Delaware Supreme Court Holds that Dissolution Statutes Do Not Extinguish a Dissolved Corporation's Potential Liability to Third Parties

The Delaware Supreme Court recently offered new insight into a dissolved corporation's exposure to liability for third party claims. In *Anderson v. Krafft-Murphy Company, Inc.*,[1] the Court held as a matter of first impression in Delaware that the statutory scheme governing the dissolution and winding up of a Delaware corporation does not contain a general statute of limitations that would shield a dissolved corporation from liability.

I. Factual Background and Procedural History[2]

Formed in 1952, Krafft-Murphy Company, Inc. (the "Company") is a dissolved Delaware corporation that, prior to its dissolution in 1999, was involved in the supply and installation of certain asbestos-containing products. By virtue of this activity, the Company found itself named as a defendant in hundreds of asbestos-related personal injury claims filed from 1989 onwards in various jurisdictions. The Company's sole assets following its dissolution (and at the time of the underlying asbestos proceedings) were certain unexhausted insurance policies which obligated the insurers to defend the Corporation in covered actions and to indemnify the Company against certain third party claims.

In the Court of Chancery, the tort claimants sought the appointment of a receiver to facilitate the litigation against the Company in the other courts. The Company moved in 2012 for summary judgment with respect to those asbestos-related claims commenced more than ten years after its dissolution, contending that it held no property that would warrant the appointment. It argued that the statutory scheme established a statute of limitations that bars claims brought more than ten years after dissolution, and thus the insurance policies are of no value with respect to these matters and do not constitute property capable of being administered by a receiver. The Court of Chancery agreed and dismissed this set of claims accordingly.

II. The Decision of the Delaware Supreme Court

On appeal, the Delaware Supreme Court addressed two interconnected issues of first impression in Delaware. The first question was whether unexhausted liability insurance policies constitute "property" under 8 *Del. C.* § 279. The second was whether the corporate dissolution scheme of Delaware contains a general statute of limitations that operates to extinguish a dissolved corporation's liability from third party claims.[3]

Section 279 of the Delaware General Corporation Law authorizes the appointment of a receiver or a trustee to advance the winding up of a dissolved corporation's affairs only where the corporation has "undistributed 'property.'"[4] Settled Delaware law provides that contingent contractual rights, such as the Company's unexhausted insurance policies, are "property" for purposes of section 279 only if and to the extent these rights are capable of vesting.[5] However, such insurance policies only vest if the claims to which they relate

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[1] *Anderson v. Krafft-Murphy Company, Inc*., No. 85, 2013 (Del. Nov. 26, 2013), available at http://courts.state.de.us/opinions/download.aspx?ID=198060 (the "Opinion").

[2] The factual background is summarized from the background set forth in the Opinion.

[3] Opinion at 2. The procedures governing the dissolution and winding up of a Delaware corporation are set forth in 8 *Del. C.* §§ 275-282.

[4] *Id*. at 15 (citing *In re Citadel Indus., Inc.*, 423 A.2d 500, 506 (Del. Ch. 1980)).

[5] *Id.*; *see Addy v. Short*, 89 A.2d 136, 140 (Del. 1952).

are not time-barred, in which case the policies obligate the insurers to bear "all sums which the insured shall become legally obligated to pay as damages" and offer "significant potential indemnification value to the" Company.[6] Otherwise, if the claims are time-barred, the policies afford no value to the Company and thus fall short of "property" that would justify the remedy of receivership.[7] Thus, the determination of whether the insurance policies are "property" under section 279 hinges on whether any statutory provision governing corporate dissolution serves to avoid the Company's liability to third parties.

In its analysis of that issue, the Court relied almost exclusively on the statutory language and legislative history to conclude that no generally applicable statute of limitations can be found in Delaware's dissolution statutes. First, section 279 authorizes the appointment of a receiver, through which a dissolved corporation may "sue and *be sued*," without mention of any limitations period.[8] In addition, sections 280(c) and 281(b) militate against the finding of a general statute of limitations, because these provisions compel a dissolved corporation to reserve assets for the payment of claims that "may arise or become known" a decade after dissolution.[9] The Court rejected the argument that the 10-year period referred to in section 281(b) was intended to be a general statute of limitations by noting that section 281(b) requires only that a dissolving corporation provide for claims that are "'*likely* to arise . . . within 10 years after the date of dissolution'—not *all* claims that *will* arise."[10] On that basis, the Court declared that "[t]he General Assembly clearly contemplated that a dissolved Delaware corporation could continue to be liable to third parties long after its formal dissolution."[11]

The Court further noted that the only provisions of the dissolution statutes that speak to continued liability in the years after dissolution are sections 281(c) and 282. Their application to the current set of facts is inappropriate, however, as they "concern only the liability of directors and shareholders—not the liability of the dissolved corporation."[12] These provisions are noteworthy nonetheless, because they limit the personal liability of directors and shareholders where the dissolved corporation has complied with either the court-supervised or the "default" claims planning procedures set forth in sections 280 and 281(b), respectively.[13]

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[6] Opinion at 17.

[7] *See Addy*, 89 A.2d at 140.

[8] Opinion at 19 (quoting *City Investing Co. Liquidating Trust v. Continental Cas. Co.*, 624 A.2d 1191, 1195 (Del. 1993)) (emphasis in Opinion).

[9] *Id.* Specifically, section 280(c) affords the dissolving corporation the option of petitioning the Court of Chancery to ascertain "the amount and form of security that will be reasonably likely to be sufficient to provide compensation for claims that have not been made known to the corporation or that have not arisen but that, based on facts known to the corporation or successor entity, are likely to arise or to become known . . . within 10 years after the date of dissolution." In the alternative, section 281(b) permits a dissolved corporation to "adopt a plan of distribution pursuant to which the dissolved corporation or successor entity . . . shall make such provision as will be reasonably likely to be sufficient to provide compensation for claims that have not been made known to the corporation or that have not arisen but that, based on facts known to the corporation or successor entity, are likely to arise or to become known . . . ."

[10] Opinion at 26 (emphasis in Opinion).

[11] *Id.* at 23.

[12] *Id.*

[13] *Id.* at 22-23. Section 281(c) provides that directors of a dissolved corporation which has complied with either procedure "shall not be personally liable to the claimants of the dissolved corporation." The future obligations of any shareholder of a dissolved corporation in compliance with either of the above statutory provisions is limited by section 282(a) to the "pro rata share of the claim or the amount so distributed to such shareholder, whichever is less."

III. Significance of the Decision

The *Anderson* decision of the Delaware Supreme Court has several implications that are of particular potential interest for Delaware corporations and their directors and shareholders in the context of dissolution. It first and foremost explains definitively that a dissolved corporation's exposure to third party claims is prolonged and poses a viable threat well after dissolution. That remains true, as the Court noted, even though future liabilities may be unforeseeable.[14] In this light, as part of the dissolution process, management should assess the long-term adequacy of the corporation's present liability reserves set aside in accordance with sections 280(c) or 281(b), particularly if the nature of the business makes it reasonably likely that claims may arise long after dissolution and the winding up process. Failure to do so may lead to entanglement in litigation for failing to satisfy the corporation's obligation to provide for the payment of all future liabilities that are likely to arise.[15]

On the other hand, this decision is self-evidently welcomed by corporate creditors and tort claimants alike. It also provides comfort to directors and shareholders of dissolved corporations, as it clearly acknowledges the opportunity for these parties to limit their personal liability to claimants of the dissolved corporation. This opinion stresses the importance of complying with either the court-supervised or "default" claims planning procedures when seeking to invoke this protection. In this regard, however, this decision further enhances the attractiveness of proceeding under a court-supervised dissolution procedure to determine the amount of security that is sufficient to satisfy future claims, as opposed to making this "reasonable provision" independently pursuant to section 281(b), as the former method "allows corporate directors to assure themselves that they have satisfied the corporation's obligations to future claimants and that they will qualify for the protections afforded by [statute]."[16]

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If you have any questions about the issues addressed in this memorandum or if you would like a copy of any of the materials mentioned, please do not hesitate to call or email Charles A. Gilman at 212.701.3403 or cgilman@cahill.com; Jon Mark at 212.701.3100 or jmark@cahill.com; John Schuster at 212.701.3323 or jschuster@cahill.com.

[14] Opinion at 26.

[15] *See In re RegO Co.*, 623 A.2d 92, 109-10 (Del. Ch. 1992) (dissolved corporation without sufficient security to satisfy all future claims that were likely to be asserted was required to establish a post-dissolution trust and implement an interim cap of claims to ensure payment of all claims reasonably likely to arise).

[16] *Id.* at 97 (observing that, because "mathematical certainty is not possible" in such forward-looking analysis, what is "reasonably likely to be sufficient" will virtually always be litigable, thereby making reliance on section 281(b) a "risky situation for corporate directors regardless of their good faith and due care").

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