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## Article

**\*275 PAYING FOR DANIEL WEBSTER: CRITIQUING THE CONTRACT MODEL OF ADVANCEMENT  
OF LEGAL FEES IN CRIMINAL PROCEEDINGS**

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## I. INTRODUCTION

In the short story, *The Devil and Daniel Webster*, [FN1] a frustrated farmer, Jabez Stone, makes a pact with the devil in exchange for worldly success. [FN2] When the devil appears to collect his soul, however, Jabez retains noted litigator, Daniel Webster, to plead his case before a jury of the damned. [FN3] Webster wins the case, Jabez keeps his soul, and the devil is left to pursue other souls who lack the benefit of counsel.

Today, middle managers frequently “sell their souls” to the organizations which employ them. Their capitulation to corporate culture or their ignorance of the laws regulating market activities may ultimately make them the target of a white collar criminal investigation. Like the erstwhile defendant in Stephen Vincent Benet's short story, such employees have a keen interest in securing the best counsel available. However, unlike the fictional Daniel Webster, knowledgeable defense counsel do not work gratis. In the real world, whether an employee has the funds to retain Daniel Webster will likely depend on whether his employer has a contractual obligation to advance legal fees pending a final determination of guilt.

This paper examines the contract paradigm which is used to structure advancement of legal fees to employees facing criminal investigation. It posits that the use of the current contract model does little to advance the traditional goals of advancement and prevents consideration of the legitimate purpose of advancement--to support fair and efficient prosecution of white collar crimes. The article proposes adoption of a duty \*276 paradigm as an alternative to the contract analysis of advancement. It argues that the use of a duty model will allow for a reevaluation of the purpose of advancement in white collar criminal proceedings and will encourage conscious consideration of legitimate interests beyond those of the immediate parties to the bargain.

Part II provides a general overview of the legal framework of advancement. Statutory regimes treating advancement are generally permissive in nature. [FN4] In effect, such provisions allow organizations to determine whether, and under what circumstances, they will advance expenses to employees facing a criminal investigation. Cognizant of the permissive nature of the statutes, courts have uncritically adopted a contract model, [FN5] effectively treating advancement as the subject of a private agreement between an organization [FN6] and its employees. In construing such “agreements,” courts have confined their analysis to the four corners of the document, effectively ignoring the interest of the larger community in the efficient prosecution of white collar crime. [FN7]

Part III criticizes the use of a contract paradigm as the legal framework for analyzing advancement. It argues that most “contracts” for advancement fail to conform to traditional notions of contracting. More importantly, the article posits that even where contractual niceties are present, application of a contract model in advancement of legal fees in criminal cases is inappropriate and distorts the prosecution of white collar crime. Contract law focuses primarily on the interests of the parties, ignoring or minimizing the interests of the larger society. Permitting advancement to be distributed through a private arrangement, outside of the scrutiny and influence of the larger community, ignores the impact of advancement on the administration of criminal justice. In addition, using a contract lens to analyze advancement decisions frustrates the announced purposes of advancement and precludes consideration of the proper role of advancement in prosecution of white collar crime.

Part IV proposes a duty model as the appropriate framework for analyzing advancement in criminal proceedings. Specifically, this section explores the inadequacies of current statutory regimes and suggests that such inadequacies are the inevitable result of continued adherence to a contract paradigm of advancement. It advocates the adoption of a duty model as a means of recalibrating advancement to balance the interests of multiple constituencies. Additionally, it suggests how adoption of a duty model might influence legislation and identifies some issues which should be addressed in defining the contour of the duty to advance fees.

\*277 Part V of this article concludes that what is required is not a change in “viewpoint” but a change in “viewing point”—a fresh perspective, rather than a tweaking of a deficient model. While not a panacea, casting advancement in terms of a duty rather than a bargainable commodity clears the way for thoughtful consideration of the legitimate purposes of advancement in criminal cases and its impact on larger community interests.

## II. THE LEGAL FRAMEWORK OF ADVANCING LEGAL FEES

The relationship between indemnification of employees who are successfully vindicated of criminal liability and those advanced legal fees to secure such vindication, is juridical dymity—a complex weave of concepts which are at once intimately related and irreconcilably distinct. Advancement of legal fees and other costs of litigation is a modern day corollary to the right to indemnification. [FN8] Advancement provides individuals who may be eligible for indemnification with immediate financial relief from the costs of defense. [FN9] However, despite this common heritage, there are significant differences between indemnification and advancement, both in the statutory framework, [FN10] which govern them, and in the organizational context in which they occur.

Indemnification generally refers to organizational reimbursement of judgments, settlements, expenses, and attorneys' fees incurred by directors, officers, and employees in defending against claims arising out of or based upon their service to the organization. [FN11] In criminal proceedings, indemnification is triggered at the conclusion of the proceedings, when the claimant has been vindicated. [FN12] In contrast, advancement occurs “upstream” of a final determination of liability, at a time when it has not yet been determined whether the claimant will qualify for indemnification. [FN13] A determination of the extent to which an organization \*278 will advance fees to employees is frequently made at the commencement of an internal investigation—without regard to whether a formal investigation has been initiated. [FN14] In effect, advancement is a prepayment of a potential indemnification obligation of the organization.

### A. The Statutory Framework

At common law, agents were generally responsible for their own tortious conduct. [FN15] Indemnification was not warranted merely because the agent suffered an injury which was “connected” to employment. [FN16] For an agent to recover, it was necessary to establish that the conduct was within one of the exceptions to the general rule: either the agent's action was directed or authorized by the principal; [FN17] the agent's actions benefited the principal; [FN18] or the failure to indemnify would be “inequitable.” [FN19] Notwithstanding the foregoing, recovery was barred if “the agent's loss resulted from an enterprise which he knew to be illegal.” [FN20] Such provisions left significant room for interpretation; it is not surprising, therefore, that common law obligations of indemnification were both inconsistent and unreliable. [FN21]

In 1939, the case of *New York Dock Company v. McCollom* [FN22] created consternation when a New York court denied indemnification to directors who had successfully defended a derivative action. [FN23] In response to New \*279 York Dock, state legislatures enacted statutes mandating some level of indemnification and permitting advancement. [FN24] The primary objective of the statutes was to affirm the right of corporations to indemnify or advance fees; they were not an effort to limit indemnification or define advancement. [FN25] To the contrary, the statutes cleared the way for the parties to enter into agreements providing for indemnification as they saw fit. In interpreting the New York indemnification statute, which was passed in the wake of New York Dock, one court noted that organizational indemnification was an “exercise of a common-law right of freedom of contract and [the statute] is merely declaratory thereof . . . .” [FN26]

Advancement provisions embedded in the statutes authorizing indemnification seem to garner little notice; they were permitted as a logical extension to the principle of indemnification. [FN27] Today, many states [FN28] follow the approach of the Model Business Corporation Act (“MBCA”) [FN29] and Delaware law, [FN30] which permit, but do not require, corporations to advance payment of fees and expenses prior to a final determination on the merits. Such statutes are frequently termed “permissive.” [FN31]

In contrast to the Delaware model of permissive advancement, seventeen states have adopted some variant [FN32] of an “opt out” model of \*280 advancement. [FN33] This approach mandates or presumes advancement of fees unless the organization affirmatively “opts out” of the statutory scheme through explicit language in the organizational documents. [FN34]

Both the Delaware model and the “opt-out” model vest organizations with enormous discretion in fashioning contracts for advancement. [FN35] Corporations have used their discretion to cap legal expenditures, limit selection of counsel and require approval of expenses. [FN36] Such limitations are not barred by the statutes provided they are clearly worded and not an abuse of discretion. [FN37]

Claimants seeking advancement must conform to the procedural requirements of both the operative state statute and the company's own policies. Statutory procedures, however, are frequently a matter of form over substance. [FN38] The MBCA, [FN39] the Delaware statute, [FN40] and at least forty states [FN41] require officers and directors requesting advancement to execute an undertaking to repay the advance in the event that indemnification is not warranted. However, the statutes do not prescribe a standard of solvency, require collateral, or specify minimum financial requirements. [FN42] In the context of criminal proceedings, undertakings to repay advances are particularly hollow. [FN43] Recipients who are found ineligible for \*281 indemnification because of a determination of guilt will presumably have few resources from which to repay any advances.

Except for the formality of an undertaking to repay the advance if the claimant is ultimately found to be ineligible, statutes impose few procedural obstacles to granting advancement. Delaware law is totally permissive;

it allows advancement upon such terms and conditions, “if any,” as the corporation deems appropriate. [FN44] The MBCA [FN45] and states adopting that model [FN46] require an affirmation of the officer's good faith belief that the conduct under investigation is not ineligible for indemnification. Other states require organizations to make an independent determination at the time of the advancement request of whether any facts known at the time would make the claimant ineligible for indemnification. [FN47] The requirement for such determinations, while well intentioned, may have little impact on the decision to advance fees; corporations effectively operate on the presumption that a targeted employee will qualify for indemnification. [FN48] While such a presumption may be appropriate at the initiation of an investigation, [FN49] once made, the statutes do not require reevaluation. [FN50] Once initiated, any change in the existence or scope of advancement is made at the discretion of the organization and not as a result of a statutory requirement.

Statutes are also silent as to the duration of advancement obligations. A contract may require advancement to continue even after it appears that the recipient will be ineligible for indemnification. In *Bergonzi v. Rite Aid Corp.*, [FN51] for example, the court granted the claimant's request for advancement of fees, despite the claimant's guilty plea admitting to falsification of financial statements and backdating an employment agreement entitling him to millions of dollars. [FN52] In making its determination, the court relied on contractual language which provided for advancement until “a court of competent jurisdiction ultimately determines \*282 in a final judgment that I am not entitled to indemnification.” [FN53] Since the acceptance of the guilty plea by the criminal court could not be deemed to be a final determination on the matter of indemnification, [FN54] the claimant continued to be entitled to advancement. [FN55]

## B. The Contract Paradigm

Operating within a statutory environment that permits, but does not require, advancement, courts have treated advancement as a matter of contract between an organization and its agents. The use of a contract model to describe advancement appears to have merited little judicial head-scratching. In the context of officers and directors, the contract structure reflected the reality of the transaction; alarmed by *New York Dock*, and influenced perhaps by the machinations of the insurance industry, [FN56] directors and officers understood the importance of indemnification and advancement and demanded such protections as a condition of service. [FN57]

As the furor over the *New York Dock* decision subsided, soothed by statutes which firmly established the power of corporations to advance fees, [FN58] organizations, motivated in part by a burgeoning catalogue of white collar crimes, [FN59] found it necessary and desirable to expand advancement beyond the executive ranks. [FN60] In effect, the contract model of advancement also expanded beyond express, negotiated, agreements to include arrangements which were more fluid, and which lacked the conditions for effective bargaining. [FN61]

Today contracts requiring advancement of legal fees generally fall into three categories: (1) provisions contained in employment or consulting agreements which predate the initiation of a criminal investigation; (2) \*283 bylaw provisions which are effectuated by board resolutions or by a contract executed in the shadow of an impending investigation; or (3) implied-in-fact agreements based on an organization's past conduct.

Where advancement is treated in explicit agreements that precede the onset of the criminal investigation, the contract model seems apposite. Advancement is frequently one of many executive perquisites that is negotiated in the context of an employment or consulting agreement. Such contracts generally require no special approval beyond that typically required for executive compensation. [FN62] As with any element of executive compensa-

tion, the vigor of such negotiation may vary. [FN63] As one commentator noted, “advancement of legal fees is among the more egregious elements in the golden parachute of perks that executives negotiate at less than arms-length with a supine or self-interested board.” [FN64]

The threat of an impending criminal investigation can further distort the bargaining process. Organizations frequently enter into explicit advancement and indemnification agreements in the shadow of a criminal investigation whose scope may not be fully delineated. While many statutes require approval of a “disinterested” directors or an assessment by “independent” legal counsel as a condition to such agreements, [FN65] such provisions do not guarantee meaningful bargaining. Frequently, the organization is represented by officers or directors who, recognizing the risk of a burgeoning investigation which might eventually include them, find it easy to agree to generous advancement provisions. [FN66] Moreover, even when advancement decisions are made by “independent” counsel, the environment may be one which is “sympathetic” to the problems of corporate management. [FN67] In reality, “independent” may merely mean not an employee of the corporation. [FN68]

Despite statutory procedural requirements, high level executives who understand the risks of criminal prosecution are well positioned to secure expansive advancement provisions. The series of cases, captioned United \*284 States v. Stein, [FN69] provides a rare and insightful glimpse into the manner in which explicit agreements on advancement are negotiated. Stein grew out of a Senate investigation of accounting firm KMPG for its role in promoting illegal tax shelters. [FN70] Anticipating possible criminal charges, KPMG decided to “clean house” [FN71] and asked Mr. Stein, then Deputy Chair of the firm, and other high level managers to leave the firm. [FN72] In negotiating Mr. Stein’s “retirement” package, KMPG was represented in the negotiation by the current chairman who, incidentally, had selected Mr. Stein for his position. [FN73] Mr. Stein was represented by counsel whose fees for the representation were paid by KMPG. [FN74] The negotiation was described as “very friendly.” [FN75] The resulting agreement provided, inter alia, [FN76] that in the event that Mr. Stein was a defendant in any suits based upon his activities on behalf of the firm, he would be represented at KPMG’s expense, by counsel “acceptable to both him and KMPG.” [FN77] There was no cap on Mr. Stein’s legal expenses. In contrast, advancement for other KPMG employees who did not have explicit agreements [FN78] was capped at four hundred thousand dollars, [FN79] and was conditioned on their “cooperation” with the investigation. [FN80]

While some advancement obligations are embedded in explicit agreements, for most employees advancement is governed by bylaw provisions. [FN81] Such provisions frequently parrot the language of the state statutes, essentially giving the company “permission” to advance fees to the fullest extent of the law. [FN82] In “opt out” states which require advancement, \*285 entities may use organizational documents to modify the statutory regime or eschew it altogether. [FN83]

Bylaw provisions have been interpreted as a matter of contract. [FN84] While treating a bylaw as a “contract” between a corporation and investors seems appropriate, the logic of this approach is problematic when the “parties” to the contract are an organization and its employees or agents. Unlike the employee handbook or perhaps the Code of Conduct, there is nothing to suggest that employees or candidates for employment review the bylaws in making their decision to accept employment. Nonetheless, courts have extended the contractual analysis used to interpret bylaws to advancement without further examination or analysis. [FN85]

Where advancement is authorized by a bylaw, the organization normally takes additional action to effectuate the terms of the bylaw. Anticipating a criminal investigation, organizations frequently appoint a committee (“Independent Committee”) to conduct an internal investigation. [FN86] The Independent Committee typically

communicates the “rules of the road” to employees, advising them of the investigation, encouraging “cooperation,” [FN87] and describing the circumstances under which the organization will pay for separate counsel for the targeted employee. [FN88] While arguably “contractual,” such arrangements are a far cry from arms-length agreements. Faced with the prospect of a criminal investigation, mid-level managers with limited resources may have little stomach for vigorous bargaining. Anticipating charges against the \*286 organization itself, corporations have free rein to utilize advancement to reinforce employee loyalty [FN89] and to ensure that the individual's legal strategy comports with the organization's perceived self-interest. [FN90]

Absent an express contract, or a bylaw authorizing advancement, claimants seeking advancement must establish the existence of an implied-in-fact [FN91] contract to advance fees. Implied-in-fact contracts have the same legal effect as express agreements; [FN92] however, the determination of whether an implied-in-fact contract exists requires inquiry into the behavior of the parties and an assessment of whether such conduct infers mutual consent. [FN93] Consequently, proving the existence of an implied-in-fact agreement can be both difficult and expensive, requiring scrutiny of prior practices, and a determination of whether such practices created a reasonable inference of an agreement between the parties. [FN94]

Cases adjudicating implied-in-fact agreements for advancement in criminal cases are scant. Again the Stein cases provide a good illustration of the challenges of establishing an implied-in-fact agreement to advance fees. In Stein, fifteen employees asserted the existence of implied-in-fact agreements with their employer, KP-MG, to advance expenses incurred in connection with a criminal investigation arising from their employment. [FN95] In rejecting the district court's exercise of ancillary jurisdiction over the advancement claims of the KM-PG employees, [FN96] the United States Court of Appeals for the Second Circuit identified some of the difficulties in establishing an implied-in-fact agreement for advancement, noting that “it would require scrutinizing decades of . . . conduct, determining the states of minds of hundreds of individuals [and] applying the findings from those inquiries to the particular circumstances of each appellee . . . .” [FN97] Clearly, such agreements are highly fact specific and subjective. As a result, it is not inconceivable that two targeted employees within the same firm could \*287 have substantially different implied-in-fact “agreements” to advance fees. Bounded by a contract analysis, there is nothing to suggest such intra-firm inequities are inappropriate, and few mechanisms to address such disparate outcomes. [FN98]

### C. Judicial Interpretation of Advancement Contracts

Relying on a contractual model, courts have treated advancement of fees in criminal matters as a perquisite of employment and an appropriate subject for a private bargain. Foregoing sweeping pronouncements based on access to counsel, [FN99] courts have focused instead on the mundane task of interpreting the expressed intention of the parties as discerned within the four corners of the document. [FN100]

The framework for interpreting contracts providing for advancement was set forth in the influential case of Citadel Holding Corporation v. Roven. [FN101] At issue was an indemnity agreement between Citadel Holding, and its director, Albert Roven, which required advancement of attorneys' fees and expenses incurred in defending “any action, suit, proceeding or investigation.” [FN102] A separate section of the agreement specifically excluded indemnification for any liability or expense related to a violation of Section 16(b) of the Securities Act of 1934. [FN103] Roven sued Citadel when Citadel refused to advance expenses incurred in Roven's defense of a Section 16(b) claim brought against him by Citadel for improperly trading in the securities of the company. [FN104] In upholding the decision of the Superior Court to compel advancement, the Delaware Supreme Court

found that, \*288 while the agreement with Roven may have made violations of Section 16(b) ineligible for indemnification, the exclusion did not affect Roven's right to advancement of funds for defense of such a claim. [FN105] Most significantly, the court noted that the purpose of the contract was to provide the claimant with “greater protection than he already enjoyed under the Certificate of Incorporation, Bylaws and insurance provided by Citadel.” [FN106] In effect, Citadel makes clear that the parties could contractually expand protection beyond what was provided by the corporate organizational documents.

In subsequent cases, courts have adhered to the contractual framework, unwilling to “rescue sinners who find religion” [FN107] by reinterpreting contractual provision to take account of extraneous matters outside the scope of the agreement. Courts have required organizations to advance fees despite allegations that the claimant's action was motivated by personal greed; [FN108] that the claimant fraudulently induced the organization to enter into the advancement agreement; [FN109] that payment of advancement might result in financial hardship to the organization; [FN110] that the advancement payment was subject to set-off by the organization; [FN111] and after a claimant admitted under oath to deliberate falsification of financial statements. [FN112] As one court noted, the organization itself must strike the “proper balance between seeking able persons to serve as directors and officers and safeguarding the expenses advanced by the company . . . .” [FN113] The balance the court refers to is solely between the organization and its employees; strikingly absent is any reference to the interests of the community beyond the office tower.

The efficacy of the contractual framework in insulating advancement decisions from the interests of the larger community was on display in the \*289 Stein cases. At issue was a policy, popularly known as the Thompson Memorandum, [FN114] which permitted the United States Attorney to consider an organization's advancement of fees to “culpable” [FN115] employees in decisions to charge the organization itself. [FN116] The increased scrutiny of advancement decisions resulting from the Thompson Memorandum effectively pressured employers to structure advancement to curry favor with prosecutors. [FN117] In a carefully crafted opinion, the court rejected the policies of the Thompson Memorandum, finding that the policy, combined with the actions of the prosecutor, violated the constitutional rights of the targeted employees. [FN118]

Whatever its constitutional shortcomings, the Thompson Memorandum represented an effort, however ham-handed, [FN119] to scrutinize the advancement decision and to recalibrate advancement to consider interests beyond those of the organization and its employee. By rejecting the policies of the Thompson Memorandum, the Stein court implicitly affirmed advancement as a private matter between an organization and its employees, effectively insulated from outside scrutiny. [FN120] This fact has led one commentator to suggest that explicit contracts requiring advancement offers the best protection against prosecutor scrutiny of advancement decisions. [FN121] In effect, the contractual structure of advancement provides a virtually impenetrable barrier to external scrutiny of advancement decisions and a formidable obstacle to consideration of larger community interests.

### \*290 III. DEFICIENCIES OF THE CONTRACT MODEL

There is a legal “fondness” for the construct of a contract as an explanation of social relationships. [FN122] A contractual framework has served as the legal infrastructure for consideration of numerous relationships. [FN123] In the context of advancement, however, such categorization is misleading and short-sighted. Not only does the “process” of most advancement transactions not resemble traditional contracts, using a contract construct fails to consider the impact of advancement of legal fees on the organization, the targeted employee and the criminal justice system as a whole. Even more important than whether advancement “fits” within the con-

tract mold is the risk that the use of a contract analysis may frustrate the announced goals of advancement and preclude consideration of what role advancement should serve in promoting the interests of the larger community.

#### A. The Contract Classification

Identifying a transaction or a relationship as a “contract” is to circumscribe the nature of the analysis, to create a filter through which all analysis must pass. As one scholar observed:

To call a thing a contract is to make a legal classification. It is to carry out that most basic step in what is sometimes called legal reasoning . . . . It is to make a move in the mind game which . . . goes something like this: given that I cannot efficiently treat this thing as *sui generis*, with what other thing or group of things can I best associate it for less-than-individual treatment. [FN124]

Such classification, while having the virtue of intellectual efficiency, also carries with it significant risks. [FN125] Perhaps the greatest risk in classification as a tool of legal analysis is the necessity of focusing on a \*291 few “identifying criteria” which are the basis of the classification, while minimizing or ignoring others. [FN126]

The traditional definition of a contract as “a promise or set of promises for the breach of which the law gives a remedy . . .” [FN127] is both simplistic and circular. It provides no guidance on which promises should be enforceable and what constitutes an appropriate topic for a transaction. In considering which transactions should be classified as contracts, scholars have focused more on the characteristics of the transaction than the subject matter. As one commentator noted, “the common law’s category ‘contract’ was developed as a method of segregating, for a particular predictable treatment, contemplated trading transactions between free-willed persons in an assumedly free enterprise, free market economic system.” [FN128]

Implicit in the contracting process is what one scholar has termed, “the bordered relationship” [FN129]--a transaction characterized by “limited bargains which allocated discrete rights and duties.” [FN130] In such relationships, the parties have the autonomy and incentive to actively pursue their own interests. In contrast to such classic criteria of contracts are what have been termed “relational arrangements”--interdependent, longer lasting relationships in which the parties may have relinquished some degree of autonomy. [FN131] One commentator has defined a “relational contract” as a “relation in which exchange occurs.” [FN132] In contrast to classic conceptions of contracting, in which a relationship is created *because of a bargain between the parties*, in the context of the firm exchanges occur *because of the relationship of the parties* necessitates any number of exchanges which are both vague and dynamic. [FN133] Because the exchanges are embedded in complex relationships, [FN134] rather than negotiated in an arms-length transaction, the parties are frequently unable or unwilling to “reduc[e] important terms of the arrangement to well defined \*292 obligations.” [FN135] Force fitting such relational “agreements” into a contract model distorts contractual jurisprudence while leaving unaddressed whether such a framework supports or impedes public policy objectives.

The “contract” for advancement appears to straddle both the bordered relationship and the more fluid relational arrangements. Directors and executives frequently negotiate provisions treating advancement as part of an employment or consulting contract, or as a stand-alone agreement. [FN136] In the context of advancement, such explicit agreements appear to typify the “bordered relationship” in which the rights and interests of the parties are delineated and defined through arm’s length negotiation. [FN137] However, for most employees, the advancement arrangement bears little resemblance to an agreement between autonomous parties which is

“knowingly” and “freely made.” [FN138] For all but directors and high level executives, the “agreement” to advance fees is but one part of the “relational contract” with the employer-- the antithesis of the traditional view of a contract as a bordered relationship. [FN139] Moreover, unlike more traditional subjects of the employment contract--wages, hours, benefits--most employees lack both the knowledge and the audacity to even discuss advancement, much less negotiate about it in any meaningful way. It is a confident and knowledgeable candidate who can inquire, “If I am charged with a crime, will this organization provide counsel?” In reality, to the extent that they think about the topic at all, most employees simply rely that, in the event of a criminal investigation, the organization's interest will align with their own. [FN140]

It is precisely when parties are so lacking in knowledge or bargaining power that the application of a contract model becomes contorted. While the courts have used the equitable doctrine of the implied covenant of good faith and fair dealing [FN141] to ameliorate the distortions caused by asymmetric knowledge and bargaining power, there are limits to the application of such doctrines. The covenant is applicable only after a contract is found to exist; it plays no role in determining contract formation. [FN142] While applying \*293 the implied covenant of good faith and fair dealing contracts dealing with advancement and indemnification, [FN143] courts have held that such concepts are to be used with great caution [FN144] and should not to be used to distort the explicit terms of an agreement. [FN145] Moreover, the implied covenant of good faith is invoked only for cases before the court; those unable to seek judicial redress are left to accept whatever advancement provisions are offered, with whatever “strings” are attached. [FN146]

Even, however, in the case of express agreements where advancement arrangements coincide precisely with traditional notions of contracting, the use of a contract model is inappropriate. In categorizing a transaction a contract, the law emphasizes the process of the transaction, rather than the subject of the transaction. Traditionally, transactions are deemed to be “contracts” not because of their subject matter, but because of the process through which they come into existence. [FN147] Relying on the self-interest of parties to arrive at a proper valuing of the rights at issues, [FN148] a traditional objective of contractual jurisprudence is to facilitate and support the parties' freedom of contract. [FN149] In effect, in identifying a transaction as an enforceable contract, the law presumes that the subject matter is essentially “private” in nature and that society will be better off--or at least no worse off--by permitting private parties to come to an agreement. [FN150] However, in blindly extending the contract model to advancement of fees in criminal investigation, the law ignored the fact that the risk of criminal sanctions involves more than private interests. The ability to financially access knowledgeable counsel has significant implications, not only for the organization and the targeted employee, but for society as a whole. [FN151] Even more than the distortion of the process of “contracting,” it is the myopia of \*294 contract law, which focuses almost exclusively on the interests of the parties, which makes it an inappropriate framework for analyzing advancement transactions. At the hypothetical bargaining table, where the “contract” of advancement is decided, there is no place set for the interests of the larger community.

## B. Frustrating Traditional Goals of Advancement

Even in those situations where the arrangement between an organization and its employees conforms to traditional notions of contracting, the question remains whether a contractual framework advances or frustrates the announced goals of the transaction. Legal classifications are potent analytical tools provided that there exists a “correlation” between the classification and the purpose of the transaction. [FN152] Absent such a connection, the use of a legal model impedes, rather than promotes, the announced objectives of the transaction.

The traditional justification for advancement of legal fees is that it is a necessary inducement to encourage capable men and women to serve in positions of responsibility. [FN153] Such an objective presumably benefits both the organization and the larger community, by encouraging efficient and effective management at all levels of the organization. Yet, it is fair to conclude that advancement policies play little role in recruiting all but the highest executive ranks. By making the existence and scope of advancement the product of an agreement between parties of varying bargaining power, the contract model creates a two-tiered system, with explicit contracts providing expansive advancement for top executive talent, and potentially less protective provisions for all other managers. Such a model works only if the goal is recruitment of executive talent; in the context of other employees, use of such a model is irrelevant at best and pernicious at worst. As one commentator noted, “two violators, subject to equal fines or judgments, may pay substantially unequal out-of-pocket amounts based on their negotiating leverage in their corporations.” [FN154]

**\*295** Advancement and indemnification provisions have also been justified as necessary to encourage prudent risk taking, [FN155] and resistance to unjustified lawsuits. [FN156] Such objectives may be difficult to reconcile with the policy objectives of organizational criminal liability--deterrence of corporate misconduct. [FN157] Ironically, the very employees who have both the knowledge and bargaining power to negotiate the most generous provisions for advancement are frequently the ones with the greatest power to influence corporate behavior. [FN158] As one commentator noted, “[i]mposing absolute liability on actors at the apex of the corporate hierarchy seems most likely to serve as an effective control over organizational conduct. Yet it is precisely here, among top corporate decision makers, that contractual devices and legal policies function most effectively to deflect personal legal risks.” [FN159]

Copious advancement provisions diminish the executive's “stake” in deterring corporate misconduct. Yet, when negotiating executive agreements, an organization has few incentives to limit advancement. [FN160] Advancement costs are frequently paid through the mechanism of directors' and officers' insurance, with costs embedded in future premium adjustments. As a result, board members may find it an easy bargaining chip to trade for concessions on compensation and other benefits which garner more scrutiny from investors. [FN161]

By making the imposition of a sanction less likely, overly generous advancement provisions can “tip” the risk/reward equation toward “imprudent” risk. In the words of one commentator, “the more funding a person can use to litigate . . . the lower the probability that a sanction will be imposed . . . . And probability of sanction is at least as important as-- **\*296** many have concluded more important than--severity of sanction in determining the effectiveness of legal prohibitions in deterring violations.” [FN162] Ironically, the diminution in deterrence would appear to be greatest in those cases involving intentional conduct which could be influenced by an analytical risk/reward analysis. [FN163]

Encapsulating advancement within a contractual framework as a private matter between organizations and their agents prevents any meaningful consideration of whether advancement is serving its announced objectives, much less whether such objectives are appropriate in the context of a criminal proceeding. In clinging to a contract model which elevates the form of the transaction over the purpose to be served by advancement, the law appears driven more by intellectual economy than reflective considerations of public policy.

### C. Insulating Advancement from Community Interests

Thoughtful consideration suggests that the use of a contract model to analyze advancement in criminal proceedings distorts traditional notions of contracting and frequently frustrates the announced goals of advance-

ment. However, the greatest risk in forcing advancement into a contract model is not that it is an imperfect fit, but that it is an inappropriate subject of a contract at all. Uncritical adoption of a contractual infrastructure effectively prevents consideration of what purpose advancement should serve and whether the contract paradigm advances that purpose.

In the context of a white collar investigation, all constituencies--the targeted employee, the organization, and the larger community--have a legitimate interest in ensuring a fair process and an accurate outcome. [FN164] When properly structured, advancement of fees can play a critical role in promoting such interests; when im-providently distributed, advancement can distort the administration of criminal justice, with the potential for significant adverse impact beyond the organization and its agent.

The financial access to counsel which is provided by advancement can reduce the risk of "false positives"--the conviction of a factually innocent defendant. [FN165] Early access to knowledgeable counsel can be crucial in \*297 determining whether a charge is brought [FN166] and how the targeted defendant is treated. [FN167] Not only is such procedural fairness important to the targeted defendant, it affirms the legitimacy of the system. [FN168] Legitimacy is particularly important in the context of organizational crime, where individual and corporate cooperation are essential to determine not only who has committed a crime, but whether a crime has been committed at all. [FN169] A process which is seen as fair is more likely to encourage cooperation; conversely, where inadequate representation skews the outcome toward liability, the result can be an "adversarial culture of resistance" [FN170] that makes compliance less certain and enforcement more expensive. [FN171]

Balanced against the community interest in avoiding "false positives," is its interest in avoiding "false negatives"--a scenario in which the guilty go free. [FN172] Not surprisingly, defendants have enormous incentive to use every resource to generate a "false negative" and avoid punishment. [FN173] As one commentator noted, "defense resources should be scant when they hurt accuracy and ample when they aid it." [FN174] When financial resources are abundant, defendants in criminal cases may "overlitigate," with questionable outcomes. [FN175] When the defense is subsidized by "other people's money," there is virtually no incentive to be frugal. [FN176] As one observer noted, when facing criminal charges, the direction of corporate \*298 executives to their lawyers is: "[D]o everything you can to keep me out of jail. Very little thought is given to cost. It is not a concern." [FN177]

For those executives with the knowledge and bargaining power to negotiate an explicit contract, advancement provisions can be generous--generous enough to prove that "the earth is flat." [FN178] For mid-level managers without express agreements, however, an organization's proffer of advancement may come with gossamer strings designed to align the employee's legal strategy with that of the organization. In the context of criminal proceedings, organizations frequently advance fees because it is in their self-interest to do so. The same misconduct that is sufficient to support charges against individual employees can be the basis of an indictment against the organization. [FN179] Consequently, the legal strategy of an individual defendant can have a material impact on the organization's own defense. While a complete vindication of an employee target benefits the organization by making it less likely that the organization will be found guilty, an employee's pursuit of vindication is not without risks to the organization. Conviction of an individual defendant might foreclose certain defenses in the organization's own trial [FN180] or may provide potential plaintiffs with information for use in subsequent civil cases. [FN181] Conversely, an employee's decision to accept an offer of immunity in exchange for information [FN182] may supply prosecutors with sufficient evidence to charge other employees or the organization itself. It is not surprising, therefore, that when facing investigation and potential criminal charges, organizations naturally seek to use advancement of fees to align the behavior and legal strategy of their employees in support

of the company's own interest.

Absent a blatant abuse of discretion, [FN183] organizations may condition advancement on selection of counsel provisions which require individuals to choose from counsel who have been approved by the organization. [FN184] \*299 Even absent such a provision, the very act of advancing fees provides an organization with significant influence over employees. Employees frequently retain counsel who have been “recommended” by the organization. [FN185] Not surprisingly, corporations frequently recommend counsel whose approach will be compatible with the organization's own legal strategy. [FN186] Some scholars suggest that that employees' use of recommended counsel, who routinely benefit from regular referrals, may promote “stonewalling” even when cooperation might be in the employee's best interest. [FN187] It can be difficult to determine when it is appropriate for employees to secure their own counsel. [FN188] The common practice is to procure separate counsel where it is “sufficiently clear” that an employee's interests are adverse to that of the company [FN189] or wait until an employee makes a reasonable request for separate counsel. [FN190]

Whatever ethical dilemmas are raised by an organization's advancement policies appear to be laid solely at the feet of counsel; [FN191] there appear to be few ethical constraints on the organization which advances the fees. Even when organizations advance fees to employees for the best of reasons--an effort to build trust [FN192] or fulfill ethical obligations [FN193]--the mere \*300 existence of an organizational “benefactor” who advances legal fees may create so many entanglements as to overwhelm even the best intentioned system of organizational ethics. As one commentator noted, “there are times when any individual will find it hard to hear a warning, no matter what is said, in the context of an internal investigation. There are also times when simple actions, or the manner in which cautionary statements are delivered, can impact how an employee responds . . . .” [FN194] Far from addressing these challenges, the use of a contract model “papers over” ethical issues by allocating advancement based on bargaining power and perceived self-interest. A contract model allocates “too much” counsel to those with significant bargaining power, and imposes real or psychological restrictions on those who lack the knowledge or power to negotiate a more equitable arrangement. Supported by the framework of contract law, the organization is generally free to pursue its own goals, [FN195] unconstrained by the interests of the targeted employees or the community at large. While determination of the optimal deployment of advancement of legal expenses in criminal matters is both complex and imprecise, a model which excludes consideration of the interests of key constituencies is bound to be inadequate.

#### IV. DISCARDING THE CONTRACT MODEL OF ADVANCEMENT FOR CRIMINAL PROCEEDING

The importance of advancement decisions in the prosecution of white collar crime has not gone unnoticed. Commentators have reported on the excesses of advancement which leaves shareholders “footing the bill” for the misconduct of greedy employees; [FN196] they have explored how advancement might undercut the deterrent effect of criminal sanctions; [FN197] and they have highlighted how advancement is one factor which distinguishes prosecution of white collar crime from street crime. [FN198] Such \*301 concerns are reflected in statutory schemes which purport to reposition advancement to better balance competing interests. What commentators and legislatures fail to realize, however, is that judicial and statutory efforts to recalibrate advancement decisions are likely to fall short as long as the contract model is the operative system used to consider advancement.

##### A. Inadequacies of Current Statutory Schemes

While advancement of legal fees has been the subject of legislation in all states, such statutes essentially preserve the contract model; [FN199] even in the context of criminal proceedings, advancement is considered a private matter between the parties. [FN200] Legislation adopting a permissive structure, such as Delaware, has been described as “strikingly lax,” [FN201] essentially abdicating responsibility to the parties themselves. [FN202]

Even in those states which have adopted an “opt-out” model of advancement, [FN203] organizations are still free to structure advancement as they deem appropriate, with few checks beyond their own self-interest. [FN204] While the imposition of an affirmative action to “opt-out” of the statutory regime makes such regimes potentially more restrictive than permissive arrangements, the “opt-out” approach “tweaks” rather than replaces the contract model. The Minnesota statute, [FN205] which follows the opt-out model, offers a more comprehensive framework than other jurisdictions, with some attempt to balance the interest of multiple constituencies. [FN206] As with other opt-out jurisdictions, once an organization has “opted out,” it has discretion on whether to restrict or condition advancement or prohibit it completely. [FN207] Unlike typical opt-out statutes, however, the Minnesota statute requires that any limitation on advancement to apply equally to “all persons within a given class.” [FN208] Despite this effort to consider other constituencies, the effort falls short. The statute does not define “class;” \*302 presumably, organizations are free to continue to offer more generous advancement provisions to “executives,” provided that all “executives” are treated similarly. Moreover, nothing in the Minnesota statute prohibits organizations from recommending counsel or providing advancement of legal fees only for counsel acceptable to the organization. [FN209] In addition, the Minnesota statute vests organizations with complete discretion to determine the amount that they elect to advance. [FN210] Although the statute announces a bias toward “reimbursement” and against “overcompensation,” [FN211] it does so in the context of avoiding claims for indemnification for expenses which were already paid by insurance. [FN212] It is silent with regard to either minimum or maximum limits of advancement. Lastly, and most importantly, the statute announces that its primary purpose is “reward and protection.” [FN213] Specifically, the provision “rewards and protects from financial injury those persons who have conducted themselves in an honest manner with respect to their dealings with the corporation.” [FN214] While a laudable goal, the statute provides no mechanism or guidance to ensure that such provisions do not “reward and protect” imprudent risk taking and criminal behavior. Cordoned within a contract model, matters such as the scope and conditions of advancement are left to the determination of the parties, presumably without regard to the interests of any constituencies who are not a party to the agreement.

At the federal level, the proposed Attorney Client Privilege Protection Act [FN215] misses an opportunity to consider the issue of advancement in the scheme of white collar prosecutions and to attempt to properly balance the interests of all parties. The Act, initially introduced in response to the governmental policies of the Thompson Memorandum, [FN216] prohibits \*303 prosecutors from considering the provision of counsel or advancement of legal fees or expenses to an employee in evaluating organizational cooperation with an investigation. [FN217] While the Act would permit a prosecutor to consider advancement of fees as a part of an overall scheme of obstruction, [FN218] the Act fails to identify when advancement becomes so excessive as to constitute obstruction or to specify a “safe harbor” of appropriate advancement levels. By failing to define the contours of advancement, the Act does little more than make a “private” agreement even more private by shielding it from prosecutor scrutiny except in the most extreme circumstances.

## B. A Duty Model of Advancement

The term “duty” is an umbrella term, covering a myriad of relations and obligations, both legal [FN219] and

ethical. [FN220] Perhaps the most significant distinction between contractual obligations and other legal and ethical duties is the consideration of interests beyond those of the immediate parties to the contract. In construing a contract, a court is almost exclusively concerned with the interests and positions of the parties themselves; it need not look beyond the metaphorical bargaining table. While equitable principles such as the implied obligation to act in good faith, [FN221] the strictures on exploitation of vulnerable parties [FN222] or the prohibition on misrepresentations in the bargaining process [FN223] been used by the law to moderate contractual terms deemed egregious, such doctrines are primarily intended as protections to the parties to the transaction, with any benefit to other stakeholders being wholly incidental. [FN224] Such \*304 considerations, however, have rarely been used to void either advancement or indemnification agreements. [FN225] In contrast, in those instances where a court or legislature discerns a noncontractual duty, the law strikes a balance, not only between the rights and obligations of the immediate parties, but all similarly situated parties, without regard to their effective bargaining power. [FN226]

The traditional definition of “duty”—a “legal obligation that is owed to another” [FN227]—begs the question of when a duty should be discerned. While there appears to be consensus that a duty arises because of a “relationship” between the parties, [FN228] the determination of which relationships give rise to a duty and the scope of such duty is one of “shifting sands.” [FN229] A court which did attempt to articulate a standard observed that the imposition of a duty turns on “whether the imposition of such a duty satisfies an abiding sense of basic fairness under all of the circumstances in light of the considerations of public policy.” [FN230] In a general sense, the imposition of a duty occurs when the contract paradigm is somehow inadequate, either because of the relationship of the parties or the nature of the subject matter makes the use of a contract model inadequate. [FN231] Both the process of “contracting” [FN232] and the critical role of advancement in criminal proceedings [FN233] suggest that advancement of legal fees is simply not an appropriate subject for contracting. Freed of the strictures of contract analysis, courts and legislatures alike would be likely to take a fresh look at advancement in the context of the larger public policy issues which it presents.

The distinction between a contractual framework of advancement and a duty model is not merely of academic interest. Unlike the current contract model which confines judicial analysis to the four corners of the document, a duty analysis would require courts to consider interests beyond \*305 those of the immediate parties. This was the approach of the court in *Fidelity Federal Savings and Loan Association v. Felicetti*. [FN234] The claimants in *Felicetti* sought advancement of fees for defense of a criminal matter based on a corporate bylaw which provided for mandatory advancement. [FN235] The directors rejected the claim, relying on language in the bylaws that required the directors to act in the best interests of the company. [FN236] The board found that since the undertaking to repay the advance if the claimant was found culpable was “illusory,” it was not in the best interests of the company to advance fees. [FN237] In upholding the directors' decision, the court observed that the directors, having determined that advancement of fees was not in the best interest of the shareholders, had a fiduciary duty to reject advancement. [FN238] In effect, the *Felicetti* court recognized a duty that superseded a contractual obligation providing for advancement. However, *Felicetti* stands alone; other courts have either distinguished the case on its facts [FN239] or effectively rejected its reasoning outright, [FN240] effectively insulating agreements from considering the interests of third parties. Moreover, even in *Felicetti*, the court considered only the duty of the directors to the shareholders; there was no consideration of the larger interests at play in a criminal proceeding. By shifting their “viewing point” from a contractual vantage point to a duty perspective, courts would be more likely to weigh the “agreement” of the parties against the larger purposes of advancement and to explicitly consider the impact of the arrangement on other stakeholders.

### C. The Contours of a Duty to Advance Fees

A shift from a contract paradigm to a duty model would inevitably trigger consideration of the contour of the duty--a rebalancing of interests of all stakeholders. Although judicial importation of a duty model is possible, recasting advancement in terms of a statutory duty would appear to offer a greater opportunity for transparency and consistency. Framed in a duty model, statutes would effectively take advancement “off the table” \*306 as a matter of private bargaining. Organizations would no longer have discretion on whether or when to advance fees, nor would they be able to “opt-out” of statutory mandates. While defining the exact contours of the duty to advance legal fees is outside the scope of this article, consideration of current practices suggest that any legislation on advancement would have to address a number of key issues.

The determination of when an employee is entitled to advancement of legal fees and expenses and how long advances are available has enormous implications for the individual employee, the organizational employer and the criminal justice system. In the context of white collar crime, legal representation is critical in determining how the investigation proceeds and whether charges are filed. [FN241] Whether advancement of legal fees should be available at the investigatory stage of a white collar proceeding, or, as comparable with street crime, only at the charging stage, [FN242] is an important issue which should not be left to the bargaining of private parties.

The duration of advancement also has significant impact, not only on targeted employees, but also on the community as a whole. While some statutes require an initial evaluation of whether there exist facts which would make a recipient ineligible for advancement, [FN243] no subsequent evaluation is required. This can result in a situation where the termination of advancement becomes less likely as the case progresses than at the time of the initial evaluation, even though more facts may emerge which suggest that a recipient is not eligible for indemnification. Presumably, had the claimant in the Bergonzi case pled guilty prior to receiving his initial advancement of attorneys' fees, denial of advancement might have been justified; ironically, however, his subsequent admission was insufficient to terminate the organization's obligation to advance fees. [FN244]

In addition to the commencement and duration of advancement, determining “how much” of a benefit a claimant receives raises important issues of fairness and efficiency. Under a contract model, there is virtually no check on the amount of organizational resources that can be advanced. Unlike street crime, where access to counsel is effectively “regulated” by the government through provision of funds for appointed counsel, [FN245] the contract model of advancement imposes no minimums or maximums on the amounts advanced, and no requirement of equitable treatment among \*307 employees. While the ability of an organization to restrict or curtail fees may leave some targeted employees vulnerable to organizational pressure, [FN246] other putative defendants in white collar cases may have the full resources of the company available for their defense. [FN247] Even the forfeiture statutes [FN248] which have been used by prosecutors to limit a defendant's access to financial resources are less of a restriction in white collar crimes. Such statutes are available only if it can be shown that the forfeited assets are the result of a defendant's criminal activity [FN249]--a difficult task when advancement is made in accordance with the terms of a pre-existing contract or through an insurance policy. Even where there exists an allegation that the actions of an individual defendant justify forfeiture, courts have still permitted of payment of advances by the organizational employer into an escrow account, [FN250] effectively preserving them for future distribution.

The determination of what is the appropriate amount of advancement is bound to be frustrating and imprecise. However, it seems clear that a model which acknowledges interests beyond those of the immediate parties

is likely to be an improvement over the current system which leaves each party to strike the best deal possible, without regard to the interests of the larger community. While simply recasting advancement in a duty analysis rather than a contract analysis will not result in an automatic rebalancing of all constituent interests, a conscious repudiation of the contract model is the first step toward freeing courts and legislatures to consider the interests beyond those of the parties to the agreement.

## V. CONCLUSION

The issue of advancement in criminal proceedings is too important to be left to the vagaries of totally private negotiation between parties with disparate bargaining power and sophistication. The use of such a model circumscribes judicial review and diverts legislative focus from comprehensive consideration of all of the constituencies affected in the prosecution of white collar crime. A shift from a contract model to a duty \*308 model would be the first step toward a fresh look at advancement in criminal cases.

It is understandable that every white collar defendant would wish to retain services of a litigator as skilled and eloquent as Daniel Webster. However, who should “pay” for Daniel Webster--whether in terms of money, influence, accuracy, or efficiency--presents complicated issues which should be settled, not in the insularity of a bargain, but in the definition of a duty which considers the interests of all of the actors--even those of the devil himself.

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[FN1]. Stephen Vincent Benet, *The Devil and Daniel Webster*, in 2 *Selected works of stephen vincent benet* 32-46 (1942).

[FN2]. *Id.* at 33-34. It is interesting to note that Jabez deceives his family about the identity of the devil by telling them that the devil is “a lawyer, come to see him.” *Id.* at 33.

[FN3]. *Id.* at 39-41.

[FN4]. See *infra* notes 28-35 and accompanying text.

[FN5]. See *infra* notes 56-61 and accompanying text.

[FN6]. Unless the context requires otherwise, as used herein the term “organization” refers to any business entity.

[FN7]. See *infra* notes 98-99 and accompanying text.

[FN8]. *Homestore, Inc. v. Tafeen*, 888 A.2d 204, 211 (Del. 2005) (“Advancement is an especially important corollary to indemnification....”).

[FN9]. *Id.* (“Advancement provides ... immediate interim relief from the personal out-of-pocket financial burden of paying the significant on-going expenses inevitably involved with investigations and legal proceedings.”).

[FN10]. See *infra* notes 15-55 and accompanying text.

[FN11]. Stephen A. Radin, “Sinners Who Find Religion:” *Advancement of Litigation Expenses to Corporate Officials Accused of Wrongdoing*, 25 *Rev. Litig.* 251, 257-58 (2006) (“Indemnification refers to reimbursement ... of liabilities, including judgments, amounts paid in settlement, expenses, and attorneys’ fees incurred by directors, officers, employees, and sometimes even agents in the course of their service to the corporation.”).

[FN12]. Edward Brodsky & M. Patricia Adamski, *Law of Corporate Officers and Directors* § 19:2 (2009) (footnotes omitted) (noting that vindication can range from “wholly successful” to “successful on the merits or otherwise”) (emphasis added).

[FN13]. *Homestore, Inc.*, 888 A.2d 204, 211-12 (observing that the right to keep advances made by an organization depends on whether the recipient is entitled to indemnification).

[FN14]. Am. Coll. of Trial Lawyers, *Recommended Practices for Companies and Their Counsel in Conducting Internal Investigations*, 46 *Am. Crim. L. Rev.* 73, 88 (2009) (suggesting that, at the commencement of an internal investigation, an organization send a memorandum to all affected employees describing *inter alia* the organization’s obligation to advance fees).

[FN15]. See, e.g., *Brady v. Roosevelt Steamship Co.*, 317 U.S. 575, 580 (1943) (“The liability of an agent for his own negligence has long been embedded in the law.”); *Gaines v. Walker*, 986 F.2d 1438, 1442 (D.C. Cir. 1993) (“[C]ommon law generally holds agents responsible for their own wrongs.”); *Hagen v. Koerner*, 166 A.2d 784, 786 (N.J. Super. Ct. App. Div. 1960) (“[T]here is a general rule in the law of agency that an employer cannot be compelled to reimburse and employee for damages the employee may be obligated to pay ... resulting from his own negligent conduct.”).

[FN16]. *Hagen*, 166 A.2d at 786 (“[T]here is a general rule in the law of agency that an employer cannot be compelled to reimburse and employee for damages the employee may be obligated to pay ... resulting from his own negligent conduct.”).

[FN17]. Restatement (Second) of Agency: When Duty of Indemnity Exists § 439(c) (1957).

[FN18]. *Id.* § 439(e).

[FN19]. *Id.*

[FN20]. *Id.* § 440(c).

[FN21]. Joseph W. Bishop, Jr., *Current Status of Corporate Directors’ Right to Indemnification*, 69 *Harv. L. Rev.* 1057, 1068-69 (1956) (noting that common law grounds for directors’ right to indemnification is a “welter of confusion”); Brodsky & Adamski, *supra* note 12, at §19:1 (observing that at common law the right to reimbursement was uncertain); John L. Cornell & James J. Little, *Indemnification of Fiduciary and Employee Litigation Costs Under ERISA*, 25 *B.C. L. Rev.* 1, 14-15 (1983) (stating that while some courts routinely denied indemnification, other courts permitted recovery when the claimant had successfully defended the action).

[FN22]. 16 N.Y.S. 2d 844 (1939).

[FN23]. *Id.* at 849 (noting that unless a director could demonstrate that in successfully defending himself he con-

ferred a benefit on the corporation, he was not entitled to reimbursement of costs).

[FN24]. Chester F. Reylea, Comment, Indemnification of Management for Litigation Expenses, 52 Mich. L. Rev. 1023, 1029-30 (1954) (observing that New York Dock prompted adoption of statutes and by-laws requiring indemnification) (citations omitted); Pamela H. Bucy, [Indemnification of Corporate Executives Who Have Been Convicted of Crimes: An Assessment and Proposal](#), 24 Ind. L. Rev. 279, 283 (1991) (observing that New York Dock sparked a “new generation” of statutes with expansive coverage); William E. Knepper & Dan A. Bailey, 2 Liability of Corporate Officers and Directors § 22.02 (2d ed. 2002) (noting that all fifty states have enacted legislation treating indemnification)(citations omitted).

[FN25]. Bucy, supra note 24, at 319 (arguing that statutory limitations on improper advances are not “meaningful”). But see Dale Oesterle, [Limits on a Corporation's Protection of Its Directors and Officers From Personal Liability](#), 1983 Wis. L. Rev. 513, 536 (1983) (suggesting a lack of a cohesive purpose laws treating indemnification and advancement).

[FN26]. [Schwarz v. General Aniline & Film Corp.](#), 305 N.Y. 395, 405 (1953) (Carswell, J., concurring).

[FN27]. [Kaung v. Cole Nat. Corp.](#), 884 A.2d 500, 509 (Del. 2005) (observing that advancement fills the gap prior to a determination of mandatory advancement); see Richard A. Rossman, Matthew J. Lund & Kathy K. Lochman, [A Primer on Advancement of Defense Costs: The Rights and Duties of Officers and Corporations](#), 85 U. Det. Mercy L. Rev. 29, 30-36 (2007) (describing the typical models used for advancement).

[FN28]. Rossman et al., supra note 27, at 34-36, 54-55 (identifying the advancement models used in each state).

[FN29]. Model Bus. Corp. Act § 8.58(a) (2007).

[FN30]. Del. Code Ann. tit.8 § 145 (e) (2009).

[FN31]. Rossman et al., supra note 27, at 34 (“[A]dvancement statutes of most states are described as “permissive” because they establish only the ability of a corporation to grant advancement” ).

[FN32]. Id. at 34-36, 54-55 (identifying some of the variations within the “opt-out” model of advancement).

[FN33]. Rossman et al., supra note 27, at 54 (identifying state statutes utilizing an “opt-out” model for advancement).

[FN34]. See, e.g., [Ohio Rev. Code Ann. § 1701.13\(E\)\(5\)\(a\)](#) (2009); [Minn. Stat. Ann. § 302A.521](#), subd. (3), (4) (2004); [Ariz. Rev. Stat. Ann. § 10.852\(B\)](#) (2004).

[FN35]. See, e.g., [Del Code Ann. tit. 8 § 145\(e\)](#) (2009) (providing that expenses shall be paid “upon such terms and conditions, if any, as the corporation deems appropriate.”); Model Bus. Corp. Act § 858(c) (2007) (providing that a corporation may limit any rights to indemnification or advancement through a provision in the articles of incorporation); [N.J. Stat. Ann. § 14A:3-5\(11\)](#) (2003) (prohibiting indemnification or advancement which is inconsistent with any corporate action which limits or restricts indemnification or advancement);

[FN36]. Limitations on advancement are not transparent and most of the restrictions are disclosed in the process of litigation contesting the limitations. See, e.g., [United States v. Stein](#), 435 F. Supp. 2d 330, 345 (S.D. N.Y. 2006) (referring to KMPG letter to employees that it would pay up to \$400,000 in legal fees); [Chamison v.](#)

[Healthtrust Inc.](#), 735 A.2d 912, 916 (Ch. Del. 1999) (citing policy of corporation to pay legal fees of firms selected by the corporation).

[FN37]. [Chamison](#), 735 A.2d at 922 (noting that in the absence of restrictive language, a corporation has broad discretion in requiring use of specified counsel, but finding that the corporation had abused such discretion).

[FN38]. Bucy, *supra* note 24, at 316-19 (arguing that it is easy for organizations to circumvent statutory standards).

[FN39]. Model Bus. Corp. Act § 8.53(a)(2) (2007).

[FN40]. [Del Code Ann. tit. 8 § 145\(e\)](#) (2009).

[FN41]. Model Bus. Corp. Act § 8.53 cmt. statutory comparison (2007).

[FN42]. Bucy, *supra* note 24, at 316 (“[S]tatutes impose no meaningful requirement or mechanism for reclaiming such advances....”); Knepper & Bailey, *supra* note 24, § 22.14 (“[T]he ability of the director or officer to repay the advanced amount is generally not a factor [in the decision to advance fees] since the contractual by-law provision is not subject to the fiduciary duties of the approving directors.”) (citations omitted).

[FN43]. Peter Margulies, Legal Hazard: Corporate Crime, Advancement of Executives Defense Costs and the Federal Courts, 7 U.C. Davis Bus. L.J. 55, 80 (2006) (noting that executive's assets may “evaporate” as a result of a criminal prosecution).

[FN44]. [Del Code Ann. tit. 8 § 145 \(e\)](#) (2009).

[FN45]. Model Bus. Corp. Act § 8.53(a)(1) (2007).

[FN46]. See Rossman et al., *supra* note 27, at 55 (identifying those states which require a claimant's affirmation that her conduct will not bar indemnification).

[FN47]. *Id.* at 38 (identifying the states which have adopted this procedure).

[FN48]. Mae Kuykendall, [Symmetry and Dissonance in Corporate Law: Perfecting the Exoneration of Directors, Corrupting Indemnification and Straining the Framework of Corporate Law](#), 1998 Colum. Bus. L. Rev. 443, 552 (1998) (observing that corporations usually advance fees with little “practical fact finding” on whether a claimant is eligible for indemnification).

[FN49]. *Id.* (arguing that “there is a useful conceptual clarity in allowing an advance of expenses without reference to any standard of conduct”).

[FN50]. See Bucy, *supra* note 24, at 318 (suggesting that that any meaningful evaluation of eligibility for indemnification would be “perilous” and could take as long as the criminal investigation itself).

[FN51]. [Bergonzi v. Rite Aid Corp.](#), No. Civ. A.20453-NC, 2003 WL 22407303 (Del. Ch. Oct. 20, 2003).

[FN52]. *Id.* at \*2.

[FN53]. [Bergonzi](#), 2003 WL 22407303, at \*3.

[FN54]. Id.

[FN55]. Accord [U.S. v. Weismann, No. S294CR.760 \(CSH\), 1997 WL 334966, at \\*16 \(S.D. N. Y. June 6, 1997\)](#) (holding that claimant was entitled to advancement despite a finding of guilt pending final adjudication).

[FN56]. Joseph W. Bishop, Jr., [Sitting Ducks and Decoy Ducks: New Trends in the Indemnification of Corporate Directors and Officers](#), 77 *Yale L. J.* 1078, 1078 (1968) (suggesting that an ad campaign by insurance industry raised awareness of directors of the risks of corporate service).

[FN57]. Edward Paul Mattar III & John Francis Hilson, 46 *J. Risk & Ins.* 411, 411 (1979) (noting that concern over personal liability became so pronounced that directors were reluctant to serve) (citation omitted).

[FN58]. See *supra* notes 24-25 and accompanying text for a discussion of the statutory responses to N.Y. Dock.

[FN59]. Bucy, *supra* note 24, at 294-95, 304 (arguing that blurring of civil and criminal liability and increases in the number of strict liability crimes have made it easier to find the requisite intent for permissive indemnification); Regina A. Robson, [Crime and Punishment: Rehabilitating Retribution as a Justification for Organizational Criminal Liability](#), 47 *Am. Bus. L. J.* 109, n.182 (2010) (noting that there are currently over ten thousand administrative regulations which are criminally enforceable).

[FN60]. See *infra* notes 179-82 and accompanying text.

[FN61]. See *infra* notes 129-35 and accompanying text.

[FN62]. Oesterle, *supra* note 25, at 543 (observing that contracts dealing with future litigation are subject to the rules on officers' and directors' compensation). But see *Minn. Stat. Ann.* § 302A.511 subd (2004) (requiring disclosure--but not approval--of actual advances to shareholders at the next regular meeting after the payment has been made).

[FN63]. Kuykendall, *supra* note 48, at 536 (“Like other compensation, indemnification is subject to legal constraints, but the restraints are loose, affected as much by public opinion and an internal sense of social limits ... as by regulation.”).

[FN64]. Margulies, *supra* note 43, at 81-82.

[FN65]. See, e.g., [Del Code Ann. tit. 8 § 145\(f\)](#) (2009) (requiring approval by shareholders, disinterested directors or “otherwise”); [Minn. Stat. Ann. § 302A.521](#) subdiv. 6 (2004) (providing for approval of disinterested members of the board and in some cases a “special” counsel).

[FN66]. Margulies, *supra* note 43, at 80 (observing that directors, who are also interested in being held harmless, often accede to managers' requests for advancement to defend against criminal charges).

[FN67]. Bishop, *supra* note 56, at 1080 (arguing that selection of independent counsel may favor corporate lawyers who have a “sympathetic understanding” of management).

[FN68]. Id.

[FN69]. [U.S. v. Stein \(“Stein I”\)](#), 435 F. Supp. 2d 330 (S.D. N.Y. 2006), *aff'd*, 541 F.3d 130 (2d Cir. 2008); [U.S. v. Stein \(“Stein II”\)](#), 440 F. Supp. 2d 315 (S.D. N.Y. 2006); [U.S. v. Stein \(“Stein III”\)](#), 495 F. Supp. 2d 390, 402

(S.D. N.Y. 2007).

[FN70]. [Stein I](#), 435 F. Supp. 2d at 338 (citing Staff of the Permanent Subcomm. on Investigations of the S. Comm. on Homeland Security and Governmental Affairs, 109th Cong., *The Role of Prof. Firms in the U.S. Tax Shelter Industry* (Comm. Print 2005)).

[FN71]. *Id.* at 339.

[FN72]. *Id.* At least one other executive, Mr. Smith, received a retirement package similar to [Mr. Stein's. Stein III](#), 495 F. Supp. 2d at 408.

[FN73]. [Stein I](#), 435 F. Supp. 2d at n.23.

[FN74]. *Id.*

[FN75]. *Id.*

[FN76]. In addition, the agreement provided for consulting payments totaling \$3.6 million dollars over three years, and continuing coverage under the company's D& O insurance. *Id.* at 339.

[FN77]. *Id.*

[FN78]. *Id.* at 356 n.119 (noting that except for Mr. Stein who had an express contract providing advancement, defendants based their claims on implied-in-fact agreements with KPMG).

[FN79]. *Id.* at 345.

[FN80]. *Id.*

[FN81]. See, e.g., [Neal v. Neumann Med. Ctr.](#) 667 A.2d 479, 480-81 (Pa. Commw. Ct. 1995) (bylaw provision providing for advancement); [Hibbert v. Hollywood Park, Inc.](#), 457 A.2d 339, 341 (Del. 1983) (bylaw providing for advancement); [Fid. Fed. Sav.& Loan Ass'n v. Felicetti](#), 830 F. Supp. 262, 264-65 (E.D. Pa. 1993) (corporate bylaw providing for advancement).

[FN82]. [Rossman et al.](#), *supra* note 27, at 34 (noting that frequently organizational documents simply adopt the statutory language which authorizes advancement).

[FN83]. [Rossman et al.](#), *supra* note 27, at 35-36 (noting that in opting out of statutory schemes, use of precise language is critical).

[FN84]. See, e.g., [Ellingwood v. Wolf's Head Oil Ref.Co., Inc.](#) 38 A.2d 743, 747 (Del. 1944) (“In interpreting the meaning of charter provisions the same method is applied as that which is followed in interpreting written contracts generally.”); [Centaur Partners IV v. Nat'l Intergruop, Inc.](#), 582 A.2d 923, 928 (Del. 1990) (“Corporate charters and bylaws are contracts among the shareholders of a corporation and the general rules of contract interpretation are held to apply”); [Heritage Lake Prop. Owners' Ass'n v. York](#), 859 N.E. 2d 763, 765 (Ind. Ct. App. 2007) (“[W]hen construing corporate organizational documents, the general rules of contract interpretation apply.”); [Fid. Fed. Sav. & Loan Ass'n.](#), 830 F. Supp. at 268 (“[T]here is nothing to preclude a corporation from contracting through its bylaws, articles of incorporation or by private contract to provide for mandatory advancements.”).

[FN85]. See, e.g., [TBG Inc. v. Bendis](#), Civ. A. No. 89-2423-0, 1991 WL 34199, at \*4 (D. Kan. Feb. 19, 1991) (citing contractual concept that subsequent changes in law become part of the contract in interpreting bylaw provision providing for advancement); [Hibbert](#), 457 A.2d at 342-43 (utilizing the rules which govern the interpretation of contracts to construe a corporate bylaw containing provisions on indemnification and advancement); [Neal](#), 667 A.2d at 484 (noting that Pennsylvania nonprofit corporations are permitted to “contract through their bylaws to indemnify their corporate officers and directors.”) (Smith, J., dissenting on other grounds).

[FN86]. Am. Coll. Trial Lawyers, *supra* note 14, at 83 (recommending, inter alia, formation of an Independent Committee to conduct an investigation and communicate with employees).

[FN87]. *Id.* (suggesting that the Independent Committee communicate an expectation of employee cooperation, a description of what constitutes cooperation and an announcement that failure to cooperate might result in termination).

[FN88]. *Id.* (suggesting that the Independent Committee make an early determination of the circumstances under which the company will pay for separate counsel for employees).

[FN89]. Margulies, *supra* note 43, at 79 (“[A]dvancement of legal fees ... promotes loyalty ... and prevents the government from ‘peeling off’ players who might wish to cooperate with the prosecutor.”).

[FN90]. See *supra* notes 178-87 and accompanying text.

[FN91]. Implied-in-fact contracts are those in which the “intention to make a promise may be manifested ... by implication from other circumstances ....” [Restatement \(Second\) of Contracts § 4](#) cmt. a (1979).

[FN92]. *Id.* (“The distinction [between express and implied contracts] involves, however, no difference in legal effect ....”).

[FN93]. *Id.* (noting that a promise may be inferred from a course of dealing, a course of performance or trade usage).

[FN94]. George P. Costigan, Jr., [Implied-in-Fact Contracts and Mutual Assent](#), 33 *Harv. L. Rev.* 376, 381-82 (1920) (arguing that a principle distinction between express and implied contracts is in the mode of proving a contract exists). See also *supra* notes 96-97 and accompanying text for a description of the proof required to establish an implied-in-fact contract.

[FN95]. [Stein v. KPMG](#), 486 F.3d 753, 757(2d Cir. 2007) (noting that fifteen of the sixteen employees claiming advancement based their claim on implied-in-fact agreements).

[FN96]. *Id.* at 761 (holding that ancillary jurisdiction was not warranted because, inter alia, the claims involved “garden variety state law claims”).

[FN97]. *Id.* at 761-62.

[FN98]. The equitable doctrines of good faith and fair dealing which have traditionally be used to ameliorate more egregious abuses of discretion are essentially tools of contract interpretation and do not affect a determination of whether a contract can be inferred in fact. See *infra* notes 141-46 and accompanying text.

[FN99]. Those cases which have relied on access to counsel as a justification for advancement have arisen in the context of insurers seeking to deny advancement which was allegedly required by an insurance policy. See, e.g., [Little v. MGIC Indem. Corp.](#), 649 F. Supp. 1460, 1486 (W.D. Pa. 1986), aff'd, 836 F.2d 789 (3d Cir. 1987), (noting that requiring the employee to pay their expenses as incurred would be “unconscionable”); [Flintkote Co. v. Lloyd's Underwriters](#), 1976 WL 16591, at \*4 (N. Y. Sup., July 27, 1976), aff'd, 391 N.Y.S.2d 1005 (1977) (observing that public policy is served by having executive properly represented, despite his conviction on anti-trust charges).

[FN100]. See, e.g., [Citadel Holding Corporation v. Roven](#), 603 A.2d 818, 824 (Del. 1992) (“When construing a contract, and unless a contrary intent appears, we will give words their ordinary meaning.”); [Hibbert v. Hollywood Park, Inc.](#), 457 A.2d 339, 343 (Del. 1983) (noting that if a bylaw is unambiguous, the court will not search out the parties' intention); [Tafeen v. Homestore, Inc.](#), No. Civ. A.023-N, 2004 WL 556733, at \*1 (Del. Ch. Mar. 22, 2004), aff'd, [Homestore Inc. v. Tafeen](#), 886 A.2d 502 (Del. 2005) (refusing to reinterpret loosely drafted bylaws to benefit organizational drafter).

[FN101]. 603 A.2d 818 (Del. 1992).

[FN102]. *Id.* at 820.

[FN103]. *Id.* (“The Corporation shall not be obligated ... to make payment in regard to any liability ... for an accounting of profits made from purchase or sale by the Agent of securities of the Corporation within the meaning of Section 16(b) of the Securities Exchange Act of 1934 ....”).

[FN104]. *Id.* at 821.

[FN105]. [Citadel](#), 603 A.2d at 826 (holding that contract exclusions relating to finding of liability under the Securities Act did not affect right to advancement prior to determination of liability).

[FN106]. *Id.* at 823.

[FN107]. [Tafeen](#), 2004 WL 556733, at \*1.

[FN108]. [Reddy v. Elec. Data Sys.](#), No. Civ. A. 19467, 2002 WL 1358761, at \*5 (Del. Ch. June 18, 2002) (noting the existence of a consistent line of authority upholding the right to advancement even when misconduct is motivated by personal greed) (citations omitted).

[FN109]. [Tafeen](#), 2004 WL 556773, at \*5 (observing that while fraudulent inducement to enter an employment agreement may be the subject of a separate action, it was not a defense to a claim for advancement).

[FN110]. See, e.g., [Dunlap v. Sunbeam Corp.](#), Civ. A. No. 17048, 1999 LEXIS 126, at \*17 (Del. Ch. June 23, 1999) (“Hardship ... is not a factor that this Court has typically considered in determining whether to provide for advancement of fees ....”); [Tafeen](#), 2004 WL 556733, at \*10 (holding that severe financial hardship is not a cognizable defense to a claim for advancement of fees).

[FN111]. [Kaung](#), 884 A.2d at 502 (holding that the summary nature of proceeding for advancement made award of recoupment inappropriate).

[FN112]. [Bergonzi v. Rite Aid Corp.](#), No. Civ. A.20453-NC, 2003 WL 22407303, at \*3 (Del. Ch. Oct. 20, 2003)

(holding that contract providing for advancement prohibits an inquiry whether claimant will qualify for indemnification).

[FN113]. [Tafeen](#), 2004 WL 556733, at \*3 n.7 (emphasis in the original).

[FN114]. Larry D. Thompson, Principles of Federal Prosecution of Business Organizations, Dept. of Justice (Jan. 20, 2003), [www.usdoj.gov/dag/cftf/corporate\\_guidelines.htm](http://www.usdoj.gov/dag/cftf/corporate_guidelines.htm) [hereinafter Thompson Memorandum].

[FN115]. The Thompson Memorandum did not define “culpable.”

[FN116]. Thompson Memorandum, *supra* note 114, at VI (B) (footnote omitted). An exception was made in those instances where advancement of attorneys' fees was required by law. *Id.*

[FN117]. [Stein I](#), 435 F. Supp. 2d at 345 (noting that the Thompson Memorandum and the actions of the prosecutor resulted in the employer capping fees and conditioning payment of legal expenses of the targeted employees on their cooperation with the government).

[FN118]. *Id.* at 382. (“[T]he Thompson Memorandum and the activities of the USAO ... violated the Fifth and Sixth Amendments to the Constitution.”).

[FN119]. The Thompson Memorandum was the subject of widespread criticism. See e.g., Earl J. Silbert & Demme Doufekias Joannou, [Under Pressure to Catch the Crooks: The Impact of Corporate Privilege Waivers on the Adversarial System](#), 43 *Am. Crim. L. Rev.* 1225, 1226-27 (2006) (labeling the policies of the Thompson Memorandum as a trampling of constitutional rights of individuals); George Ellard, [Making the Silent Speak and the Informed Wary: False Statements to Impede Government Investigations](#), 42 *Am. Crim. L. Rev.* 985, 991 (2005) (calling the Thompson Memorandum a seismic shift from an accusatorial to an inquisitional systems of justice); Noah D. Stein, [Prosecutorial Ethics and the McNulty Memo: Should The Government Scrutinize An Organization's Payment of Its Employees' Attorneys' Fees?](#), 75 *Fordham L. Rev.* 3245, 3273-74 (2007) (observing that policy embodied in Thompson Memorandum encouraged a premature labeling of an employee as “culpable”).

[FN120]. [Stein III](#), 495 F. Supp. 2d at 402 (noting that even when operating under the Thompson Memorandum, prosecutors did not demand that an organization breach an explicit contractual obligation to advance fees).

[FN121]. Darryl K. Brown, [Challenges to the Attorney-Client Relationship: Threats to Sound Advice?](#), 57 *DePaul L. Rev.* 365, 388-89 (2008) (arguing that contract law provides courts with an easier judicial mechanism to discourage prosecutor interference with advancement than does constitutional law).

[FN122]. Eli Bukspan, [The Notion of Trust as a Comprehensive Theory of Contract and Corporate Law: A New Approach to the Conception that the Corporation Is a Nexus of Contract](#), 2 *Hastings Bus. L. J.* 229, 236 (2006) (arguing that contract law is the foundation of most legal and social interaction).

[FN123]. See, e.g., *id.* at 233 (observing that a corporation is the “quintessential embodiment of contract.”); Victor Brudney, [Corporate Governance, Agency Costs, and the Rhetoric of Contract](#), 85 *Colum. L. Rev.* 1403, 1403 (1980) (noting the current trend to analyze corporations as a “nexus of contracts”); Frank H. Easterbrook & Daniel R. Fischel, [Contract and Fiduciary Duty](#), 36 *J. Law & Economics* 425, 427 (1993) (arguing that fiduciary “duties” are a variant of contract law in which courts supply the terms that the parties would have negotiated with respect to the subject); Arthur Allen Leff, [Contract as Thing](#), 19 *Am. U. L. Rev.* 131, 131 (1970) (arguing

that classification of consumer transactions as “contracts” is appropriate).

[FN124]. Leff, *supra* note 123, at 132 (emphasis in the original) (footnotes omitted).

[FN125]. See, e.g., Deborah A. DeMott, [Beyond Metaphor: An Analysis of Fiduciary Obligation](#), 1988 *Duke L. J.* 879, 879-80 (applying contract jurisprudence to fiduciary obligations is “misleading” and “provides no rationale for further development ....”); Leff, *supra* note 123, at 132 (arguing that legal classification which groups “identical” things is a “sticky business,” fraught with risks).

[FN126]. Leff, *supra* note 123, at 136 (positing that once an item or transaction is “classified,” it is tempting to ignore significant differences among transactions within the class).

[FN127]. Restatement (Second) of Contracts: Contract Defined § 1 (1979).

[FN128]. Leff, *supra* note 123, at 138 (citations omitted).

[FN129]. *Id.* at 138 (observing that the “bordered relationship” is characterized by “the deal,” rather than long term, non-limited relationships).

[FN130]. Pamela S. Karlan, [Discrete and Relational Criminal Representation: The Changing Vision of the Right to Counsel](#), 105 *Harv. L. Rev.* 670, 673 (1992).

[FN131]. *Id.* at 674 (noting that classical theory of contracts may not accommodate long-term arrangements with fluid obligations).

[FN132]. Ian R. Macneil, [Relational Contract Theory, Challenges and Queries](#), 94 *Nw. U. L. Rev.* 877, 878 (2000) (defining a contract as a relationship in which exchange occurs).

[FN133]. Stewart Macaulay, [An Empirical View Of Contract](#), 1985 *Wis. L. Rev.* 465, 467 (1985) (“Contract planning and contract law, at best, stand at the margin of important, long-term continuing business relationships.”).

[FN134]. Macneil, *supra* note 132, at 884-86 (arguing that every transaction is embedded in a complex relationship which must be considered in analyzing contracts); Macaulay, *supra* note 133, at 468 (arguing that “relational sanctions” outweigh contract law in determining behavior in the firm).

[FN135]. Charles J. Goetz & Robert E. Scott, [Principles of Relational Contracts](#), 67 *Va. L. Rev.* 1089, 1090-91 (1981).

[FN136]. See *supra* notes 62-64 and accompanying text.

[FN137]. See *supra* notes 129-30 and accompanying text.

[FN138]. Brudney, *supra* note 123, at 1404.

[FN139]. Macaulay, *supra* note 133, at 469 (“Continuing relationships are not necessarily nice. The value of arrangements locks some people into dependent positions. They can only take orders.”).

[FN140]. Karlan, *supra* note 130, at 374 (observing that both in general and when facing criminal investigation,

the relationship of the employer and employees in modern organizations may be closer to “joint venturers” than “bargainers”).

[FN141]. Restatement (Second) of Contracts: Duty of Good Faith and Fair Dealing § 205 (1979) (imposing a duty of good faith upon each party to a contract).

[FN142]. *Id.* cmt. c (“This Section [§ 205] ... does not deal with good faith in the formation of a contract.”). See also DeMott, *supra* note 125, at 893 (“In applying this obligation [of good faith and fair dealing], the analysis focuses on the parties' relationship following their agreement, not prior to it.”).

[FN143]. *Chamison*, 735 A.2d at 920 (holding, in construing a contract for indemnification, that there exists an obligation of good faith and fair dealing implied in every contract) (citations omitted).

[FN144]. See, e.g., *id.* at 921 (“implied covenant [of good faith] cannot contravene the parties' express agreement and cannot be used to forge a new agreement beyond the scope of the written contract”); *Cincinnati SMSA Ltd. P'ship v. Cincinnati Bell Cellular Sys. Co.*, 708 A.2d 989, 992 (Del. 1998) (“implying obligations of good faith and fair dealing is a cautious enterprise”).

[FN145]. *Cincinnati SMSA Ltd. P'ship*, 708 A.2d at 992 (“absent grounds for reformation ... it is not the proper role of a court to rewrite or supply omitted provisions to a written agreement.”).

[FN146]. See *infra* notes 178-91 and accompanying text.

[FN147]. See Leff, *supra* note 123, at 137-38. (identifying five criteria for classifying an arrangement as a contract but not including subject matter).

[FN148]. John D. Calamari & Joseph M. Perillo, *Contracts* §§ 1-3 (3d ed. 1987) (“Most of contract law is premised upon a model consisting of two alert individuals, mindful of their self-interest, hammering out an agreement by a process of hard bargaining.”).

[FN149]. *Id.* at §§ 1-4 (noting that the following rationales have been advanced as justifying enforcement of contracts: “(a) human will either as a source of sovereignty or (b) as a source of moral compulsion, (c) private autonomy, (d) reliance, and (e) the needs of trade”).

[FN150]. Brudney, *supra* note 123 at 1404 (“[I]f the contract ... is ‘knowingly’ and ‘feely’ made by the parties, then ... its performance makes each of the parties better off and creates a pie for society .... Such a vision of the world and of the effects of the agreement proclaims private autonomy in the contract field.”).

[FN151]. See *infra* notes 164-77 and accompanying text.

[FN152]. Leff, *supra* note 123, at 135-35 (noting that the correlation between a classification and the purpose to be achieved may be less precise than another classification which could have been used).

[FN153]. *Mooney v. Willis-Overland Motors, Inc.*, 204 F.2d 888,898 (3d Cir. 1953) (observing that promise of reimbursement is necessary to secure capable individuals); *Homestore*, 888 A.2d at 211 (noting that advancement attracts capable individuals into corporate service); *Fasciana v. Elec. Data Sys. Corp.*, 829 A.2d 160, 170 (Del. Ch. 2003) (stating that advancement provisions are necessary to encourage talented people to serve in corporations). But see Margulies, *supra* note 43, at 60-61 (noting that during the New Deal expansive advancement pro-

visions were neither viewed as necessary nor desirable); Oesterle, *supra* note 25, at 536 (arguing that a lack of cohesive purpose is the greatest deficiency of the laws protecting executives from personal liability).

[FN154]. Oesterle, *supra* note 25, at n.224.

[FN155]. Kaung, 884 A.2d at 509 (noting that Delaware advancement provisions are part of a policy to manage risk/reward balance for organizations); Fasciana, 829 A.2d at 170 (observing that advancement encourages officers and directors to undertake risk in exchange for lucrative return).

[FN156]. Hibbert, 457 A.2d at 343-44 (holding that advancement and indemnification serve the public policy of encouraging managers to resist unjustified lawsuits).

[FN157]. *N.Y. Cent. & Hudson River R.R. v. U.S.*, 212 U.S. 481, 496 (1909) (reasoning that imposition of organizational criminal liability is necessary to control misconduct). See also Robson, *supra* note 49, at 121 (observing that both courts and scholars readily accepted deterrence as a goal of organizational criminal liability); V.S. Khanna, *Corporate Criminal Liability: What Purpose Does It Serve?*, 109 *Harv. L. Rev.* 1477 (1996) (noting that imposition of corporate criminal liability was necessary to deter misconduct but suggesting that it has outlived its usefulness).

[FN158]. Bucy, *supra* note 24, at 286 (arguing that bylaws and corporate resolutions providing indemnification tend to favor corporate executives); Samuel W. Buell, *Criminal Procedure Within the Firm*, 59 *Stan. L. Rev.* 1613, 1656 (2007) (observing that indemnification and advancement are likely to be used by agents who have the greatest influence policies on indemnification).

[FN159]. Reinier H. Kraakman, *Corporate Liability Strategies and the Cost of Legal Controls*, 93 *Yale L. J.* 857, 859 (1984).

[FN160]. Margulies, *supra* note 43, at 81 (arguing that when fees are being subsidized by the organization, neither the targeted executive nor the board of directors has incentives to hold down costs).

[FN161]. *Id.* at 83 (noting that details of D&O insurance “fly under the radar”).

[FN162]. Buell, *supra* note 158, at 1655 (footnote omitted).

[FN163]. *Id.* (suggesting that deterrence is most effective in the context of intentional violations); Lynn M. LoPucki, *The Death of Liability*, 106 *Yale L. Rev.* 1, 72 (1996) (arguing that, unlike unintentional, violations, purely intended events are completely “deterable”).

[FN164]. Brown, *supra* note 121, at 365 (suggesting that the operative principle regarding access to counsel is not only fairness but effectiveness of criminal law enforcement); Karlan, *supra* note 132, at 689 (arguing that the interests of a defendant and the criminal justice system in avoiding false positives “dovetail”).

[FN165]. Karlan, *supra* note 130, at 689 (defining false positives as those occurrences when the positive answer to the question of guilt is incorrect).

[FN166]. In the context of white collar prosecution, the existence of “secondary offenses” such as obstruction of justice or lying to the prosecutor raises the possibility that an employee may be convicted of a crime which is committed after the investigation has begun. In *Computer Associates International*, for example, an executive

pleaded guilty to a charge of obstruction based upon false statements made in a report that the executive knew would be submitted to the prosecutor. Indictment, PP 51-59, 75-79, *United States v. Kumar*, Cr. No. 04 Cr. 0846 (E.D. N.Y. Sept. 20, 2004).

[FN167]. Brown, *supra* note 121, at 376 (noting that targeted employees who are represented by counsel can negotiate concessions for their cooperation with the investigation).

[FN168]. Darryl K. Brown, *Street Crime, Corporate Crime and the Contingency of Criminal Liability*, 14 U. Pa. L. Rev. 1295, 1303-04 (2001) (describing a “crisis of legitimacy” in criminal prosecution which undermines efforts to promote compliance).

[FN169]. Buell, *supra* note 158, at 1627 (contrasting street crime, where the principle challenge is collection of evidence, with some white collar crimes where the investigation focuses on whether a crime was committed at all).

[FN170]. Brown, *supra* note 168, at 1306.

[FN171]. *Id.* (describing the efforts to use collaboration and cooperation to reduce corporate misconduct).

[FN172]. Karlan, *supra* note 130, at 689 (defining “false negatives” as occurring where the negative answer to the question of guilt is incorrect).

[FN173]. Brown, *supra* note 121, at 373 (noting that defendants have incentives to overlitigate cases to avoid the “day of reckoning”).

[FN174]. *Id.* at 374.

[FN175]. *Id.* at 373-74 (arguing that wealthy defendants can overlitigate cases resulting in unmerited acquittals).

[FN176]. Margulies, *supra* note 43, at 81 (observing that executives have little incentive to hold down litigation costs).

[FN177]. Carrie Johnson, *After the Enron Trial, Defense Firm Is Stuck with the Tab*, Wash. Post, June 16, 2006, at D1 (quoting John Marquess, president of a New Jersey firm which monitors legal fees).

[FN178]. Dunlap, 1999 Del. Ch. LEXIS at \*19 (citing the contention of the corporate employer that claimant's hiring of accounting firm to perform forensic accounting was equivalent of trying to prove that the earth is flat).

[FN179]. *N.Y. Cent. & Hudson River R.R.*, 212 U.S. at 494 (holding that corporations are vicariously liable for the actions of their agents); *U. S. v. Hilton Hotels Corp.*, 467 F. 2d 1000, 1007 (9th Cir. 1972) (holding that corporations are criminally liable for acts of employees committed within the scope of employment even when the acts contravene the directives of the corporation).

[FN180]. *Simon v. Socony-Vacuum Oil Co.*, 38 N.Y.S. 2d 270, 275 (N.Y. Sup. Ct. 1942) *aff'd*, 47 N.Y.S. 2d 589 (1944) (observing that an executive's plea of *nolo contendere* benefited the corporation since the plea could not be used as evidence against the company).

[FN181]. Bucy, *supra* note 24, at 346 (suggesting that potential collateral estoppel effect of criminal action in a subsequent civil suit may be the reason that corporations advance fees).

[FN182]. Buell, *supra* note 158, at 1647 (proffer of immunity may induce targeted employees to make statements).

[FN183]. *Chamison v. Healthtrust Inc.*, 735 A.2d at 922-23 (holding that a selection of counsel provision cannot be construed so broadly as to require a defendant to accept inferior counsel).

[FN184]. See, e.g., Del. Code Ann. tit.8 § 145 (e) (2009) (advancement may be made on such terms and conditions as the corporation deems appropriate); Model Bus. Corp. Act § 8.58(a) (2007) (providing that corporation may limit indemnification or advancement by a provision in its articles of incorporation); Minn. Stat. Ann. § 302A.521, subd. 4 (2004) (providing that articles or bylaws may impose limits or conditions on advancement).

[FN185]. Buell, *supra* note 158, at 1633 (observing that although given the opportunity to choose their own lawyers and eschew joint defense arrangements, employees seldom do).

[FN186]. James B. Stewart, *Den of Thieves* 314-15 (1991) (stating that making recommendations to employees who were the subject of criminal investigation, Drexel Burnham Lambert, Inc. recommended “friendly” attorneys who had received previous referrals from counsel retained by Drexel).

[FN187]. Margulies, *supra* note 43, at n.91 (stating that lawyers for corporations maintain a network of other lawyers, who are dependent on referrals, and who might influence a client against cooperation, even against the client's best interest); Daniel C. Richman, *Cooperating Clients*, 56 Ohio St. L.J. 69, 126 (1995) (describing a hypothetical attorney whose desire for future fees and referrals taints her representation of targeted employees).

[FN188]. Sarah Helene Duggin, *The McNulty Memorandum, the KPMG Decision and Corporate Cooperation: Individual Rights and Legal Ethics*, 21 Geo. J. Legal Ethics 341, 406-07 (2008) (discussing approaches used by counsel to advise employees during internal investigations, including a corporate version of a Miranda warning).

[FN189]. Am. Coll. of Trial Lawyers, *supra* note 14, at 94.

[FN190]. *Id.*

[FN191]. Oesterle, *supra* note 25, at 566 (noting that the only check on organizational influence over the legal strategy of targeted defendant is the lawyer's code of ethics). See also Model Code of Prof'l Responsibility EC 5-23 (1983) (acknowledging that organizations who pay for legal services for others may exert pressure on such lawyers in order to advance their own objectives); Duggin, *supra* note 188, at 348 (arguing that corporate cooperation controversy must be solved within the system of legal ethics).

[FN192]. John Hasnas, *Managing the Risks of Legal Compliance: Conflicting Demands of Law and Ethics*, 39 Loy. U. Chi. L. J. 507, 516-17 (2008) (instituting programs of procedural justice encourages employee compliance and law-abidingness); Stein, *supra* note 119, at 3249 (observing that many corporations believe that payment of legal expenses boosts morale and is required by fundamental fairness).

[FN193]. Hasnas, *supra* note 192, at 521 (arguing that organizations have an ethical obligation to treat employees who are under suspicion fairly).

[FN194]. Duggin, *supra* note 188, at 405.

[FN195]. But see *supra* notes 141-46 and accompanying text describing the equitable limits on interpreting con-

tacts.

[FN196]. Bucy, *supra* note 24, at 317-19 (arguing that the current provisions on advancement permit executives to receive indemnification without meeting statutory standards); Oesterle, *supra* note 24, at 545-46 (stating that courts have been “surprisingly lenient” in approving board decisions on advancement, especially since the advances are not likely to be repaid); Rossman, *supra* note 28, at 41 (noting that the right to advancement is not forfeited by the claimant's misconduct or self-interest).

[FN197]. Bucy, *supra* note 24, at 342 (positing that the scope of indemnification and advancement provisions may help to encourage or discourage white collar crime); Margulies, *supra* note 43, at nn.49-53 (arguing that payment of legal fees to corporate wrongdoers may create moral hazard and encourage a “race to the bottom”).

[FN198]. Brown, *supra* note 121, at 370-71 (observing that in the context of street crime, courts and legislatures effectively determine access to legal assistance by setting funding levels for counsel and expert assistance); Buell, *supra* note 158, at 1633-34 (contrasting advancement of legal fees, recommendation of counsel and joint defense agreements, typical of white collar cases, with legal representation in street crimes).

[FN199]. See *supra* notes 35-42 and accompanying text.

[FN200]. See *supra* notes 99-119 and accompanying text.

[FN201]. *Tafeen v. Homestore, Inc.*, 2004 WL 556733, at \*10 n.71 (Del. Ch. March 22, 2004).

[FN202]. *Id.* at \*3 (observing that it is left for organizations themselves to weigh need to attract talented managers against the potential costs to shareholders).

[FN203]. See *supra* notes 32-34, and accompanying text.

[FN204]. See *supra* notes 35-37, 197-214 and accompanying text.

[FN205]. Minn. Stat. Ann. § 302A.521 (2004).

[FN206]. See, e.g., *id.* § 302A.521, subdiv. (6) (providing for detailed procedure for determining eligibility), subdiv. (8) (providing for notice to shareholders post payment); and subdiv. (4) (requiring equal benefits for employees within the same class).

[FN207]. *Id.* at subdiv. (4) (2008) (providing that articles or bylaws may prohibit advancement); *Barry v. Barry*, 824 F. Supp. 178, 183 (D. Minn. 1993), *aff'd*, 28 F.3d 848 (8th Cir. 1994) (holding that Minnesota statute makes advancement mandatory unless organization elects to prohibit or limit in bylaws).

[FN208]. Minn. Stat. Ann. § 302A.521, subdiv. (4) (2004).

[FN209]. Minn. Stat. Ann. § 302A.521, subdiv. (4) (specifically permitting organizations to impose “conditions” on advancement). Presumably such conditions would include selection of counsel provisions.

[FN210]. *Id.* (providing that an organization can impose monetary limits on advancement).

[FN211]. *Id.* at cmt.

[FN212]. Id.

[FN213]. Id.

[FN214]. Id.

[FN215]. Attorney-Client Privilege Protection Act of 2009, S. 445, 111th Cong. (2009); Attorney-Client Privilege Protection Act of 2009, H.R. 4326, 111th Cong. (2009).

[FN216]. The Attorney-Client Privilege Protection Act of 2006 was introduced in the Senate to ensure inter alia that advancement of fees to target employees, as well as joint defense agreements and information sharing would not be considered by prosecutors in evaluating organizational cooperation. Attorney-Client Privilege Protection Act of 2006, S.30, 109th Cong. § 3(a) (2006). Although the 2006 Act was not reported out of Committee, revised versions were introduced in 2007, 2008 and 2009 to address the issues first raised by the Thompson Memorandum and in reaction to perceived inadequacies in the revised guideline issued by the Department of Justice. Attorney-Client Privilege Protection Act of 2007, S. 186, 110th Cong. (2007); Attorney-Client Privilege Protection Act of 2007 H.R. 3013, 110th Cong. (2007); Attorney-Client Privilege Protection Act of 2008, S. 3217, 110th Cong. (2008); Attorney-Client Privilege Protection Act of 2009, S. 445, 111th Cong. (2009); Attorney-Client Privilege Protection Act of 2009, H.R. 4326, 111th Cong. (2009).

[FN217]. Attorney-Client Privilege Protection Act of 2009, S. 445, 111th Cong. § 3(a) (2009); Attorney-Client Privilege Protection Act of 2009, H.R. 4326, 111th Cong. § 3(a) (2009).

[FN218]. Id.

[FN219]. Black's Law Dictionary 580 (9th ed. 2009) (defining a “duty” as “a legal obligation that is owed or due to another that needs to be satisfied”). Black's Law Dictionary identifies thirty-one types or classification of duties, including a “noncontractual duty” which arises independently of a contract. Id.

[FN220]. Edward Soule, Trust and Managerial Responsibility, 8 Bus. Ethics Q. 249, 268 (1995) (employers who actively encourage employees to trust them create moral obligations toward such employees); John Hasnas, *Ethics and the Problem of White Collar Crime*, 54 Am. U. L. Rev. 579, 648 (2005) (fostering trust requires assumption of a duty by the trusted actor to protect the interests of the vulnerable party).

[FN221]. Restatement (Second) of Contracts: Duty of Good Faith and Fair Dealing § 205 (1979) (“Every contract imposes upon each party a duty of good faith and fair dealing in its performance and its enforcement.”).

[FN222]. Restatement (Second) of Contracts: When Undue Influence Makes a Contract Voidable § 177(1) (1979) (providing that a contract is voidable if assent was the result of unfair undue influence exerted by a person in a dominant relationship).

[FN223]. Restatement (Second) of Contracts: When a Misrepresentation Makes a Contract Voidable § 164(1) (1979) (providing that a contract is voidable if agreement was induced because of a material misrepresentation upon which a party reasonably relied).

[FN224]. DeMott, *supra* note 125, at 905-06 (observing that contractual doctrines which address misconduct focus on the unfairness of the transaction to one of the parties to the contract).

[FN225]. Bucy, *supra* note 24, at 314 (courts have ignored public policy considerations in analyzing indemnification and advancement); Rossman, *supra* note 28, at 39 (noting that courts have required advancement notwithstanding allegations of misconduct, even when allegations are made by the corporation itself).

[FN226]. As one commentator noted on the discernment of a duty, “[E]ach duty itself defines the types of relationship to which it applies .... [E]ach duty exacts its own standard of acceptable conduct from the fiduciary to whom it applies.” DeMott, *supra* note 125, at 915 n.160 (quoting P. Finn, *Fiduciary Obligations* 4 (1977)).

[FN227]. Black's Law Dictionary 580 (9th ed. 2009).

[FN228]. William L. Prosser, *Palsgraf Revisited*, 52 Mich. L. Rev. 1, 13 (1953) (arguing that the consensus of opinion suggests that a duty arises out of a “relation” between parties).

[FN229]. *Id.* at 14.

[FN230]. *Hopkins v. Fox & Lazo Realtors*, 625 A.2d 1110, 1116 (N.J. 1993).

[FN231]. Cf. DeMott, *supra* note 125, at 892-09 (contrasting the obligations of a fiduciary duty with the contractual obligation of good faith and fair dealing and suggesting that fiduciary duties transcend contractual obligations).

[FN232]. See *supra* notes 136-46 and accompanying text.

[FN233]. See *supra* notes 165-77 and accompanying text.

[FN234]. 830 F.Supp. 262, 268 (E.D. Pa. 1993).

[FN235]. *Id.* at 268. Although Felicetti applied Pennsylvania law, the court observed that the Pennsylvania statute was modeled on the Delaware statutes and the MBCA. *Id.*

[FN236]. *Id.* at 270.

[FN237]. *Id.* at 264-65.

[FN238]. *Id.* at 270.

[FN239]. Neal, 667 A.2d at 482 (1995) (distinguishing Felicetti, by observing that the instant case presented no conflict between the by-law provision and fiduciary duty of directors); Ridder, 47 F.3d at 87 (holding that Felicetti construed Pennsylvania law and should not be applied in a case involving Delaware law). But see *supra* note 235.

[FN240]. Ridder, 47 F.3d at 87 (distinguishing Felicetti by noting that it is rare that directors could breach a fiduciary duty by complying with a duly approved bylaw). But see Felicetti, 830 F. Supp. at 270 (distinguishing other Delaware case law by noting that in prior cases bylaw had not conflicted with fiduciary duties of the directors).

[FN241]. Brown, *supra* note 121, at 378 (observing that provision of counsel by an organization to employee targets during the investigative stage affords them an advantage over the discrete representation typical of street criminals).

[FN242]. *Id.* at 377 (observing that right to court appoint counsel occurs at the charging stage).

[FN243]. See Rossman, *supra* note 28, at n.43 for a list of states requiring a preliminary factual inquiry prior to advancing fees.

[FN244]. See *supra* notes 51-55 and accompanying text for a discussion of Bergonzi.

[FN245]. Brown, *supra* note 121, at 373 (legislatures set de facto limits on availability of counsel to indigent defendants by setting funding levels which act as a disincentive for attorneys to overlitigate cases).

[FN246]. See *supra* notes 179-91 and accompanying text.

[FN247]. Brown, *supra* note 121, at 378-79 (observing that defense resources in white collar crime cases can frequently match the government's resources).

[FN248]. See, e.g., 21 U.S.C. § 853(b) (2006) (requiring forfeiture of all property derived from commission of a crime); 18 U.S.C. § 982(a)(1) (2006) (authorizing forfeiture of money traceable to money laundering); 18 U.S.C. §§ 3681-82 (2006) (providing for forfeiture of defendant's profits from movies, books and other media related to the crime, but allowing twenty percent of such profits for use as attorneys' fees).

[FN249]. 21 U.S.C. § 853(a); 18 U.S.C. § 982(a); 18 U.S.C. § 3681(a).

[FN250]. See *United States v. Wittig*, No. 03-40142-JAR, 2004 WL 1490406 (D. Kan. June 30, 2004), modified, 333 F. Supp. 2d 1048 (D. Kan. 2004), reinstated, 2005 WL 1227914 (D. Kan. May 23, 2005) (court ordered corporation to pay attorneys' fees it owed under its bylaws into escrow).

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