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SUPREME COURT OF THE STATE OF NEW YORK — NEW YORK COUNTY

PRESENT: [redacted] PART 99

Index Number : 602748/2003

KENSINGTON INTERNATIONAL

VS

HINER, GLEN

Sequence Number : 1

DISMISS

INDEX NO. _____

MOTION DATE 5/2/05

MOTION SEQ. NO. _____

MOTION CAL. NO. _____

The following papers, numbered 1 to _____ were read on this motion to/for _____

	PAPERS NUMBERED
Notice of Motion/ Order to Show Cause — Affidavits — Exhibits ...	
Answering Affidavits — Exhibits	
Replying Affidavits	

Cross-Motion: ☐ Yes ☐ No

Upon the foregoing papers, it is ordered that this motion

FILED

AUG 29 2006

COUNTY CLERK'S OFFICE
NEW YORK

MOTION IS DECIDED IN ACCORDANCE WITH ACCOMPANYING MEMORANDUM DECISION IN MOTION SEQUENCE . . . . .

MOTION/CASE IS RESPECTFULLY REFERRED TO JUSTICE FOR THE FOLLOWING REASON(S):

Dated: 8/22/06

J.S.C.

Check one: ☑ FINAL DISPOSITION ☐ NON-FINAL DISPOSITION

Check if appropriate: ☐ DO NOT POST

SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK : IAS PART 49

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KENSINGTON INTERNATIONAL LIMITED and SPRINGFIELD ASSOCIATES, LLC,

Plaintiffs,

-against-

Index No. 602748/03

GLEN HINER, MICHAEL THAMAN, J. THURSTON ROACH, DEYONNE F. EPPERSON, LANDON HILLIARD, MAURA ABELN SMITH, NORMAN P. BLAKE, JR., LEONARD S. COLEMAN, W. ANN REYNOLDS, CURTIS H. BARNETTE, ANN IVERSON, W. WALKER LEWIS, FURMAN C. MOSELEY, GASTON CAPERTON, and WILLIAM W. COLVILLE,

Defendants.

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Herman Cahn, J.:

Defendants move to dismiss the complaint, CPLR 3211 (a) (1) and (7), and 3016 (b).

Background:

This action arises out of the Chapter 11 bankruptcy filing of nonparty Owens Corning, a Delaware corporation that manufactures and sells building materials systems and composites systems, following its increased exposure to asbestos-related personal injury claims. *See In re Owens Corning*, US Bankr Ct, Dist Del, case no. 00-3837 [JKF].

Plaintiffs Kensington International Limited and Springfield Associates, LLC, allege that they are direct and indirect assignees of the rights to pursue and collect some $ 275,000,000, of debt owed to certain financial institutions (the assignors). The assignors had entered into a revolving credit agreement with Owens Corning on June 26, 1997, pursuant to which $ 275,000,000 was owed by Owens Corning. Plaintiffs bought these rights following Owens Corning's bankruptcy filing for on October 5, 2000.

Defendants Glen Hiner, Michael Thaman, J. Thurston Roach, Deyonne F. Epperson, Landon Hilliard and Maura Abeln Smith (collectively, the officer defendants) were officers of Owens Corning at various times during 1999 and 2000. Defendants Norman P. Blake, Jr., Leonard S. Coleman, W. Ann Reynolds, Curtis H. Barnette, Ann Iverson, W. Walker Lewis, Furman C. Moseley, Gaston Caperton and William W. Colville (collectively, the director defendants) were outside directors of Owens Corning during those years.

Plaintiffs allege breach of fiduciary duty and fraud claims based on the following factual allegations: In December 1998, Owens Corning was facing a very large number of personal injury claims in connection with injuries sustained by many persons on account of their exposure to asbestos. In order to better manage the claims, Owens Corning, with the acquiescence of some law firms representing plaintiffs in asbestos litigation, set up a National Settlement Program (NSP). Owens Corning was required to deposit money into the NSP in order to fund the settlements arrived at and to resolve the asbestos-related personal injury claims.

It is alleged that in the seven-month period leading up to the bankruptcy filing, the officer and director defendants engaged in a scheme to curry favor with the law firms representing NSP claimants. The claimed scheme was to transfer substantial sums totalling hundreds of millions of dollars into escrow accounts maintained by NSP claimants' attorneys, purportedly as security for future settlement payments, prior to the bankruptcy filing. To fund transfers, the defendants caused Owens Corning to increase its drawings under the revolving credit agreement from the lending banks (plaintiffs' assignors) from $ 675,000,000 to $ 1,312,000,000. Plaintiffs allege that the real purpose of these transfers, which took place before Owens Corning had a legal obligation to make them, was to put as much money as possible into the hands of law firms representing plaintiffs in the asbestos litigation before the bankruptcy filing. Plaintiffs allege

that defendants acted on the belief that, after the company's reorganization in bankruptcy, said law firms would effectively control Owens Corning and, thus, defendants' continued employment.

Plaintiffs also allege that, at the same time as the transfers were made, defendants withheld critical information from the lending banks; information that plaintiffs allege was secretly disclosed to the asbestos litigation firms. Defendants allegedly withheld the fact that the NSP was not working as anticipated and, therefore, that Owens Corning was in a precarious financial condition. They assert that, by no later than March 2000, defendants were aware of that problem, as well as the fact that Owens Corning had exceeded the schedule of payments underlying the NSP by more than $ 500,000,000.

Specifically, plaintiffs allege that, on March 12, 2000, various defendants met with the NSP executive committee and disclosed that:

- Owens Corning's scheduled payment obligations to the NSP over the next 18 months exceeded its ability to pay by at least $ 575,000,000;
- Owens Corning needed to defer payments of more than $ 500,000,000 to continue as a viable entity;
- Owens Corning's financial stability was threatened by the NSP payments;
- Owens Corning needed to borrow an additional $ 600,000,000 to pay the $ 950,000,000 of asbestos claims due in 2000.

Plaintiffs further allege that had their assignors been aware of the true facts, they would not have advanced these sums to Owens Corning.

This action is brought to recover losses allegedly sustained by the assignors when Owens

Corning borrowed substantial sums under the revolving credit agreement during the same period in which it was making prepayments to the NSP claimants.

Defendants move to dismiss the complaint as fatally defective on its face.

Discussion:

Conflict of Law:

As a threshold matter, the court notes that the parties do not raise any conflicts of law issues. They apparently agree that, because the claim of breach of fiduciary duty is asserted against officers and directors of a Delaware corporation, New York choice-of-law rules dictate that Delaware law governs. *Hart v General Motors Corp.*, 129 AD2d 179, 183-85 [1st Dep't], *appeal denied,* 70 NY2d 608 [1987]; *Solow v Stone*, 994 F Supp 173, 177 [SDNY 1998], *affd,* 163 F3d 151 [2d Cir 1998]. Indeed, "only one State should have the authority to regulate a corporation's internal affairs -- matters peculiar to the relationships among or between the corporation and its current officers, directors, and shareholders -- because otherwise a corporation could be faced with conflicting demands" (*Edgar v Mite Corp.*, 457 US 624, 645 [1982]), and "it is Delaware, not New York, which has an interest superior to all other States in deciding issues concerning directors' conduct of the internal affairs of corporations chartered under Delaware law." *Hart v General Motors Corp.*, 129 AD2d, at 185.

The parties also agree that the fraud claim and procedural issues are subject to the law of the forum state, New York. *Ground to Air Catering Inc. v Dobbs Intl. Servs. Inc.*, 285 AD2d 931, 932 [3d Dep't 2001]; *Solow v Stone*, 994 F Supp, at 177.

Motion to Dismiss:

On a motion to dismiss pursuant to CPLR 3211, the Court "must accept as true the facts

as alleged in the complaint and submissions in opposition to the motion, accord plaintiff the benefit of every possible favorable inference, and determine only whether the facts as alleged fit within any cognizable legal theory." *Sokoloff v Harriman Estates Dev. Corp.*, 96 NY2d 409, 414 [2001]. *See also Leon v Martinez*, 84 NY2d 83, 87-88 [1994]. However, "allegations consisting of bare legal conclusions, as well as factual claims either inherently incredible or flatly contradicted by documentary evidence, are not entitled to such consideration." *Franklin v Winard*, 199 AD2d 220, 220 [1st Dep't 1993] (citing *Mark Hampton, Inc. v Bergreen*, 173 AD2d 220 [1st Dep't 1991], *lv denied*, 80 NY2d 788 [1992]).

Fiduciary Duty Claim:

Defendants contend that the breach of fiduciary duty claim is fatally defective because the limited fiduciary duties that may arise when a company is close to insolvency does not bar corporate officers and directors from preferring one creditor over another. They further assert that Delaware law does not prohibit them from using their business judgment to determine how best to conserve the company's assets while satisfying the corporate debts they deem appropriate to pay. In opposition, plaintiffs argue that they have asserted a legally viable direct claim for breach of fiduciary duty since they allege self dealing on the part of the defendants.

Plaintiffs' arguments fail because any fiduciary duty owed to the assignors, because Owens Corning was in the zone of insolvency, does not overcome the exculpatory clause in the Owens Corning Certificate of Incorporation and the actions of the defendants do not constitute self dealing.

Zone of Insolvency and Fiduciary Duty:

The claim that the officer and director defendants owed a fiduciary duty to the assignors

is based on allegations that the assignors were Owens Corning creditors when the company was in the zone of insolvency. Delaware law does not recognize a general fiduciary duty owed by corporate directors and officers toward creditors. *Prudential-Bache Secs., Inc. v Franz Mfg. Co.*, 531 A2d 953, 955 [Del Supr 1987]. However, Delaware law has long recognized that fiduciary duties may arise in favor of creditors over shareholders when a corporation is insolvent, or in the zone of insolvency. *See Asmussen v Quaker City Corp.*, 156 A 180, 181 [Del Ch 1931]).

Insolvency, or being in the zone of insolvency, does not turn breach of fiduciary duty claims into direct creditor claims, however. Rather, insolvency provides creditors with the standing required to assert the breach of fiduciary duty claims. *Production Resources Group, L.L.C. v NCT Group, Inc.*, 863 A2d 772, 776 [Del Ch 2004]. "At all times claims of this kind belong to the corporation itself because . . . they operate to injure the firm in the first instance by reducing its value, injuring creditors only indirectly by diminishing the value of the firm and therefore the assets from which creditors may satisfy their claims. *Id.* Thus, although the breach of fiduciary duty claims asserted by plaintiffs belong to the corporation, insolvency places the plaintiffs, as purchasers of the assignors' rights, as creditors, in "the shoes normally occupied by the shareholders." *Id.* at 791.

Exculpatory Clause:

Defendants argue that the exculpatory provision in the Owens Corning's Certificate of Incorporation bars the fiduciary duty claims against the director defendants. They note that the exculpatory provision reads as follows: "[n]o director of the corporation shall be personally liable to the corporation or its stockholders for monetary damages for any breach of fiduciary duty by such a director as a director." Certificate of Incorporation of Owens Corning, Art. 14.

Defendants aver that because plaintiffs' claims are derivative in nature, they are limited to those claims that Owens Corning would itself be permitted to raise. Since Owens Corning could not bring the claim itself, plaintiffs are prohibited from bringing the claims for breach of fiduciary duty against any of the director defendants derivatively.

However, the exculpatory clause in Owens Corning's Certificate of Incorporation actually bars and/or provides indemnification for additional claims asserted by plaintiffs as well. The beginning of Article 14 of the Certificate of Incorporation has clear and significantly broader language.

> FOURTEENTH. The corporation shall indemnify to the full extent authorized or permitted by law any person made, or threatened to be made, a party to any action or proceeding (whether civil or criminal or otherwise) by reason of the fact that he, his testator or intestate, is or was a director or officer of the corporation or by reason of the fact that such director or officer, at the request of the corporation, is or was serving any other corporation, partnership, joint venture, trust, employee benefit plan or any other enterprise, in any capacity.

Id. (emphasis added). Thus, Article 14 actually indemnifies both directors and officers. Moreover, this language is significantly broader than merely an exculpation of derivative claims of breach of fiduciary duty.

Broad indemnifications are permitted under Delaware law. Indeed, the language in this portion of the clause clearly parallels the language of 8 Del C § 145, on the indemnification of officers and directors, etc.[1] Delaware courts have long upheld a broad interpretation of such

[1] In particular, 8 Del C § 145 includes the following:
145. Indemnification of officers, directors, employees and agents; insurance
(a) 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

indemnification clauses. In fact, where the "bylaw contains no limitation on the type of action for which an individual, otherwise qualified under the bylaw, must be indemnified" then the indemnification must be interpreted based on the language used. *Hibbert v Hollywood Park*, 457 A2d 339, 343 [Del. 1983]. Thus, there is no question that under Delaware law, a "corporation can also grant indemnification rights beyond those provided for by the statute." *Id.* at 344.

As such, the motion to dismiss the breach of fiduciary duty claims is granted, with regard to the officer defendants.

The indemnification of the director defendants, however, involves additional analysis. The exculpation clause continues, and includes language that is directed only at directors of the

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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. The termination of any action, suit or proceeding by judgment, order, settlement, conviction, or upon a plea of nolo contendere or its equivalent, shall not, of itself, create a presumption that the person did not act in good faith and in a manner which 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 reasonable cause to believe that the person's conduct was unlawful.

. . .

(f) 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.

. . .

(j) The indemnification and advancement of expenses provided by, or granted pursuant to, this section shall, unless otherwise provided when authorized or ratified, continue as to a person who has ceased to be a director, officer, employee or agent and shall inure to the benefit of the heirs, executors and administrators of such a person.

. . .

directors of the corporation,[2] there is language laying out exceptions wherein director liability can be found. It reads:

> Not withstanding the foregoing sentence, a director shall be liable to the extent provided by applicable law (I) for any breach of the director's duty of loyalty to the corporation or its stockholders, (ii) for acts or omissions not in good faith or which involve intentional misconduct or a knowing violation of law, (iii) pursuant to Section 174 of the Delaware General Corporation Law,[3] or (iv) for any transaction from which such director derived an improper personal benefit.

Certificate of Incorporation of Owens Corning, Art. 14.

The Supreme Court of Delaware analyzed a nearly identical exculpatory provision in *Malpiede v Townson.* 780 A2d 1075, 1090 (Del 2001). Both the clause in that case and in this one closely track the statutory language regarding the exculpation of directors that may be included in a Delaware certificate of incorporation. *See* 8 Del C § 102 (b) (7).[4] In

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[2] "No director of the corporation shall be personally liable to the corporation or its stockholders for monetary damages for any breach of fiduciary duty by such a director as a director." Certificate of Incorporation of Owens Corning, Art. 14.

[3] Section 174 of the Delaware General Corporation Law addresses the liability of directors for unlawful payment of dividends or unlawful stock purchase or redemption; exoneration from liability; contribution among directors; and subrogation.

[4] 8 Del C § 102 (b) (7) states:
A provision eliminating or limiting the personal liability of a director to the corporation or its stockholders for monetary damages for breach of fiduciary duty as a director, provided that such provision shall not eliminate or limit the liability of a director: (i) For any breach of the director's duty of loyalty to the corporation or its stockholders; (ii) for acts or omissions not in good faith or which involve intentional misconduct or a knowing violation of law; (iii) under § 174 of this title; or (iv) for any transaction from which the director derived an improper personal benefit. No such provision shall eliminate or limit the liability of a director for any act or omission occurring prior to the date when such provision becomes effective. All references in this paragraph to a director shall also be deemed to refer (x) to a member of the governing body of a corporation which is not authorized to issue capital stock, and (y) to such other person or persons, if any, who, pursuant to a provision of the certificate of incorporation in accordance with § 141(a) of this title, exercise or perform any of the powers or duties otherwise conferred or imposed upon the board of directors by this title.

Malpiede, the motion to dismiss was made pursuant to Chancery Rule 12(b)(6) based on an alleged breach of the duty of care. 780 A2d 1075 (Del 2001). Nonetheless, the great deference given to the existence and legal effect of the exculpatory provision, as a bar for claims against the directors and as a basis for the court's decision to uphold the dismissal of the complaint, is highly influential to the within analysis of plaintiffs' claims. Delaware law clearly upholds such exculpatory provisions, and looks narrowly at the facts alleged in the pleadings with regard to the exceptions.

Self Dealing:

At bottom, the exceptions to the bar against directors liability all relate to plaintiffs' allegations that the defendants engaged in conduct that constitutes self dealing. Thus, inasmuch as plaintiffs have not pled claims stemming from the explicit exceptions enumerated in the exculpation clause, if the pleadings do not adequately allege a claim of self dealing, which might then be developed at trial to fall within the exceptions to the exculpation of directors for breaches of fiduciary duty, then the plaintiffs' claim of breach of fiduciary duty against the director defendants must necessarily be dismissed. Such is the situation here.

Plaintiffs base their assertions of self dealing on allegations that Owens Corning wasted corporate assets when it made prepayments to NSP claimants and that defendants engaged in self dealing by attempting to protect their corporate positions by currying favor with the NSP executive board. However, plaintiffs offer no support for the proposition that these allegations, even if true, constitute self dealing. If the NSP is considered a creditor, it is clear that one creditor may be preferred over others. Moreover, even if the moneys due to NSP does not render

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imposed upon the board of directors by this title.

it a creditor, because the payments at issue were prepayments rather than payments due or past due, the payments are protected by the business judgement rule.

Under Delaware law, directors of insolvent corporations may prefer one creditor over another and "may dispose of its assets so as to prefer favorite creditors, although the result may be to leave nothing for others who stand on a footing equally meritorious." *Asmussen*, 156 A, at 181, *supra.* Indeed, "the mere fact that directors of an insolvent firm favor certain creditors over others of similar priority does not constitute a breach of fiduciary duty, absent self-dealing." *Production Resources Group*, 863 A2d at 791-792 (citing *Asmussen*). Thus, any alleged - - or proven - - preference by the defendants to the assignors, by itself, does not constitute self dealing. Rather, the plaintiffs must plead other facts that, if true, would constitute self dealing. This they have failed to do.

Even if the NSP is not considered a creditor, the prepayments made are covered by the business judgement rule. Delaware courts take a broad view of the protection of business judgement, and business decisions from which a defendant profits or that advance a defendant's interest to a greater extent than the allegations in this case are covered by the business judgement rule. For example, the business judgement rule protects increases of salary and bonus payments, which are insufficient to state a claim for breach of fiduciary duty and self dealing. *In Re Network Access Solutions v Aust*, 330 BR 67, 77 [D Del 2005]. "Informed decisions regarding employee compensation by independent boards are usually entitled to business judgment protection." *Id.* (citing, *Production Resources Group,* 863 A2d at 799). Even more notably, self dealing was not found where management actively sold assets while entering into proposed employment and business arrangements with the intended purchaser. *In Re Decora Industries,*

Inc., 2002 US Dist Lexis 8689 [D Del May 10, 2002]. Here, the accusations of self dealing stem from the defendants allegedly trying to keep their jobs and compensation. Even if true, these accusations are, at bottom, only attempts to maintain the status quo. Given that Delaware courts do not find self dealing with regards to attempts to collect greater income or new employment, the allegations in this action are simply not enough to make out a claim for self dealing.

For the foregoing reasons, the breach of fiduciary duty claim against the director defendants is fatally defective and must be dismissed.

Fraud Claim:

Defendants seek to dismiss the fraud claim as fatally defective for failure to plead supporting facts with the particularity required by New York statutory law.

To state a prima facie claim for common law fraud, a plaintiff must allege in sufficient detail: allegations of a representation of a material fact; falsity; scienter; reliance; and injury. *Small v Lorillard Tobacco Co.*, 94 NY2d 43, 57 [1999]. *See also New York Univ. v Continental Ins. Co.*, 87 NY2d 308, 318 [1995] (holding that "the essential elements of a cause of action for fraud are 'representation of a material existing fact, falsity, scienter, deception and injury.'" (internal citations omitted)). In pleading these elements, a plaintiff's allegations must be sufficiently particularized so as to give adequate notice, to the court and to the parties, of the transactions and occurrences intended to be proved. *Foley v D'Agostino*, 21 AD2d 60, 63-64 [1st Dep't 1964] (citing CPLR 3013, 3016 (b)).

In support of their fraud claim, plaintiffs allege that defendants concealed a scheme to loot the plaintiffs' assignors by failing to disclose to them that Owens Corning was on the verge

of bankruptcy, although they warned the NSP executive board, at the March 12, 2000 meeting, of this fact. Specifically, plaintiffs aver that, as of the meeting date, plaintiffs' assignors were not told that:

- the NSP was not working;
- the NSP was oversubscribed;
- the original liability protections underlying the NSP were too low by at least 33% (some $ 575,000,000);
- Owens Corning could not meet its obligations under the NSP;
- NSP's financial failure threatened Owens Corning's continued existence.

Plaintiffs also contend that defendants' omissions constituted fraud because they knew that the anticipated payments to be made to NSP claimants would increase the company's debt beyond the maximum allowed by the revolving credit agreement, resulting in a breach of the agreement. At bottom, plaintiffs allege that defendants knowingly failed to fully disclose Owens Corning's true financial health, in breach of the revolving credit agreement.

Although the defendants point to many areas where plaintiffs may not, at this time, have asserted sufficient detail to prove a claim for fraud, that is not the standard on a motion to dismiss. Prior to discovery, plaintiffs need only plead sufficient detail "to apprise defendants of the alleged wrongs." *Bernstein v Kelso & Co., Inc.*, 231 AD 2d 314, 321 [1st Dep't 1997]. The pleading requirements of CPLR 3016 (b) should not be so narrowly and strictly interpreted to create an impossible burden for plaintiffs, especially where facts and details are "peculiarly within the knowledge of the party against whom the [fraud] is being asserted." *Id.*, at 320 (citing *Jered Contracting Corp v New York City Transit Auth.*, 22 NY2d 187, 194 [1968]). *See also*

Kaufman v Cohn, 307 AD2d 113, 121 [1st Dep't 2003]. Here, plaintiffs have alleged sufficient detail to support their claim for fraud, at this stage of the case.

However, the exculpatory clause, discussed above (*see supra* Certificate of Incorporation of Owens Corning, Art. 14), is broad and its plain language indemnifies the officer and director defendants from plaintiffs' fraud claim.

Therefore, defendants' motion to dismiss the fraud claim is granted.

Accordingly, it is

ORDERED that the motion to dismiss the fraud and breach of fiduciary duty claims is granted, and the complaint is dismissed in its entirety; and it is further

ORDERED that the Clerk is directed to enter judgment accordingly.

Dated: August 22, 2006

ENTER:

J.S.C.