EFiled: Mar 30 2017 04:32PM EDT
Filing ID 60406641
Case Number 67,2017

IN THE

Supreme Court of the State of Delaware

ACCENTCARE, INC., Defendant and Counterclaim Plaintiff Below, Appellant v. FRIEDMAN FLEISCHER & LOWE, LLC, Plaintiff and Counterclaim Defendant Below, Appellee	No. 67, 2017 COURT BELOW: COURT OF CHANCERY OF THE STATE OF DELAWARE C.A. NO. 12026-VCL

APPELLANT'S OPENING BRIEF

Norman M. Monhait (Del. Bar No. 1040)
Jessica Zeldin (Del. Bar No. 3558)
ROSENTHAL, MONHAIT & GODDESS, P.A.
919 N. Market Street, Suite 1401
P.O. Box 1070
Wilmington, Delaware 19899
(302) 656-4433
Attorneys for Defendant and Counterclaim Plaintiff Below, Appellant

OF COUNSEL:

Roger J. Bernstein
535 Fifth Avenue, 35th Floor
New York, New York 10017
(212) 748-4800

March 30, 2017

TABLE OF CONTENTS

Exhibits

TABLE OF AUTHORITIES

Cases — Page(s)

Statutes and Rules

Other Authorities

NATURE AND STAGE OF PROCEEDINGS

This appeal concerns indemnification procedures and obligations in a matter involving seller liability for post-closing third-party claims. The lower court's rulings improperly denied the buyer's indemnification claims by misapplying, or failing to apply, Delaware law concerning equitable recoupment, acquiescence in modification of a contractual statute of limitations, and interpretation of ambiguous contract terms.

The lower court's decision concerns the following transaction. In 2010, AccentCare, Inc. ("AccentCare" or the "Buyer") paid $215 million to acquire Guardian Home Care Holdings, Inc. ("Guardian") from its stockholders (the "Sellers"). Guardian is a firm engaged in providing hospice care to terminally ill Medicare patients. It receives payment for each eligible patient from the Medicare program run by the U.S. Department of Health and Human Services ("HHS").[1]

AccentCare, Guardian, and the Sellers entered into a Stock Purchase Agreement ("SPA"). In the SPA, Guardian represented that it was in compliance with the federal statutes concerning submission to HHS of claims for Medicare payments. The Sellers further agreed that, in the event of a breach of Guardian's

[1] The Sellers were represented in the transaction, and are represented here, by Appellee Friedman Fleischer & Lowe, Inc. ("FFL" or "Seller Representative").

representation that it had not violated HHS requirements for payments for hospice care, they would indemnify AccentCare for any losses or claims or liabilities or contingent liabilities related to or arising out of the breach. The Sellers also agreed to pay AccentCare for defense costs when three types of specific circumstances (discussed *infra)* precluded the Sellers from providing a defense. The SPA provided that certain actions for indemnification had to be filed within the two years following closing. A95. Claims for defense costs, however, were not subject to this two-year contractual limitations period. A92-94.

AccentCare and the Sellers entered into an Escrow Agreement concurrently with the signing of the SPA. In the Escrow Agreement, AccentCare and the Sellers agreed to create a $20.5 million Escrow Account for payment of indemnification claims. At the end of two years after closing, the balance then in the Escrow Account was to be released to the Sellers. A138-39.

The sale of Guardian to AccentCare closed on December 22, 2010. A year and half later the federal government began investigating whether Guardian had violated the federal False Claims Act by submitting certifications that improperly stated that its hospice patients met the Medicare criteria for terminal illness. In addition, a sealed *qui tam* action against Guardian, AccentCare, AccentCare's corporate owner, and others by whistleblowers (who were former Guardian

employees) was served. The allegations in the whistleblower case paralleled those in the federal government investigation.

Under the SPA, the Sellers could not assume Guardian's defense in these proceedings because the government investigation could result in criminal liability or equitable remedies. A93 (SPA § 11.3(a)). Accordingly, the Sellers agreed that AccentCare would shoulder the entire burden for the defense of these proceedings – including with respect to the period in which the Sellers owned Guardian. The Sellers participated in AccentCare's defense of the investigation and whistleblower case pursuant to a Joint Defense and Confidentiality Agreement. A192.

On December 22, 2012, the "Final Release Date", the balance in the Escrow Account was approximately $10,000,000. Although the Sellers were entitled under the SPA and the Escrow Agreement to release of the Escrow Account balance, they made no effort to have the Escrowed Funds released on the Final Release Date.

The government investigation and the parallel civil case continued for more than two years after the Escrowed Funds became available to the Sellers. In March of 2015, AccentCare negotiated a $3.2 million settlement with HHS and

the whistleblowers, for which it secured the Sellers' consent. A233.[2] The Sellers did not seek release of any of the Escrowed Funds between December of 2012 and March of 2015.

With the two cases settled, AccentCare began seeking indemnification from the Sellers for the $3.2 million settlement payment plus its defense costs of $2.8 million. Negotiations concerning indemnification took place between April 14, 2015 and January 18, 2016. During the entire time period between the OIG subpoena in June of 2012 and the end of these negotiations in January 2016, Sellers' counsel did not challenge AccentCare's indemnification claim as untimely. Not until January 18, 2016 – over three years after the Final Release Date and the deadline for making indemnification claims – did the Sellers first contend that AccentCare had not timely pursued its indemnification rights under the SPA.

In February of 2016, the Sellers, through their representative FFL, filed an action requesting a declaration that the Sellers were entitled to the entire amount in the Escrow Account, due to (among other things) the two-year limitation on indemnification claims. AccentCare filed counterclaims for indemnification and

---

[2] The Sellers dispute whether consent was given. However, on this motion, AccentCare's allegation that the Sellers consented to the settlement payments is controlling. A233.

payment of defense costs. With respect to Sellers' claims, AccentCare interposed the defense of recoupment to the extent of its settlement payment and defense costs, based on the obligations that the Sellers assumed in the SPA. AccentCare also interposed the defense of waiver of the two-year limitations period in the SPA. And, given that the recovery sought in AccentCare's best case was $3.1 million plus interest (A265), AccentCare initiated a reduction of the amount being held in the Escrow Account from $10.7 million down to $3.5 million. A276.

The Sellers moved to dismiss AccentCare's counterclaims citing the two-year contractual limitation on bringing an action for indemnification. The Sellers also contended that the counterclaims did not allege a breach of Guardian's representation that it had not violated the Healthcare Law. AccentCare opposed this motion on several grounds. With respect to the statute of limitations, AccentCare noted that its recoupment defense was not subject to the statute of limitations. In the alternative, AccentCare also contended that the Sellers had acquiesced in modification of the contractual limitations period by disregarding it for over three years. AccentCare also contended that the Sellers' approval of the $3.2 million settlement obviated any need to allege a breach of the applicable representation. AccentCare further contended that its defense costs were a separate obligation in the SPA that was not subject to the contractual statute of limitations.

The lower court granted FFL's motion to dismiss and also held that recoupment was "inapplicable". Order at 13.[3] It held that the two-year contractual limitation period in the SPA on the filing of an action for indemnification made AccentCare's counterclaims untimely. *Id.* at 6. It rejected the recoupment defense without reference to any of the controlling principles of equity or to applicable recent precedent from this Court. *Id.* at 12-13. It relied on the novel ground that recoupment would not apply to funds that had been set aside in an escrow account. *Id.* at 13. It also held, notwithstanding the terms of the Escrow Agreement, that the money in escrow belonged to the Sellers until an indemnification claim is proven. It concluded that the Sellers' acquiescence in modification of the statute of limitations was not unequivocal. *Id.* at 12. Here, it hypothesized possible reasons for delay which not only had not been asserted by the Sellers, but also supported AccentCare's claim of acquiescence. *Id.* at 12. The lower court also held that the SPA provision for Seller consent to the Buyer's proposed settlement of a claim did not necessarily imply that the parties to the contract contemplated indemnification for that claim. *Id.* at 10-11. And the lower court disregarded ambiguities in the SPA and reached the conclusion that reimbursement of defense costs – even in the special situation in which

[3] The Court of Chancery's Order Granting Motion to Dismiss First Amended Counterclaims is attached hereto as Exhibit B and is referred to as the "Order".

AccentCare found itself of being required to assume those costs – was not a separate Seller obligation. *Id.* at 6-9.

AccentCare moved for certification of the lower court's decision on the motion to dismiss as a partial final judgment pursuant to Court of Chancery Rule 54(b). A368-72. The parties agreed that the availability of indemnification and defense cost reimbursement were the central issues in the case and warranted an immediate appeal. The lower court granted the motion under Rule 54(b) and certified its decision as a partial final judgment. *See* Exhibit A hereto.

SUMMARY OF ARGUMENT

1. The Court of Chancery erred in holding that the defense of recoupment, which is not subject to the statute of limitations, was unavailable. Under this Court's controlling precedent, the defense of recoupment is applicable when the claims of plaintiff and defendant arise out of a single transaction and are based on the same contract, as is indisputably the case here. As this Court has held, when a plaintiff alleges that a defendant has breached contractual obligations, the defendant is entitled to allege a failure of the plaintiff to meet its own obligations in the same transaction. The Court of Chancery also erred in holding that recoupment would not apply when the parties' competing claims concern funds held in an escrow account. Referring to the general rule that recoupment does not permit an "affirmative recovery from the plaintiff", the Court of Chancery reached the conclusion that a recovery from the escrow account would be an impermissible "affirmative recovery" from a source other than the plaintiff. However, as shown by abundant case law, the "no affirmative recovery from the plaintiff" rule only means that a recoupment defense must be for an amount less than the plaintiff's claim; it does not refer to the source of payment. Moreover, a recovery by the Buyer from the Escrowed Funds would in all events be a recovery from the plaintiff in all but the most mechanical sense, because it would reduce the amount of Escrowed Funds otherwise available to the Sellers.

2. The Court of Chancery erred in holding acquiescence to be unavailable to AccentCare in response to Sellers' limitations defense. The facts in this case are more than sufficient to demonstrate the Sellers' acquiescence in extending the time for the Buyer to seek indemnification. After the Hospital Billing Actions began, the Sellers did not exercise their contractual right to release of $10 million in Escrowed Funds. Instead, the Sellers actively participated in the defense of the Hospice Billing Actions under a joint defense agreement from November of 2012 until March of 2015. Then, they actively negotiated as to the amount due for indemnification for another nine months while still remaining silent about release of any of the Escrowed Funds. Thus, the Sellers by conduct and by silence agreed to a modification of the time schedule for indemnification claims. Although the Court of Chancery offered possible alternative explanations for this delay, the rationales that it articulated are entirely consistent with acquiescence. The Court of Chancery's decision to reject the allegations of acquiescence by relying on inferences in favor of the moving party was error. Acquiescence is a fact-intensive issue, and this defense should not have been rejected on a motion to dismiss by drawing inferences against the non-moving party.

3. The SPA is ambiguous with respect to the Sellers' liability for consented-to settlements of Third Party Claims. There was no reason to give the Sellers' veto power over settlements of such claims if the Sellers were not to be responsible for

funding those settlements. The Court of Chancery erred because it insisted on its own interpretation of the SPA. It failed to recognize that, on a motion to dismiss, the existence of competing interpretations of a contract – interpretations that it acknowledged were equally viable – required it to favor the interpretation most favorable to the non-moving party. The Court of Chancery also erred in concluding that the SPA did not call for indemnification for the Third Party Claims in this case. The Hospice Billing Actions alleged that Guardian had submitted false claims to the federal government in order to secure payments for hospice care. These allegations were manifestly related to a breach of the Sellers' representation in the SPA that Guardian had not made any false claims to obtain such payments. The Court of Chancery failed to recognize that, in Section 11.1(a) of the SPA, the Sellers had assumed responsibility for claims and contingent liabilities related to a breach of their representations.

4. Section 11.3(a) of the SPA requires the Sellers to pay for the Buyer's defense costs in those instances where the Sellers are disqualified from defending a Third Party Claim. The lower court considered this obligation to defray Buyer defense costs to be inapplicable on the grounds that there was no "indemnifiable claim". However, the Sellers' defense cost obligation in Section 11.3(a) is not keyed to any of the Sellers' indemnification obligations. Section 11.3(a) does not use the term "Indemnifying Person" in defining the defense cost obligation.

Rather, Section 11.3(a) uses the word "Sellers" with respect to defense costs incurred by the Buyer. The drafters' choice of words may not be disregarded. In Section 11.3(a), the duty to defray expense costs is imposed on the "Sellers" only because the Sellers are disqualified from conducting the defense of the Third Party Claims, not because they are "Indemnifying Persons" under other provisions of the SPA. The SPA does not call for the Sellers to indemnify the Buyer for defense costs whenever a Third Party Claim is asserted against the Buyer. The obligation to repay Buyer defense costs applies only in certain narrowly defined circumstances where the Sellers are disqualified from defending themselves.

STATEMENT OF FACTS

A. The Subject Transaction

At the end of 2010, AccentCare and the stockholders in Guardian entered into the SPA pursuant to which AccentCare acquired ownership of Guardian from its stockholders for the sum of $215 million. A47.

Guardian is engaged in providing hospice care to terminally ill Medicare patients. Periodically it submits reimbursement claims to HHS in which it certifies that the patients in its care meet the Medicare criteria for payment for hospice care for terminally ill patients. In Section 3.20 of the SPA, Guardian represented that it had not violated the "Healthcare Laws," which as pertinent here included the federal statute prohibiting Guardian from submitting false claims to HHS for Medicare payments. A62-63. In the SPA, the Sellers not only agreed to indemnify AccentCare against "Third Party Claims" relating to or arising from breaches of this representation, but also agreed that AccentCare would be entitled to assume the defense of certain Third Party Claims at the expense of the Sellers. A92-93.

At the closing on December 22, 2010, $20.5 million (the "Escrowed Funds") was deposited in an interest-earning account (the "Escrow Account") at JP Morgan Chase Bank (the "Escrow Agent") to deal with post-closing matters. Disbursement of the Escrowed Funds, which to date have been partially paid out,

is controlled by an Escrow Agreement between AccentCare, FFL and the Escrow Agent. A135-58.

Under the SPA and the Escrow Agreement, the Escrowed Funds may eventually be paid entirely to the Buyer for indemnification claims, or entirely to the Sellers, or in part to the Buyer and in part to the Sellers. The Buyer may obtain a payment in satisfaction of the Sellers' indemnification obligations by delivering a "Claim" to the Escrow Agent and the Seller Representative. The Claim is to be paid to the Buyer unless a written objection by the Seller Representative is received by the Escrow Agent within fifteen days. Escrowed Funds for any Claims that are disputed by the Sellers ("Disputed Claim Amounts") are to be held by the Escrow Agent until there is a "Final Determination" of the disputed claim by an arbitrator or a court. A138-39 (Escrow Agreement ¶ 3(d)).

The Escrow Agreement provides for an "Initial Release" to the Sellers of a part of the Escrowed Funds on March 22, 2012. A138. It provides for a "Final Release" to the Sellers on December 22, 2012 of the balance then in the Escrow Account, less any then-pending or disputed claim amounts. *Id.* The Final Release Date in the Escrow Agreement coincides with Section 11.4(c) of the SPA. Section 11.4(c) states that no action for "Damages" under Section 11.1(a) of the

SPA may be brought after December 22, 2012 (the date which was two years after the closing). A95.

The Initial Release Amount was (i) the balance in the Escrow Account on March 22, 2012 minus (ii) any pending and disputed Buyer Claims, minus (iii) $10,750,000, minus (iv) Tax Interest Payments,[4] with the proviso that no funds would be released if this calculation resulted in a negative number. The Initial Release of Escrowed Funds to the Sellers took place as scheduled and the required amount was disbursed to the Sellers. This left approximately $9.7 million in the Escrow Account at the end of March, 2012. A136; A138; A255 (FAC ¶ 17).[5]

For over a year and a half after the closing, no violations of the Healthcare Laws were alleged. Then, in June of 2012, Guardian received a federal government subpoena for a wide range of documents pertaining to the claims it had submitted to HHS in order to receive Medicare payments. According to the HHS Office of the Inspector General ("OIG"), between 2009 and March of 2012 Guardian had submitted incorrect certifications that patients met the Medicare criteria for hospice care payment by Medicare, resulting in the receipt of Medicare

---

[4] Under the Escrow Agreement, the Buyer is charged with reporting the interest earned on the Escrowed Funds to the Internal Revenue Service, and the "Tax Interest Payments" are reimbursements to the Buyer for the income taxes due from it on the interest amounts. A139-40.

[5] "FAC" refers to AccentCare's First Amended Answer and Counterclaims.

payments to which Guardian was not entitled. AccentCare promptly notified FFL of the receipt of this subpoena. A187; A252 (FAC ¶ 9).

In August of 2012, AccentCare determined that the OIG investigation could result in criminal liability and/or equitable remedies against it. Accordingly, pursuant to a specific provision in the SPA, AccentCare notified the Seller Representative that AccentCare would assume the defense of the OIG investigation.[6] FFL and AccentCare entered into a joint defense agreement and AccentCare undertook the defense of the government investigation with FFL's consent. AccentCare also undertook the defense of a parallel "whistleblower" action against Guardian that made the same allegations that the federal government was pursuing. The OIG investigation and the whistleblower lawsuit are referred to as the "Hospice Billing Actions". A251-52 (FAC ¶ 8).

The Final Release Date for the Escrowed Funds, which was December 22, 2012, arrived six months after the OIG investigation was disclosed to AccentCare and, through AccentCare, to the Sellers. Although AccentCare had not filed a Claim with the Escrow Agent, the Sellers did not seek the release of any of the approximately $10.7 million then in the Escrow Account to the Sellers. Instead,

---

[6] Section 11.3(a) of the SPA provides that ". . . the Seller Representative will not be entitled to assume the defense of any such Third Party Claim if (a) such claim, based on the remedy being sought, could result in criminal liability of, or equitable remedies against, the Indemnified Person . . . ." A93.

the entire balance remained in the Escrow Account while the Hospice Billing Actions continued. The Sellers participated in the defense of the Hospice Billing Actions and made no effort to effectuate a release of any of these funds for over two years after the Final Release Date. A20-21 (Compl. ¶ 22); A21 (Compl. ¶ 24); A255 (FAC ¶ 17); A259 (FAC ¶ 34).

After discovery, exchanges of expert reports, and mediation efforts in 2013 and 2014, AccentCare reached an agreement in principle with the government and the whistleblowers in March of 2015 to settle their claims for $3.2 million. Although Sellers dispute the point, AccentCare's First Amended Answer and Counterclaims alleges that the Sellers consented to this settlement. A233. By that time, some $2.8 million in defense costs for counsel, experts, and other litigation costs had been paid out exclusively by AccentCare. A254 (FAC ¶ 13).

Having arrived at a settlement in principle, AccentCare began seeking indemnification from the Sellers for the $3.2 million settlement and the $2.8 million in defense costs. Negotiations concerning indemnification were carried on between April 14, 2015 and January 16, 2016. During this entire time period, Sellers' counsel only raised issues concerning the application of the deductible in the indemnification clause, whether there was Seller liability for post-closing violations of the Healthcare Laws, and whether the Sellers had consented to the settlement. Only on January 18, 2016 – over four years after the ostensible

deadline of December 22, 2012 for making indemnification claims – did the Sellers start to contend that AccentCare had not timely pursued its indemnification rights under the SPA. A209-16; A255 (FAC ¶ 17).

B. Applicable Indemnification Provisions

The indemnification clauses in the SPA are spread over five pages. The applicable provisions of the SPA are as follows:

First, Section 11.1(a) provides that the Sellers will indemnify the Buyer for "Damages" arising from or related to a breach of a representation. A93. The definition of "Damages" in Section 11.1(a) includes damages, counsel fees, judgments, and claims; it refers to "claims" twice:

> [E]ach Seller shall indemnify . . . the Buyer . . . for any and all claims, Liabilities, losses, damages, costs and expenses, including the fees and disbursements of counsel, judgments, fines, claims (whether monetary, equitable, declaratory and/or injunctive) . . . (collectively, "Damages"), related to or arising out of (i) any breach of any representation . . . .

A93 (emphasis added). Section 11.3(a) then provides that:

> In the event that [the Buyer] desires to make a claim for indemnification against any of the Sellers under Section 11.1(a) in connection with any Action by any third party for which the Buyer may seek indemnification hereunder (a "Third Party Claim") the Buyer shall promptly notify the Seller Representative of such Third Party Claim and of the [Buyer's] claim of indemnification with respect thereto. . . .

A93-94.

Section 11.3(a) also contains the following provisions:

> The Seller Representative shall have thirty (30) days after receipt of such notice to notify the Buyer if the Seller Representative will assume the defense of such Third Party Claim; provided, however, that the Seller Representative will not be entitled to assume the defense of any such Third Party Claim if (a) such claim, based on the remedy being sought, could result in criminal liability of, or equitable remedies against, the [Buyer] . . . .
>
> . . .
>
> If the Seller Representative is entitled to assume and does assume the defense of such Third Party Claim, the Seller Representative shall be entitled to conduct and control the defense and settlement of such Third Party Claim through counsel of its own choosing. If the Seller Representative (i) fails to notify the Buyer in writing or fails to assume the defense of the Third Party Claim on the terms provided above, in either case within thirty (30) days after receipt of the Buyer's notice of a Third Party Claim or (ii) is not entitled to assume the defense of such Third Party Claim in accordance with the second sentence of this Section 11.3(a), the Buyer shall be entitled to assume the defense of such Third Party Claim at the expense of the Sellers (and such expenses shall constitute indemnifiable Damages); provided, however, that the Seller Representative may participate in the defense of such Third Party Claim with its own counsel at the expense of the Sellers and the Buyer may not settle any Third Party Claim without the consent of the Seller Representative (not to be unreasonably withheld). . . . . Notwithstanding the foregoing, neither the Indemnifying Person nor the Indemnified Person shall settle or compromise any such claim or demand without the consent of the other unless the Indemnified Person and/or the Indemnifying Person, as applicable, and their respective officers, directors, employees and Affiliates are given a full and complete release of any and all Damages by all relevant parties relating thereto. To the extent the defense of any Third Party Claim is assumed by the Seller Representative, at the election of the Seller Representative, the reasonable out-of-pocket costs and expenses of such defense of such Third Party Claim, and any payment in respect of any settlement of such Third Party Claim, shall be paid from the Escrowed Funds, ...

A93-94 (emphasis added).

Section 11.4(c) provides that "[n]o action or claim for Damages pursuant to Section 11.1 . . . may be brought or asserted after the applicable Release Date. A95 (emphasis added). Section 11.5 provides that Guardian's representations with respect to compliance with the Healthcare Laws survive for two years after the closing (*i.e.*, until the Final Release Date in the Escrow Agreement). A96.

ARGUMENT

I. THE LOWER COURT ERRED BY FAILING TO APPLY RECOUPMENT TO OBLIGATIONS UNDER THE SAME CONTRACT AND BY MISAPPLYING THE RECOUPMENT DOCTRINE IN THE CONTEXT OF TEMPORARILY ESCROWED FUNDS.

A. Question Presented

Did the Court of Chancery err by failing to apply equitable principles to the defense of recoupment, by misapprehending the meaning of "affirmative recovery" and by relying on a faulty premise that funds in the Escrow Account had already become the Sellers' property? This issue was raised below at A303-306.

B. Scope of Review

The Court of Chancery's ruling on a motion to dismiss is subject to *de novo* review. *Cent. Mortg. Co. v. Morgan Stanley Mortg. Capital Holdings, LLC*, 27 A.3d 531, 535 (Del. 2011). When considering a motion to dismiss for failure to state a claim under Court of Chancery Rule 12(b)(6), the Court is required to "(1) accept all well pleaded factual allegations as true, (2) accept even vague allegations as 'well pleaded' if they give the opposing party notice of the claim, (3) draw all reasonable inferences in favor of the non-moving party, and (4) do not affirm a dismissal unless the plaintiff would not be entitled to recover under any reasonably conceivable set of circumstances." *Id.* at 535.

C. Merits of Argument

The common law doctrine of recoupment is based on equity. This Court has recognized the equitable nature of the recoupment doctrine in *Finger Lakes Capital Partners, LLC v. Honeoye Lake Acquisition, LLC*, 151 A.3d 450, 454 (Del. 2016). As the Court there noted, when a recoupment defense is available, it is not subject to the statute of limitations. *Id.* at 453.

Many other courts have also recognized the equitable foundation of this defense. The Michigan Supreme Court has held that recoupment:

> presents to the court an equitable reason why the amount payable to the plaintiff should be reduced, and the plaintiff will not be permitted to insist upon the statute of limitations as a bar to such a defense when he is seeking to enforce payment of that which is due him under the contract out of which the defendant's claim for recoupment arises.

Mudge v. Macomb County, 580 N.W.2d 845, 855 (Mich. 1998) (citation omitted). Similarly, the Pennsylvania Supreme Court has held that recoupment:

> is a doctrine of an intrinsically defensive nature founded upon an equitable reason, inhering in the same transaction, why the plaintiff's claim in equity and good conscience should be reduced.

Household Consumer Discount Co. v. Vespaziani, 415 A.2d 689, 694 (Pa. 1980) (footnote omitted). In *Household Finance Corp. v. Pugh,* 288 N.W.2d 701, 704 (Minn. 1980), the Minnesota Supreme Court held that:

> There is a natural equity, especially as to claims growing out of the same transaction, that one claim should compensate the other, and that the balance only should be recovered (citation omitted).

In short, recoupment "is the crediting against [an obligation] of a reciprocal obligation arising from the same transaction, typically from the same contract . . . . Recoupment is applied when the relevant claims arise out of the same contract or a single, integrated transaction, such that it would be inequitable for the debtor to enjoy the benefits of that transaction without also meeting its obligations." 31 Williston on Contracts § 78:106 (4th Ed. 2007) (citations omitted). As this Court held in *Finger Lakes Capital Partners,* "the defense of recoupment goes to the reduction of the plaintiff's damages for the reason that he, himself, has not complied with the cross obligations arising under the same contract." 151 A.3d at 453 (citation omitted).

In *Finger Lakes Capital Partners*, this Court referred to recoupment as "a narrow equitable doctrine designed to permit a summing up of liabilities in a tightly connected factual dispute." 151 A.3d at 454 (citation omitted). This case readily meets the "tightly connected factual dispute" criterion set forth in *Finger Lakes Capital Partners*. The parties' claims not only arise out of the same transaction and the same contract; they concern a single fund that both parties intended to be divided between them when they created it in the SPA and Escrow Agreement. Unlike *Finger Lakes Capital Partners*, this case does not involve "stale claims" that are factually unrelated to the plaintiff's claim.

In this case, it would inequitable to permit one of the parties to "enjoy the benefits of the transaction without meeting its obligations." Williston on Contracts § 78:106. The Sellers should not be able to enjoy the benefit of receiving funds in the Escrow Account without also meeting their "cross obligations [for indemnification] arising under the same contract." *Finger Lakes Capital Partners,* 151 A.3d at 453. Under applicable equitable principles and the holding in *Finger Lakes Capital Partners*, the Sellers are required to meet their indemnification obligation before receiving the balance of the funds in the Escrow Account.[7]

The Court of Chancery misapplied the phrase that recoupment does not support an "affirmative recovery from the plaintiff." Order at 12 (citing *TIFD III-X LLC v. Fruehauf Prod. Co., L.L.C.*, 883 A.2d 854, 859 (Del. Ch. 2004) (Strine, V.C.)). The court below erred in two respects. First, it incorrectly carved out and relied upon the three words "from the plaintiff" as if they were part of the holding in *Fruehauf.* However, the court in Fruehauf was only concerned with whether the claims of the defendant arose out of the same transaction; it held that they did not. *See* 883 A.2d at 859. It was not concerned with the source of funds.

[7] Although not a dispositive factor, it can be noted that the Sellers will receive approximately $17 million of the $20.5 million in Escrowed Funds even at the highest level of indemnification sought by AccentCare. A265.

Second, the concept that recoupment does not permit an "affirmative recovery" is a comparison of relative amounts; it is not a doctrine that concerns the source of funds. The actual meaning of "affirmative recovery" has been clearly elucidated in many other jurisdictions: it simply means that a recoupment defense is limited to the amount of the plaintiff's claim and cannot be greater than that amount. Thus, the Maryland Court of Appeals has observed:

> Recoupment as opposed to set-off is allowable under the general issue plea when the claim arises from the same contract or same transaction as the plaintiff's claim and no affirmative relief is sought in excess of plaintiff's claim.

Billingsley v. Kelly, 274 A.2d 113, 117 (Md. 1971) (emphasis added; citations omitted). Similarly, the Arizona Supreme Court has set forth the meaning of these terms as follows:

> Recoupment is an equitable doctrine and, therefore, the claim of the defendant can be used to reduce or to eliminate a judgment, but it cannot be used for purposes of affirmative relief.

W. J. Kroeger Co. v. Travelers Indem. Co., 541 A.2d 385, 388 (Az. 1975). In the same vein, the Pennsylvania Supreme Court has noted:

> recoupment goes to the justice of the plaintiff's claim, and no affirmative judgment can be had thereon, while setoff is not necessarily confined to the justice of such particular claim, and an affirmative judgment may be had for any amount to which the defendant establishes his right over and above the amount to which the plaintiff has proved he is entitled.

Household Consumer Discount Co., 415 A.2d at 694 n.8 (emphasis added; citation omitted); *see also Quechee Lakes Corp. v. Terrosi,* 451 A.2d 1080, 1082 (Vt. 1982):

> Recoupment is a species of counterclaim which a defendant may assert only if it arises out of the same transaction as the plaintiff's claim, and then only as a defensive device to defeat or diminish the plaintiff's recovery. 6 C. Wright and A. Miller, Federal Practice and Procedure § 1401 (1971). It is to be distinguished from a set-off, which does permit affirmative relief . . . .

Thus, the court below erred not only by failing to apply the equitable considerations supporting the application recoupment to obligations in the same transaction, but also by misapplying the concept of "affirmative recovery from the plaintiff". The legal significance of this phrase is simply a comparison of the defendant's claim to the amount of the plaintiff's claim. AccentCare is not seeking an amount greater than the amount that the plaintiff Sellers are claiming via recoupment. It is seeking a partial reduction in the amount of the declaratory judgment that plaintiff can obtain – with the balance being paid to the Sellers. The lower court erred in recasting AccentCare's defense of recoupment as an "affirmative claim" (Order at 13) when, as a matter of law, it actually refers to a reduction in the amount to be awarded plaintiff based on cross obligations in the same transaction.

The lower court also erred in supposing that a diminution in the amount of Escrowed Funds being paid to the Sellers would not be a "recovery from the

plaintiff". Order at 12-13. This could only be so in the most mechanical sense. On a realistic level, however, a reduction in the amount of Escrowed Funds available to the Sellers in the Escrow Account is a recovery from the Sellers.

Finally, the Court of Chancery erred in supposing that the money in the Escrow Account "belongs to the Seller." Order at 13. The ownership of the Escrowed Funds is in fact indeterminate until there is a Final Determination of all disputed amounts. Neither party owned those monies when the Escrow Account was funded. Rather, as is made clear in the Escrow Agreement, the parties intended to divide the Escrowed Funds between Buyer and Seller depending upon the amount of Buyer Claims, "Tax Payments", and "Final Determination[s]" of any disputes concerning Buyer Claims. A138-39. Indeed, in the Escrow Agreement, the Sellers agreed that they might have no right to any of the funds in the Escrow Account since all of the Escrowed Funds could land with the Buyer. It was not only incongruous to consider the funds in the Escrow Account as belonging to the Sellers; it was plain error to do so. And even if one were to accept the lower court's premise that the Escrowed Funds "belonged to the Sellers", then it is even clearer that recoupment would be a "recovery from the plaintiff".

In short, the Court of Chancery erred by failing to recognize that equitable recoupment applies to this tightly connected dispute involving a single transaction

and a single contract, by misapplying the concept of affirmative relief from the plaintiff, and by making the mistaken assumption that the Escrowed Funds belonged to the Sellers. Since a recoupment defense is not subject to the statute of limitations, the decision below that held this defense to be "inapplicable" must be reversed.

II. THE LOWER COURT ERRED IN REJECTING ACCENTCARE'S ARGUMENT THAT SELLERS ACQUIESCED IN AN EXTENSION OF THE STATUTE OF LIMITATIONS BECAUSE IT RELIED UPON INFERENCES THAT IN FACT DEMONSTRATED ACQUIESCENCE.

A. Question Presented

Did the Court of Chancery err in dismissing AccentCare's acquiescence defense, at the motion to dismiss stage, by relying on a factual inference *that actually favored AccentCare*? This issue was raised below at A306-09 and A347-49.

B. Scope of Review

See supra, Section I.B.

C. Merits of Argument

An alternate basis for rejecting Sellers' statute of limitations defense is its acquiescence in extending the time for AccentCare to file an indemnification action well beyond the contractual limitation periods. This Court has held that acquiescence is established where a party:

> has full knowledge of his rights and the material facts and (1) remains inactive for a considerable time; or (2) freely does what amounts to recognition of the complained of act; or (3) acts in a manner inconsistent with the subsequent repudiation, which lead the other party to believe the act has been approved.

Klaassen v. Allegro Dev. Corp., 106 A.3d 1035, 1047 (Del. 2014) (emphasis added; quotation omitted). In *Klaassen*, this Court further explained that for acquiescence to apply, conscious intent to approve the act is not required, nor is a

change of position or resulting prejudice. *Id.; see also In re Celera Corp. S'holder Litig.*, 2012 WL 1020471, at *9 (Del. Ch. Mar. 23, 2012) (acquiescence requires that a party "(1) have full knowledge of his [or her] rights and all material facts; (2) possess a meaningful choice in determining how to act; and (3) act voluntarily in a manner showing unequivocal approval of the challenged conduct") (internal quotations and citations omitted), *aff'd in part, rev'd in part on other grounds,* 59 A.3d 418 (Del. 2012). This Court has held that acquiescence is a fact intensive inquiry. *See, e.g., Julin v. Julin*, 787 A.2d 82, 84 (Del. 2001) ("Application of the standards underlying the defense of acquiescence is fact intensive, often depending, as here, on an evaluation of the knowledge, intention and motivation of the acquiescing party").

FFL acquiesced in a modification of the SPA to forego application of the two-year contractual time limitation during the three years that the Hospice Billing Actions were pending. The last date for release of all funds from the Escrow Account was two years after the Closing, *i.e.,* December 22, 2012. A53 (Escrow Agreement, ¶ 3(b)). After the Sellers were informed of the OIG subpoena, however, they did not seek to have any of the approximately $10 million in Escrowed Funds released on December 22, 2012. The Sellers did not seek release of any of the funds in the Escrow Account at any time during the

three years that the Hospice Billing Actions were pending. A255 (FAC ¶ 17); A259 (FAC ¶ 34).

First, the Seller Representative indisputably had full knowledge of, and is chargeable with knowledge of, the Sellers' right under the Escrow Agreement to demand release of the $10 million remaining in the Escrow Account on December 22, 2012. Second, it unquestionably had a meaningful choice to make such a demand. Third, the circumstances are sufficient to support an inference – in favor of the non-moving party – that the Seller Representative acted freely and voluntarily in approving the holding of the approximately $10 million in escrow for four years after "Release Date" while the Hospice Billing Actions were pending and negotiations with AccentCare were continuing.[8] Its conduct

---

[8] Even the Court below concluded that the "no waiver" provision in SPA Section 13.16 (and, by implication, the written modification proviso in Section 13.21 of the SPA) did not preclude a finding of post-closing acquiescence by conduct. A115-17. "[A] non-waiver clause in a contract may itself be waived through knowledge, coupled with silence and conduct inconsistent with the terms of the contract." *Good v. Moyer*, 2012 WL 4857367, at *6 (Del. Super. Oct. 10, 2012) (internal quotation and citation omitted); s*ee also Pepsi-Cola Bottling Co. of Asbury Park v. Pepsico, Inc.*, 297 A.2d 28, 33 (Del. 1972) ("We think the existence of (a joint integration and no-oral modification clause) does not prohibit the modification of making of a new agreement by conduct of the parties, despite a prohibition . . . against any change except by written bilateral agreement"); s*ee also Norberg v. Sec. Storage Co. of Washington*, 2000 WL 1375868, at *7 (Del. Ch. Sept. 19, 2000) ("an implied waiver can be established by acts and conduct from which an intention to waive may reasonably be inferred") (citation omitted). The Court of Chancery did err, however, when it found – without citation to any relevant authority – that "[g]iven this language (cont'd.)

constituted acquiescence in a modification of the SPA so that the time limitations for an indemnification claim concerning the Hospice Billing Actions would not apply before those cases were resolved. The Sellers by their silence also agreed to a modification of the Escrow Agreement so that its provisions for release of funds on or before December 22, 2012 would not apply until the Hospice Billing Actions were resolved. A233.

The Court of Chancery, however, found that these allegations were not sufficiently unequivocal to establish an acquiescence rebuttal to the Sellers' statute of limitations defense at the motion to dismiss stage. Order at 12.[9] It posited that this conduct was "equally consistent with a desire on the part of the Seller (i) not to fight about the issue until after the Hospice Billing Actions were resolved and (ii) to litigate over the allocation of the Escrowed Funds only after a consensual resolution could not be achieved." *Id.* But the Court of Chancery's

---

(cont'd.)
[Section 13.16], the 'unequivocal' action would need to be particularly plain and obvious." Order at 12. Nothing in the SPA changed the relevant standard for acquiescence or AccentCare's pleading burden on a motion to dismiss.

[9] The lower court relied on the standard articulated by the Court of Chancery in *Celera*. Order at 11. This Court's more recent and refined acquiescence standard, articulated in *Klaassen*, does not require that the party against whom acquiescence is asserted act in an "unequivocal" manner. That issue, however, is not dispositive because the trial court erred under either standard. This is especially so given that the Court of Chancery's decision was in the context of a motion to dismiss where all reasonable inferences are to be drawn in the non-moving party's favor.

reasoning does not undermine AccentCare's argument, it actually supports it: both of these hypothetical motivations, and particularly the supposed desire not to litigate immediately, are consistent with the Sellers agreeing to a belated indemnification claim. Such a desire makes logical sense given the parties' shared interest in defeating the government's claim.[10]

Indeed, the record fully supports the inference that the parties treated the indemnification claim as viable and not time-barred well after the Release Date. For example, throughout the course of the Hospice Billing Actions, which began before the Release Date and stretched into 2015, the Seller Representative by its own admission "attempted to participate in the defense of the Hospice [Billing Actions]" precisely because it was concerned that "such claims may be the basis for indemnification." A20-21 (Compl. ¶ 22); *see also* A21 (Compl. ¶ 24). In October 2013, counsel for the Sellers contacted government counsel to interject themselves into settlement negotiations. *See* A192. Then, beginning in March of 2015, which was three years after the Release Date, the parties actively negotiated as to the amount the Sellers should pay with respect to their indemnification liability for the Hospice Billing Actions. *See, e.g.,* A194-95; A197-99 (noting the

[10] It would have been highly problematic, to say the least, for AccentCare to have filed suit against the Sellers immediately upon receipt of the OIG subpoena alleging that the Sellers had been operating Guardian in violation of the Healthcare Laws while at the same time vigorously asserting in the OIG investigation and the whistleblower case that Guardian had not been doing so.

Seller Representative's disagreement with how AccentCare factored the deductible into its calculations of amounts owing) & A206-208 (noting once again Seller Representative's objection to AccentCare's calculation methodology). The Seller Representative was also requesting "information regarding the claimed losses." A26 (Compl. ¶ 40).

These actions are wholly inconsistent with a claim that the Sellers were invoking a limitations bar. Despite these numerous communications back and forth, it was not until January 2016 – more than three years after the Release Date – that the Seller Representative even mentioned the time limitations in the SPA and the Escrow Agreement for a buyer claim. A210; 215. *See Oakview Treatment Centers of Kansas, Inc. v. Garrett*, 53 F. Supp. 2d 1196, 1204-05 (D. Kan. 1999) (defendants' conduct, including participation in defense of action in recognition of their duties under an indemnification agreement, and otherwise remaining non-committal about their intent to honor those duties, supported a conclusion that defendants did not want to address issue of indemnification during pendency of action) (applying Kansas law).

As this Court held in *Julin,* a determination as to acquiescence is a fact-intensive one. The facts involved here are more than sufficient to demonstrate acquiescence, and this contention cannot be dismissed on a motion to dismiss without a complete evaluation of the facts. Here, the inferences that the Court of

Chancery articulated actually support AccentCare's view that the Sellers acquiesced in extending the statute of limitations so that the allocation of the Escrowed Funds could be litigated after the Hospice Billing Actions were resolved. The Court of Chancery's decision to reject the allegations of acquiescence on this basis was in error and should be reversed.

III. THE SPA HAS PROVISIONS EVIDENCING AN INTENT TO MAKE THE SELLERS LIABLE FOR CONSENTED-TO SETTLEMENTS OF THIRD PARTY CLAIMS WITHOUT PLEADING A BREACH OF A REPRESENTATION

A. Question Presented

Did the Court of Chancery err in failing to recognize that there is a reasonable interpretation of the SPA that demonstrates the Sellers' agreement to indemnify the Buyer for settlements to which the Sellers have consented? This issue was raised below at A300-03.

B. Scope of Review

See supra, Section I.B.

C. Merits of Argument

The SPA is ambiguous with respect to the Sellers' liability for consented-to settlements of third-party claims. The Court of Chancery erred because it failed to recognize the existence of competing – and equal – interpretations and insisted on its own interpretation. As a result, it failed to interpret the SPA in the light most favorable to the non-moving party, even though this is required by Delaware law with respect to a motion to dismiss that concerns contract provisions. *VLIW Tech., LLC v. Hewlett-Packard Co.*, 840 A.2d 606, 615 (Del. 2003); *Veloric v. J.G. Wentworth, Inc.*, 2014 WL 4639217, at *8 (Del. Ch. Sept. 18, 2014) ("At the motion to dismiss stage, ambiguous contract provisions must be interpreted most favorably to the non-moving party") (citation omitted).

The Sellers contended in the court below that AccentCare was required to allege a breach of Guardian's representation concerning the Healthcare Laws in order to make a claim for indemnification. However, when a Third Party Claim is settled by the Buyer with the Sellers' consent, the SPA does not require that AccentCare prove a breach of a representation before the Sellers' indemnification obligation applies. There are multiple provisions in the SPA that support this reading.

First, the SPA provides that when the Buyer assumes the defense of a Third Party Claim, it "may not settle any Third Party Claim without the consent of the Seller Representative (not to be unreasonably withheld)." A93 (SPA § 11.3(a)). Without an obligation to fund a settlement of a Third Party Claim by indemnifying the Buyer, there would be no reason for the parties to the SPA to provide the Sellers with the power to approve or disapprove a settlement negotiated by the Buyer.

Section 11.3 of the SPA also permits the Buyer to settle a Third Party Claim that it is defending without the Sellers' consent, provided it secures a general release for the Indemnitors. The question thus arises: why two different routes to settling Third Party Claims when the Buyer is settling a Third Party Claim? What is the difference that Sellers' consent is supposed to make? Both clauses, of course, must be given meaning. The Sellers have a choice: they can give or

withhold consent to a proposed Buyer settlement of a Third Party Claim. There would be no reason for the parties to include an approval option unless the parties intended settlement with approval to have a different meaning than settlement without approval. The only logical inference is that the Sellers reserved a Seller-approval requirement for settlements for which they would be liable.

The Court of Chancery opined that the Seller consent requirement was "equally" consistent with an intent to give the Sellers the right to deny consent to settlement if a Third Party Claim was not indemnifiable at all. Order at 12. Be that as it may, the very existence of two "equally" valid interpretations connotes ambiguity. The lower court was not free to ignore the interpretation that favors the non-moving party. *VLIW Tech., LLC,* 840 A.3d at 615 ("the trial court cannot choose between two differing reasonable interpretations of ambiguous provisions") (citation omitted). Moreover, even under the Court of Chancery's preferred interpretation, there would be no reason to require Seller approval of a settlement unless the parties contemplated that the Sellers would be defraying the cost.

Second, Section 11.3(a) also contains a provision for a settlement payment to be made out of the Escrowed Funds when the Sellers have assumed the defense of a Third Party Claim. A93. The funds being disbursed amount to the Sellers indemnifying the Buyer against the Third Party Claim using funds in the Escrow

Account, because the amount of money that will eventually flow to the Sellers from the Escrow Account is reduced by these payments. Here, the intent to have the Sellers provide indemnification for settlement of Third Party Claims – without any requirement for proof of breach of a representation – is additional evidence that the parties who drafted Section 11.3(a) intended that settlement payouts be indemnified out of the Escrow Account.[11]

The Court of Chancery erred because it considered Section 11.3(a) to require an "indemnifiable claim" under Section 11.1(a) without inquiring into what that could mean. Order at 10-11. The term "indemnifiable claim" that guided the decision of the Court of Chancery does not appear anywhere in the SPA. Instead, the scope of the Sellers' indemnification obligation must be discerned in two broad and unhelpful clauses. First, Section 11.1(a) sweeps in "claims" – twice – as indemnifiable if they are related to a breach of a representation. A "claim" need not be a judgment or a loss. It can be a cause of action, as in *Citigroup Inc. v. AHW Inv. Partnership*, 140 A.3d 1125, 1132 (Del. 2016). It can also be a written or oral demand for payment, as this Court held in *AT&T Corp. v. Faraday Capital Ltd.*, 918 A.2d 1104, 1109 (Del. 2007). Section 11.1(a) also creates indemnification liability for "Liabilities", which is defined to

[11] Notably, the Sellers potential liability for indemnification payments to the Buyer is limited to the amount in the Escrow Account. A96 (SPA ¶ 11.4(f)).

include "contingent liabilities". A92. Turning to Section 11.3(a), we find that a "Third Party Claim" is one for which the Buyer "may seek indemnification" under Section 11.1(a). A93. This refers back to the Sellers' obligation to provide indemnification against claims and contingent liabilities – such as a false billing claim by HHS and a contingent liability to repay HHS for false claims for payment for hospice care.

The SPA sheds no further light on the meaning of "indemnification" in this context. The Sellers prefer for it to mean only a Third Party Claim that the Buyer has independently proven to be indemnifiable in a second case. Their preferred meaning, however, is at odds with Section 11.1(a). Instead, in accordance with Section 11.1(a) the word "indemnification" in the definition of "Third Party Claim" must include a claim, or liability, or contingent liability. Insofar as a claim or liability of contingent liability must "relate to" a breach of a representation in the SPA, the expansive definition of "relates to" applies. "Relates to" means a relationship or connection. *See* https://www.merriam-webster.com/dictionary/relate. Here, the Third Party Claims of the government and the whistleblowers related to Guardian's breach of the representation that there was no violation of the Healthcare laws.

The court below also erred in considering the statute of limitations as a barrier to indemnification liability for a consented-to settlement. It held that

because more than two years had gone by "there is no indemnifiable claim that can support a claim for a settlement payment." Order at 11. This was also error. Doubling down on the statute of limitations in interpreting Section 11.3(a) was erroneous. The definition of indemnifiable "Damages" in Section 11.1(a) does not include a statute of limitations condition. Rather, issues concerning the statute of limitations are controlled by Section 11.4(c) and the doctrines of recoupment and acquiescence.

By demanding proof of breach even where a claim is one which relates to a breach of a representation, the Sellers are, in effect, asking this Court to add the following clause to the SPA: "Indemnification is not available for a settlement that the Sellers have consented to unless the Buyer also establishes a breach of the applicable representation post-settlement." No such language appears in the SPA. Furthermore, the Sellers' approach would needlessly prolong indemnification proceedings where a potential indemnitor has approved a settlement, contrary to the policy of Delaware favoring settlements. *See Christiana Care Health Services v. Davis*, 127 A.3d 391, 395 (Del. 2015).

IV. THE SELLERS ARE LIABLE FOR ACCENTCARE'S DEFENSE COSTS IN THIS CASE UNDER A VALID INTERPRETATION OF THE SPA

A. Question Presented

Did the Court of Chancery err by not applying the covenant in Section 11.3(a) of the SPA concerning the Sellers' obligation to defray the Buyer's defense costs in the limited circumstances where the Sellers were disqualified from defending against a Third Party Claim? This issue was raised below at A291-300.

B. Scope of Review

See supra, Section I.B.

C. Merits of Argument

The SPA contains a separate covenant by the Sellers in Section 11.3(a) to reimburse the Buyer for the cost of defending a Third Party Claim if, as here, the Third Party Claim could result in criminal liability or equitable remedies against the Buyer. In this circumstance, as well as for two other circumstances, Section 11.3(a) of the SPA states:

> the Buyer shall be entitled to assume the defense of such Third Party Claim at the expense of the Sellers (and such expenses shall constitute indemnifiable Damages) . . . .

A93. This clause requires Seller reimbursement of defense costs in a circumscribed and well-defined group of cases. The two-year time limitation in

Section 11.4(c) by its terms does not apply to defense costs under 11.3(a). A92-94; A95.

The Court of Chancery concluded that *Winshall v. Viacom International, Inc.*, 76 A.3d 808 (Del. 2013), foreclosed a claim for defense cost reimbursement under Section 11.3(a). It relied upon the requirement in *Winshall* that the defense costs be incurred for an "indemnifiable claim". Order at 8. However, Section 11.3(a) of the SPA imposes a liability on "the Sellers," not on an "Indemnifying Person." A93; A94. This choice of words should not be disregarded. *Osborn ex rel. Osborn v. Kemp*, 991 A.2d 1153, 1159 (Del. 2010) ("We will read a contract as a whole and we will give each provision and term effect, so as not to render any part of the contract mere surplusage . . . ."). The use of the words "the Sellers" makes this case different from *Winshall*. *See Winshall v. Viacom Int'l. Inc.*, 2012 WL 6200271, at *4 (Del. Ch. Dec. 12, 2012) (holding that use of the words "the indemnifying parties" brought indemnification liability into play), *aff'd,* 76 A.3d 808 (Del. 2013). In Section 11.3(a) the duty to defray expense costs is imposed on the Sellers in limited circumstances only because the Sellers are disqualified from conducting the defense of the Third Party Claim in those circumstances, not because they are "Indemnifying Persons" under other provisions of the SPA. A reasonable interpretation of Section 11.3(a), therefore, is that the duty to pay

defense costs in this case is not tied to indemnification liability as it was in *Winshall*.

There are additional circumstances that make this case unlike the situation in *Winshall*. *Winshall* did not involve a contract that required the Buyer to assume defense costs only in defined and limited circumstances, as is the case here. To the contrary, in *Winshall* the position of the party seeking indemnification was that, under the very broad contract language that was involved in that case, mere notice of any third-party claim was sufficient to impose a defense obligation. 76 A.3d at 821. That position was patently untenable. In this case, Section 11.3(a) does not give the Buyer *carte blanche* to obtain reimbursement of defense costs merely upon notice. Here, the Sellers could not by contract conduct the defense of the Hospice Billing Actions.

Requiring proof of breach of a representation as a condition for paying for defense of third-party claims that relate to breaches of a representation would lead to anomalous results. If AccentCare had to take on the defense of a third-party claim and litigate that claim through to a judgment of dismissal, it would not be entitled to recover its defense costs if a breach of a representation is required even though AccentCare has just proven that there was no breach. A reading of the SPA that would require such an absurd result would not be reasonable.

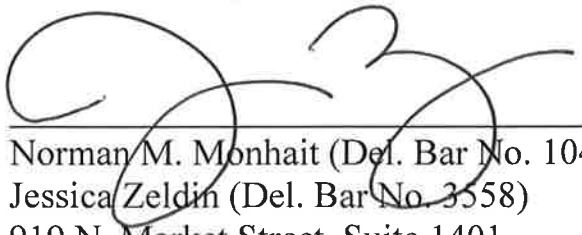
The Court of Chancery attempted to avoid this conundrum by using a concept that the parties did not include in the SPA. It suggested that even after proving that a Third Party Claim had no merit and was not indemnifiable, AccentCare could still seek its defense costs if it were "reasonably conceivable that the underlying claim was indemnifiable." Order at 9. This did not come from the SPA, which does not have a "reasonably conceivable" category of indemnifiable claims. But what this improvisation does mean is that a breach of a representation cannot be a condition for recovery of defense costs when the Sellers are required to defray them under Section 11.3(a) because it would lead to absurd results.

For all of the above reasons, the Court of Chancery erred in holding that the Sellers' covenant in Section 11.3(a) to cover defense costs did not apply to the Hospice Billing Actions.

CONCLUSION

For all of the reasons provided above, the Partial Final Order, dated February 7, 2017, and the Order Granting Motion to Dismiss First Amended Counterclaims, dated November 29, 2016, should be reversed, and the matter remanded for further proceedings.

ROSENTHAL, MONHAIT & GODDESS, P.A.



Norman M. Monhait (Del. Bar No. 1040)
Jessica Zeldin (Del. Bar No. 3558)
919 N. Market Street, Suite 1401
P.O. Box 1070
Wilmington, Delaware 19899
(302) 656-4433
Attorneys for Defendant and Counterclaim Plaintiff Below, Appellant

OF COUNSEL:

Roger J. Bernstein
535 Fifth Avenue, 35th Floor
New York, New York 10017
(212) 748-4800

March 30, 2017