

**PRESENTATION OF  
APPOINTMENT OF INDEPENDENT DIRECTORS ON THE  
EVE OF BANKRUPTCY: WHY THE GROWING TREND?**

**EXAMINING DELAWARE CORPORATE GOVERNANCE THROUGH THE  
NEBULOUS ZONE OF INSOLVENCY LENS AND DELAWARE ABO RELATED  
ISSUES IN THE BANKRUPTCY CONTEXT**

Materials by:

Former Chief Justice Myron T. Steele & Peter I. Tsoflias

Potter Anderson & Corroon LLP  
Hercules Plaza  
1313 North Market Street  
Wilmington, Delaware 19801

**American Bar Association  
Business Law Section Spring Meeting**

Los Angeles, California  
April 10-12, 2014

**MODERATOR**

Regina Stango Kelbon  
Blank Rome, LLP  
1201 Market Street Suite 800  
Wilmington, DE 19801  
Telephone: (302) 425-6400  
Fax: (302) 425-6464

One Logan Square  
Philadelphia, PA 19103  
Telephone: (215) 569-5507  
Fax: (215) 832-5507  
E-Mail: [kelbon@blankrome.com](mailto:kelbon@blankrome.com)

**PANELISTS**

Former Chief Justice Myron T. Steele  
Potter Anderson & Corroon LLP  
Hercules Plaza  
1313 North Market Street, 6<sup>th</sup> Floor  
Wilmington DE 19801  
Telephone: (302) 984-6030  
E-Mail: [msteele@potteranderson.com](mailto:msteele@potteranderson.com)

Keith Maib  
Mackinac Partners LLC  
180 High Oak, Suite 100  
Bloomfield Hills, MI 48304  
Telephone: (248) 258-6900  
Mobile: (646) 591-4749  
E-Mail: [kmaib@mackinacpartners.com](mailto:kmaib@mackinacpartners.com)

Mary E. McCutcheon  
Farella Braun + Martel LLP  
Russ Building  
235 Montgomery Street, 17<sup>th</sup> Floor  
San Francisco, CA 94104  
Telephone: (415) 954-4404  
Fax: (415) 954-4480  
E-Mail: [mmccutcheon@fbm.com](mailto:mmccutcheon@fbm.com)

Martin A. Sosland  
Weil, Gotshal & Manges LLP  
200 Crescent Court, Suite 300  
Dallas, TX 75201  
Telephone: (214) 746-7730  
Fax: (214) 746-7777  
E-Mail: [martin.sosland@weil.com](mailto:martin.sosland@weil.com)

## I. INTRODUCTION

This Article supplements other materials our colleagues prepared for this American Bar Association presentation.<sup>1</sup> Here, we discuss the corporate governance implications corporate fiduciaries are confronted with when the corporation is operating in the zone of insolvency and when the company is actually insolvent. We also discuss some of the bankruptcy related issues concerning Delaware’s alternative business organizations (“ABOs”)—specifically, limited liability companies (“LLCs”), limited partnerships (“LPs”) and statutory trusts (“DSTs”).

## II. CORPORATE GOVERNANCE IMPLICATIONS UNDER DELAWARE LAW WHEN THE CORPORATION IS INSOLVENT OR OPERATING IN THE ZONE OF INSOLVENCY

### a. *Fiduciary duties owed to the corporation and its shareholders*

Charged with the task of managing a corporation’s business and affairs,<sup>2</sup> directors owe to the corporation and its shareholders the fiduciary duties of care and loyalty.<sup>3</sup> The duty of good faith is a subsidiary component of the duty of loyalty<sup>4</sup> and, in like manner, the duties of care and loyalty subsume a duty of disclosure.<sup>5</sup> As discussed in greater detail in a companion piece to this Article,<sup>6</sup> corporate fiduciaries must act in good faith, on an informed basis and in the best interest of the corporation and its shareholders to satisfy their unremitting fiduciary obligations.<sup>7</sup> These principles are well established in Delaware’s corporate law.<sup>8</sup>

---

<sup>1</sup> Regina Stango Kelbon, Michael DeBaecke & Jonathan K. Cooper, *Appointment of Independent Directors on the Eve of Bankruptcy: Why the Growing Trend?*, American Bar Ass’n Business Law Section Spring Meeting (2014); Rafael X. Zahralddin, Shelley Kinsella and Michelle L. Modery, *Appointment of Independent Directors on the Eve of Bankruptcy: Why the Growing Trend?, D&O Indemnification and Bankruptcy*, American Bar Ass’n Business Law Section Spring Meeting (2014); Mary E. MCutcheon and Unnati Gandhi, *Appointment of Independent Directors on the Eve of Bankruptcy: Why the Growing Trend?, D&O Insurance Issues in the Bankruptcy Context*, American Bar Ass’n Business Law Section Spring Meeting (2014).

<sup>2</sup> 8 Del. C. § 141(a).

<sup>3</sup> *Stone v. Ritter*, 911 A.2d 362 (Del. 2006). Although this Article makes reference to “directors” we note that officers and majority or controlling shareholders owe fiduciary duties to the corporation and its shareholders as well. See *Gantler v. Stephens*, 965 A.2d 695, 709 (Del. 2009); *Bershad v. Curtiss-Wright Corp.*, 535 A.2d 840 (Del. 1988).

<sup>4</sup> *Stone v. Ritter*, 911 A.2d 362 (Del. 2006).

<sup>5</sup> *Pfeffer v. Redstone*, 965 A.2d 676 (Del. 2009).

<sup>6</sup> Regina Stango Kelbon, Michael DeBaecke & Jonathan K. Cooper, *Appointment of Independent Directors on the Eve of Bankruptcy: Why the Growing Trend?*, American Bar Ass’n Business Law Section Spring Meeting (2014).

<sup>7</sup> *Gantler v. Stephens*, 965 A.2d 695 (Del. 2009); *McMullin v. Beran*, 765 A.2d 910 (Del. 2000); *Aronson v. Lewis*, 473 A.2d 805 (Del. 1984).

<sup>8</sup> See *N. Am. Catholic Educ. Programming Found., Inc. v. Gheewalla*, 930 A.2d 92, 101 (Del. 2007).

**b. *Fiduciary duties owed to the corporation's creditors***

While Delaware courts are loath to expand existing fiduciary duties, an equally clear principle under Delaware law is that when a corporation becomes insolvent, directors owe fiduciary duties to the company's creditors.<sup>9</sup> By extension, Delaware courts grant creditors of an insolvent corporation *derivative* standing to pursue breach of fiduciary duty claims on the entity's behalf.<sup>10</sup> This deviates from the general rule that corporate fiduciaries do not owe any duties to the company's creditors beyond those obligations contracted for.<sup>11</sup> This deviation is fueled, in large part, by "the idea that an insolvent corporation's creditors (having been effectively placed 'in the shoes normally occupied by the shareholders – that of residual risk-bearers') should be granted standing because they are the principal remaining constituency with a material incentive to pursue derivative claims on behalf of the corporation."<sup>12</sup> The Delaware Supreme Court has made clear, however, that a corporation's creditors cannot bring a *direct* breach of fiduciary duty cause of action despite the company's insolvency.<sup>13</sup>

Notably, in defining insolvency, Delaware law allows claimants to adopt both the "equitable" approach and "balance sheet" method.<sup>14</sup> To this end, a claimant may demonstrate insolvency by either showing "(1) 'a deficiency of assets below liabilities with no reasonable prospect that the business can be successfully continued in the face thereof,' or (2) 'an inability to meet maturing obligations as they fall due in the ordinary course of business.'"<sup>15</sup> Insofar as this definition applies to a breach of fiduciary duty analysis under Delaware law, non Delaware courts must allow parties to adopt either equitable or balance sheet approach.

Some plaintiffs have argued that, when a corporation is not deemed insolvent but, rather, is operating in the zone of insolvency, courts should grant creditors a similar right to pursue derivative claims on behalf of the corporation.<sup>16</sup> This argument generally stems from varying approaches to defining "zone of insolvency."<sup>17</sup> In *Production Resources Group, L.L.C. v. NCTGroup, Inc.*, for example, then Vice Chancellor, now Chief Justice Strine noted these

---

<sup>9</sup> *Gheewalla*, 2006 WL 2588971, \*11–12, republished in 32 Del. J. Corp. L. 612 (Del. Ch. 2006).

<sup>10</sup> *Gheewalla*, 2006 WL 2588971, \*12, republished in 32 Del. J. Corp. L. 612 (Del. Ch. 2006).

<sup>11</sup> *Gheewalla (Supreme Ct.)* (Citations omitted).

<sup>12</sup> *N. Am. Catholic Educ. Programming Found., Inc. v. Gheewalla*, 2006 WL 2588971 at \*12 (Del. Ch. Sept. 1, 2006).

<sup>13</sup> *Gheewalla*, 930 A.2d at 101.

<sup>14</sup> *Gheewalla*, 2006 WL 2588971.

<sup>15</sup> *Id.*

<sup>16</sup> *Id.*

<sup>17</sup> See, e.g., *Production Resources Group, L.L.C. v. NCTGroup, Inc.*, 863 A.2d 772 (Del. Ch. 2004).

inconsistent definitions and admonished that granting creditors standing in this metaphysical vicinity of insolvency would produce undesirable results:

Defining the “zone” for these purposes would also not be a simple exercise and talented creditors' lawyers would no doubt press for an expansive view. As our prior case law points out, as discussed above, it is not always easy to determine whether a company even meets the test for solvency. *See, e.g., Keystone Fuel Oil v. Del-Way Petroleum, Co.*, 1977 WL 2572 (Del.Ch. Jun. 16, 1977). Given that reality and the plaintiff-friendly standard that applies to attacks on pleadings, it is not surprising that in the past there have been (and inferably in the future there will be) situations when creditors are accorded standing to assert fiduciary duty claims at the pleading-stage and when, after discovery, courts determine that the companies were not insolvent. Going further and recognizing standing for creditors to bring fiduciary duty claims when a company is in the zone of insolvency would logically require this court to allow creditors standing if the complaint pleads facts that, if true, suggest that a company is within some imprecise and hard-to-define vicinity of insolvency. This means that creditors will be able to get discovery in situations when it is ultimately determined that the relevant company was not only solvent, but never even within the so-called zone of insolvency.<sup>18</sup>

In *Gheewalla*, our Supreme Court quelled the argument that directors owe fiduciary obligations to the corporation’s creditors when the company is operating in the amorphous zone of insolvency.<sup>19</sup> Citing the need to provide clarity to corporate directors, the Court held that “[w]hen a solvent corporation is navigating in the zone of insolvency, the focus for Delaware directors does not change: directors must continue to discharge their fiduciary duties to the corporation and its shareholders.”<sup>20</sup> Thus, although the line separating “insolvency” and the “zone of insolvency” is easily obfuscated, corporate fiduciaries do not owe any fiduciary duties to their creditors while operating outside insolvency.

***c. As a matter of corporate governance, what does Delaware’s insolvency jurisprudence mean for corporate fiduciaries?***

First, corporate fiduciaries must recognize that, although they do not owe *fiduciary* duties to the corporation’s creditors when operating outside the insolvency vicinity, creditors still have rights and potential causes of action against the corporation. Creditors often impose liens on corporate assets and negotiate certain contractual covenants and warranties to protect themselves in lending transactions. Creditors may also assert legal, nonfiduciary, claims against the corporation and may seek redress through the involuntary bankruptcy process, among other remedies.

---

<sup>18</sup> *Id.* at 790 n.56.

<sup>19</sup> *Gheewalla*, 930 A.2d at 101 (emphasis added).

<sup>20</sup> *Id.* (emphasis added)

Second, we must note that a corporation's creditors only have standing to maintain *derivative*, not direct, claims for breaches of fiduciary duties.<sup>21</sup> If a party brings a direct claim, that party can prevail without demonstrating an injury or breach of duty to the corporation, and any relief obtained flows to the claimant, as opposed to the company.<sup>22</sup> Derivative claims, however, are those brought on the corporation's behalf and, therefore, any recovery or remedy obtained goes back into the hands of the injured corporation.<sup>23</sup> This is an important distinction because creditors may deem it too costly to bring derivative claims against corporate fiduciaries in situations where the creditor will share any remedy obtained with multiple parties.

Finally, even if a creditor brings a derivative claim on the corporation's behalf, the creditor must overcome the hurdle of proving the underlying cause of action—that is, a breach of fiduciary duty. Under Delaware law, simply demonstrating that a strategy may result in greater loss to the insolvent company, by itself, is insufficient to create an inference that the corporate fiduciaries breached their duties.<sup>24</sup> Similarly, allegations that an insolvent firm assumed more debt to continue operating,<sup>25</sup> or continued employing and paying its officers and directors despite the company's lack of success, each taken alone, will not give rise to a breach of fiduciary duty cause of action.<sup>26</sup> The Court of Chancery made clear in *Trenwick America Litigation Trust* that the concept of “deepening insolvency,” despite its acceptance in federal jurisprudence, does not exist in Delaware.<sup>27</sup> By extension, under Delaware law, there is no absolute obligation on an insolvent company's board to commence operations and liquidate.<sup>28</sup> The board, acting with reasonable diligence and in good faith, may pursue strategies to maximize the firm's value.<sup>29</sup> Thus, when an insolvent company's fiduciaries act with due diligence, good faith, and in the corporation's best interest, despite the company's insolvency, the fiduciaries will be afforded protection under the business judgment rule.

#### ***d. Hypothetical***

---

<sup>21</sup> *Id.* at 101–102.

<sup>22</sup> *Tooley v. Donaldson, Lufkin & Jenrette, Inc.*, 845 A.2d 1031 (Del. 2004).

<sup>23</sup> *Id.*

<sup>24</sup> *Trenwick Am. Litigation Trust v. Ernst & Young, L.L.P.*, 906 A.2d 168, 174 (Del. Ch. 2006).

<sup>25</sup> *Id.* at 204–05 (“If the board of an insolvent corporation, acting with due diligence and good faith, pursues a business strategy that it believes will increase the corporation's value, but that also involves the incurrence of additional debt, it does not become a guarantor of that strategy's success. That the strategy results in continued insolvency and even more insolvent entity does not in itself give rise to a cause of action. Rather, in such a scenario the directors are protected by the business judgment rule. To conclude otherwise would fundamentally transform Delaware law.”).

<sup>26</sup> *Growbow v. Perot*, 539 A.2d 180, 188 (Del. 1988).

<sup>27</sup> *Trenwick Am. Litigation Trust*, 906 A.2d 168.

<sup>28</sup> *Id.*

<sup>29</sup> *Id.*

The following hypothetical, taken verbatim from the Court of Chancery’s decision in *Credit Lyonnaise Bank Nederland, N.V. v. Pathe Communications Corp.*, underscores the conflicting incentives directors may face when making decisions while operating in the zone of insolvency:

The possibility of insolvency can do curious things to incentives, exposing creditors to risks of opportunistic behavior and creating complexities for directors. Consider, for example, a solvent corporation having a single asset, a judgment for \$51 million against a solvent debtor. The judgment is on appeal and thus subject to modification or reversal. Assume that the only liabilities of the company are to bondholders in the amount of \$12 million. Assume that the array of probable outcomes of the appeal is as follows:

		Expected Value
25% chance of affirmance	(\$51mm)	\$12.75
70% chance of modification	(\$4mm)	2.8
5% chance of reversal	(\$0)	0
<hr/>		
Expected Value of Judgment on Appeal		

Thus, the best evaluation is that the current value of the equity is \$3.55 million. (\$15.55 million expected value of judgment on appeal—\$12 million liability to bondholders). Now assume an offer to settle at \$12.5 million (also consider one at \$17.5 million). By what standard do the directors of the company evaluate the fairness of these offers? The creditors of this solvent company would be in favor of accepting either a \$12.5 million offer or a \$17.5 million offer. In either event they will avoid the 75% risk of insolvency and default. The stockholders, however, will plainly be opposed to acceptance of a \$12.5 million settlement (under which they get practically nothing). More importantly, they very well may be opposed to acceptance of the \$17.5 million offer under which the residual value of the corporation would increase from \$3.5 to \$5.5 million. This is so because the litigation alternative, with its 25% probability of a \$39 million outcome to them (\$51 million *[sic]* – \$12 million = \$39 million) has an expected value to the residual risk bearer of \$9.75 million (\$39 million x 25% chance of affirmance), substantially greater than the \$5.5 million available to them in the settlement. While in fact the stockholders' preference would reflect their appetite for risk, it is possible (and with diversified shareholders likely) that shareholders would prefer rejection of both settlement offers.

But if we consider the community of interests that the corporation represents it seems apparent that one should in this hypothetical accept the best settlement offer available providing it is greater than \$15.55 million, and one below that amount should be rejected. But that result will not be reached by a director who thinks he owes duties directly to shareholders only. It will be reached by directors who are capable of conceiving of the corporation as a legal and economic entity. Such directors will recognize that in managing the business affairs of a solvent corporation in the vicinity of insolvency, circumstances may arise when the right

(both the efficient and the fair) course to follow for the corporation may diverge from the choice that the stockholders (or the creditors, or the employees, or any single group interested in the corporation) would make if given the opportunity to act.<sup>30</sup>

### III. ABO RELATED ISSUES IN THE BANKRUPTCY CONTEXT

Unlike corporations, Delaware’s alternative business organizations—specifically, LLCs, LPs and DSTs—are creatures of contract. The ABO statutes—the Delaware Limited Liability Company Act (“LLC Act”), the Delaware Limited Partnership Act (“LP Act”) and the Delaware Statutory Trust Act (“DSTA”)—are unique in that they each have an enumerated purpose to give maximum effect to the principles of freedom of contract and to the enforceability of an ABO’s governing instrument or agreement.<sup>31</sup> With very few mandatory provisions, the ABO statutes allow the ABO’s parties to define nearly all aspects of their business relationship within the four corners of the governing instrument or agreement. Where the parties fail to agree to a specific provision, default rules in the ABO statutes (and, in very limited situations, common law principles) serve as “gap fillers.”

#### *a. The ABO statutes deny derivative standing to an insolvent company’s creditors*

In light of these unique characteristics, our analysis concerning derivative creditor standing changes in the ABO context. In the first instance, even if an ABO’s creditors were granted similar derivative standing rights as they are in the corporate setting (which we indicate below they are not), the creditors would merely stand in the members’ (in the case of LLCs and LPs) or beneficial owners’ (in the case of DSTs) shoes, only taking the rights (if any) these members or beneficial owners have. Accordingly, because parties may expand, restrict or wholly eliminate any fiduciary duties (to the extent they exist) in the ABO’s governing instrument or agreement, the derivative creditor’s underlying cause of action may not exist.<sup>32</sup>

Each of the LLC Act, the LP Act and the DSTA unambiguously limit derivative standing to “member[s]” or “assignee[s]” (in the case of LLCs and LPs) and “beneficial owner[s]” (in the case of DSTs).<sup>33</sup> To be sure, Sections 18-1001 and 18-1002 of the LLC Act (which is nearly identical to the LP Act and the DSTA in this regard)<sup>34</sup> read:

---

<sup>30</sup> *Credit Lyonnais Bank Nederland, N.V. v. Pathe Communications Corp.*, 1991 WL 277613, republished in 17 Del. J. Corp. L. 1099, 1159 n.55 (Del. Ch. 1991).

<sup>31</sup> 6 Del. C. § 17-1101(c) (LP Act); 6 Del. C. § 18-1101(b) (LLC Act); 12 Del. C. § 3825(b) (DSTA).

<sup>32</sup> 6 Del. C. § 17-1101(d) (LP Act); 6 Del. C. § 18-1101(c) (LLC Act); 12 Del. C. § 3806(c) (DSTA).

<sup>33</sup> 6 Del. C. §§ 17-1001, 17-1002 (LP Act); 6 Del. C. §§ 18-1001, 18-1002 (LLC Act); 12 Del. C. §§ 3816(a), (b) (DSTA).

<sup>34</sup> 6 Del. C. §§ 17-1001, 17-1002 (LP Act); 6 Del. C. §§ 18-1001, 18-1002 (LLC Act); 12 Del. C. §§ 3816(a), (b) (DSTA).

### **§ 18-1001 Right to bring action.**

A member or an assignee of a limited liability company interest may bring an action in the Court of Chancery in the right of a limited liability company to recover a judgment in its favor if managers or members with authority to do so have refused to bring the action or if an effort to cause those managers or members to bring the action is not likely to succeed.

### **§ 18-1002 Proper plaintiff.**

In a derivative action, the plaintiff must be a member or an assignee of a limited liability company interest at the time of bringing the action and:

- (1) At the time of the transaction of which the plaintiff complains; or
- (2) The plaintiff's status as a member or an assignee of a limited liability company interest had devolved upon the plaintiff by operation of law or pursuant to the terms of a limited liability company agreement from a person who was a member or an assignee of a limited liability company interest at the time of the transaction.<sup>35</sup>

Interpreting these provisions, the Delaware Supreme Court in *CML V, LLC v. Bax* held this “statutory language is clear, unequivocal, and exclusive, and operates to deny derivative standing to creditors who are not members or assignees of membership interest.”<sup>36</sup> What’s more, the Court held that this limitation is constitutional (under the Delaware Constitution) despite the Delaware Constitution’s prohibition against the General Assembly’s limiting the Court of Chancery’s jurisdiction.<sup>37</sup> Indeed, the Court admonished that LLCs are statutorily created business vehicles that came into existence when the General Assembly passed the LLC Act—a statute passed expressly in derogation of the common law.<sup>38</sup> In this vein, courts must look to the LLC Act when adjudicating the rights, remedies and obligations associated with LLCs because the LLC Act is the only statute that creates those rights, remedies and obligations.<sup>39</sup>

Recognizing that common law equity principles supplement the LLC Act’s express provisions, the Court correctly noted that these equity principles merely act as statutory gap fillers where the General Assembly has not defined a right, remedy or obligation with respect to LLCs.<sup>40</sup> Where the General Assembly has defined such a right, remedy or obligation, however,

---

<sup>35</sup> 6 *Del. C.* §§ 18-1001, 18-1002 (LLC Act).

<sup>36</sup> *CML V, LLC v. Bax*, 28 A.3d 1037, 1041 (2011).

<sup>37</sup> *Id.* at 1043–46.

<sup>38</sup> *Id.*

<sup>39</sup> *Id.* at 1045.

<sup>40</sup> *Id.* (citing 6 *Del. C.* § 18-1104 (“In any case not provided for in this chapter, the rules of law and equity, including the law merchant, shall govern.”)).



“courts cannot interpret the common law to override the express provisions the General Assembly adopted.”<sup>41</sup> The General Assembly clearly and unequivocally defined the right to bring a derivative action under the LLC Act and, therefore, courts must limit this right to those parties enumerated in the statute.

This same analysis applies equally to LPs and DSTs as each of their respective governing statutes include nearly identical provisions to the LLC Act’s sections discussed above.<sup>42</sup>

***b. The ABO statutes provide “bankruptcy remoteness” features***

As we highlighted above, Delaware’s ABO statutes offer many benefits to business professionals. These benefits are often utilized in asset securitization enterprises because Delaware ABOs help minimize many of the risks associated with asset securitization. Most often, LLCs and DSTs are used in this context; accordingly, this section only discusses the statutory provisions relating to these business entities.

These risks are minimized through a mechanism termed “bankruptcy remoteness.” “This risk management mechanism involves effectively separating the assets being securitized from the originator of those assets, and implementing measures to protect against financial problems or bankruptcy of the securities issuer.”<sup>43</sup> By utilizing bankruptcy remoteness provisions, parties can temper concerns that the originating company’s creditors will be capable of reaching the ABO’s assets in bankruptcy proceedings involving the originator.<sup>44</sup> As a result of these decreased risks, unincorporated entities may raise capital at a lower cost.

The ABO statutes contain several enabling provisions and default rules to achieve bankruptcy remoteness. The following is a nonexhaustive list of bankruptcy remoteness features the ABO statutes offer:

1. Separateness between the ABO and its members, managers, beneficial owners or trustees (each, an “ABO party” and, collectively, “ABO parties”);<sup>45</sup>
2. The ABOs have perpetual existence (unless the governing instrument or agreement provides otherwise);<sup>46</sup>
3. ABO parties’ creditors do not have a right to obtain possession of, or exercise remedies with respect to, the ABO’s property;<sup>47</sup>

---

<sup>41</sup> *Id.*

<sup>42</sup> See 12 *Del. C.* §§ 3825(a), 3809 (DSTA); 6 *Del. C.* §§ 17-1101(b), 17-1105 (LP Act).

<sup>43</sup> Robert L. Symonds, Jr. & Matthew J. O’Toole, *Uses and Advantages of Delaware Statutory Trusts and Delaware Limited Liability Companies in Securitizations*, available at [http://www.globalrestructuring.com/05North%20America/104\\_107.htm](http://www.globalrestructuring.com/05North%20America/104_107.htm).

<sup>44</sup> *Id.*

<sup>45</sup> See 12 *Del. C.* § 3803 (DSTA); 6 *Del. C.* § 18-303 (LLC Act).

<sup>46</sup> See 12 *Del. C.* § 3808 (DSTA); 6 *Del. C.* § 18-8-801(a)(1) (LLC Act).

<sup>47</sup> See 6 *Del. C.* § 18-703 (LLC Act); 12 *Del. C.* § 3805(b) (DSTA).

4. ABO parties do not have an interest in specific ABO property (unless the ABO governing instrument or agreement provides otherwise);<sup>48</sup>
5. ABO parties' interest in the ABO is personal property;<sup>49</sup>
6. The bankruptcy of the an ABO party will not dissolve the ABO (unless the organizational instrument or agreement provides otherwise);<sup>50</sup>
7. The ABO parties may limit or define the events causing the ABO's dissolution;<sup>51</sup>
8. An LLC's member may continue to be a member to the LLC even upon that party's bankruptcy;<sup>52</sup>
9. The ABO parties can contractually implement bankruptcy procedures, including the appointment of a special independent committee, acting with or without fiduciary obligations, to determine, among other things, whether to file a voluntary bankruptcy petition;<sup>53</sup>
10. The ABO parties may limit the ABO's purpose and powers;<sup>54</sup> and
11. The ABO parties may modify the ABO's management and decision making authority.<sup>55</sup>

These bankruptcy remoteness features, and the concept of bankruptcy remoteness, are discussed in greater detail in an article authored by our colleagues: Robert L. Symonds, Jr. and Matthew J. O'Toole.<sup>56</sup>

#### IV. CONCLUSION

Although Delaware's corporate fiduciaries may conceive dilemmas when the corporation is operating in the zone of insolvency, Delaware's corporate fiduciaries should take solace in the fact that, in this context, their duties remain with the corporation and its shareholders. Only when the corporation is actually insolvent are the fiduciaries obligated to consider the company's

---

<sup>48</sup> See 6 Del. C. § 18-701 (LLC Act); 12 Del. C. § 3805(c) (DSTA).

<sup>49</sup> See 6 Del. C. § 18-701 (LLC Act); 12 Del. C. §3805(c) (DSTA).

<sup>50</sup> See 6 Del C. § 18-801(b); 12 Del. C. § 3808(b) (DSTA).

<sup>51</sup> See 6 Del. C. § 18-801 (LLC Act); 12 Del. C. §§ 3808 (DSTA).

<sup>52</sup> See 6 Del. C. § 18-304 (LLC Act). Note that under the DSTA, a beneficial owner may grant an irrevocable power of attorney that will withstand that beneficial owner's bankruptcy. See 12 Del. C. § 3811(d).

<sup>53</sup> Robert L. Symonds, Jr. & Matthew J. O'Toole, *Uses and Advantages of Delaware Statutory Trusts and Delaware Limited Liability Companies in Securitizations*, available at [http://www.globalrestructuring.com/05North%20America/104\\_107.htm](http://www.globalrestructuring.com/05North%20America/104_107.htm).

<sup>54</sup> See 6 Del. C. § 18-106 (LLC Act); 12 Del. C. § 3813801(g) (DSTA).

<sup>55</sup> See 6 Del. C. § 18-402 (LLC Act); 12 Del. C. § 3806 (DSTA).

<sup>56</sup> Robert L. Symonds, Jr. & Matthew J. O'Toole, *Uses and Advantages of Delaware Statutory Trusts and Delaware Limited Liability Companies in Securitizations*, available at [http://www.globalrestructuring.com/05North%20America/104\\_107.htm](http://www.globalrestructuring.com/05North%20America/104_107.htm).

creditor's interests. Nonetheless, even when the company is deemed insolvent, creditors still must overcome a number of hurdles to maintain a breach of fiduciary duty claim.

Delaware's unincorporated entities offer many unique benefits to business professionals unavailable through Delaware's corporate law. Delaware's ABO statutes make clear that a company's creditors have no right to bring derivative claims on the entity's behalf. These statutes also allow the ABO's parties to contractually shape their business relationship and minimize risk through "bankruptcy remoteness."