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Re: *Peter Tafeen v. Homestore, Inc.*
Civil Action No. 023-N

Dear Counsel:

This is the Court's post-trial decision in this advancement case under 8 *Del. C.* § 145. After the Court's March 22, 2004 summary judgment Opinion,¹ only one issue remained for trial: whether unclean hands barred Peter Tafeen's claim to advancement? That is, did Peter Tafeen shelter assets in an effort to circumvent his obligation to repay to Homestore any fees and expenses for which Tafeen was not ultimately entitled to indemnification under Homestore's bylaws?

Having considered the evidence presented during a two-day trial, involving testimony by Tafeen, Ash Narayan (Tafeen's financial advisor) and Terry

¹ *Tafeen v. Homestore, Inc.*, C.A. No. 023-N, Chandler, C. (Mar. 22, 2004, Del. Ch.).

Kontonickas (Homestore's Vice President of Litigation and Administration), the Court concludes that Homestore has failed to meet its burden of persuasion on its unclean hands defense. Accordingly, and for the reasons stated herein and in the Court's March 22, 2004 Opinion, the Court concludes that Homestore is required to advance Tafeen all reasonable attorney's fees and costs associated with the various legal proceedings in which Tafeen is involved by reason of his service as an officer of Homestore, as well as his fees incurred in prosecuting this action.

Most of the history of this litigation (and the background facts surrounding it) is set forth in the Court's March 22, 2004 Opinion and will not be repeated. Homestore is a Delaware corporation engaged in providing online media and technology to the real estate industry. Peter Tafeen was employed as an officer of Homestore from September 22, 1997 through November 30, 2001, first as Vice President of Business Development and later as Executive Vice President of Business Development Ads and Sales. Homestore's bylaws contain a broad advancement and indemnification provision for officers and directors, as well as for former officers and directors. Although the provisions are conditioned on the officer or director having acted in good faith, the advancement provision in Homestore's bylaws contain no requirement that a former officer or director execute an undertaking to repay advanced sums to which the former officer or director is ultimately found not to be entitled.

In mid-November 2001, Homestore's audit committee first reported to Homestore's board of directors the potential problem that led to an internal investigation. The internal investigation by Homestore's audit committee was authorized by the board of directors on November 15, 2001. Tafeen became aware of the internal investigation sometime in mid November 2001. In late December 2001, Homestore publicly announced that its audit committee was conducting an inquiry into potential improprieties in its accounting practices and financial statements and that certain financial results would be restated. A host of lawsuits followed, with the Securities and Exchange Commission and the Department of Justice conducting investigations into possible criminal conduct by employees and former employees of the Homestore.

In early 2002 Tafeen, through his counsel, requested advancement from Homestore of his legal fees and costs and indemnification for the various proceedings in which he was involved. On April 30, 2002, Homestore advised Tafeen that it would honor its indemnification obligations with respect to the pending proceedings. Regarding advancement of expenses, Homestore informed Tafeen that he was required to execute an undertaking to repay all amounts advanced if it should be determined that he was not entitled to indemnification. Tafeen did not tender the required undertaking. Slightly over a year later, in July 2003, Tafeen made another request through his counsel for advancement. On July

11, 2003, Tafeen again sought advancement and tendered a slightly different form of undertaking than Homestore had provided to him. This lawsuit was filed in late October 2003.

Following the Court's decision on the motion for summary judgment, Homestore pursued its theory that Tafeen's claim for advancement was barred by unclean hands, *viz*, Tafeen's having engaged in efforts to shelter his assets so as to prevent Homestore from collecting on any ultimate obligation to repay. First, Homestore notes that Tafeen, in barely four years of employment with Homestore, pocketed about \$15 million from the timely sale of stock options granted during his employment. Yet in July 2003, Tafeen's counsel advised Homestore that Tafeen was out of funds. Three days later, Tafeen tendered a form of undertaking that was different than the form provided by Homestore and, according to Homestore, Tafeen had no intention of ever repaying any advanced funds should he be found ultimately not entitled to indemnification. As evidence of his unclean hands, Homestore further points to the fact that in February 2000, Mr. Tafeen and his wife, as trustees of the Tafeen Family Trust, purchased a home in Prembrook Pines, Florida. This property was evidently purchased for Mr. Tafeen's in-laws. Homestore next points to the Tafeen's purchase in 2001 of a \$1.45 million home in Parkland, Florida, together with improvements exceeding \$270,000. Given that Tafeen was an executive in one of the largest internet real estate companies, had

lived and purchased property in Florida and was familiar with Florida real estate transactions, Homestore insists that Tafeen was aware of the strong “homestead” exemption provided by Florida law. It was Tafeen’s plan, according to Homestore, to acquire property in Florida so as to shelter it from any future obligation to repay Homestore for the monies advanced to Tafeen.

No credible proof adduced at trial, however, demonstrates by a preponderance of the evidence that Tafeen intended to shelter assets from potential creditors, whether Homestore or others. Tafeen purchased his Florida properties in question long before the internal and external investigations into Homestore’s accounting practices and financial statements. Nor is there persuasive evidence that Tafeen was aware of the homestead exemption under Florida law at the time he purchased either the Prembrook Pines or the Parkland homes. Even if he were aware of the homestead exemption, it seems unlikely that he would try to take advantage of it only to the limited extent of the two homes that he purchased. Were Tafeen’s intention to shelter the \$15 million he earned from the sale of stock options, it would appear more likely that he would have invested far more than he did. The circumstances surrounding his sale of the first Parkland home and his significant mortgage payment advances are explicable on a far more benign basis than Homestore’s theory. The first Parkland home was sold and another less expensive home was purchased in the Fox Ridge area. Buying a less expensive

house is inconsistent with Homestore's thesis that Tafeen was seeking to shelter assets. Tafeen's mortgage pay down was the result of financial advice from Narayan, who urged Tafeen to reduce his exposure to the capital markets and move more of his financial investments into his home for economic reasons. Thus, having considered all the circumstances surrounding Tafeen's purchase of the Florida properties, together with the related family trusts and limited partnerships created at Narayan's direction for tax and estate planning purposes, I am satisfied that Homestore has failed to demonstrate that Tafeen took these actions for the purpose of placing assets beyond the reach of potential creditors, including Homestore's potential claim for reimbursement. Accordingly, Homestore has failed to demonstrate the factual basis for its unclean hands defense.²

Homestore has also pointed to Tafeen's extravagant personal expenditure's and lifestyle, ranging from the use of a private jet, expensive trips to Las Vegas, excessive expenditures for personal vehicles and home entertainment (for example, \$50,000 for a fish tank in his Parkland home) and significant losses from investments (almost \$4 million lost investing in the "Shutdown Production" concert). Although many of these facts are very troubling to the Court, the record

² Nothing in this Opinion precludes Homestore from asserting fraudulent conveyance-type claims against Tafeen in Florida (or elsewhere) if there are facts to support such claims. The type of claims and arguments Homestore makes here, in the guise of an unclean hands defense, are more aptly characterized as a type of fraudulent conveyance designed to thwart a creditor's effort to recover on an outstanding debt.

does not support a finding that Tafeen has been engaged in a deliberate effort to waste assets in a manner intended to thwart potential creditors such as Homestore from seeking repayment of legitimate obligations. First, an inability to repay is not a disqualification for advancement. Second, although Tafeen's extravagant lifestyle makes him less than sympathetic to the Court, Tafeen's conduct does not give rise to an unclean hands defense to Homestore's legal obligation under its own bylaws. Nor is it evident that Tafeen breached an implied covenant of good faith and fair dealing with respect to his contractual right under Homestore's bylaws to advancement and indemnification. It would be odd for the Court to interpret Homestore's bylaws as impliedly obligating Tafeen to maintain and demonstrate financial ability to repay when the express terms of Homestore's bylaws do not require a secured undertaking or any showing of financial ability to repay. Furthermore, Tafeen had no role in drafting Homestore's bylaws and, to that extent, the judicial convention of implying a covenant to a written agreement so as to honor the parties' reasonable expectations would appear inappropriate in this context. Even if it were appropriate to apply the concept of the implied covenant of good faith and fair dealing in the context of advancement or indemnification bylaws, nothing in this case suggests that the parties would have agreed that an officer or director, in order to receive advancement, must refrain from estate and tax planning, from buying a home in a state that has any form of

homestead protection, or from incurring extravagant living expenses. The words in Homestore's bylaws required to achieve that end could have been plainly written. They were not, and it is not this Court's role to rewrite a company's bylaws.

Finally, Homestore has argued throughout this litigation that requiring it to pay in advance the legal fees and expenses incurred by Tafeen in the various legal proceedings will create a financial hardship for Homestore. I have already found this argument unavailing. Evidence introduced at trial, moreover, suggests that this argument comes with ill grace from Homestore, given its own recent actions to indemnify broadly its officers and directors and to provide lucrative compensation packages for its CEO, as well as reimbursement for the CEO's use of a private jet in which he has a financial interest for travel purposes. In addition, Homestore's counsel in this litigation has repeatedly justified Homestore's generous indemnification and advancement bylaws on the ground that such incentives are necessary in order to attract men and women of substance to serve on boards of directors. Although this argument is used in broad-brush fashion to justify capacious advancement and indemnification bylaws, it falls woefully short of explaining the basis for exempting from *any* form of secured undertaking corporate officers who have been compensated at levels that would make it relatively simple to provide secured undertakings for the advancement of fees and costs. People with far less substantial bank accounts than corporate executives are required to

post secured bonds every day in this Court and in our general jurisdiction law courts. For a corporate executive being paid hundreds of thousands of dollars or more a year in salary and benefits, this Court is hard pressed to understand why it would be difficult to attract people to such positions if they were required to post a bond to secure the advancement of fees and costs related to litigation arising from their service in that capacity.

Nevertheless, for all the reasons above stated, the Court concludes that Homestore has failed to demonstrate its affirmative defense of unclean hands or that there has been a breach of the implied covenant of good faith and fair dealing in connection with Tafeen's assertion of his right to advancement under Section 6.2 of Homestore's bylaws. Tafeen is also entitled to payment of his attorney's fees for bringing this lawsuit.

Counsel shall confer and agree upon a form of order implementing this decision.

Very truly yours,

/s/ William B. Chandler III

William B. Chandler III

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