

The Metropolitan Corporate Counsel®

www.metrocorpcounsel.com

Volume 21, No. 3

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March 2013

Pack Your Bags And Renew That Passport: Duties Of Independent Directors Of Delaware Corporations Having Significant Operations Or Assets Abroad

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On February 6, 2013, Chancellor Strine of the Delaware Chancery Court issued a bench ruling addressing the duty of independent directors of a Delaware corporation with significant operations or assets outside the United States. In re Puda Coal, Inc. Stockholders Litigation, C.A. No. 6476-CS (Del. Ch. Feb. 6, 2013). In a short but important bench ruling, Chancellor Strine refused to dismiss a breach of fiduciary duty claim against independent directors of a Delaware corporation who had failed to discover the unauthorized sale of assets located in China by the company's chairman. Importantly, Chancellor Strine's remarks implicated the duty of loyalty, which creates a risk of personal liability for directors and, potentially, the absence of corporate indemnification. While the facts in the case were somewhat extreme, the ruling in *Puda Coal* highlights the risks and challenges that may exist for directors of Delaware corporations with significant foreign assets or operations. Although Chancellor Strine recognized that each situation is undoubtedly depen-

dent on its facts and will turn on the nature of the foreign operations, his ruling did include the following remarks:

[I]f you're going to have a company domiciled for purposes of its relations with its investors in Delaware and the assets and operations of that company are situated in China that, in order for you to meet your obligation of good faith, you better have your physical body in China an awful lot. You better have in place a system of controls to make sure that you know that you actually own the assets. You better have the language skills to navigate the environment in which the company is operating. You better have retained accountants and lawyers who are fit to the task of maintaining a system of controls over a public company.

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Independent directors who step into these situations involving essentially the fiduciary oversight of assets in other parts of the world have a duty not to be dummy directors. I'm not mixing up care in the sense of negligence with loyalty here, in the sense of your duty of loyalty. I'm talking about the loyalty issue of understanding that if the assets are in Russia, if they're in Nigeria, if they're in the Middle East, if they're in China, that you're not going to be able to sit

in your home in the U.S. and do a conference call four times a year and discharge your duty of loyalty. That won't cut it. That there will be special challenges that deal with linguistic, cultural and others in terms of the effort that you have to put in to discharge your duty of loyalty. There's no such thing as being a dummy director in Delaware, a shell, someone who just puts themselves up and represents to the investing public that they're a monitor. Because the only reason to have independent directors – remember, you don't pick them for their industry expertise. You pick them because of their independence and their ability to monitor the people who are managing the company...

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If it's a situation where, frankly, all the flow of information is in the language that I don't understand, in a culture where there's, frankly, not legal strictures or structures or ethical mores yet that may be advanced to the level where I'm comfortable? It would be very difficult if I didn't know the language, the tools. You better be careful there. You have a duty to think. You can't just go on this [board] and act like this was an S&L regulated by the federal government in Iowa and you live in Iowa.

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