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**SUPERIOR COURT OF THE STATE OF CALIFORNIA
COUNTY OF ALAMEDA
UNLIMITED JURISDICTION**

DAVID ADELSON, et al.,
Plaintiffs,

v.

PACIFICA FOUNDATION, et al.,
Defendants.

PEOPLE OF THE STATE OF
CALIFORNIA, ex rel. CAROL
SPOONER, et al.,

Plaintiffs,

v.

PACIFICA FOUNDATION, et al.,
Defendants.

) Consolidated Case No.: 814461-0
) [Consolidated with No. 831252-3
) and No. 831286-0]

) **PLAINTIFFS AND CROSS-**
) **COMPLAINANTS' MEMORANDUM OF**
) **POINTS AND AUTHORITIES IN SUPPORT**
) **OF MOTION TO PROHIBIT**
) **ADVANCEMENT OF DIRECTORS'**
) **DEFENSE EXPENSES, OR, IN THE**
) **ALTERNATIVE, TO ENFORCE THE**
) **COURT'S MAY 22, 2001 ORDER**
) **REQUIRING AN UNDERTAKING BY**
) **THE INDIVIDUAL DEFENDANTS**

1	ROBERT ROBINSON, et al.,)	Date: September 13, 2001
	Plaintiffs,)	Time: 9:00 a.m.
2	v.)	Dept.: 22
)	Judge: Hon. Ronald M. Sabraw
3	PACIFICA FOUNDATION, et al.,)	
	Defendants.)	
4)	
5	TOMAS MORAN, et al.,)	
	Cross-Complainants,)	
6	v.)	
7	PACIFICA FOUNDATION, et al.,)	
	Cross-Defendants.)	
8)	
9)	

1 **INTRODUCTION**

2 Directors' defense expenses can only be advanced by a corporation only if approved by a
3 majority of the non-interested directors. Otherwise, it would be self-dealing for such directors to
4 approve advancement of their own defense fees. Posting an undertaking would not cure the
5 situation, since posting an undertaking in effect turns the advancement of defense expenses into a
6 loan by the corporation for the benefit of the individual directors. Here, since there has been no vote
7 by the non-interested directors of Pacifica to authorize advancement of defense expenses for the
8 individual director defendants, no advancement is permitted.

9 Even were the Court to hold that a vote of the non-interested directors approving any
10 advancement of defense expenses is not required, the individual defendants still are required to post
11 an undertaking prior to any such advancements. On May 22, 2001, the Court ordered that “if the
12 representation of the individual defendants imposes any additional cost on Pacifica, then . . . the
13 individual defendants would need to post an undertaking for that additional cost.” At the time of that
14 order, counsel for defendants had argued that there had been no additional costs incurred for the
15 individual defendants than was expended on behalf of the Foundation, and that the legal services
16 provided for the individual director defendants was coincident with the services provided to the
17 Foundation due to the fact that such counsel represented a majority of the Foundation’s then-current
18 board of directors.

19 There have been changed circumstances since the May 22 Order, such that both of these
20 representations are no longer valid. Despite this, the individual defendants have not posted the
21 required undertaking. These circumstances demonstrating that the Foundation is currently paying
22 for legal expenses that relate solely to the individual director defendants: (1) the Foundation has paid
23 counsel to prepare and file pleadings that are addressed solely to the defense of the individual
24 director defendants; (2) current defense counsel, purportedly representing both the Foundation and
25 the individual director defendants, no longer represent a majority of the Foundation’s board of
26 directors; (3) currently, none of the work performed by the new law firms is being paid by the
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1 “no increase in the attorneys’ fees incurred in defending any of these cases by reason of the fact that
2 [insurance defense counsel was] representing the Foundation and the directors.” Declaration of
3 Daniel Rapaport in Opposition to Plaintiffs’ Motion For Undertaking, dated May 3, 2001, ¶ 3 (a copy
4 of this declaration is attached as Exhibit A to the Declaration to Terry Gross (“Gross Dec.”), filed
5 herewith).^{1/} At oral argument on this motion, defense counsel rested their argument that no
6 additional work was performed for the individual directors than was already performed for the
7 Foundation on the contention that defense counsel then represented a majority of the board. For
8 example, defense counsel Temchine stated: “The fact of the matter is we represent *the majority of*
9 *the Board*. The positions that have been espoused are the position *of the majority of the Board*.
10 They speak for the corporation. They are the corporation until that changes. And so all we have
11 done with the exception of the undertaking motion is represented by the interests of the Foundation
12 *as expressed by the majority of the Board*.” Transcript of proceedings on May 21, 2001, related to
13 Plaintiffs’ Motion For Undertaking, at 13:22-14:1 (Gross Dec. Ex. B).

14 On May 22, 2001, the Court issued an Order granting the prior motion regarding
15 advancement of defense fees and costs, holding that “Pacifica is required to comply with
16 Corporations Code 5238(f) and require an undertaking from the individual defendants before
17 advancing expenses to them for their defense of this consolidated action.” The Court further stated
18 that “if counsel retained by Pacifica also represent individual defendants, then those individual
19 defendants do not need to post an undertaking if the representation of those individual defendants
20 does not impose any additional cost on Pacifica. If the representation of the individual defendants
21 imposes any additional cost on Pacifica, then that additional cost is an advance by Pacifica for the
22 benefit of the individual defendant and the individual defendants would need to post an undertaking

23 ^{1/} However, defense counsel Daley Temchine stated that his firm, Epstein, Becker & Green, a firm
24 retained by Pacifica Foundation and not paid by insurance, *had* incurred expenses solely on behalf of the
25 individual directors in opposing the original motion to disqualify. Transcript of proceedings on May 21, 2001,
related to Plaintiffs’ Motion For Undertaking, at 13:17-20 (Gross Dec. Ex. B).

1 for that additional cost.” The Court concluded: “In this case, counsel for Pacifica has submitted
2 declaration testimony that all the cost and expenses incurred to date (with the exception of
3 appearance fees for the individual defendants) would have been incurred in the defense of Pacifica
4 and that there has been no additional expense related to the defense of the individual defendants.
5 . . . The undertaking required to the individual defendant is, therefore, limited to the amount of the
6 appearance fees advanced on their behalf.” Order Granting Motion of the People/Spooner Plaintiffs
7 For a Preliminary Injunction Regarding Advancement of Defense Fees and Costs, dated May 22,
8 2001 (Gross Dec. Ex. C).

9 **2. New circumstances demonstrate that the representation of the**
10 **individual defendants is imposing additional cost of Pacifica.**

11 Until late July 2001, the Pacifica Foundation and the Controlling Director Defendants were
12 represented jointly by two law firms, one of which was paid by Pacifica Foundation (Epstein, Becker
13 & Green P.C. (the “Epstein firm”)) and the other which was paid by a policy of insurance (Wendel,
14 Rosen, Black & Dean, LLP (the “Wendel firm”)). On or about July 23, 2001, Bessie Wash, the
15 Executive Director of Pacifica, fired both the Epstein firm and the Wendel firm, and hired two new
16 law firms to represent Pacifica, *i.e.*, Williams & Connolly, LLP (the “Williams firm”) and Fulbright
17 & Jaworski LLP (the “Fulbright firm”). The Executive Director took these actions without
18 consultation with or direction from Pacifica’s Board of Directors or the Executive Committee.
19 Declaration of Pete Bramson (“Bramson Dec.”) ¶¶ 3-4.

20 Pacifica’s prior counsel estimated that it would cost in excess of \$100,000 for the two new
21 law firms to come up to speed in this matter. Declaration of Terry Gross (“Gross Dec.”) ¶ 5.

22 Neither of the two current law firms are being paid under a policy of insurance. Current
23 counsel has stated that neither firm was being paid by insurance, and that both firms were retained.
24 Gross Dec. ¶ 6. In addition, in the *Robinson* action, there is *no* insurance coverage in any event, as
25 Pacifica’s insurance carrier has refused to provide any defense to Pacifica or any individual directors,
26 stating that there is no coverage in a case in which one director sues other directors. Declaration of
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1 Timothy Fox (“Fox Dec.”) ¶ 3. Further, it is unlikely that Pacifica’s insurance carrier will agree to
2 retain either of Pacifica’s two new firms, since with respect to the representation of some of the
3 individual director defendants in the *People ex rel. Spooner* action who at the time were not involved
4 in any other of these consolidated lawsuits, Pacifica’s insurance carrier refused to select counsel that
5 had been hired by the individual directors, and instead selected a separate law firm as their insurance
6 defense firm. Fox Dec. ¶ 4.

7 The two new law firms, in addition to appearing on behalf of Pacifica Foundation, have also
8 entered appearances on behalf of some of the individual director defendants – in fact, on behalf of
9 five out of eleven current directors. At present, there are eleven current directors of Pacifica
10 Foundation. Bramson Dec. ¶ 5. To date, the two new law firms each have submitted Substitution
11 of Counsel forms for Pacifica Foundation and only three individual director defendants (Murdock,
12 Johns and Chambers), but have filed pleadings on behalf of five of the current director defendants
13 (Murdock, Johns, Chambers, Ford and Lee). *See* Demurrer to First Amended Complaint, and
14 Motion to Strike, both filed on August 8, 2001 in the *People ex rel. Spooner* action.^{1/} However, the
15 new law firms have not filed any pleadings on behalf of current director Robert Farrell. In fact,
16 Farrell has sent a letter to the executive director of Pacifica stating that he “do[es] not wish to be
17 represented by the new law firms retained by the Pacifica Foundation.” Bramson Dec. ¶ 10 & Ex.
18 A.^{1/}

19 Thus, the new law firms represent at most five of eleven current directors: Murdock, Johns,
20 Chambers, Lee and Ford. Bramson Dec. ¶ 5. Five current directors are plaintiffs or cross-
21 complainants: Moran, Bramson, Cagan, Robinson and Kriegel. Farrell, who previously had been

22 ^{2/} The new firms have also filed pleadings on behalf of seven other individual defendants who were
23 formerly, but are not currently, directors of Pacifica Foundation (Andrea Cisco, David Acosta, Michael Palmer,
24 Karolyn Van Putten, Mary Frances Berry, June Makela and Frank Millsbaugh).

25 ^{3/} Farrell also stated in his letter: “I believe that initiatives to find common ground, lower the levels of
26 animosity and hostility that exist, and seek a peaceful resolution to the problems that have contributed to a
27 divided board, staff and audience are necessary and imperative. To that end I am in conversations with my
own lawyer and board members with whom I share points of view.” Bramson Dec. ¶ 10 & Ex. A.

1 represented by the Epstein and Wendel firms, is currently unrepresented.^{1/}

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5 **ARGUMENT**

6 **I. PACIFICA CANNOT ADVANCE DEFENSE EXPENSES FOR THE INDIVIDUAL**
7 **DIRECTOR DEFENDANTS, SINCE THIS TRANSACTION HAS NOT BEEN**
8 **APPROVED BY A MAJORITY OF THE NON-INTERESTED DIRECTORS**

9 Corporations Code § 5233 requires that any transaction in which a director has a material
10 financial interest is valid only if approved by the Attorney General or a court, or if the transaction
11 is approved by a vote of a majority of the non-interested directors. Here, there has been no vote by
12 the non-interested directors of Pacifica approving the advancement of defense expenses to the
13 individual director defendants.

14 The fact that Corp. Code § 5238(f) provides that a corporation “may” advance defense
15 expenses does not override the provisions of Corp. Code § 5233. There is no explicit statement in

16 ^{4/} Last week, on August 17, 2001, an attorney from Williams & Connolly, counsel for Pacifica and five
17 of the eleven directors, sent a notice that David Bramson will not be allowed to participate in the September
18 19, 2001 board meeting, stating that Bramson’s term had expired. Gross Dec. ¶ 7 & Ex. D. Such an action
19 is improper and in violation of law, since (1) neither Pacifica nor the five individual defendant directors had
20 the right to make such a determination by themselves; (2) under general corporation law, a director who has
21 not been removed from his position continues to serve as a director until his or her replacement is elected; and
22 (3) since Ford’s term on the board has also expired and Farrell has been removed by the local advisory board
23 that elected him, it is irrational to disqualify Bramson from participating in any board meeting unless Ford and
24 Farrell are also similarly disqualified. See Plaintiffs’ Memorandum of Points and Authorities in Support of
25 Motion for Preliminary Injunction Governing Conduct of September 2001 Meeting of the Pacifica National
26 Board, filed concurrently.

1 Section 5238(f) of an intent to override the self-dealing provisions in Section 5233. Moreover,
2 Section 5238(f) applies not just to advancement of expenses for directors, but to officers, employees
3 and agents of the corporation.

4 Thus, any advancement by Pacifica of the defense expenses of the individual director
5 defenses is a self-dealing transaction in violation of Corp. Code § 5233.

6 **II. ASSUMING ADVANCEMENT OF EXPENSES IS NOT A SELF-DEALING**
7 **TRANSACTION, THE INDIVIDUAL DIRECTOR DEFENDANTS ARE REQUIRED**
8 **BY CORP. CODE § 5238(f) AND PRIOR COURT ORDER TO POST AN**
9 **UNDERTAKING TO PROTECT THE FOUNDATION FOR LEGAL**
10 **EXPENSES ADVANCED FOR THE INDIVIDUAL DEFENDANTS' DEFENSE**

11 Pursuant to Corp. Code § 5238, a non profit corporation can indemnify its directors from
12 claims and expenses incurred by reason of said director's relationship with the corporation in two
13 different ways: (1) by purchasing insurance on behalf of such directors, Corp. Code 5238(i),^{1/} or (2)
14 if certain criteria are met, by providing such indemnification from the corporation's funds. Corp.
15 Code § 5238(c), (d), (e).^{1/} However, the Code clearly makes a distinction between *indemnification*,
16 *i.e.*, the corporation's agreement to reimburse a director for expenses incurred in defending an action,
17 and *advancement of expenses* for that action prior to completion or settlement of the action. Corp.
18 Code § 5238(i) explicitly provides that a corporation *cannot* advance expenses prior to the final
19 disposition of a proceeding *except* if the director posts an undertaking to repay the expenses if it is
20 determined ultimately that the director is not entitled to indemnification.

21 In fact, the Court here has already held that the individual directors are required to post such
22 an undertaking for any expenses incurred in the individual directors' defense that were in excess of
23 expenses incurred on behalf of the Foundation's defense, before the Foundation can advance any
24 expenses for their defense in this consolidated action. Order of May 22, 2001.^{1/} At the time of the

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26 ^{5/} However, a corporation cannot provide insurance indemnification "to indemnify any agent of the
27 corporation for a violation of Section 5233 [self-dealing]." Corp. Code § 5238(i).

28 ^{6/} Corp. Code § 5328(b) allows for indemnification for actions not relevant here, *i.e.*, actions that do
29 not involve self-dealing, breach of charitable trust, or are not brought by the Attorney-General or a relator.

30 ^{7/} To further illustrate the difference between *indemnification* and *advancement of expenses*, it is

1 May 22 Order, the Court limited the amount of the undertaking to the filing fees paid on behalf of
2 the individual director defendants, based on declaration testimony by defense counsel that defense
3 counsel “did not incur any material costs or attorneys’ fees in connection with the services rendered
4 for the individual directors” and that there had been “no increase in the attorneys’ fees incurred in
5 defending any of these cases by reason of the fact that [defense counsel was] representing the
6 Foundation and the directors.” Declaration of Daniel Rapaport in Opposition to Plaintiffs’ Motion
7 For Undertaking, dated May 3, 2001, ¶ 3. At oral argument on this motion, defense counsel rested
8 their argument that no additional work was performed for the individual directors than was already
9 performed for the Foundation on the contention that defense counsel then represented a majority of
10 the board. For example, defense counsel stated: “The fact of the matter is we represent *the majority*
11 *of the Board*. The positions that have been espoused are the position *of the majority of the Board*.
12 They speak for the corporation. They are the corporation until that changes. And so all we have
13 done with the exception of the undertaking motion is represented by the interests of the Foundation
14 *as expressed by the majority of the Board*.” Transcript of Proceedings related to Plaintiffs’ Motion
15 For Undertaking hearing, at 13:22-14:1 (Gross Dec. Ex. B).

16 **A. The Foundation Is Currently Paying for Legal Expenses That Relate Solely to**
17 **the Individual Director Defendants, Though No Undertaking Has Been Posted**

18 significant that, under the circumstances here, there has not yet been any indemnification by Pacifica of its
19 directors under Corp. Code § 5238(c)-(e). Corp. Code § 5238(d) provides for indemnification if a director is
20 successful in his or her defense, which obviously can only occur after a determination on the merits is made.
21 This has not yet occurred. Corp. Code § 5238(e) provides for indemnification in situations other than success
22 on the merits only if “any indemnification under this section shall be made by the corporation only if
23 authorized “*in the specific case*” upon a determination that indemnification is proper by the court, a vote of
24 directors who are not parties, or a vote of members of the corporation. No such authorization has yet occurred
25 in this specific case and, thus, at the present time there can be no claim that any director has an entitlement to
26 indemnification from the Foundation’s funds under Corp. Code § 5238(c)-(e).
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1 Since the court's May 22, 2001 ruling, it is readily apparent that, due to new circumstances,
2 these representations by defense counsel can no longer be accurate, that the Foundation has and is
3 paying legal expenses to joint counsel that relate solely to the defense of the individual director
4 defendants, and, moreover, that retained Foundation counsel no longer represent a majority of the
5 board. Despite this, the individual director defendants have not complied with the May 22 order and
6 posted the required undertaking.

7 The following facts demonstrate that the Foundation has incurred legal expenses for legal
8 work performed solely on behalf of the individual director defendants:

9 **The Foundation has paid counsel to prepare and file pleadings that are
10 addressed solely to the defense of the individual director defendants**

11 On August 8, 2001, Foundation-paid counsel filed a demurrer to the First Amended
12 Complaint, and a Motion to Strike portions of the First Amended Complaint. Both of these
13 pleadings, however, addressed causes of action that were filed against the individual director
14 defendants, and were *not* filed against the Foundation.

15 The Demurrer addressed solely the Twelfth and Thirteen Causes of Action; the Motion to
16 Strike addressed the Sixth, Twelfth and Thirteen Causes of Action. The Sixth Cause of Action is
17 solely against the individual director defendants for self-dealing, in violation of Corp. Code § 5233.

18 Similarly, the Thirteenth Cause of Action is directed solely against some of the individual director
19 defendants (those currently members of the board) for usurpation of the corporate franchise through
20 improper use of corporate funds, under CCP § 803. These two causes of action clearly do not and
21 cannot be directed at the Foundation itself, but are for the benefit of the Foundation. The Twelfth
22 Cause of Action again is directed solely against those individual director defendants currently on the
23 board, for usurpation of corporate franchise by acting as directors though not properly elected.

24 Defense counsel filed both of these pleadings *on behalf of the Foundation* as well as some
25 of the individual defendants, despite the fact that the causes of action addressed are solely against
26 the individual director defendants and *not* against the Foundation.

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1 · **Current defense counsel, purportedly representing both the**
2 **Foundation and the individual director defendants, no longer**
3 **represent a majority of the Foundation's board of directors**

4 The May 22 Order was based in part on an oral representation by defense counsel that since
5 the individual director defendants that counsel represented constituted a majority of the board, that
6 work performed for the defense of the individuals was coincident with the defense of the Foundation.
7 However, this is no longer the case – defense counsel have asserted appearances for at most *five out*
8 *of eleven current directors*. Bramson Dec. ¶ 5.

9 Therefore, defense counsel can no longer argue that the work performed in defense of the
10 individual director defendants is identical to work performed on behalf of the Foundation.^{1/}

11 · **Currently, none of the work performed by the new law**
12 **firms is being paid by the directors' insurance carrier**

13 Defendants had argued, in opposition to the prior motion for an undertaking, that much of
14 the work performed on behalf of the individual defendants was being performed by counsel paid by
15 the directors' insurance carrier, the Wendel firm. However, at the present, *neither* of the two new
16 firms are being paid by the directors' insurance carrier. Gross Dec. ¶ 6; Fox Dec. ¶¶ 3-4. Even were
17 the insurance carrier to agree to pay one of the new firms, it is extremely unlikely that the carrier
18 would pay all of the fees of the firm, since insurance carriers usually pay significantly reduced rates
19 to defense counsel.

20 · **The First Amended Complaint, in addition to numerous causes of action solely**
21 **against the individual directors for diversion of assets to *ultra vires* activities,**
22 **contains a cause of action for self-dealing pursuant to Corp. Code § 5233, and**
23 **work performed in defense of these causes of action by definition is solely on**
24 **behalf of the individual defendants, and by statute work on the self-dealing**
25 **cause of action cannot be paid by insurance**

26 The Sixth Cause of Action of the First Amended Complaint alleges self-dealing by the

27 ^{8/} Moreover, it is completely inappropriate that a *minority* of the board of directors can direct the
28 Foundation to advance defense expenses on their behalf so they can retain high-priced counsel, rather than
29 simply utilizing insurance-paid counsel, while at the same time denying any advancement of expenses to other
30 directors who are involved in these consolidated lawsuits.

1 individual director defendants, in violation of Corp. Code § 5233. Clearly, this cause of action is
2 asserted not against the Foundation, but for the benefit of the Foundation. Thus, any legal work
3 performed by defense counsel concerning this cause of action is necessarily performed solely on
4 behalf of the individual director defendants, and *not* on behalf of the Foundation.

5 Prior defense counsel conceded that in such a situation, an undertaking would be required.
6 During oral argument on the prior motion for an undertaking, defense counsel for the Foundation
7 and the individual defendants stated that he “could understand requiring the undertaking of the
8 individual Directors to the extent that fees are incurred for dealing with issues that are specific to
9 their interests or to them.” Gross Dec. Ex. B at 13:19-20; *see also* 13:27-14:1.

10 Moreover, defendants cannot credibly claim that insurance defense counsel will perform the
11 legal work for the individual director defendants to defend against this cause of action. Corp. Code
12 § 5238(i) explicitly states “that a corporation shall have no power to purchase and maintain such
13 insurance to indemnify any agent of the corporation for a violation of Section 5233.”

14 Thus, in any situation involving a cause of action against directors for self-dealing under
15 Corp. Code § 5233, the directors must post an undertaking for defense expenses if the Foundation
16 is paying defense counsel on their behalf.

17 In addition, a review of the First Amended Complaint demonstrates that, of thirteen causes
18 of action, only three name the Foundation as a defendant, *i.e.*, three causes of action seeking
19 declaratory relief compelling the adoption of the Foundation’s bylaws in accordance with the law.
20 First Amended Complaint, Causes of Action 8-10. The other ten causes of action name as
21 defendants *solely* the individual director defendants, and address conduct by the individual directors,
22 such as self-dealing, breach of charitable trust, gross abuse of authority, improper use of corporate
23 funds, and refusal to vacate office at expiration of term or removal by members. These causes of
24 action seek damages against the individual director defendants on behalf of the Foundation in an
25 amount in excess of \$500,000, and also seek removal of these directors for gross abuse or fraud or
26 dishonest acts. None of these causes of action can properly be defended by the Foundation, as the
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1 Foundation is in direct conflict with the directors on these causes of action. Thus, any legal work
2 performed by defense counsel concerning these ten causes of action directed solely against the
3 individual director defendants will by necessity be in excess of the legal work necessary for the
4 defense of the Foundation, and the individual director defendants must be required to post an
5 undertaking for all such legal work that is paid for by the Foundation.^{1/}

6 **Since the individual director defendants have fired prior retained**
7 **counsel and insurance defense counsel, there will be significant**
8 **costs in paying new counsel that will not be paid by insurance**

9 In July 2001, the Foundation's executive director unilaterally fired prior privately retained
10 and insurance-retained counsel and, in their place, retained two new law firms. A number of the
11 individual director defendants have also terminated prior counsel, including insurance defense
12 counsel, and have retained the same two new law firms.

13 Clearly, given the complexity of this litigation, it is obvious that there will be a significant
14 expense in paying new counsel to become familiar with the facts of this case and its procedural
15 history. In fact, prior defense counsel stated that such cost would be in the six figures. Gross Dec.
16 ¶ 5.

17 This cost will have to be paid for by the Foundation. Even assuming that one of the new
18 firms will be partially paid by the insurance carrier, it is extremely unlikely that the insurance carrier
19 providing insurance defense counsel for the individual directors will be willing to pay such
20 substantial sums for new counsel, when prior insurance counsel was performing adequately and was
21 terminated solely at the whim of the individual directors.

22 Moreover, insurance defense counsel traditionally is paid at a reduced rate negotiated with

23 ^{2/} Moreover, prior defense counsel previously informed the Court that it had performed legal work solely
24 for the defense of the individual directors in opposing the prior Motion Prohibiting Advancement of Attorney's
25 Fees and Costs on Behalf of Individually Named Defendants. Transcript of May 21, 2001 hearing at 13:17-20
26 ("but for the motion expecting the undertaking, all the work that we have done would have been done anyway
27 to defend the Foundation") (Gross Dec. Ex. 5). Thus, the individual directors should be required to post an
28 undertaking that includes the expenses advanced by the Foundation opposing such motion and in opposing
29 this motion.

1 the insurance carrier. Here, the two law firms currently representing the individual director
2 defendants were not chosen by the insurance carrier. If the individual director defendants' insurer
3 will reimburse one or both of these firms at a rate less than the rate charged by the firms, with the
4 Foundation responsible for the difference, then the excess payment by the Foundation will be an
5 advance for the benefit of the individual directors.

6 Thus, the individual directors should be required to post an undertaking that includes the
7 expenses of the new law firms to come up to speed in this litigation, and for any fees charged by the
8 firms in excess of that paid by the individual defendants' insurance carrier.^{10/}

9 **B. An Adequate Mechanism Must Be Instituted To Ensure That Any
10 Undertaking is Adequate To Cover Anticipated Advancements**

11 Though the Court's May 22 Order required the posting of an undertaking for any work
12 performed by Foundation-retained counsel solely on behalf of the individual director defendants,
13 there was no mechanism in the Order to ensure that such an undertaking would be posted concerning
14 future such work. Thus, when defense counsel did perform such additional work and the Foundation
15 paid such expenses, the defendants failed to post the required undertaking.

16 There are several solutions to this situation: (1) the individual director defendants can be
17 represented solely by insurance defense counsel, and not by Foundation-retained counsel, and in such
18 a situation the individual director defendants would have to post an undertaking only for prior

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20 ^{10/} The Foundation cannot properly authorize the advance of any expenses on behalf of the individual
21 director defendants absent an undertaking, since this would be a self-dealing transaction subject to the
22 procedures of Corp. Code § 5233.
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1 expenses and for work to be performed on the self-dealing allegation;^{11/} or (2) if the individual
2 director defendants insist on being jointly represented with Foundation by retained counsel,^{11/} then
3 a meaningful undertaking must be posted that will cover any past and anticipated fees on behalf of
4 the individual director defendants.

5 Plaintiffs conservatively estimate the defense costs for the litigation to be approximately
6 \$300,000. Gross Dec. ¶ 8. Thus, if the individual director defendants are represented solely by
7 insurance defense counsel, then an undertaking by all thirteen director defendants in the total amount
8 of \$60,000 would be sufficient. However, if the individual defendants insist on being jointly
9 represented by Foundation-retained counsel, then an undertaking in the total amount of \$300,000
10 should be required.

11 Further, whatever amount of an undertaking is ordered at the present time, the amount of the
12 undertaking should be regularly reevaluated to ensure that the amount of the undertaking remains
13 sufficient to protect the Foundation's assets.

14 CONCLUSION

15 Accordingly, the moving parties respectfully request that the Court enter an order prohibiting
16 the advancement of defense expenses by Pacifica for the benefit of the individual director
17 defendants; or, in the alternative, requiring the individual director defendants to post an undertaking
18

19 ^{11/} To date, such work would necessarily include legal services on the prior motion for an undertaking,
20 the current demurrer and motion to strike, the opposition to this motion, and legal work analyzing the
21 individual defendants' defense and liability under the First Amended Complaint. A reasonable estimate of
these expenses, plus legal work to defend the self-dealing cause of action, would be approximately \$60,000.
Gross Dec. ¶ 8.

22 ^{12/} However, as argued in the concurrently-filed Motion to Disqualify Defendants' Law Firms, the
23 individual director defendants cannot be represented by the same counsel as represents the Foundation.

1 in the total amount of \$300,000, and providing that the amount of the undertaking should be
2 reevaluated at regular intervals.

3 Dated: August 23, 2001

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