



Implications of Conflicting D&O Indemnification Provisions

By Ryan Thomas

The Delaware Chancery Court has issued an opinion that addresses an issue that can arise when a director's or officer's right to indemnification or advance on legal fees flow from multiple organizational documents. Historically, the assumption has been that when the bylaws conflict with the certificate of incorporation, the bylaws are invalidated to the extent of the conflict.

However, in *Xu Hong Bin v. Heckmann Corp.*, decided in January of this year, the Delaware court ruled that if a corporation's current certificate of incorporation and bylaws were simultaneously adopted, then the courts would make every effort to reconcile conflicting provisions of the certificate of incorporation and bylaws, rather than per se invalidating the conflicting provision of the bylaws. This is based in part, on the practical assumption that the drafters did not intend for these documents to conflict.

Therefore, contrary to traditional expectations for conflicting organizational documents, the court concluded that Heckmann's bylaws effectively limited the provision providing for mandatory advancement of legal expenses in its certificate of incorporation and, therefore, allowed the company to impose (pursuant to those bylaws) reasonable terms and conditions on the director's right to advancement of legal ex-

penses, despite the fact those limitations were not set forth in the certificate of incorporation.

TAKE-AWAYS FOR COMPANIES

Companies should consider whether their intentions and policies regarding advancement and indemnification rights will be most effectively preserved if they flow from a single, carefully drafted source and whether that source should be the company's certificate of incorporation or bylaws.

If those rights are currently set forth in more than one document, including in separate indemnification agreements, the documents should be carefully reviewed together to ensure that they consistently express the intent of the company. Consider amending them if necessary. Keep in mind the need to consider potential shareholder vote and disclosure issues with respect to the feasibility of any amendments to its charter or bylaws.

As a related best practice, a company's indemnification documents should also be reviewed periodically by the company and qualified legal counsel to ensure that they adequately address recent developments in the law, include state-of-the-art indemnification concepts, and provide the breadth of protection intended in light of the circumstances.

TAKE-AWAYS FOR DIRECTORS AND OFFICERS

Before accepting an appointment, directors and officers (as potential indemnitees) should review the various organizational documents to ensure there are no potentially conflicting provisions that could limit their advancement or indemnification rights. Indeed, courts may not be sympathetic to directors or officers who do not do so.

For example, the court in Heckmann indicated that it typically would assume a director had reviewed such provisions before accepting a directorship, given their critical importance to directors generally. Incumbent directors also have a strong personal interest in reviewing these documents, specifically to assess if there is a potential adverse conflict.

At the end of the day, it is in the interest of both companies and directors to ensure that the advancement and indemnification protection offered to directors and officers is both clearly drafted and consistent with mutual expectations and best practices.



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in-house review tool? If the vendor lacks experience with the elements of workflow, mistakes are likely.

No one solution will handle all permutations of e-discovery and ECA challenges. Each ECA tool can serve a specific purpose. None will win a case by itself. None will reduce the volume of data without a well conceived strategy, and none will be able to pinpoint every responsive document without significant human intervention.

What ECA can do is significantly aid in the quick review of data sets, providing a draft strategic overview of the case at an early point. ECA tools can allow end users to cull data themselves, and to analyze that data in ways previously not available.

Unfortunately ECA has become a buzz word, and it has become more difficult to sort out conflicting and overlapping standards in order to determine which tool is best for a particular matter. Clients need to ask: Is the main issue culling and data reduction? Is it data analysis? Is it some of both? And, does the vendor know how to use the tool, and can it offer resources that will help achieve the desired result?

ECA can be a useful approach to a significant cost center facing any company. By reducing the quantity of data, ECA tools effectively impact data review, the most expensive portion of e-discovery. But to choose the right ECA tool, clients must understand the vocabulary, be willing to ask questions, and consider how the prospective tools will address their particular needs.



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