Research" pull-down menu button, then select Virtual Library. Type in your keywords and search to see the other resources we have available.

to a customer for a fee. With the possible exception of the staffing industry and outside placement of legal counsel and contract attorneys, the "professional services" definition does not typically extend to in-house lawyers in their legal capacities. Nor would in-house lawyers typically provide legal services to the company's customers for a fee, as would generally be required by the E&O insuring agreement.

E&O policies also frequently exclude claims made against insureds arising out of the rendering of professional services to any other insured entity, affiliate or individual; thus, traditional malpractice claims asserted by your corporate "client" or its constituents would be excluded in any event. Other governmental, regulatory, and criminal exposures, such as the SEC and DOJ examples discussed above, likewise do not fall within the scope of many standard E&O policies. Still other E&O policies expressly exclude exposures typically covered elsewhere such as securities claims, employment-related exposures, ERISA exposures, and/or intellectual property claims.

### D&O Coverage

You may have some coverage under the D&O policy, but it is likely limited in scope. Initially, you should review how your policy defines "insured persons." Some policies extend coverage only to duly elected or appointed directors and officers. Therefore, under such policies, only in-house lawyers who also serve as "duly elected" directors or "duly appointed" officers qualify as an "insured," and coverage may be limited to claims asserted against such individuals solely in those capacities.

Some, but not all, policies expressly include the general counsel position within the definition of insured persons. Many policies also extend some coverage to all employees generally. Private company D&O forms, in particular, often include broader coverage to corporate employees generally than do their public company D&O counterparts. Public company D&O policy forms, on the other hand, frequently extend coverage to all employees solely in connection with securities claims, or only when sued jointly with other director or officer insureds.

In-house lawyers, as corporate employees, should receive the benefit of any such coverage granted to all corporate employees; nevertheless, D&O policies are not typically crafted with in-house lawyer liability exposures in mind. Most policies exclude claims brought by the company or other insured persons, eliminating any potential coverage under the D&O policy for direct claims of legal malpractice. Securities claims filed by a court-appointed bankruptcy trustee or examiner—similar to the examples discussed above—may or may not be covered depending on the scope of your policy's grant of coverage to employees, as well as the wording of your "securities claim" definition and "insured vs. insured" exclusion.

Other D&O policies expressly exclude claims arising out of the rendering of professional services (E&O claims), or other

claims for which the insurer affords coverage under a different policy form (such as Employment Practices Liability, ERISA/Fiduciary Liability, Patent/Trademark/Intellectual Property exposures, etc.). And while in-house lawyers employed by public companies may find employee coverage for claims within the policy's definition of "securities claim," other liability exposures to third parties may be left uninsured.

In the past, some D&O insurers agreed to add in-house attorneys as covered insureds by endorsement to the D&O policy, either by amending the policy definition of "Directors and Officers" to include in-house attorneys or by specifically listing by name those in-house attorneys the insureds wished to include as "additional insureds" under the policy. While doing so expands the scope of D&O insurance protection afforded to in-house lawyers, certain exposures—such as direct malpractice liability and/or pro bono work—remain uninsured with this approach. Moreover, with the introduction of new insurance products specifically tailored to meet the claim risks faced by in-house lawyers, fewer insurers are willing to permit modification to their D&O program in this manner.

Nevertheless, a few insurers today will agree to provide a separate, sub-limit of liability coverage for in-house lawyers via endorsement to the D&O policy. Such endorsements vary significantly and should be closely scrutinized. "Employed Lawyers" sublimit endorsements to D&O policies do not typically extend to all in-house lawyer liability exposures. For example, direct claims of legal malpractice brought by the company or other insured persons are frequently excluded. Nor do such endorsements typically extend coverage to pro bono work for others, or to paralegals or other non-attorneys within the legal department. Many such endorsements further exclude coverage for in-house lawyers unless other director or officer insureds are and remain named defendants alongside the in-house lawyer. And, some endorsements fail to address how the sublimit of liability granted to in-house lawyers in the endorsement will apply in the context of claims where employee coverage may already exist. Finally, any coverage extension for employed lawyers under the D&O policy is likely subject to a very large corporate retention to the extent indemnification is legally and financially permissible (whether or not granted), and your directors and officers may be uncomfortable sharing their D&O limits with legal malpractice exposures.

### **Employed Lawyers Professional Liability Insurance Coverage**

Fortunately, many insurers today now offer a separate liability insurance policy specifically designed for in-house lawyers called employed lawyers professional liability insurance (ELP). While a few insurers still only offer the coverage via endorsement to an E&O or D&O policy, a number of leading insurers today now offer a stand-alone

ELP policy form. Such policies typically provide a separate, dedicated limit of liability to in-house lawyers from that available in the corporate E&O or D&O program, and cover the company's indemnification obligation to its in-house lawyers, as well as afford coverage to in-house lawyers individually when corporate indemnification is unavailable.

A principal advantage of purchasing separate ELP coverage (rather than obtaining an endorsement to the company's existing E&O or D&O policy) is that the ELP policies were specifically designed to address the unique exposures facing in-house lawyers. For example, several new ELP policy forms or endorsements expressly include as covered "claims" bar proceedings and claims or charges arising out of the "up the ladder" reporting obligations issued pursuant to Section 307 of the Sarbanes-Oxley Act.


Additionally, many ELP policy forms provide defense costs coverage for direct malpractice claims brought by corporate employers against in-house lawyers, while such claims are likely excluded (*including coverage for defense costs*) in most E&O and D&O policy forms by the insured vs. insured exclusion. Other potential benefits of ELP coverage, not provided by typical E&O or D&O policy forms, include coverage for claims arising out of moonlighting, pro bono, or other legal services provided by the in-house lawyers at the request of their corporate employer (where the legal department maintains an active company pro bono initiative for example), as well as coverage for "personal injury" claims such as false arrest or imprisonment, malicious prosecution, defamation, and/or violation of the right to privacy. Additionally, if your circumstances in-house require you to render personal legal advice to various corporate constituents (directors or members of senior management, for example) and the more stereotypical role of rendering legal advice solely on behalf of your corporate entity employer, ELP forms can be structured to afford coverage for certain limited personal malpractice exposures as well.

As with other lines of insurance, not all policy forms are created equal and you get what you pay for. ELP coverage has historically been relatively inexpensive. A \$1 million ELP policy with basic coverage might have been obtained in recent past for as little premium as \$2,000-3,000 per in-house lawyer. As limits of liability and the size and exposure of your legal department increase, so does the cost of ELP coverage.

Whether you address in-house lawyer liability exposure under the company's D&O program or choose to mitigate the risk by purchasing a separate ELP policy, in either case, coverage enhancements to the existing policy forms may be desirable. For example, as previously noted, in-house lawyers today face greater liability exposure in the bankruptcy context. Insureds may accordingly wish to negotiate a carve out to any insured vs. insured exclusionary language,

such as that claims brought by bankruptcy trustees or other parties standing in the shoes of the debtor client find coverage both in terms of defense costs, as well as settlement and other loss. Moreover, important coverage issues in structuring a D&O policy, such as severability as to application defenses and exclusions, as well as trigger language in personal conduct or fraud exclusions, deserve equal attention in negotiating ELP coverage. In light of the lower premiums typically associated with ELP coverage, substantial coverage enhancements may be difficult to achieve. Assuming you are able to convince the underwriter to extend further coverage, keep in mind also that there may be an additional premium cost associated with manuscripting coverage enhancements.

You will also want to pay careful attention to how your ELP coverage may interact with other existing D&O coverage. Some ELP policies will limit securities claim coverage to a designated sublimit of liability. Other ELP policies are expressly in excess of any coverage afforded in-house lawyers under the company's existing D&O program. It should be noted that certain coverage issues, such as the lack of coverage for disgorgement, fines, or penalties, might remain without an insurance solution. Many insurance policies, for example, exclude coverage for disgorgement or restitu-

tion, as well as criminal and most, if not all, civil fines and penalties. ELP coverage may nevertheless be structured to afford a legal defense to in-house lawyers facing exposure to regulatory or criminal investigations or proceedings. Finally, even if despite recent examples, you still believe that your legal department faces minimal exposures, ELP coverage can nevertheless serve as a valuable recruiting tool to attract high quality lawyers to your team. 

*Have a comment on this article? Email [editorinchief@acc.com](mailto:editorinchief@acc.com).*

#### NOTES

- 1 *J&B Indus., Inc. v. Abood*, No. L-02-1062, 2002 WL 31420110 (Ohio Oct. 25, 2002).
- 2 *See, e.g., Shadwick v. Butler Nat'l Corp.*, 950 F. Supp. 302 (D. Kan. 1996) (sued former assistant general counsel for legal malpractice); *J&B Indus., Inc. v. Abood*, No. L-02-1062, 2002 WL 31420110 (Ohio Oct. 25, 2002) (corporation filed action against former in-house lawyer for breach of fiduciary duty, legal malpractice and theft after corporation entered into transactions allegedly approved or caused by lawyer); *Dash v. Chicago Ins. Co.*, No. Civ. A. 00-11911-DPW, 2004 WL 1932760 (D. Mass. Aug. 23, 2004) (in prior suit, company sued former in-house for legal malpractice, breach of fiduciary duty, and other claims based on assistance allegedly provided to company competitor).

- 3 294 B.R. 449 (S.D.N.Y. 2003), *vacated and remanded by*, 413  
 4 F.3d 330 (2d Cir. 2005).
- 4 *Id.* at 522.
- 5 *Id.* at 523.
- 6 *Id.* at 524.
- 7 *Id.*
- 8 *Id.*
- 9 *See, e.g., In re Enron Corp.*, No. 01-16034 (AJG) (Bankr.  
 S.D.N.Y. Nov. 4, 2003) (Final Report of Neal Batson, Court-  
 Appointed Examiner).
- 10 *See Sheet Metal Workers Local #218(S) Pension Fund v. Hills*,  
 No. 1:07-CV-01957 (D.D.C. filed Oct. 31, 2007) (alleging that  
 Olson “provided legal counsel and advice to many of the [d]  
 efendants and Chiquita”).
- 11 *Schnelling v. Budd (In re Agribiotech, Inc.)*, 291 F. Supp. 2d  
 1186, 1193 (D. Nev. 2003) (Chapter 11 Trustee suit against  
 corporate general counsel stated claim for negligent misrepresen-  
 tation by nondisclosure of material information where principal  
 allegation was that defendant made affirmative misrepresenta-  
 tions by attending and remaining silent at a critical meeting and  
 by reviewing and approving a letter which purportedly contained  
 misrepresentations by corporate officers).
- 12 *See, e.g., S.E.C. v. Olesnyckyj*, No. 07 CV 1176 (S.D.N.Y. filed  
 Feb. 15, 2007) (SEC claims filed against Monster Worldwide, Inc.  
 former general counsel for his role in stock options backdating  
 scheme); *United States v. Sorin*, No. 1:06 CR 00723 (E.D.N.Y.  
 filed Aug. 9, 2006) (DOJ charges filed against Comverse Technol-  
 ogy, Inc. former general counsel for his role in backdating stock  
 options); *In re Google, Inc., and David C. Drummond*, Admin.  
 Proc. File No. 3-111795 (filed Jan. 13, 2005) (SEC claims filed  
 against general counsel of Google, Inc., alleging that his failure to  
 properly advise the board led the company to issue \$80 million  
 worth of unregistered stock options); *United States v. Grass*, No.  
 1:02-CR-00146 (M.D. Penn. filed June 21, 2002) (SEC claims  
 filed against Rite-Aid Corp.’s former chief counsel, alleging that he  
 conspired to inflate the company’s earnings); *S.E.C. v. Jordan H.*  
*Mintz and Rex R. Rogers*, No. 07-1027 (S.D. Tex. filed Mar. 28,  
 2007) (SEC claims filed against two former Enron in-house attor-  
 neys for their role in making material misrepresentations in, and  
 omitting material disclosures from, the company’s public filings).
- 13 Christopher Cox, Chairman, Sec. & Exch. Comm’n, Address to  
 the 2007 Corporate Counsel Institute (Mar. 8, 2007).
- 14 Giovanni P. Prezioso, General Counsel, Sec. & Exch. Comm’n,  
 Remarks before the Spring Meeting of the Association of General  
 Counsel (Apr. 28, 2005).
- 15 *See, e.g., S.E.C. v. Alexander*, No. 1:06-CV-03844 (E.D.N.Y. filed  
 Jan. 19, 2007); *S.E.C. v. Mercury Interactive*, No. 5:07-CV-02822  
 (N.D. Cal. filed May 31, 2007); *S.E.C. v. Olesnyckyj*, No. 1:07-  
 CV-1176 (S.D.N.Y. filed Mar. 27, 2007); *S.E.C. v. Roberts*, No.  
 1:07-CV-00407 (D.D.C. filed Feb. 28, 2007); *S.E.C. v. Heinen*,  
 No. 5:07-CV-2214 (N.D. Cal. filed Apr. 24, 2007); *S.E.C. v.*  
*Berry*, No. 5:07-CV-4431 (N.D. Cal. filed Aug. 28, 2007).
- 16 *See S.E.C. v. Alexander*, No. 1:06-CV-03844 (E.D.N.Y. filed Jan.  
 19, 2007).
- 17 *See S.E.C. v. Berry*, No. 5:07-CV-4431 (N.D. Cal. filed Aug. 28,  
 2007).
- 18 *See United States v. Sorin*, No. 1:06-CR-00723 (E.D.N.Y. filed  
 May 15, 2007) (sentencing Sorin to one year in prison and  
 requiring him to pay \$51,784,888 in restitution and a \$100,000  
 fine); *see also United States v. Olesnyckyj*, No. 1:07-CR-00120  
 (S.D.N.Y. filed Aug. 21, 2007) (adjourning sentencing until Feb-  
 ruary 2008); *United States v. Roberts*, No. 07-0100 (N.D. Cal.  
 filed Feb. 27, 2007).
- 19 *See S.E.C. v. Jordan H. Mintz and Rex R. Rogers*, No. 07-1027  
 (S.D. Tex. filed Mar. 28, 2007) (charging two former Enron  
 in-house attorneys with securities fraud for their role in making  
 material misrepresentations in, and omitting material disclosures  
 from, the company’s public filings); *S.E.C. v. Lapine*, No. C-01-3650  
 (N.D. Cal. filed Sept. 27, 2001) (charging former general counsel of  
 HBOC/McKesson Corp. with securities fraud for allegedly negotiat-  
 ing “side letters” permitting premature revenue recognition); *S.E.C.*  
*v. Bruce Hill*, No. 02-CV-11244 (D. Mass. filed June 21, 2002)  
 (filing civil injunctive action against former general counsel of Inso  
 Corp. for his alleged role in negotiating \$3 million sham transac-  
 tion); *see also S.E.C. v. Pietrzak*, No. 03C-1507 (N.D. Ill. filed  
 Mar. 6, 2003); *S.E.C. v. Universal Express, Inc.*, No. 04 CV 02322  
 (S.D.N.Y. filed Mar. 24, 2004); *In re Google, Inc. and David C.*  
*Drummond*, Admin. Proc. File No. 3-111795 (filed Jan. 13, 2005);  
*S.E.C. v. Isselmann*, No. 04-1350 (D. Ore. filed Sept. 24, 2004);  
*S.E.C. v. Scott*, No. 3-05 CV 0302 (N.D. Tex. filed Feb. 14, 2005);  
*In re Phlo Corp.*, Admin. Proc. File No. 3-11909 (filed Apr. 21,  
 2005); *S.E.C. v. Grotto*, No. 05-CV-5880 (S.D.N.Y. filed June 24,  
 2005); *In re Carley*, Admin. Proc. File No. 3-11626 (filed Sept. 1,  
 2004); *S.E.C. v. Biopure Corp.*, No. 05-11853 (D. Mass. filed Sept.  
 14, 2005); *S.E.C. v. Ferguson*, No. 06 Civ 0778 (S.D.N.Y. filed Feb.  
 2, 2006); *United States v. Black*, No. 05 CR 727 (N.D. Ill. filed Nov.  
 17, 2005); *United States v. Stein*, No. 05 CR 888 (LAK) (S.D.N.Y.  
 filed Oct. 17, 2005); *United States v. Benyo*, No. 1:05 CR 12 (E.D.  
 Va. filed July 11, 2005); *United States v. Smith*, No. CR 05-282 (D.  
 Minn. filed Jan. 24, 2006); *United States v. Ferguson*, No. N-06-1  
 (D. Conn. filed Sept. 20, 2006); *United States v. Gardner*, No. 04  
 CR 2605W (S.D. Cal. filed July 19, 2006); *United States v. Crook*,  
 No. 04-CR-2605 (S.D. Cal. filed Apr. 25, 2007); *United States*  
*v. Woghin*, No. 1:04 CR 00847 (E.D.N.Y. filed Sept. 21, 2004);  
*United States v. Collins*, No. 1:07-CR-01170 (S.D.N.Y. filed Dec.  
 18, 2007); *State v. Grabinski* (Ariz. St. Ct. filed May 4, 2001).
- 20 *See S.E.C. v. Tenet Healthcare Corp.*, No. CV-07-2144, ¶8 (C.D.  
 Cal. filed Apr. 2, 2007). Tenet agreed to pay a civil penalty of  
 \$10 million in order to settle the charges against the company. To  
 settle the charges against them, Tenet’s former CFO and co-pres-  
 ident agreed to pay a \$150,000 penalty, while the former chief  
 accounting officer agreed to pay a \$240,000 civil penalty. As of  
 the time this article went to publication, the charges against the  
 former general counsel were still pending.
- 21 *Id.* at ¶96.
- 22 303 F. Supp. 2d 672 (D. Md. 2003).
- 23 166 Fed. Appx. 4, 11 (4th Cir. 2006) (affirming the district  
 court’s denial of Cohn’s fourth motion for a new trial).
- 24 *See, e.g., S.E.C. v. Woghin*, 04 Civ. 4087 (E.D.N.Y. filed Sept. 22,  
 2004); *S.E.C. v. Bruce Hill*, No. 02-11244 (D. Mass. filed June 6,  
 2005); *United States v. Grass*, No. 1:02-CR-00146 (M.D. Penn.  
 filed June 21, 2002).
- 25 Sue Reisinger, *Blood Money Paid by Chiquita Shows Company’s*  
*Hard Choices*, Corporate Counsel, Dec. 2007, at 90.
- 26 *Id.* at 90.
- 27 *Id.* at 92-94.
- 28 *Id.* at 92.
- 29 *Id.* at 93.
- 30 *Id.* at 94.
- 31 *Id.* at 94-95.

- 32 See, e.g., *In re Comverse Tech., Inc. Derivative Litig.*, No. 2:06-CV-01849 (E.D.N.Y. filed Apr. 20, 2006) (naming William F. Sorin as a defendant); *In re Mercury Interactive Corp. Derivative Litig.*, No. 5:05-CV-04642 (N.D. Cal. filed Nov. 14, 2005) (naming Susan Skaer as a defendant); *In re Monster Worldwide, Inc. Sec. Litig.*, No. 1:07-CV-02237 (S.D.N.Y. filed Mar. 15, 2007) (naming Myron Olesnyckyj as a defendant); *Webb v. McAfee, Inc.*, No. 5:07-CV-04048 (N.D. Cal. filed Aug. 7, 2007) (naming Kent Roberts as a defendant).
- 33 *In re Qwest Comm'cns Int'l, Inc. Sec. Litig.*, 396 F. Supp. 2d 1178 (D. Colo. 2004).
- 34 See also, e.g., *In re Tenet Healthcare Corp. Derivative Litig.*, No. 01098905 (Cal. Super. Ct. filed Nov. 12, 2002) (alleging that Tenet's former General Counsel and Chief Compliance Officer knew or should have known that the company was fraudulently inflating its revenues).
- 35 114 S. Ct. 1439 (1994).
- 36 *In re Enron Corp. Sec., Derivative, & "ERISA" Litig.*, 236 F.R.D. 313 (S.D. Tex. 2006), *reversed by*, *Regents of Univ. of Cal. v. Credit Suisse First Boston (USA), Inc.*, 482 F.3d 372 (5th Cir. 2007), *cert. denied*, *Regents of Univ. of Cal. v. Merrill, Lynch, Pierce, Fenner & Smith, Inc.*, 128 S. Ct. 1120 (U.S. 2008).
- 37 *Regents of Univ. of Cal. v. Credit Suisse First Boston (USA), Inc.*, 482 F.3d 372 (5th Cir. 2007).
- 38 *Regents of Univ. of Cal. v. Merrill, Lynch, Pierce, Fenner & Smith, Inc.*, 128 S. Ct. 1120 (U.S. 2008).
- 39 128 S. Ct. 761 (U.S. 2008).
- 40 *Id.* at 772.
- 41 *Id.* at 773-74.
- 42 *Id.* at 773.
- 43 *Id.*
- 44 *JP Morgan Chase Bank v. Winnick*, 406 F. Supp. 2d 247 (S.D.N.Y. 2005).
- 45 *Id.* at 250.
- 46 *Id.* at 255.
- 47 *Id.* at 257.
- 48 *Id.* (quoting *Primavera Familienstiftung v. Askin*, 137 F. Supp. 2d 438, 511-12 (S.D.N.Y. 2001)).
- 49 *Id.*
- 50 *Id.* at 258.
- 51 *Davis & Cox v. Summa Corp.*, 751 F.2d 1507, 1527 (9th Cir. 1985), *overruled on other grounds by Northrop Corp. v. Triad Int'l Mktg., S.A.*, 842 F.2d 1154 (9th Cir. 1988); see also Joseph Warren Bishop II, *Law of Corporate Officers and Directors: Indemnification and Insurance* § 6:27 (2005) ("It is generally held that indemnification, like other corporate internal affairs, is governed by the law of the state of incorporation.")
- 52 Del. Code Ann. tit. 8, §145. Because many state indemnification statutes are not as broadly drafted, careful review of the statutory language governing your company will be important.
- 53 Prior to its amendment in 1997, the mandatory indemnification provision of subsection (c) extended to employees and agents. *Perconti v. Thornton Oil Corp.*, No. 18630-NC, 2002 WL 982419, at \*2 n.1 (Del. Ch. May 3, 2002).
- 54 Laura Thatcher, *Indemnification Issues for Board Members and Management in an Era of Enhanced Scrutiny*, (2002).