

# ANDERSON KILL POLICYHOLDER ADVISOR

The Policyholder Law Firm



## A D&O's Success on "the Merits or Otherwise" Should Eliminate Insurance Company Attempts to Recoup Defense Costs

By William Passannante

**D**&O liability insurance is specifically designed to protect individual directors and officers from crushing defense costs related to claims made against them. The D&O liability insurance protection works alongside the usual "corporate indemnity" protection available to many directors and officers.

Some insurance companies have argued that "improper" advancement of defense costs by the corporation pursuant to corporate indemnity statutes somehow permits the insurance company to "recoup" defense costs they previously advanced by re-litigating the policyholder's entitlement to defense costs even after a successful defense. In one recent case, the insureds under a D&O liability insurance policy asserted that under Delaware law, since their defense had been "successful on the merits or otherwise," that corporate indemnification was beyond being second-guessed by the D&O liability insurance company. Order Affirming Commissioner's Report and Recommendation, *HLTH Corporation v. New Hampshire Ins. Co.*, C.A. No. 07C-09-102 RRC (July 23, 2013). This inquiry involves a determination of whether the advancement of defense

costs would be "permissive indemnification" as opposed to "mandatory indemnification" under corporate indemnification statutes.

A policyholder may request a threshold legal determination regarding whether the D&Os were entitled to mandatory indemnification because they have "been successful on the merits or otherwise in defense of" the underlying matter within the meaning of Section 145(c). Del. Code Ann. tit. 8, § 145(c) (2008). Under Section 145 and established Delaware practice, that determination is to be made by the court as a threshold matter, prior to discovery, because "[t]his approach . . . avoids, where possible, prolonged and expensive discovery into the facts behind a particular dismissal, settlement, or plea." *Hermelin v. K-V Pharmaceutical Co.*, 54 A.3d 1093, 1111 (Del. Ch. 2012). Thus, if the court determines that the D&Os are entitled to mandatory indemnification, then none of the extensive litigation on permissive indemnification issues is necessary. Under section 145(c), "Any result other than conviction must be considered success in a criminal action." *Merritt-Chapman & Scott Corp. v. Wolfson*, 321 A.2d 138, 141 (Del. Super. 1974). Thus, the phrase "successful on

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the merits or otherwise” permits indemnification if a defendant is successful on a “technical” defense even if that does not involve the defendant being adjudged “innocent.” See, e.g., *Perconti v. Thornton Oil Corp.*, 2002 WL 982419, at \*4 (Del. Ch. May 3, 2002). In a situation in which the D&Os were acquitted, or had charges dismissed — even on supposedly “technical grounds” — Delaware law mandates indemnification of their defense costs, and the insurance company argument that the corporation “improperly” advanced defense costs must fail.

Moreover, if a D&O is “successful on the merits or otherwise” under section 145(c), the D&O is entitled to indemnification without the necessity of any analysis of the requirements of section 145(a). See, e.g., *Perconti* at \*3 (“[i]f

the former officer is ‘successful on the merits or otherwise’ in a proceeding described in Section 145(a), then he is entitled to indemnification regardless of whether or not he acted in good faith or in what he perceived to be the best interests of the corporation.”) *Green v. Westcap Corp. of Delaware*, 492 A.2d 260, 265 (Del. Super. 1985); *Hermelin* at 1114 (contrasting requirements of section 145(a) and 145(c)); Donald J. Wolfe, Jr. & Michael A. Pittenger, *Corporate and Commercial Practice in the Delaware Court of Chancery* § 8.02[a] [2] (2012).

States with corporate indemnification statutes that largely favor the ability of individual D&O’s to protect themselves via advancement of defense costs also may put to rest recent insurance company arguments regarding attempted “recoupment” of defense costs.▲

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## About Anderson Kill

Anderson Kill practices law in the areas of Insurance Recovery, Commercial Litigation, Environmental Law, Estate, Trusts and Tax Services, Corporate and Securities, Antitrust, Bankruptcy, Real Estate and Construction, Public Law, Government Affairs, Anti-Counterfeiting, Employment and Labor Law, Captives, Intellectual Property, Corporate Tax and Health Reform. Recognized nationwide by Chambers USA for Client Service and Commercial Awareness, and best-known for its work in insurance recovery, the firm represents policyholders only in insurance coverage disputes — with no ties to insurance companies and has no conflicts of interest. Clients include Fortune 1000 companies, small- and medium-sized businesses, governmental entities, and nonprofits as well as personal estates. Based in New York City, the firm also has offices in Ventura, CA, Dallas, TX, Stamford, CT, Washington, DC, Newark, NJ, and Philadelphia, PA.

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