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ARTICLES

Attorney Fees for Enforcing Indemnification Rights in Litigation under Delaware Law

Are attorney fees incurred in indemnification lawsuits between parties to a contract an indemnifiable loss?

By Jason J. Rawnsley

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Parties entering into transactions often provide for indemnification rights in their agreements. Those agreements typically provide for reimbursement of attorney fees and costs as indemnifiable losses. For instance, the ABA Model Stock Purchase Agreement defines "Loss" as "any cost, loss, liability, obligation, claim, cause of action, damage, deficiency, expense (including costs of investigation and defense and reasonable attorney fees and expenses), fine, penalty, judgment, award, assessment, or diminution of value." ABA Mergers & Acquisitions Comm., *Model Stock Purchase Agreement with Commentary* 30–31 (2d ed. 2010). When a dispute arises about responsibility for an indemnifiable loss, the dissatisfied indemnitee not uncommonly initiates litigation. Can the indemnitee recover its attorney fees for bringing suit to enforce the indemnification right under so-called "standard" indemnity provisions? Stated differently, are attorney fees incurred in indemnification lawsuits between parties to a contract an indemnifiable loss?

A series of decisions under Delaware law (primarily from the Delaware Superior Court) has consistently concluded that the answer is "no," unless the agreement clearly and unambiguously reflects the parties' intent to that effect. This amounts to a presumption *against* recovery of attorney fees in what are described as "first-party" or "*inter se*" lawsuits—that is, lawsuits between the indemnitor and the indemnitee—to enforce indemnification rights.

But how clear largely remains unexplored territory. Because of the current state of the law on this doctrine, as discussed below, contracting parties should make explicit whether indemnification applies in litigation with one another, to avoid later surprises or frustrated expectations.

The Clear and Unambiguous Intent Requirement

In Delaware, the requirement that indemnification provisions must clearly and unambiguously reflect an intent to apply to litigation between the parties was first articulated in the Superior Court's decision in *TranSched Systems Ltd. v. Versyss Transit Solutions, LLC*, a case involving claims for breach of an asset-purchase agreement. 2012 WL 1415466 (Del. Super. Ct. Mar. 29, 2012). Versyss, the seller indemnitor, had agreed to indemnify and hold harmless TranSched, the buyer indemnitee, for all "Adverse Consequences" (defined to include attorney fees) arising from breaches of the representations, warranties, and covenants of the agreement. Relying on this clause, TranSched moved for attorney fees under the agreement after prevailing on breach claims at trial.

The parties did not dispute that Versyss would have to indemnify TranSched for its attorney fees if a third party had sued TranSched for claims attributable to a breach by Versyss. But Versyss disputed that the indemnification clause exposed it to attorney fees that TranSched incurred suing Versyss on TranSched's breach claims.

The court sided with Versyss. Recognizing that different jurisdictions had reached different conclusions in this situation, the court found more persuasive those cases that did not award attorney fees under language similar to the indemnification clause at issue. According to the court, "clear and unequivocal articulation" of the parties' intent must be present to overcome the American Rule (by which each side is ordinarily responsible for its own attorney fees in litigation, regardless of outcome). And looking to the agreement in the case, the court also found that the notice requirements for seeking indemnification and the indemnitor's right to select counsel and manage litigation were inconsistent with an intent to shift fees among the parties—another reason to require clear and unequivocal articulation.

Citing the clear-statement requirement, decisions since *TranSched* have been nearly uniform in denying requests for attorney fees sought under indemnification clauses. *See Balt. Pile Driving & Marine Constr., Inc. v. Wu & Assocs., Inc.*, 2022 WL 3466066 (Del. Super. Ct. Aug. 18, 2022); *Paul Elton, LLC v. Rommel Del., LLC*, 2022 WL 793126 (Del. Ch. Mar. 16, 2022); *Murfey v. WHC Ventures, LLC*, 2022 WL 214741 (Del. Ch. Jan. 25, 2022); *Great Hill Equity Partners IV, LP v. SIG Growth Equity Fund I, LLLP*, 2020 WL 7861336 (Del. Ch. Dec. 31, 2020); *Ashland LLC v. Samuel J. Heyman 1981 Continuing Tr. for Heyman*, 2020 WL 6582958 (Del. Super. Ct. Nov. 10, 2020); *Nasdi Holdings, LLC v. N. Am. Leasing, Inc.*, 2020 WL 1865747 (Del. Ch. Apr. 13, 2020); *In re Bracket Holding Corp. Litig.*,

2020 WL 764148 (Del. Super. Ct. Feb. 7, 2020); *Winshall v. Viacom Int'l Inc.*, 2019 WL 5787989 (Del. Super. Ct. Nov. 6, 2019), *aff'd*, 237 A.3d 67 (Del. 2020); *SARN Energy LLC v. Tatra Def. Vehicle A.S.*, 2019 WL 6525256 (Del. Super. Ct. Oct. 31, 2019); *Deere & Co. v. Exelon Generation Acquisitions, LLC*, 2016 WL 6879525 (Del. Super. Ct. Nov. 22, 2016); *Data Ctrs., LLC v. 1743 Holdings LLC*, 2015 WL 9464503 (Del. Super. Ct. Oct. 27, 2015); *Senior Hous. Capital, LLC v. SHP Senior Hous. Fund, LLC*, 2013 WL 1955012 (Del. Ch. May 13, 2013).

In the typical scenario, the indemnitee has prevailed on summary judgment or at trial and moves for attorney fees, citing the indemnification clause of the agreement in dispute. While decisions often state that the language of each indemnification agreement is unique, *see, e.g.*, *TranSched*, 2012 WL 1415466, at *2 ("Each provision is unique and must be decided under the facts of that particular case."), they offer scant guidance as to what language parties should include to indicate an agreement to shift fees for litigation between one another.

Clear and Unambiguous Intent Not Required for Indemnification Authorized by Statute

In *International Rail Partners LLC v. American Rail Partners*, Vice Chancellor Fioravanti of the Delaware Court of Chancery declined to apply the presumption to the indemnification and advancement provisions of a limited liability company (LLC) agreement. 2020 WL 6882105, at *1 (Del. Ch. Nov. 24, 2020). The plaintiffs, who qualified as "covered persons" under the indemnification clause at issue, sought advancement of fees and costs to defend against a separate lawsuit filed against them by the defendant. The defendant argued that the LLC agreement lacked language reflecting an intent to permit fee shifting in first-party litigation. According to the defendant, the claims could therefore never be indemnifiable, and so advancement was unavailable.

Reviewing the leading Delaware decisions addressing the clear-statement presumption, Vice Chancellor Fioravanti noted that the disputes all arose in cases involving commercial contracts, merger agreements, and stock or asset purchase agreements, but not in cases involving certificates of incorporation, bylaws, or (as here) LLC agreements.

That distinction took this case outside the ambit of the presumption. By statute, Delaware authorizes LLCs to indemnify and hold harmless members and managers. *See* 6 Del. Code § 18-108 ("Subject to such standards and restrictions, if any, as are set forth in its LLC agreement, a

limited liability company may, and shall have the power to, indemnify and hold harmless any member or manager or other person from and against any and all claims and demands whatsoever."). That statute does not limit indemnification and advancement to claims brought by a third party. Instead, it applies to "any and all claims and demands whatsoever," language echoed in the LLC agreement at issue in *International Rail*. And the court noted that the broad enablement of the statute further serves the policy goal of encouraging service in management positions at LLCs.

Thus, the court would not read into the broad language of the indemnification provision a distinction between third- and first-party disputes that was not present in the text and that would be at odds with a goal of the enabling statute.

Distinctions Between the Sources of Losses in Indemnification Provisions Can Overcome the Presumption

While sitting as a Superior Court judge by designation (as permitted under Delaware Constitution Article IV, section 13(2)) in *Schneider National Carriers, Inc. v. Kuntz*, Vice Chancellor Fioravanti received another opportunity to opine on whether a litigant could seek attorney fees as indemnifiable losses, this time in a commercial contract. 2022 WL 1222738 (Del. Super. Ct. Apr. 25, 2022). In *Schneider*, the court awarded the defendants attorney fees under the indemnification clause of a stock purchase agreement for the sale of a trucking company, even though the relevant section of the agreement did not include an "express reference to litigation between the parties." *Id.* at *30.

The parties disputed whether the buyer had complied with certain operating covenants, as the sellers alleged that the buyer's failure to comply caused it to fall short of the criteria for earnout payments. As to the indemnification clause in particular, the buyer argued that the language failed to overcome the presumption against first-party fee shifting, citing the long line of cases applying the presumption and noting that stare decisis required its application here. The court disagreed, holding that under the "well-established principles of contract construction," *id.* at *31, the indemnification clause clearly and unambiguously reflected the parties' intent to include attorney fees for enforcing an indemnification right in litigation for the following reasons:

- The provision specifically mentioned deferred consideration and contingent earnout payments owed to the sellers—payments that do not arise from a third-party claim—so the

indemnification clause necessarily covered claims not arising from third parties.

- The agreement excluded punitive and other special damages from the definition of indemnifiable "Losses"—but made an exception only for third-party claims, *id.* at *30 ("[T]he definition of 'Losses' makes an express distinction between indemnifiable damages arising from third-party claims and non-third-party claims.").

- The notice provision for seeking indemnification required that the indemnitee provide a claim notice for "any event or condition that could reasonably be expected to result in a Loss"—but separately "addresse[d] rights and obligations in the event that the claim notice 'identifie[d]' a third-party claim," *id.* ("This distinction reflects that the parties understood that claims within the scope of the indemnity clause were not limited to third-party claims.").

- There was no provision for fee shifting elsewhere in the agreement, whereas in some previous decisions the court had denied recovery of attorney fees under an indemnification clause if the contract elsewhere included a prevailing-party clause. *See id.* at *31.

According to the court, these distinctions made the agreement unlike those indemnification provisions found not to allow for first-party fee shifting in previous decisions. Instead, the language suggested that the parties foresaw the possibility of indemnifiable disputes arising directly between them. Thus, having found for the sellers, the court awarded attorney fees under the indemnification clause.

Questions Following *Schneider*

The principle underlying *Schneider* appears to be that *if* the parties agree that indemnifiable losses include attorney fees and *if* the indemnification provisions suggest that one party to the agreement directly causes the indemnitee to suffer indemnifiable losses (in contrast to losses that would arise from a claim by a third party), then by the plain text of the agreement, the parties must have intended indemnifiable losses to include *all* attorney fees—even for litigation between one another. As the court noted, "*TranSched* and its progeny do not require that an indemnity clause expressly state that it covers first-party claims." *Schneider*, 2022 WL 1222738, at *31.

But *Schneider* prompts further questions. To what degree do the provisions have to reflect that intent? What if only one of the four considerations identified by the *Schneider* court had been present? In an earlier decision, the court rejected a request for attorney fees even though the

definition of "Losses" specified "whether or not involving a Third Party Claim," *Ashland LLC v. Samuel J. Heyman 1981 Continuing Tr. for Heyman*, 2020 WL 6582958, at *6 (Del. Super. Ct. Nov. 10, 2020)—which would seem to show that the parties appreciated that indemnification claims could arise from first or third parties. Yet, the court there dismissed this argument: "Third Party Claim" was a defined term and not a general reference, and the definition of "Losses" did not include "explicit language applying to first-party claims." *Id.* at *7.

As noted in *Schneider*, the Delaware Supreme Court has not yet weighed in on the clear-and-unambiguous statement presumption. So how to draft indemnification clauses that *would* permit the indemnitee to recoup fees for prosecuting actions to enforce its indemnification rights? Because the decisions have largely told us only what won't work, the best guidance remains the same as what the court wrote in *TranSched* in 2012: Because "there is no definitive language that must be used or phrases that have been routinely held to allow for such recovery in first-party actions," it is "critical when drafting agreements that counsel use clean and precise language to set forth the parties' intentions." 2012 WL 1415466, at *2. In that regard, note that in *LPPAS Representative LLC v. ATH Holding Co.* Chancellor McCormick awarded attorney fees to one of the litigants under an indemnification clause that defined "Losses" to include "reasonable attorneys' fees, costs, and expenses incurred in connection with . . . *asserting or enforcing its rights* under this Agreement." 2022 WL 94610, at *7 (Del. Ch. Jan. 10, 2022) (omission in original, emphasis added).

In sum, parties negotiating indemnification terms under Delaware law should be aware of this interpretive doctrine that lurks in the background and that may or may not match the expectations they have when entering into an agreement. Although *Schneider* required only that the language explicitly reflect intent and not expressly state applicability to first-party claims, not all decisions characterize the presumption in that way. *See, e.g.*, *Winshall v. Viacom Int'l Inc.*, 2019 WL 5787989, at *5 (Del. Super. Ct. Nov. 6, 2019) ("The indemnification provision must unequivocally state that it applies to suits between the parties to apply to first-party claims."); *Deere & Co. v. Exelon Generation Acquisitions, LLC*, 2016 WL 6879525, at *1 (Del. Super. Ct. Nov. 22, 2016) ("In order for an indemnification provision to cover fee-shifting among parties, the contract must specifically state that requirement."). Parties would be best advised not to leave interpretive wiggle room to litigation—when agreeing to indemnification, be explicit about whether attorney fees incurred in litigation with your counterparty qualify as indemnifiable losses.

Jason J. Rawnsley is with Richards, Layton & Finger, P.A., in Wilmington, Delaware.