IN THE COURT OF CHANCERY OF THE STATE OF DELAWARE

MAKEDA BREEDY-FRYSON, ANDRE FRYSON, KADUE SAYID, REBECCA MUNDOPA, EDWARD CUNNINGHAM and JEWEL CUNNINGHAM,	)	
Plaintiffs,	)	
v.	)	C.A. No. 3577-VCS
TOWNE ESTATES CONDOMINIUM OWNERS ASSOCIATION, INC. and TOWNE ESTATES CONDOMINIUM ASSOCIATION	)	
Nominal Defendants,	)	
DAVID FAJARDO, MARY ANN O'BRIEN, KRISTEN KINGERY, JAMES MCGILVRA, PAUL HILLER, JEFF KOCAR, VERED PRIFER-VERANDAK, CHARLENE ANDERSON, TOM SOUTHARD, EMORY HILL REAL ESTATE SERVICES, INC.,	)	
Defendants.	)	

MEMORANDUM OPINION

Date Submitted: November 30, 2009
Date Decided: February 25, 2010

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STRINE, Vice Chancellor.

I. Introduction

In February 2007, a fire destroyed certain condominium units in the Towne Estates Condominium complex ("Towne Estates"). A number of the affected unit holders later brought this suit advancing direct claims and claims purportedly brought derivatively on behalf of the Towne Estates Condominium Owners Association (the "Owners Association").

After the fire, it turned out that Towne Estates did not procure sufficient insurance coverage to replace the condominium units and repair the common areas damaged by the fire. By this action, the plaintiffs seek to require the defendants to come up with the shortfall, thereby eliminating the need for the plaintiffs to cover the shortfall themselves. According to the Complaint, the council of individuals responsible for administering the affairs of Towne Estates (the "Council"), and Emory Hill Real Estate Services, Inc. ("Emory Hill"), the manager of Towne Estates, should be held liable for procuring an inadequate amount of insurance.

In this decision, I address separate motions by the Council members to dismiss the claims against them and by Emory Hill for summary judgment and dismissal. First, I find that the Complaint fails to plead facts supporting a rational inference that any failure by the Council in procuring adequate coverage was the result of bad faith or willful misconduct. At best, the Complaint suggests that the Council may have been negligent. Because the code of regulations and the enabling declaration governing Towne Estates exculpate Council members for liability to Towne Estates or its unit holders for any acts that are not the result of

bad faith or willful misconduct,[1] and because I conclude that the exculpatory provisions are permissible under the authority of *Greloch v. Council of Parkridge at Bellevue Condominiums*,[2] the plaintiffs' claims against the Council for monetary relief are dismissed.

Second, the Complaint fails to plead facts supporting a rational inference that Emory Hill can be held responsible for the shortfall in coverage. By the plain terms of its retention agreement, Emory Hill was not charged with advising the Council about the adequacy of insurance coverage. All it was obligated to do was provide certain information if requested to do so by the Council in the Council's own efforts to obtain coverage. The Complaint does not plead that Emory Hill failed to provide such information after a request. Moreover, summary judgment is appropriate on this claim because the plaintiffs were afforded discovery and the undisputed evidence reveals that Emory Hill never received any request for information or assistance in the insurance procurement process.

Finally, the plaintiffs advance a number of subsidiary claims that are styled as derivative. But the plaintiffs do not plead particularized facts supporting an inference that the Council cannot fairly consider a demand. Those claims are therefore dismissed.

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[1] *See* Compl. Ex. A (Enabling Declaration Establishing a Plan for Condominium Ownership of Towne Estates Condominium Apartments (Oct. 5, 1988)) (the "Enabling Declaration") Art. 14 § C; Compl. Ex. D (Code of Regulations of Towne Estates Condominium Apartments (Oct. 5, 1988)) ("Code of Regulations") Art. 3 § R.
[2] 1994 WL 384614 (Del. Ch. July 12, 1994).

II. Procedural Background

This case arises from a fire in February 2007 that destroyed portions of two Towne Estates buildings, Buildings J and K. Regrettably, the fire damaged not only some of the common areas of those buildings, but also the condominium units of several of the plaintiff unit owners. Insurance on the destroyed buildings, Buildings J and K, had been procured by the Council but in an amount of only $633,281.24, short of the $1,107,263.33 in estimated damage.[3]

On February 27, 2008, a group of unit owners whose condominiums had been destroyed in the fire — plaintiffs Fostina Dixon Kilgoe, Susanna Walton, Makeda Breedy-Fryson, Andre Fryson, Tirus Brown, Kadue Sayid, Maxine West, and Rebecca Mundopa — initially brought this suit.[4] In the original complaint, the plaintiffs sued the Council as a collective body and not merely as a nominal party, as well as individual Council members Bob Holt, Mary Ann O'Brien and David Fajardo, defendant Emory Hill, and BC Consulting, Inc, another professional management firm that advised the Council. Much like the current Complaint, the original complaint alleged that the Council failed to secure

[3] Second Amended Complaint ("Complaint") ¶ 13.

[4] The original complaint was not brought as a class action. But in late 2008, the plaintiffs' counsel decided to seek class certification. The putative class is identified as all 90 unit owners of Towne Estates, on the theory that the insurance shortfall will affect all unit owners, and not only those who units were destroyed. The rationale for this is that the Council sought to have all unit owners contribute toward restoration of the common areas that were damaged by the fire, with the unit owners who suffered the destruction of their condominiums bearing the costs of rebuilding those specific units. A motion for class certification was filed on January 22, 2009, but the plaintiffs' and the defendants' counsel have yet to agree upon a briefing schedule, and plaintiffs' counsel has yet to press the motion. But, because I dismiss all the plaintiffs' claims, there will likely be no need to ever address the class certification motion.

adequate insurance coverage to cover the cost of rebuilding, and failed to promptly proceed with repairs to the damaged portions of Towne Estates.[5] The objective of the original complaint was to get Buildings J and K rebuilt, with the costs for doing so being shifted from the plaintiff unit owners whose homes had been burned to the defendants. Because the plaintiff unit owners were out of their homes, the plaintiffs said they wished to move very quickly.

Unfortunately, that wish was not matched by an efficient approach to prosecuting the litigation. As an initial snaggle, the parties bogged down into extended argument over whether Master Ayvazian's determination that the plaintiffs' invocation of 10 *Del. C.* § 348 was improper because the plain language of § 348 applies only to homeowners associations and lot owners of a subdivision, not condominium associations.[6] When the matter reached me, it was clear that the plaintiffs wanted an expedited hearing but that the defendants had substantial defenses, and that it was unrealistic to hold an expedited trial without discovery and briefing.[7] Rather than spend scarce resources on whether § 348 applied, I encouraged the parties to agree that they should spend their resources focusing on finishing the case in an expedited manner, and believed that I had obtained such an

[5] Verified Complaint ¶¶ 16-21.

[6] *Breedy-Fryson v. Towne Estates*, C.A. No. 3577-MA, at 14 (Del. Ch. Mar. 31, 2008) (TRANSCRIPT); *see also* 10 *Del. C.* § 348(a) (authorizing a Master in Chancery to mediate a dispute involving "the enforcement of deed covenants or restrictions" where "[a]t least one party is an association or other entity representing homeowners or lot owners of a subdivision").

[7] *See* 10 *Del. C.* § 348(c) (giving the Court of Chancery discretion to set a schedule different than the typical schedule followed by § 348 if the court concludes that it is warranted).

agreement. To that end, I set aside time in early Spring 2009 for a trial and instructed the parties to move with alacrity to either resolve the case consensually or prepare it for resolution at trial.

Unfortunately, the plaintiffs themselves did not complete the work necessary to allow a trial to fairly proceed on the expedited basis they wished. As a result of the plaintiffs' failure to meet key deadlines, the trial had to be postponed. By that time, it had also become clear that the plaintiffs had presented a bit of a moving target to the defendants through evolutions in their pleadings. Therefore, to get this case back on a track toward resolution, I put in place a schedule that required the plaintiffs to stand behind an amended complaint. Given that the plaintiffs had already been afforded written discovery by the defendants and that the plaintiffs, and not the defendants, had been the primary cause of the foregone trial date, it seemed advisable and fair to give the defendants a chance to address the viability of the plaintiffs' amended complaint and then proceed to trial only on whatever claims survived dispositive motion practice. Even then, the plaintiffs failed to verify their Second Amended Class Action Complaint, and eventually filed it properly three weeks after the June 18, 2009 deadline to do so. The parties then spent months briefing and arguing the motions I now decide.

By the time the second amended Complaint was filed on July 9, 2009, new Council members had been elected on March 25, 2009 (the "New Council"). The Complaint names as defendants both the New Council members — Paul Heller, Jeff Kocar, Vered Prifer-Verandak, Charlene Anderson, and Tom Southard — and

former Council members David Fajardo, Mary Ann O'Brien, Kristen Kingery, and James McGilvra (the "Old Council"), who were in office when the February 2007 fire occurred.[8] The Complaint also names the Towne Estates Condominium Owners Association, Inc. and the unincorporated Owners Association as nominal defendants, and dropped the Council itself as a collective body as a defendant.

In their briefs to this court addressing the viability of the claims in the plaintiffs' Complaint, the parties have covered a number of subtle issues in a very cursory manner. In so saying, I am being observational, not critical. The reality is that all of the parties have limited resources and the intricacy and novelty of some of the issues presented is out of sync with the dollars at stake. I approach these issues seeking to make as modest an imprint upon our law as possible, given that the parties' arguments often come unaccompanied by the submission of any reliable authority. Where this is so (for example, as to the question of what, if any, demand excusal standard applies when unit owners seek to bring suit on behalf of a condominium association), I will say so and give an answer, but I candidly admit that I lacked the time and resources to conduct anything like the full-blown independent research project the parties' cursory briefs left me with. Thus, the very narrow prism on the relevant jurisprudential world given to me by the parties is the one I primarily use, supplementing it to some extent with targeted additional research.

[8] Compl. ¶ 3.

With that context in mind, I turn to resolving the motions at hand. The two motions are brought by different defendants. One motion is brought by the Owners Association and the individual New and Old Council members (the "Council Defendants"). Essentially, the Council Defendants argue that the Complaint fails to plead non-exculpated claims against them, and that, as to certain claims that the plaintiffs style as derivative, the Complaint must be dismissed for lack of demand excusal. In keeping with the odd nature of the briefs submitted by the plaintiffs and the Council Defendants, the Council Defendants have styled their motion as a motion for judgment on the pleadings, despite their failure to answer the latest Complaint.[9] For that reason, the plaintiffs have treated the Council Defendants' motion as a motion to dismiss under Court of Chancery Rules 12(b)(6) and 23.1. I find that treatment apt because a motion for judgment on the pleadings may only be heard "[a]fter the pleadings are closed."[10] Thus, I treat the Council Defendants' motion as one for dismissal.

The other motion is brought by defendant Emory Hill. This motion is brought in the alternative as a motion for summary judgment or for dismissal. Emory Hill has filed a motion for summary judgment because the plaintiffs were given access to written discovery and the chance to file a Rule 56(f) affidavit if

[9] Former defendants, the Towne Estates Condominium Association Council and Bob Holt, as well as current defendants Mary Ann O'Brien, and David Fajardo, filed an answer only to the original complaint. No answer was filed by defendants Holt, O'Brien, and Fajardo to the First Amended Class Action Complaint, which named Holt, O'Brien, Fajardo, Emory Hill, and BC Consulting as defendants.
[10] Ch. Ct. R. 12(c).

they believed they needed further discovery to address fairly the motion for summary judgment. The plaintiffs failed to do so, and I treat Emory Hill's motion as one for summary judgment.

In order to provide context for the factual background that follows, the plaintiffs' key claims against the Council Defendants and Emory Hill can be simply summarized. The plaintiffs contend that the Council Defendants breached their fiduciary duties by failing to procure insurance of an amount adequate to ensure that if Buildings J and K were destroyed, the insurance proceeds would be sufficient to permit them to be rebuilt promptly without additional expense to the unit holders. The plaintiffs seek to require the Council Defendants to fund the shortfall between the insurance coverage and replacement costs, and to pay the plaintiffs' attorneys fees and costs.

Similarly, the plaintiffs argue that Emory Hill, which served as the manager of Towne Estates under specific contractual terms, breached contractual obligations it owed to its client by failing to provide information needed by Towne Estates' insurance broker, The Addis Group, in order to determine what amount of insurance should be obtained by the Council. As with the Council Defendants, the plaintiffs seek to have Emory Hill pay the shortfall.

Absent from this case now is one key defendant, BC Consulting, Inc. ("BC Consulting"). That defendant was originally sued by the plaintiffs in this case. When litigation was brought by the Owners Association against BC Consulting in Superior Court, the plaintiffs dropped BC Consulting as a defendant in this

litigation. The Superior Court action is active and shortly before this decision issued there was news that the case may have settled.

III. Factual Background

With that context, I now outline the key facts regarding the governance structure of Towne Estates, using the complaint and its attachments. I address the facts specific to Emory Hill's summary judgment motion when I address that motion.

A. The Governance Structure Of Towne Estates

Towne Estates is a multi-building, multi-unit condominium complex located in New Castle, Delaware that is subject to the Delaware Unit Property Act, 25 *Del. C.* § 2201 *et seq.*, by its adoption of an enabling declaration (the "Enabling Declaration"). In addition to the Enabling Declaration, which is essentially a master deed that classifies the condominium property into "common elements" and "units," Towne Estates is governed by a code of regulations that provides for "the operation, management, and administration" of the condominium (the "Code of Regulations").[11] The Code of Regulations is authorized by the Delaware Unit Property Act.[12]

Each of the owners of condominium units in Towne Estates, including the plaintiff unit owners, is a member of the Owners Association, which is responsible for "administering the Property, establishing the means and methods of collecting

[11] Code of Regulations at 1.
[12] *See* 25 *Del. C.* § 2206 ("The administration of every property shall be governed by a code of regulations . . . .").

the contribution to the Common Expenses, arranging for the management of the Property, and performing all other acts that may be required."[13] Additionally, the Owners Association is governed by a Council which is charged with "manag[ing] the business, operation and affairs of the Property on behalf of the Unit Owners."[14]

In 2004, Towne Estates established the Towne Estates Condominium Owners Association, Inc. as a non-profit corporation. Although the Certificate of Incorporation of Towne Estates Condominium Owners Association, Inc. (the "Certificate of Incorporation") states that the incorporated Owners Association is governed by a board of directors,[15] the "board" described by the Certificate of Incorporation and the "Council" established in the Enabling Declaration are apparently one in the same. Both the "board" and the Council seem to be comprised of the same individuals, and are referred to interchangeably in the Complaint.

I say "apparently" and "seem to be" for a reason. The Complaint focuses, as do the plaintiffs' briefs, on duties owed by the individual defendants in their capacities as Council members.[16] The Enabling Declaration and the Code of Regulations are the documents that set forth the managerial duties that the plaintiffs argue were breached. As we shall see, where convenient, the plaintiffs

[13] Code of Regulations Art. 2 § A.
[14] Enabling Declaration Art. 2 § G.
[15] Compl. Ex. C (Certificate of Incorporation of Towne Estates Condominium Owners Association, Inc. (filed Dec. 17, 2004)).
[16] *E.g.*, Compl. ¶ 3.

seek to downplay the importance of those documents, or to argue that the provisions of the Delaware General Corporation Law somehow trump them. I will address that issue later.

Suffice it to say, however, that it appears that corporate law was not much on the minds of either the unit owners or the Council members as they concerned themselves with life in and the governance of Towne Estates. Rather, they appear to have looked (to the extent that volunteer-led condominium associations do) to the primary documents and the primary source of legal authority relevant to the governance of a condominium association for guidance. In this case, as illustrated by the Complaint itself, those documents were the Enabling Declaration and Code of Regulations, drafted under authority of the Delaware Uniform Property Act.[17]

B. The Duties Of The Council

The responsibilities of the Council to the unit owners and the Towne Estates property are outlined in both the Enabling Declaration and Code of Regulations, as contemplated by the Delaware Unit Property Act.[18] The Enabling Declaration gives the Council broad authority to "have charge of, be responsible for . . . and manage the affairs of the Property, the common elements[19] and other

[17] 25 *Del. C.* § 2201 *et seq.*
[18] *See* 25 *Del. C.* § 2208 (explaining that the duties of the officers shall be provided for in the code of regulations); § 2211(4) (stating that the duties of the council include those duties "set forth in the declaration or code of regulations").
[19] The Enabling Declaration defines "common elements" as "all the parts of the Property other than the Units." Enabling Declaration Art. 2 § C.

assets held by the Council on behalf of the Unit Owners."[20] Under the Code of Regulations, the Council is responsible for, among other things, "[m]aking assessments against Unit Owners to defray the costs and expenses of the Property," "[p]roviding for the operation, care, upkeep, and maintenance of the Common Elements," and "[m]aking, or contracting for the making of repairs to . . . the Property."[21]

Most pertinent to this case, the Council is required by statute to "insure the building against loss or damage by fire" if "required by the declaration, the code of regulations, or by a majority of the unit owners."[22] The Code of Regulations implements this requirement by providing that:

> [A]ll insurance policies relating to the Property shall be purchased by the Council as Trustee for the unit owners and their respective mortgagees, as their interest may appear, which insurance shall to the extent available be at least equal to the following:
>
> (1) Casualty or physical damage insurance in an amount equal to the full replacement value (i.e., 100% of "replacement costs" less any deductible amount not to exceed One Thousand Dollars ($1,000) per loss per occurrence) with an "agreed amount" endorsement and a "Condominium replacement cost" endorsement, without deduction or allowance for depreciation (said amount to be redetermined annually by the Council with the Assistance of the insurance company affording such coverage) . . . .[23]

And, under the Enabling Declaration,

> The Council shall insure the Property against loss or damage by fire and such hazards as are required by the Code of Regulation without prejudice to

[20] *Id*. at Art. 14 § B.
[21] Code of Regulations Art. 3 § B.
[22] 25 *Del. C.* § 2238.
[23] Code of Regulations Art. 6 § A.

> the right of each Unit Owner to insure such Owner's own Unit for such Owner's own benefit. The premiums for insurance placed on the Property through the Council shall be deemed a Common Expense.[24]

C. Exculpatory Provisions Provide Liability Protection To The Council Members

As one might expect would be offered to a unit holder of a condominium association volunteering to serve as a council member, certain protections from personal liability were promised to the Council members of Towne Estates for acts taken while serving on the Council. Specifically, both the Enabling Declaration and Code of Regulations limit the liability for members of the Council against any suits brought by unit owners. Under the Enabling Declaration, "[t]he Council and its members shall have no liability to the Unit Owners for any error of judgment or otherwise, *except for willful misconduct or bad faith*."[25] Similarly, the Code of Regulations provides that members of the Council "shall not be liable to the Unit Owners for any mistake of judgments, negligence, or otherwise *except for their own individual willful misconduct or bad faith*."[26]

D. The Council Hires A Manager And Secures Insurance

The Code of Regulations also permits the Council to enter into "management contracts for the operation, maintenance, and management of the Property."[27] In February 2006, the Council hired Emory Hill, a professional management firm, to act as the manager of Towne Estates, and entered into a

[24] Enabling Declaration Art. 14 § D.
[25] Enabling Declaration Art. 14 § C (emphasis added).
[26] Code of Regulations Art. 3 § R (emphasis added).
[27] Code of Regulations Art. 3 § B(11).

management agreement that outlines the responsibilities of Emory Hill as manager (the "Management Agreement"). Under the terms of the Management Agreement, Emory Hill's job was to "manage, maintain and operate the Premises [of Towne Estates] in an efficient manner and in keeping with the Board's plans, needs and desires as communicated to [Emory Hill]."[28]

But Emory Hill's duties under the Management Agreement *did not* include a role for it to act as the Council's advisor in obtaining insurance. Rather, as to insurance, Emory Hill's role was limited to "furnish[ing] whatever information [was] requested by the [Council] for the purpose of establishing the placement of insurance coverage and . . . aid[ing] and cooperat[ing] in every reasonable way with respect to such insurance and any loss thereunder."[29]

With these important provisions in mind, I now address the plaintiffs' allegations regarding what the Council and Emory Hill supposedly did wrong with respect to the procurement of insurance.

E. The Old Council Secures Insurance For Towne Estates

In May 2006, the Old Council, which included current defendants Mary Ann O'Brien, David Fajardo, Kristen Kingery, and James McGilvra, as well as Bob Holt, who has been dropped as a defendant, secured insurance for Towne Estates through the Owners Association's insurance broker, The Addis Group.

[28] Compl. Ex. E (Management Agreement between Towne Estates Condominium Association and Emory Hill Real Estate Services, Inc. (February 29, 2006)) ("Management Agreement") Art. 2 § A.
[29] *Id*. at Art. 3 § A.

According to the Complaint, The Addis Group could not properly advise the Old Council on the proper amount of coverage for each building of the Towne Estates complex because Emory Hill failed to provide The Addis Group with the Code of Regulations or the replacement values for the Towne Estates condominiums.[30] But nowhere does the Complaint allege that the Council (or anyone else) requested that Emory Hill furnish that information, or any other information, to The Addis Group to assist the Council in obtaining insurance. Indeed, there is no record evidence that Emory Hill was ever asked for information or advice about the level of coverage. As noted, by contract, Emory Hill's role in insurance was simply to provide "whatever information [was] requested by the Board for the purpose of establishing the placement of insurance coverage."[31] But the Complaint does not allege that it failed to meet this duty, because the Complaint does not allege that Emory Hill was ever asked.

The plaintiffs also attempt to imply that the Council was remiss in securing insurance coverage because it allowed Fajardo to work with the Council's insurance broker and bind them to a policy without first holding a Council meeting to review the policy.[32] But it, of course, is not unusual for a board to divide up primary responsibilities for certain tasks among its members, and even if this could be regarded as negligent in some way, it in no way suffices to create an inference of willful misconduct or bad faith. Critically, the Complaint does not

[30] Compl. ¶ 9.
[31] Management Agreement Art. 3 § A.
[32] Compl. ¶ 10.

plead any facts suggesting that any member of the Old Council had any economic or personal motive to procure less insurance than was necessary to enable the replacement of any building that might be destroyed or damaged. Nor does the Complaint plead facts suggesting in any way that Fajardo had gone to a disreputable insurer or insurance broker, or frankly, that the insurer had any rational incentive to write less than the full replacement value of coverage. At best, therefore, the Complaint suggests that a mistake was made, and in reliance upon a reputable insurance broker.

F. The Insurance Shortfall And The Council's Attempt To Collect An Assessment

As noted, the insurance shortfall was first recognized after the February 2007 fire occurred. The plaintiffs allege that the Council is responsible for the shortfall, because the Enabling Declaration and Code of Regulations required the Council to insure Towne Estates to its "full replacement value" against fire damage. Because casualty insurance up to the full replacement value was not obtained, the Council issued an assessment for the shortage in the summer of 2008, in accordance with the express terms of the Enabling Declaration, which states that:

> In the event of damage to or destruction of any portion of the Property as a result of fire . . . [i]f the proceeds of insurance are not sufficient to defray the estimated costs of reconstruction and repair as determined by the Council . . . assessments shall be made against the Unit Owners directly affected by the damage or destruction, in proportion to their respective proportionate interests in sufficient amounts to provide payment of such costs.[33]

[33] Enabling Declaration Art. 21 §§ A(1), (3).

The Enabling Declaration goes on to explain that "in the event of the substantially total destruction of the Building(s) or any one or more of the Units, all of the Unit Owners of Towne Estates Condominium Apartments are directly affected thereby."[34]

All of the unit owners of Towne Estates were assessed for a portion of the damage to the common areas of Buildings J and K, while the owner of each damaged unit in those buildings was assessed for the cost of repairing his or her own unit.[35]

The original plaintiffs in this case fought the assessment by seeking a preliminary injunction in this court to prevent the Council from collecting it.[36] Their primary argument was that it was unfair that the individually affected unit holders should bear not only the brunt of being homeless, but also of the shortfall in replacement costs. The plaintiffs sought to shift the cost to the Council, Emory Hill, and BC Consulting.

Unfortunately, due to the shortfall, the damage from the February 2007 fire has apparently not yet been repaired.[37]

G. The Claims Asserted In The Complaint

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[34] *Id.* at Art. 21 § C(3).
[35] *See* Plaintiffs' Mot. for Prelim. Injunction (Aug. 6, 2008) Ex. A (Loss Assessment Statement).
[36] *See* Plaintiffs' Mot. for Prelim. Injunction (Aug. 6, 2008). The Council agreed not to proceed with the assessments until the other claims in this case are definitively resolved. Council's Op. Br. on their Mot. to Dismiss and Mot. for Judg. on the Pleadings at 5.
[37] Compl. ¶ 30.

The Complaint purports to set forth both direct claims (the "Direct Claims"), and derivative claims brought on behalf of the Owners Association (the "Derivative Claims"). The Direct Claims allege that the Old Council failed to provide fire insurance coverage equal to the "full replacement value" as required by the Enabling Declaration and Code of Regulations (Count I); and that the New Council has failed to proceed with the repair and restoration of the areas affected by fire damage as required by the Enabling Declaration (Count II). One can rationalize these claims as direct because the original plaintiffs were owners of units destroyed in the fire and the shortfall's burden fell primarily on them, given that the Enabling Declaration requires that the affected unit owners, rather than all unit owners, make up the difference.[38] Mind you, this is my rationalization, not one found in the briefs.

Meanwhile, the plaintiffs have styled the remainder of their claims as derivative. These include the claim that Emory Hill is responsible for the failure of Towne Estates to secure fire insurance equal to the "full replacement value" as allegedly required by the Management Agreement (Count I);[39] that Old Council members Mary Ann O'Brien and David Fajardo have breached their duties of loyalty by using corporate funds to pay for their defense of this action (Count III); that both the Old and New Councils failed to designate an insurance trustee as required by the Code of Regulations (Count V); and that the Old Council, aided

[38] Enabling Declaration Art. 21 §§ A(1), (3).
[39] Count I, by its own terms, purports to bring a direct claim against the Old Council and a derivative claim against Emory Hill.

and abetted by Emory Hill, breached its duty of care by negligently securing inadequate insurance coverage (Count VI). [40]

IV. Legal Analysis

A. Standards Of Review

A motion to dismiss a complaint for failure to state a claim is governed by Court of Chancery Rule 12(b)(6). In considering a motion to dismiss, I must accept as true all well-pled allegations, drawing all reasonable inferences in favor of the plaintiff.[41] Dismissal will be granted where a plaintiff fails to "plead enough facts to plausibly suggest that the plaintiff will ultimately be entitled to the relief she seeks."[42]

A party is entitled to summary judgment under Court of Chancery Rule 56 only if the record indicates that "there is no genuine issue of material fact and that the moving party is entitled to a judgment as a matter of law."[43] The moving party bears the burden of demonstrating a lack of genuine issues of material fact.

Court of Chancery Rule 23.1 requires that a plaintiff in a derivative action "allege with particularity" in the complaint either the efforts made by the plaintiff to demand action by the directors of a corporation "or comparable authority", or

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[40] The plaintiffs also request attorneys' fees under the corporate benefit doctrine (Count IV).
[41] *Savor, Inc. v. FMR Corp.*, 812 A.2d 894, 897 (Del. 2002) (quoting *Kofron v. Amoco Chems. Corp.*, 441 A.2d 226, 227 (Del. 1982)).
[42] *Desimone v. Barrows*, 924 A.2d 908, 929 (Del. Ch. 2007).
[43] Ct. Ch. R. 56(c).

the reasons why such a demand would be futile.[44] A motion under Rule 23.1 requires the court to limit its inquiry to the well-pled allegations of the complaint, documents incorporated into the complaint by reference, and judicially noticed facts.[45] "Mere notice pleading is insufficient to meet the plaintiff's burden to show demand excusal in a derivative case."[46]

B. The Claims Against The Council Defendants For Monetary Relief, Whether Denominated Direct Or Derivative, Are Dismissed For Failure To State A Claim

The Council argues that the claims against them seeking monetary relief for the insurance shortfall and any delay in rebuilding must fail because both the Enabling Declaration and Code of Regulations include exculpatory provisions providing that the Council cannot be liable to unit owners except in cases of willful misconduct or bad faith.[47] The plaintiffs request that the Council be held jointly and severally liable for the insurance shortfall to remedy these claims. But, because the Council is exculpated from personal liability under the Enabling Declaration and Code of Regulations, Counts I, II, and VI as brought against the Council Defendants are dismissed.

Specifically, Count I is brought against the Old Council for failure to obtain fire insurance equal to the "full replacement value" as allegedly required by the Enabling Declaration and Code of Regulations, and Count II is brought against the

[44] Ct. Ch. R. 23.1.
[45] *See, e.g.*, *Albert v. Alex. Brown Mgmt. Servs., Inc.*, 2005 WL 1594085, at *12 (Del. Ch. 2005); *E4e, Inc. v. Sircar*, 2003 WL 22455847, at *2 (Del. Ch. Oct. 9, 2003).
[46] *Desimone*, 924 A.2d at 928.
[47] *See* Code of Regulations Art. 3 § R; Enabling Declaration Art. 14 § C.

New Council for failure to proceed with prompt repair and restoration of the Towne Estates property as allegedly required by the Enabling Declaration.[48] Count VI is brought derivatively, and explicitly alleges that the Old Council breached its duty of care to the Owners Association by "negligently securing the incorrect coverage amounts for the casualty insurance."[49]

Count I must be dismissed because the Complaint is entirely devoid of facts suggesting that the Old Council acted willfully or in bad faith in obtaining an inadequate amount of insurance. Indeed, if anything, the Complaint suggests that the Council acted in good faith by attempting to procure adequate insurance,[50] and by hiring The Addis Group as an advisor on the adequate amount of insurance coverage needed.[51] Likewise, Count VI is a negligence claim explicitly barred by the exculpatory provisions.

Count II is equally deficient because the Complaint pleads no facts that suggest a rational inference that the Council failed to try to address the difficult situation created by the fire other than in good faith, or that any delay in rebuilding was attributable to wrongful acts of the Council, rather than to a lack of funds. It was the plaintiffs themselves who opposed the efforts of the Council to begin reconstruction using assessed funds, while the Council undertook collecting funds from the Council's insurance broker, The Addis Group, and its former manager,

[48] Compl. ¶¶ 25-27, 29-31.
[49] *Id*. ¶ 44.
[50] *Id*. ¶¶ 9, 13, 15.
[51] Compl. ¶ 9.

BC Consulting, to reduce the financial hardship on the affected unit owners. As the plaintiffs admit, the Council has sued both the The Addis Group and BC Consulting to recover the shortfall. Given the pleadings, the plaintiffs fail to state a non-exculpated claim for damages against the Council Defendants on this point, and have also not pled any basis for the issuance of declaratory or injunctive relief.

But the plaintiffs make two legal arguments as to why the exculpatory provisions do not bar their claims. First, the plaintiffs argue that the Unit Property Act does not permit either an enabling declaration or a code of regulations to diminish the personal liability of a council. Second, the plaintiffs argue that the Certificate of Incorporation of the Owners Association does not contain a Section 102(b)(7) exculpatory provision and, therefore, the liability limitations in the Code of Regulations and Enabling Declaration are ineffective and contrary to the Delaware General Corporation Law. I address and reject these two arguments now.

1. A Cause Of Action Under The Unit Property Act Does Not Negate The Exculpatory Provisions In The Code Of Regulations And Enabling Declaration

The plaintiffs make much of the fact that they purport to bring Counts I and II, which allege that the Council should be held liable for failing to procure sufficient insurance and to promptly proceed with repairs, under § 2210 of the Delaware Unit Property Act. Section 2210 provides a cause of action by "an aggrieved unit owner" against a condominium's council for "[f]ailure to comply with the code of regulations," enabling declaration, or other administrative

provisions of the condominium.[52] The plaintiffs argue that, because they are bringing statutory causes of action under the Delaware Unit Property Act, the liability limitations in the Enabling Declaration and Code of Regulations are inoperative.[53]

But, the mere fact that § 2210 of the Unit Property Act contemplates certain suits against councils and council members by unit owners does not invalidate the Towne Estates exculpatory provisions. In *Greloch v. Council of Parkridge at Bellevue Condominiums*, then-Vice Chancellor, now Justice, Berger held that a similar exculpatory provision in a condominium's code of regulations, which

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[52] The direct claims alleged in Counts I and II are brought pursuant to 25 *Del. C.* § 2210, which provides:

> Failure to comply *with the code of regulations* and with such rules governing the details of use and operation of the property and the use of the common elements as may be in effect from time to time and with the covenants, conditions and restrictions *set forth in the declaration* or in deeds of units or in the declaration plan shall be grounds for an action for the recovery of damages or for injunctive relief of both maintainable by any member of the council on behalf of the council or the unit owners or in a proper case by an aggrieved unit owner or by any person who holds a mortgage lien upon a unit and is aggrieved by any such noncompliance.

25 *Del. C.* § 2210 (emphasis added).

[53] In responding to the Council Defendants' motion, the plaintiffs have also argued that Counts I and II are brought under § 2238 of the Unit Property Act in addition to § 2210. Section 2238 provides that:

> The council shall, *if required by the declaration, the code of regulations, or by a majority of the unit owners*, insure the building against loss or damage by fire and such hazards as shall be required or requested without prejudice to the right of each unit owner to insure each such unit owner's own unit for each such unit owner's own benefit.

25 *Del. C.* § 2238 (emphasis added).

But the plaintiffs do not even cite to § 2238 in the Complaint. That, however, is of little moment, as the plaintiffs did raise a claim against the Council under Section A of Article 6 of the Code of Regulations, which generally required the Council to obtain insurance for all units covering the full replacement value, and did cite to § 2210 of the Unit Property Act, which provides for certain causes of action for breaches of codes of regulations.

limited the liability of council members to acts of willful misconduct or bad faith, protected the council members from liability, despite the fact that the unit owners brought their claims pursuant § 2210.[54] In that case, a council approved the installation of aluminum siding and a security fence without first seeking the approval of the unit owners, as required by the condominium's code of regulations. The court stated that:

> [Section 2210] merely provides that, "[f]ailure to comply with [a condominium's] code of regulations . . . shall be grounds for an action for the recovery of damages or for injunctive relief or both . . . ." *It does not suggest that a limitation on liability, such as the one found in [the condominium's] code of regulations, is ineffective*.[55]

Because the council members had not acted willfully or with bad faith, Vice Chancellor Berger granted summary judgment for the council members on the unit owners' claims.[56]

Greloch was decided over 15 years ago and has existed as good precedent without contradiction for that entire time. The exculpatory provision at issue in *Greloch*, like the exculpatory provisions here, is not novel in condominium law. Such provisions appear to be standard.[57] Exculpatory provisions act, quite obviously, as an inducement to community members to take on difficult volunteer

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[54] 1994 WL 384614, at *3.
[55] *Id*. (quoting 25 *Del. C.* § 2210 (emphasis added)).
[56] *Id*.
[57] PATRICK J. ROHAN & MELVIN A. RESKIN, CONDOMINIUM LAW & PRACTICE (2009) at § 48.05[2] (noting that "[m]ost condominium documents provide that individual board members will be indemnified and held harmless by the association unless they have acted willfully or in wanton disregard of their duties").

roles by assuring them that, so long as they do not act in willful misconduct or bad faith, they will not risk their net worth by serving. *Greloch* found no conflict between § 2210 of the Unit Property Act and exculpatory provisions like the ones in the Towne Estates Code of Regulations and Enabling Declaration, and I see no basis to upset that well-reasoned conclusion.

In so finding, I perceive no conflict between giving effect to exculpatory provisions in a code of regulations or declaration and a statute authorizing actions against council members in certain situations when they do not follow the code of regulations. Section 2210 of the Unit Property Act refers back to the condominium's governing documents, and allows unit owners to sue the council for violations of a condominium's "code of regulations . . . [and] the covenants, conditions and restrictions set forth in the declaration."[58] In other words, § 2210 requires the council of an owners association to take action only to the extent that action is required under the condominium's governing documents. If, as here, a code of regulations creates a duty on the part of the council to procure insurance coverage, but the same document also limits the liability of the council, the document must be read as a whole in determining liability under the Unit Property Act. Thus, in reading the Code of Regulations and Enabling Declaration as a whole, the liability limitations in the Code of Regulations and Enabling Declaration are in force and apply to the plaintiffs' claims in Counts I and II about alleged violations of those same documents.

[58] 25 *Del. C.* § 2210.

2. The Exculpatory Provisions Are Binding Despite The Lack Of A Section 102(b)(7) Provision In The Certificate Of Incorporation Of The Owners Association

The plaintiffs' other argument, that the exculpatory provisions in the Code of Regulations and Enabling Declaration cannot be upheld because the Certificate of Incorporation of the Owners Association does not contain a § 102(b)(7) provision, also fails. Under 8 *Del. C.* § 102(b)(7), a provision limiting the personal liability of a corporation's directors may be contained only in the certificate of incorporation.[59] But, § 102(b)(7) typically applies in the case of a corporation that is not subject to another specific statutory regime, such as the Unit Property Act. In the standard case of a for-profit corporation, the certificate and bylaws of a corporation further detail, along with the mandatory terms of the Delaware General Corporation Law, the key duties of the directors.

But, in the case of individuals like the Council members here who agree to serve on the council of a condominium owners association, the fact that the condominium in question has, likely upon the advice of lawyers working with whoever set up the governing structure of the condominium in the first instance, formed the owners association as a corporation does not, in my view, disable the operation of an exculpatory provision, adopted as part of a code of regulations,

[59] 8 *Del. C.* § 102(b)(7) (permitting a corporation to include in its certificate of incorporation a provision "eliminating or limiting the personal liability of a director to the corporation or its stockholders for monetary damages for breach of fiduciary duty as a director" in certain cases).

under § 2208 of the Unit Property Act.[60] The Unit Property Act is a specific statutory enactment designed to address the governance of multi-unit buildings. *Greloch* found that codes of regulations could contain exculpatory provisions that address the circumstances in which council members could be held liable for violating a code of regulations.[61] Given this unique policy context and the existence of multiple statutory regimes, the one most specifically tailored should be given primacy, especially when it has been given a consistent interpretation by this court for fifteen years.

To rule otherwise would make the already complicated and perilous governance of communities like the Towne Estates Owners Association even more problematic. To expose Council members who served in good faith reliance on exculpatory provisions in the Code of Regulations and Enabling Declaration to monetary liability for negligence would be inequitable and discourage future service. Moreover, to apply the exculpatory provisions here works no inequity to the plaintiffs because all of their claims center on alleged failures of the defendants, as Council members, to fulfill their responsibilities under the Code of Regulations and Enabling Declaration, not any duties related to the Owners Association's corporate form.[62] The affirmative governance duties of the Council

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[60] 25 *Del. C.* § 2208 (discussing the required and permissible contents of a code of regulations).
[61] 1994 WL 384614, at *3.
[62] One suspects that the Town Estates situation is simply one example of the tensions that might exist when the corporate form (or another entity form) is used for an owners association that is also governed by the Unit Property Act.

that are relevant here — such as the duty to procure insurance — are set forth in the Enabling Declaration and Code of Regulations, which include a liability limitation for the Council. Thus, because the exculpatory provisions are in effect, and because no facts are alleged in the Complaint that would support a reasonable inference that the Council Defendants acted willfully or in bad faith, Counts I, II, and the duty of care claim in Count VI are dismissed as brought against the Council members.

C. Emory Hill's Motion For Summary Judgment Is Granted

Emory Hill argues that summary judgment must be granted on the claims against it in Counts I and VI because Emory Hill was not asked to assist the Council in procuring casualty insurance. In Count I, which is brought derivatively against Emory Hill for breach of the Code of Regulations and Management Agreement, the Complaint alleges that Emory Hill failed to "secure fire insurance equal to the 'full replacement value' in 2006."[63] Similarly, Count VI claims that Emory Hill aided and abetted the Old Council's alleged breaches of fiduciary duty by "failing to provide essential information to the Insurance Broker so that the correct coverage amount could be secured by the Old Council."[64] But Emory Hill was not required to procure insurance, or participate in the procuring of insurance for Towne Estates, under the terms of both the Code of Regulations and the Management Agreement unless the Council requested its help.

[63] Compl. ¶ 25.
[64] *Id*. ¶ 44.

Although the Management Agreement broadly delegated duties to Emory Hill in areas including the "manage[ment], maint[enance] and operat[ion] of" the premises, employees, and budget of Towne Estates, no such delegation was made in the area of procuring insurance.[65] The Council chose to keep for itself the responsibility of "obtain[ing] and keep[ing] in force insurance against physical damage . . . and against liability for loss, damage or injury to property or persons."[66] Emory Hill's only insurance-related duty was to "furnish whatever information [was] requested by the Board for the purpose of establishing the placement of insurance coverage and [to] aid and cooperate in every reasonable way with respect to such insurance and any loss thereunder."[67]

Nowhere in the Complaint do the plaintiffs allege that the Council asked Emory Hill to provide it with any information pertaining to insurance coverage, or that the Council asked Emory Hill to cooperate with the Council's efforts to secure insurance. Instead, the Complaint simply states that Emory Hill "failed to provide the Code of Regulations or replacement values of [Towne Estates] to the Insurance Broker so that it could have properly advised the Old Council as to the correct amount of coverage for each of the buildings in [Towne Estates]."[68] Likewise, in confronting Emory Hill's motion for summary judgment, the plaintiffs fail to address the record evidence that Emory Hill has provided that indicates that during

[65] Management Agreement Art. 2 (setting forth the responsibilities of the Manager).
[66] *Id*. at Art. 3 § A.
[67] *Id*.
[68] Compl. ¶ 9.

the insurance procurement process, the Vice President of The Addis Group sent an email to Fajardo about the summaries of Towne Estates' insurance policies, but made a critical typographical error and sent a copy intended for Emory Hill to an erroneous e-mail address.[69] The plaintiffs do not provide any contrary evidence suggesting that Emory Hill actually received a request for information in the insurance procurement process and failed to adequately respond to it.

Instead, the plaintiffs respond by trying to expand the scope of Emory Hill's agency, by arguing that as a retained agent Emory Hill somehow had the wide-ranging duty to provide advice about the adequacy of insurance coverage despite the fact that its contractual duties on the subject were extremely narrow. In other words, the plaintiffs seek to charge Emory Hill with a range of duties that Towne Estates did not pay Emory Hill to undertake. Absent a duty in the first instance to act as the insurance advisor for the Council, Emory Hill cannot be faulted for not providing such advice. For this court to expand Emory Hill's role after the fact for the purpose of subjecting it to liability would not only be legally and equitably improper, it would set a precedent that would raise the price for condominium associations seeking to retain property managers. If property managers cannot rely upon the agreed upon scope of duties when pricing their services, they will have to raise their prices to take into account the possible costs of being held liable for breaching duties they had never contractually assumed in

[69] Appendix to Ans. Br. of Def. Emory Hill in Opp. to Pl.'s Mot. to Compel (March 25, 2009) at 23.

the first instance. A traditional adherence to the contractual scope of duties avoids that unproductive incentive.

Therefore, because no genuine issue of material fact remains on whether Emory Hill was required to furnish information to Towne Estates' insurance broker, summary judgment in favor of Emory Hill is granted.[70]

D. The Remaining Derivative Counts Must Also Be Dismissed

The plaintiffs have styled several of their remaining claims as derivative. The claims not previously dismissed include:[71] a claim that two members of the Old Council — O'Brien and Fajardo — breached "their fiduciary duty of loyalty to the [Owners Association]" by using corporate funds to pay for their defense in

[70] In its brief arguing this motion, Emory Hill asks that it be awarded costs and legal fees pursuant to Court of Chancery Rule 11, and 10 *Del. C.* § 5106. Attorneys' fees are generally awarded to the prevailing party "only when the party against whom the fees are assessed acted in bad faith, fraudulently, negligently, frivolously, vexatiously, wantonly or oppressively." *Judge v. City of Rehoboth Beach*, 1995 WL 198700, *2 (Del. Ch. Apr. 29, 1994). In other words, the conduct of the party against whom fees are sought must demonstrate "glaring egregiousness." *Kaung v. Cole Nat'l Corp.*, 2004 WL 1921249, at *6 (Del. Ch. Aug. 27, 2004) (awarding attorneys' fees to the defendant, where the plaintiff had filed a complaint in bad faith, had made purposely burdensome discovery requests, and sought to drag the case out for improper reasons). But, although the plaintiffs have unnecessarily dragged out this litigation, and have brought meritless claims against Emory Hill, I do not believe that they have acted with the "glaring egregiousness" that would require them to pay Emory Hill's fees. *See, e.g.*, *Nagy v. Bistricer*, 770 A.2d 43, 64 (Del. Ch. 2000) (explaining that the Court of Chancery will not lightly award attorneys' fees under the bad faith exception to the American Rule that each party bears his own costs); WOLFE & PITTENGER § 13.03[b] ("Attorney's fees will not be awarded in the absence of intentional misconduct, nor will they be awarded if a party has merely acted pursuant to an innocent perception of its legal rights.") (citations omitted). I do, however, award Emory Hill its costs as a prevailing party.

[71] The plaintiffs' claim that the Old Council, aided and abetted by Emory Hill, breached its duty of care by failing to secure adequate insurance coverage is also a derivative claim (Count VI). I have already dismissed this claim under Rule 12(b)(6) against the Council Defendants, and against Emory Hill under Rules 12(b)(6) and 56.

this action (Count III);[72] and a claim that the Council Defendants have failed to comply with the Code of Regulation's requirement that an insurance trustee be designated to hold insurance funds and any funds collected as a result of the Council's assessment (Count V).[73] As to these claims, it is plausible to conceptualize most of them as, at least in large measure, ones belonging to the Owners Association as an entity, because all of the unit owners arguably suffered injury as an Association if, for example, Association funds were improperly spent on attorneys' fees for the defendants or if insurance proceeds were misappropriated due to the lack of a trustee.[74]

What the parties disagree about, however, is not whether the claims may be styled as derivative; they share that premise. What they disagree about is whether a demand excusal standard of some kind applies. For their part, the Council

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[72] Compl. ¶ 33-34.

[73] *Id*. ¶ 42. Under the Code of Regulations, the Council is required to deposit "[t]he net proceeds of insurance collected on account of a casualty and the funds collected by the Council from assessments against the unit owners on account of such a casualty" which total over $50,000 with a designated "Insurance Trustee." Code of Regulations Art. 6 § G(1). An "Insurance Trustee" may properly include "any bank, trust company, savings and loan association, building loan association, insurance company, or any institutional lender . . . ." *Id*. at Art. 6 § (D)(1).

[74] *See, e.g.*, *In re TD Banknorth*, 938 A.2d 654, 665 (Del. Ch. 2007) ("The determination of whether a claim is direct or derivative in nature turns on two questions: '(1) who suffered the alleged harm (the corporation or the suing stockholders, individually); and (2) who would receive the benefit of any recovery or other remedy (the corporation or the stockholders, individually)?'" (quoting *Tooley v. Donaldson, Lufkin & Jenrette, Inc.*, 845 A.2d 1031, 1033 (Del. 2004))); *see also Caprer v. Nussbaum*, 825 N.Y.S.2d 55, 67 (N.Y. App. Div. 2006) ("The same factors that caused the courts to fashion the derivative action procedure for shareholders and limited partners . . . apply to condominium unit owners. All are owners of fractional interests in a common entity run by managers who owe them a fiduciary duty that requires protection. Condominium unit owners are therefore entitled to the same consideration by the courts as the litigants in those situations in which courts have historically allowed derivative actions to proceed, independent of any statutory authority.").

Defendants argue that those claims should be dismissed for failure to make a demand on the Council or plead demand futility. The plaintiffs, while styling their claims as derivative ones, argue that condominium unit holders may assert derivative claims without any showing of demand futility.

Both sides make these arguments without citing any substantial authority. Both advert in inconsistent ways to the reality that the Towne Estates Owners Association is a corporation, even though, as indicated previously, the claims in this case really center on the defendants' actions as Council members under the Code of Regulations. And, the most pertinent statute, the Unit Property Act, simply states that a suit alleging noncompliance with a condominium's code of regulations or administrative provisions may be brought "*in a proper case* by an aggrieved unit owner," rather than by a member of the council.[75]

Having little help from the parties, I simply reach the tentative conclusion that, to the extent that the General Assembly was going to allow unit holders to assert claims belonging to an owners association, it intended, by the words "proper case,"[76] to impose a demand excusal requirement as is typical not only when stockholders attempt to bring derivative claims,[77] but also when limited partners,[78] equity holders in limited liability companies,[79] and beneficial owners of statutory

[75] 25 *Del. C.* § 2210 (emphasis added).
[76] *Id.*
[77] Del. Ch. R. 23.1.
[78] 6 *Del. C.* § 17-1003.
[79] 6 *Del. C.* § 18-1003.

trusts[80] do so. Before individual unit holders usurp the authority of a council to control claims belonging to an owners association, they should make a showing as to why the council cannot be trusted to do so.[81] That is, the Council is the "authority" that is "comparable" to a corporate board for purposes of our Rule 23.1.

Lacking input from the parties on the standards to apply, I apply the basic principles of the familiar *Aronson* test. Under *Aronson*, in cases challenging director's actions in the underlying transaction, demand is excused if the complaint creates a reasonable doubt that (1) the directors are disinterested and independence; or (2) the transaction was otherwise the product of a valid business judgment.[82] Translated into this context, *Aronson* essentially requires a unit owner to plead that a majority of its council has a material conflict of interest, or that the plaintiff has pled a particularized claim for a non-exculpated breach of a duty that renders the council so susceptible to personal liability that they cannot impartially consider a demand.[83] Here, the plaintiffs have not pled particularized facts that excuse demand.

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[80] 12 *Del. C.* § 3816(a).
[81] *See Longanecker v. Diamondhead Country Club*, 760 So.2d 764, 768-69 (Miss. 2000) (upholding the trial court's dismissal of a suit brought by a property owners association, organized as a non-profit corporation, derivatively against the association's board for failure to make a demand or plead demand futility).
[82] *Aronson v. Lewis*, 473 A.2d 805, 818 (Del. 1984); *see also* WOLFE & PITTENGER § 9.02[b][3][i] (2009).
[83] *E.g.*, *Guttman v. Huang*, 823 A.2d 492, 501 (Del. Ch. 2003) (explaining the policy for *Aronson* and related cases).

1. Failure To Designate An Insurance Trustee

First, no facts are pled to suggest that demand was futile on the claim for failure to designate an insurance trustee. The plaintiffs claim that the Council Defendants have not designated an insurance trustee, as required by the Code of Regulations, to hold the insurance funds and any funds collected from the assessment in order to create a reconstruction fund.[84]

That claim is brought against both the Old and New Council but, because it was first raised in the Complaint at a time when the New Council was already in place, I need only consider the qualification of the New Council to assess a demand.[85] There is no reason to believe that the New Council cannot objectively consider a demand.

The Complaint suggests that the failure to designate an insurance trustee first occurred when the Old Council was in place. At best, the Complaint implies that the original decision to place the insurance funds with someone other than a formal insurance trustee was maintained by inertia. The Complaint does not even hint at the notion that the failure to designate an insurance trustee has, in reality, led to any financial harm to the Owners Association or any misuse of the insurance proceeds. It may well be that the Old Council, most likely upon the

[84] Compl. ¶ 42.

[85] *See, e.g.*, *Harris v. Carter*, 582 A.2d 222, 229-30 (Del. Ch. 1990) ("The *Aronson* test . . . does focus upon the board at the time of the transaction challenged and not exclusively on the independence, etc. of the board upon whom demand might be made."); WOLFE & PITTENGER § 9.02[b][3] (stating that "the qualification of the board to consider a demand pursuant to the *Aronson* tests is to be determined as of the time of the filing of the original complaint").

advice of lawyers or other professionals, placed the insurance funds in the hands of a trusted recipient in the honest belief that would be the best way to administer the reconstruction fund, and did not consider the specific requirement in the Code of Regulations that the Council designate a "bank, trust company, savings and loan association, building loan association, insurance company, or other institutional lender" to act as an insurance trustee.[86]

Given the absence of particularized facts regarding the failure to designate an insurance trustee — a failure, one senses, far more likely to result from advisorial oversight than a deliberate Council decision to violate the Code of Regulations — and, as important, the absence of pled facts suggesting any improper motivation on the part of the Council to fail to designate a trustee, the plaintiffs have not pled demand excusal.

The New Council seems well positioned to consider a demand for the appointment of an insurance trustee and an accounting from whoever was entrusted with the funds for the use of those funds.[87] If the New Council refuses, upon proper demand, to ensure compliance with the Code of Regulations once its

[86] Code of Regulations Art. 6 § D(1).
[87] *Kaufman v. Belmont*, 479 A.2d 282, 288 (Del. Ch. 1984) (stating that "the mere approval of a corporate action, absent any allegation of particularized facts supporting a breach of fiduciary duty or other indications of bias, will not disqualify [a] director from subsequently considering a pre-suit demand to rectify the challenged transactions").

clear terms have been brought to the Council's attention, the plaintiffs may bring a suit for wrongful refusal.[88] Count V is dismissed.

2. The Improper Advancement Claim

The closest issue, I suppose, is whether the plaintiffs have pled demand excusal in alleging that Fajardo and O'Brien, two members of the Old Council, have caused the Owners Association to cover the defense costs they incurred in responding to this lawsuit.[89] This claim was raised in the first complaint filed in this case and the plaintiffs have continued to pursue it. Thus, by analogy to corporate practice, demand will be measured against the Old Council.[90]

In support of this claim, the plaintiffs point out that although the Code of Regulations has a broad indemnification provision that indemnifies a Council member "against any expense (including attorneys' fees), judgments, fines and amounts paid in settlement incurred by [the Council member] in good faith and in a manner he reasonably believed to be in or not opposed to the best interest of the

[88] *See Scattered Corp. v. Chicago Stock Exchange, Inc.*, 1996 WL 417507 (Del. Ch. July 12, 1996) (explaining that, where a demand is wrongfully refused, a case may go forward where a plaintiff "allege[s] with particularity facts that create a reasonable doubt that the corporation's board of directors wrongfully refused the demand").
[89] Compl. ¶ 33-34.
[90] Because I believe that the plaintiffs do not plead demand excusal against even the Old Council, I do not address whether rote application of this corporate rule makes sense in the condominium association context. At first thought, I would be inclined to think that it does not. Rather, it would seem to make sense to require that a plaintiff who has not left the pleading gate be required to show demand excusal based on the council in place at the time of the complaint he seeks to stand or fall upon is tested. If a plaintiff in a case like this meanders and a new council is composed that can address the pled claims impartially, it is not clear to me why that community council's judgment should easily be bypassed. But I do not resolve that unbriefed legal policy question.

plaintiffs,"[91] the Code of Regulations lacks any provision providing for advancement. Thus, the plaintiffs say, the decision of the Old Council, of which Fajardo and O'Brien were members, to advance the Council Defendants their defense costs must be seen as conflicted self-dealing and because of that, the Old Council could not be an impartial arbiter of whether this claim should have been brought by the Council.

There is some facial logic to this assertion. But in this unique context, I do not believe that the mere pleading that a condominium association council permitted its members to be advanced their legal costs is, alone, sufficient to plead demand excusal. In this regard, I note several factors. First, there is no dispute that if the Council Defendants prevail, they will be entitled to indemnification. Second, under corporate law principles, the absence of a mandatory advancement provision does not preclude a board from making a discretionary business judgment decision about advancement, so long as an undertaking is in place.[92]

Third, a decision to advance fees, subject to a promise to repay the funds if indemnification is ultimately improper, does not strike me as inherently suspect as the prototypical unfair asset sale or merger that is the traditional grist for the entire fairness standard mill. Notably, the plaintiffs do not even challenge in the

[91] Code of Regulations Art. 3 § R.

[92] *Carlson v. Hallinan*, 925 A.2d 506, 541 (Del. Ch. 2006) ("Delaware corporation may advance litigation expenses to directors 'upon receipt of an undertaking by or on behalf of such director or officer to repay such amount if it shall ultimately be determined that such is not entitled to be indemnified by the corporation . . . .'" (quoting 8 *Del. C.* § 145(e)); WOLFE & PITTENGER § 8.02[b] ("In the absence of . . . a contractual provision (*e.g.*, a bylaw) providing for mandatory advancement, the decision to accept an undertaking and to advance expenses is left to the business judgment of the board . . . .").

Complaint the advancement of fees to the defendants who are members of the New Council and have been forced to defend this action. Indeed, the plaintiffs do not challenge the advancement of fees to defendants Kingery and McGilvra, who were also members of the Old Council. Thus, the plaintiffs seem to admit that the advancement of funds to Council members is not in itself wrongful, and that it was only in some unexplained way wrong to advance funds to the particular members of the Old Council, defendants Fajardo and O'Brien, who the plaintiffs single out as most responsible for the insurance shortfall.[93] But the plaintiffs do not plead any facts suggesting that the advancement decision was made in bad faith or somehow constituted willful misconduct.

Fourth, the plaintiffs do not plead facts indicating that the individual defendants have not bound themselves, by an undertaking, to repay advanced fees if indemnification is ultimately found to be inappropriate.[94] Fifth, the plaintiffs confused things themselves by naming the "Towne Estates Condominium Association Council" as a non-nominal defendant in their initial complaint, thus causing not only the individual defendants but the "Council" as a body to have to

[93] In this regard, in their original and first amended complaints, the plaintiffs sued only three members of the five-member Old Council, even though the Code of Regulations makes the Council responsible for insurance procurement. In those complaints, the plaintiffs complained that defendants Fajardo, O'Brien, and Holt — a majority of the Old Council — were improperly being advanced fees. Then, in their most recent Complaint, the plaintiffs dropped defendant Holt but added Old Council members Kingery and McGilvra. But they only complain that defendants Fajardo and O'Brien have breached their duty of loyalty by having the Association bear their defense costs, and do not complain about the costs of defense of Kingery and McGilvra.

[94] *See Breedy-Fryson v. Fajardo et al.*, C.A. No. 3577-VCS, at 28 (Del. Ch. Nov. 30, 2009) (TRANSCRIPT) (noting that the plaintiffs were not aware of an undertaking, and alleged nothing about an undertaking in their Complaint).

defend the suit. In this regard, the defense of individual Council members and the defense of the broader Council were one in the same. Indeed, the individual Council Defendants and the Towne Estate defendants (*i.e.*, the Owners Association) appear to have tried to conserve defense costs by using the same counsel, and it is likely that counsel provided the Council members with the advice that they could advance fees for their own defense costs.

Finally, I am reluctant to embrace the notion that a condominium association board cannot authorize the advancement of defense costs that its volunteer members may not individually be able to bear except upon the consequence of enabling a trial within a trial about the fairness of doing so. Absent pled facts that suggest that the advancement decision was tainted by something other than a good faith belief that the defense costs would be subject to indemnification, and were not advanced subject to a promise to repay if indemnification was not ultimately proper, I believe that the mere fact that Council members advanced themselves fees does not, in itself, excuse a demand. My finding in this regard is influenced not only by the specific context of a volunteer condominium owners council protected by strong exculpatory provisions, but also by the dearth of authority cited by the parties on this point. Put simply, in a derivate case, it is the burden of the plaintiffs to plead particularized facts

supporting demand excusal.[95] All I hold is that the plaintiffs have failed to meet that burden here.

As with the prior claim, if the plaintiffs make a demand on the Council and the Council refuses to address it, the plaintiffs may attempt to prove wrongful refusal.[96] But, at this stage, no facts are pled that would be sufficient to excuse demand, and Count III is dismissed.[97]

V. Conclusion

For the foregoing reasons: 1) Emory Hill's motions for dismissal and summary judgment are granted, and Counts I and VI are dismissed as brought against Emory Hill; 2) costs are awarded to Emory Hill; 3) the Council Defendants' motion to dismiss for failure to state a claim is granted as to Counts I, II, and VI; and 4) the Council Defendants' motion to dismiss under Rule 23.1 is

[95] Ct. Ch. R. 23.1.

[96] For example, if it turns out that the Council did not procure an undertaking, is unable to procure a curative undertaking from any Council Defendant, and then refuses to sue that Council Defendant, a wrongful refusal claim might be successful.

[97] Count VI, which brings a breach of the duty of care claim against the Old Council, and an aiding and abetting claim against Emory Hill, for failure to secure adequate insurance coverage, has already been dismissed for failure to state a claim. *See supra* pages 20-22, 28-30. Count VI is also dismissed under Rule 23.1 because demand is not excused. This claim was not added until the Second Amended Class Action Complaint, therefore, demand excusal is measured by the New Council's ability to fairly contemplate a demand. *See supra* note 85. Count VI alleges that the Old Council negligently secured insufficient insurance coverage, and there are no facts alleged that would suggest that the New Council is unable to impartially consider whether to press those claims.

granted as to Counts III and V, and Count VI is also dismissed on this alternative basis.[98] IT IS SO ORDERED.

[98] Count IV of the Complaint simply involves a request for attorneys' fees from the Council under the corporate benefit doctrine. Compl. ¶ 36. The corporate benefit doctrine is an exception to the generally followed principle that litigants are responsible for their own attorneys' fees, regardless of the outcome of a case, and provides that litigants who confer a benefit upon an ascertainable class may receive an award of attorneys' fees and expenses from the class for the litigants' efforts in creating the benefit to the class. *See, e.g.*, *Alaska Elec. Pension Fund v. Brown*, 941 A.2d 1011, 1014 (Del. 2007).

The briefs of the Council Defendants and the plaintiffs do not address this Count. This Count, if it has any vibrancy, involves the notion that this case inspired the Council to sue BC Consulting and The Addis Group in Superior Court. As indicated previously, the plaintiffs dropped BC Consulting as a defendant when they filed their Second Amended Class Action Complaint. If the plaintiffs wish to argue for fees based on their causal role in inspiring the Council to bring the Superior Court litigation, they must present a motion for attorneys' fees promptly. Before bringing such a motion, they should consult with the Council and satisfy themselves that they have a *good faith basis* to argue that this case played a causal role that was beneficial. If the Council was already attempting to recover from The Addis Group and BC Consulting, the mere fact that the plaintiffs filed a case against BC Consulting first is unlikely to satisfy the plaintiffs' burden to demonstrate that they produced a corporate benefit.