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RELIEF IN THE BOARDROOM: HOW THE THIRD CIRCUIT'S *CITX* DECISION WEAKENED DEEPENING INSOLVENCY AS AN INDEPENDENT CAUSE OF ACTION

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I. INTRODUCTION

DIRECTORS and officers of corporations have always had to worry about certain causes of action being brought against them, including breach of fiduciary duty, fraud and negligence. But recently there has been a new cause of action to worry about. The recent trend is for the fiduciaries of a bankruptcy estate to include deepening insolvency as a cause of action brought against directors and officers—a trend that has caused much tension in the boardroom. While the concept of deepening insolvency was first discussed in case law over twenty years ago, only in the recent years since the Enron and WorldCom collapses has deepening insolvency made its way back into the courts. As a result of the increasing popularity of deepening insolvency, a growing number of courts have faced the question of whether to recognize deepening insolvency as (1) a valid independent cause of action itself; (2) a measure of damages for an independent tort; or (3) neither as a valid independent cause of action nor a measure of damages. The Third Circuit has been an influential court in developing this area of law, having issued two important and precedential opinions in recent years, with the most recent coming in the summer of 2006. Although the first Third Circuit deepening insolvency opinion helped shape and develop the concept as an independent tort, the most recent Third Circuit opinion on deepening insolvency, as well as the opinions of the influential Delaware Chancery and Supreme Courts, will drastically limit courts' acceptance and application of this theory.

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II. WHAT EXACTLY IS DEEPENING INSOLVENCY? TRACING ITS ROOTS

Deepening insolvency is a developing theory that is generally described as “an injury to the Debtors’ corporate property from the fraudulent expansion of corporate debt and prolongation of corporate life.”¹ The first case to discuss the general concept of deepening insolvency was *Bloor v. Dansk* (*In re Investors Funding Corporation of New York Securities Litigation*).² In *Investors Funding*, the plaintiff brought a cause of action against the debtor’s auditors for, among other things, committing fraud on the debtor.³ The defendants argued that any fraud perpetrated actually benefited the debtor by allowing the debtor to continue operations three years past the point of insolvency.⁴ The court rejected this argument, however, noting that “[a] corporation is not a biological entity for which it can be presumed that any act which extends its existence is beneficial to it.”⁵

The second case that helped spark the discussion of deepening insolvency came a few years later. In *Schacht v. Brown*,⁶ the Director of Insurance of the State of Illinois, as statutory liquidator of Reserve Insurance Company (“Reserve”), brought an action against Reserve’s former directors and officers, as well as other related defendants.⁷ As the court noted:

The main focus of the allegations is that, as a result of the fraudulent actions of the various defendants, Reserve’s corporate parent was caused to continue Reserve in business even though the latter was insolvent[] and was caused to saddle Reserve with additional liabilities and drive it deeper into insolvency, all of which consequences resulted in damage to Reserve, as well as its policyholders and creditors⁸

The court recognized that the actions of Reserve’s directors, among other parties, led to Reserve continuing in business “past the point of insolvency”⁹ The defendants’ response was that by virtue of Reserve remaining in business beyond insolvency and to the detriment of the creditors, Reserve actually benefited.¹⁰ The court did not find this argument persuasive in the least, however, stating that “the prolonged artificial insolvency

1. Official Comm. of Unsecured Creditors v. R.F. Lafferty & Co., 267 F.3d 340, 347 (3d Cir. 2001).

2. 523 F. Supp. 533 (S.D.N.Y. 1980).

3. *See id.* at 541 (discussing cause of action).

4. *See id.* (same).

5. *Id.*

6. 711 F.2d 1343 (7th Cir. 1983).

7. *Id.* at 1343.

8. *Id.* at 1345.

9. *Id.* at 1348.

10. *See id.* at 1348 (discussing defendants’ argument). “These defendants argue that, since Reserve was a wholly-owned subsidiary of ARC, the owners of Reserve, i.e. ARC shareholders, automatically benefited from the direct draining of Reserve and the fraudulent prolongation of Reserve’s life.” *Id.* at n.4.

of Reserve benefited only Reserve's managers and the other alleged conspirators, not the corporation."¹¹

The defendants also argued that the plaintiff lacked standing to sue on behalf of the corporation, and they cited to several cases to support the proposition that "a corporation may never sue to recover damages alleged to have resulted from the artificial prolongation of an insolvent corporation's life."¹² The court rejected this argument as well, stating that it would not speculate whether the Illinois state courts would accept such a restriction on the plaintiff's action.¹³ The court reasoned as follows:

[E]ach of these cases rests upon a seriously flawed assumption, *i.e.*, that the fraudulent prolongation of a corporation's life beyond insolvency is automatically to be considered a benefit to the corporation's interests. This premise collides with common sense, for the corporate body is ineluctably damaged by the deepening of its insolvency through increased exposure to creditor liability. Indeed, in most cases, it would be crucial that the insolvency of the corporation be disclosed, so that shareholders may exercise their right to dissolve the corporation in order to cut their losses. Thus, acceptance of a rule which would bar a corporation from recovering damages due to the hiding of information concerning its insolvency would create perverse incentives for wrong-doing officers and directors to conceal the true financial condition of the corporation from the corporate body as long as possible. We are not prepared to conclude that the Illinois courts would adopt such a regime.¹⁴

11. *Id.* at 1348.

12. *Id.* at 1349-50. Three of the cases the defendants cited were *Bergeson v. Life Insurance Corporation*, 265 F.2d 227, 232 (10th Cir. 1959), *Kinter v. Connolly*, 81 A. 905, 905 (Pa. 1911) and *Patterson v. Franklin*, 35 A. 205, 206 (Pa. 1896). In *Bergeson*, the plaintiffs alleged that the corporation was harmed because the defendants initially asserted that subscription notes had value and then later acknowledged that the notes did not have value. 265 F.2d at 232. The court stated that "[t]he situation may cause one to lift a querulous eyebrow but it does so because the company received a benefit, not because the company suffered any detriment." *Id.* In *Kinter*, the Court stated:

If the defendants published statements which they knew, or ought to have known, to be false, with the result that their company gained a fictitious credit at the expense of those thus encouraged to do business with it, the wrong was suffered by the latter, and not by the corporation, and gave rise to no liability on the part of the defendants that the corporation or its receiver can enforce.

81 A. at 905 In *Patterson*, the Court held that while parties who were affected by the fraud perpetuated by the defendants had cause to complain, the corporation itself could not complain. 35 A. at 206. After all, "[t]he fraud was perpetuated for its benefit. It was a gainer, not a loser, because of it." *Id.*

13. See *Schacht v. Brown*, 711 F.2d 1343, 1350 (7th Cir. 1983) ("This premise collides with common sense, for the corporate body is ineluctably damaged by the deepening of its insolvency, through increased exposure to creditor liability.").

14. *Id.* (citations omitted).

It was through this language that the court opened the door for causes of action against directors and officers who prolong the life of a corporation and thereby drive the corporation deeper into debt.

III. THE THIRD CIRCUIT'S FIRST INTERPRETATION OF THE DEEPENING INSOLVENCY THEORY

The next seminal case in the development of the cause of action of deepening insolvency after *Schacht* was the Third Circuit's decision in *Official Committee of Unsecured Creditors v. R.F. Lafferty & Co.*¹⁵ In *Lafferty*, the Third Circuit addressed whether deepening insolvency should be recognized as an independent tort.¹⁶ The plaintiff, a committee of creditors, filed its complaint against numerous parties, including the debtors and the debtors' principals.¹⁷ In the complaint, the plaintiff alleged that the defendants caused the debtors' deepening insolvency.¹⁸ In addressing the question of "[w]hether deepening insolvency is a valid theory that gives rise to a cognizable injury under state law," the court noted that neither the Pennsylvania appellate courts nor any federal courts interpreting Pennsylvania law had yet addressed the issue of deepening insolvency and whether it was a viable independent cause of action.¹⁹ The court, therefore, looked to the policy that underlies Pennsylvania tort law and decisions that have interpreted the law of other jurisdictions with regard to deepening insolvency.²⁰ The court concluded that, "if faced with the issue, the Pennsylvania Supreme Court would determine that 'deepening insolvency' may give rise to a cognizable injury."²¹

The Third Circuit based its finding on the following:

First and foremost, the theory is essentially sound. Under federal bankruptcy law, insolvency is a financial condition in which a cor-

15. 267 F.3d 340 (3d Cir. 2001).

16. *See id.* at 350-52 (discussing tort of deepening insolvency and challenges raised by defendant).

17. *See id.* at 344 (setting forth factual and procedural background of case). The debtors were two related companies, namely Walnut Associates, Inc. and ELCOA. *See id.* ELCOA was formed by Walnut's principals after Walnut began experiencing financial difficulties. *See id.* ELCOA was wholly owned by Walnut. *See id.* The committee alleged in its lawsuit that the defendants fraudulently induced the debtors to issue debt certificates, thereby deepening the debtors' insolvency and forcing the debtors into bankruptcy. *See id.* at 344-45. The defendants filed a motion to dismiss, and the district court granted the motion, finding that the defendants had a complete *in pari delicto* defense. *See id.* at 346. The committee then appealed. *See id.*

18. *Id.* at 344-45 (arguing that defendants "deepened the insolvency of Walnut and ELCOA, and put them on the path to bankruptcy").

19. *Id.* at 349. The court, therefore, recognized that it "must don the soothsayer's garb and predict how that court would rule if it were presented with the question." *Id.*

20. *See id.* (determining whether Pennsylvania courts would recognize deepening insolvency as cause of action).

21. *Id.*

poration's debts exceed the fair market value of its assets. Even when a corporation is insolvent, its corporate property may have value. The fraudulent and concealed incurrence of debt can damage that value in several ways. For example, to the extent that bankruptcy is not already a certainty, the incurrence of debt can force an insolvent corporation into bankruptcy, thus inflicting legal and administrative costs on the corporation Aside from causing actual bankruptcy, deepening insolvency can undermine a corporation's relationships with its customers, suppliers[] and employees. The very threat of bankruptcy, brought about through fraudulent debt, can shake the confidence of parties dealing with the corporation, calling into question its ability to perform, thereby damaging the corporation's assets, the value of which often depends on the performance of other parties. In addition, prolonging an insolvent corporation's life through bad debt may simply cause the dissipation of corporate assets.²²

In addition, the Third Circuit noted the increasing acceptance of the theory of deepening insolvency and highlighted the venerable principle of Pennsylvania jurisprudence that "where there is an injury, the law provides a remedy."²³ In light of this "remedial theme," the Third Circuit found that the Pennsylvania Supreme Court would recognize deepening insolvency as an independent tort giving rise to a cognizable injury.²⁴

22. *Id.* at 349-50 (citations omitted).

23. *Id.* at 351.

24. *Id.* at 352. It should be noted that, despite recognizing the independent tort of deepening insolvency, the Third Circuit dismissed the plaintiff's claim because of the *in pari delicto* defense. *See id.* at 354. After determining that the plaintiff had standing to bring its deepening insolvency claims, the Third Circuit analyzed the defendant's asserted *in pari delicto* defense. *See id.* at 354-60 (addressing defendant's defense to deepening insolvency claim). The court first explained that "[t]he doctrine of *in pari delicto* provides that a plaintiff may not assert a claim against a defendant if the plaintiff bears fault for the claim." *Id.* at 354. As such, the plaintiff is barred from asserting such a claim. *See id.* Whether the defendant may validly assert such a defense depends on whether the wrongdoer's conduct can be imputed to the debtor and, consequently, the plaintiff who stands in the shoes of the debtor. *See id.* at 355.

In analyzing whether the wrongdoer's conduct can be imputed to the plaintiff, the court first set forth the principle that "courts impute the fraud of an officer to a corporation when the officer commits the fraud (1) in the course of his employment[] and (2) for the benefit of the corporation." *Id.* at 358. The court quickly found that the fraud committed by the defendants did in fact take place in the course of their employment with the debtors. *See id.* at 359. With regard to the second requirement, the court noted that this question is typically analyzed under the adverse interest exception. *See id.* Under the adverse interest exception, "fraudulent conduct will not be imputed if the officer's interests were adverse to the corporation and 'not for the benefit of the corporation.'" *Id.* (citing *Waslow v. Grant Thornton L.L.P. (In re Jack Greenberg, Inc.)*, 212 B.R. 76, 83 (Bankr. E.D. Pa. 1997)). As the court noted, however, the adverse interest exception has an exception itself: the "sole actor" exception. *See id.* at 359. The sole actor exception states that "if an agent is the sole representative of a principal, then that agent's

IV. A SURVEY OF RECENT DEEPENING INSOLVENCY CASES: INDEPENDENT CAUSE OF ACTION, MEASURE OF DAMAGES OR NEITHER?²⁵

In the recent years since the *Lafferty* decision, several courts have addressed the validity of the concept of deepening insolvency. The courts that have addressed this concept are divided over whether deepening insolvency is an independent cause of action, a measure of damages for an independent tort or neither. The majority of courts finding deepening insolvency to be an independent cause of action hold that, to be successful, the moving party must demonstrate that the defendants engaged in fraudulent conduct and, therefore, committed an intentional tort. The minority of courts, on the other hand, hold that a party can succeed in bringing a deepening insolvency claim by showing that the defendant either engaged in negligent conduct or negligently failed to act.

A. *Deepening Insolvency as an Independent Cause of Action*

The courts that have recognized deepening insolvency as an independent cause of action have followed one of two paths, with the majority view requiring an additional showing of fraudulent conduct. Specifically, the elements of the majority view are: (1) the fraudulent or wrongful prolongation of an insolvent business entity's life; (2) that causes the entity to become more insolvent by incurring additional liabilities or dissipating assets; (3) so that the value that could have been realized if the entity's business activity had not been improperly prolonged is lost; and (4) as a result, the entity suffers harm distinct from the harm suffered by its creditors. In contrast, the elements of the minority view are: (1) a party engaged in a negligent act or negligently failed to act; (2) the act prolonged the life of the insolvent entity or allowed it to take on additional debt; and (3) as a result, the entity suffered harm distinct from the harm suffered by its creditors.

1. *Intentional Tort — Fraud Required*

Following in the footsteps of the Third Circuit in *Lafferty*, the United States Bankruptcy Court for the District of Delaware held in *Official Committee of Unsecured Creditors v. Credit Suisse First Boston (In re Exide Technologies, Inc.)*²⁶ that the "Delaware Supreme Court would recognize a claim for

fraudulent conduct is imputable to the principal regardless of whether the agent's conduct was adverse to the principal's interest." *Id.* The court found that the sole actor exception applied because, among other factors, one of the wrongdoers was the sole shareholder of the debtors. *See id.* at 360. As a result, the Third Circuit affirmed the district court's dismissal of the plaintiff's cause of action. *See id.* (determining that defendant had complete defense to defendant's cause of action).

25. It must be noted that certain cases discussed in the survey have since been superceded by subsequent case law from the relevant state supreme court or court of appeals. These cases are included in the survey, however, to illustrate the development of deepening insolvency and the Third Circuit's impact in this area.

26. 299 B.R. 732 (Bankr. D. Del. 2003).

deepening insolvency when there has been damage to corporate property.²⁷ In reaching this conclusion, the court first noted that the Delaware Supreme Court had not yet addressed the issue of whether deepening insolvency is a valid tort.²⁸ The court then looked to the *Lafferty* opinion and agreed with the view of the Third Circuit that the theory of deepening insolvency is sound and that there is growing acceptance of the theory.²⁹ The court found that Delaware, like Pennsylvania, has adopted the principle that “the ‘function of a damage award in a civil litigation is to provide just and full compensation to a plaintiff who suffers injury or loss by reason of the conduct of the tortfeasor.’”³⁰ The court then predicted that the Delaware courts would recognize deepening insolvency as a valid cause of action.³¹

The United States Bankruptcy Court for the Middle District of Tennessee addressed the question of whether deepening insolvency is an independent intentional tort in *Limor v. Buerger (In re Del-Met Corp.)*.³² In *Del-Met*, one of the claims the trustee brought against the director and other defendants was a claim for deepening insolvency.³³ Tennessee courts had not yet addressed the issue, making it necessary for the court to determine “whether the Tennessee Supreme Court would recognize deepening insolvency as an actionable breach of duty.”³⁴ In its analysis, the Court reviewed the Third Circuit’s decision in *Lafferty* and found it to be “sound.”³⁵ As a result, the court concluded that “if presented with compelling facts, the Tennessee Supreme Court would recognize deepening insolvency as an actionable breach of duty to a corporation.”³⁶

Later that year, the District Court for the District of Delaware discussed deepening insolvency in *Stanziale v. Pepper Hamilton LLP (In re Student Finance Corporation)*.³⁷ In *Student Finance*, the Chapter 7 trustee brought an action against a number of defendants, including a law firm, an attorney and other related individuals.³⁸ In the second count, the trustee alleged that “all Defendants engaged in tortious conduct that caused

27. *Id.* at 752. It should be noted, as discussed below, that the Delaware Supreme Court has subsequently held that deepening insolvency is not a valid cause of action in Delaware. See *infra* text accompanying notes 91-97.

28. *Id.* at 751 (explaining that court “must predict how the Delaware Supreme Court would rule on the claim if such claim was presented to it”).

29. *Id.* at 751-52.

30. See *id.* (quoting *Maier v. Santucci*, 697 A.2d 747, 749 (Del. 1997)) (determining that deepening insolvency would be recognized by Delaware courts).

31. See *id.* (same).

32. 322 B.R. 781 (Bankr. M.D. Tenn. 2005).

33. See *id.* at 807 (discussing claims brought by trustee).

34. *Id.* at 813 (recognizing that court’s task was same task that Third Circuit had undertaken in *Lafferty*).

35. See *id.* at 815 (discussing *Lafferty*’s analysis of deepening insolvency).

36. *Id.*

37. 335 B.R. 539 (D. Del. 2005).

38. *Id.* at 545.

injury to SFC [the debtor] through the wrongful expansion of corporate debt and prolongation of corporate life beyond insolvency.”³⁹ The defendants responded that, among other things, the trustee failed to allege all necessary elements of a deepening insolvency claim and, in particular, failed to allege fraud with the required particularity.⁴⁰ The court agreed.⁴¹ In so finding, the court noted that while the Third Circuit in *Lafferty* did not specify the necessary elements of deepening insolvency, the Third Circuit “did state that ‘the Committee alleges an injury to the Debtors’ corporate property from the fraudulent expansion of corporate debt and prolongation of corporate life. This type of injury has been referred to as ‘deepening insolvency.’”⁴² Further, the court made reference to the fact that the United States District Court for the Eastern District of Pennsylvania had also concluded that fraud must be alleged for a deepening insolvency claim to stand.⁴³

A few months later, the Bankruptcy Court for the District of Delaware issued another deepening insolvency opinion in *OHC Liquidation Trust v. Credit Suisse First Boston (In re Oakwood Homes Corporation)*.⁴⁴ In *Oakwood*, the court was faced with a motion to dismiss in which one of the matters at issue was a deepening insolvency count.⁴⁵ The court first noted that North Carolina, New York or Delaware law applied.⁴⁶ The court, however, did not decide which law should apply because it believed the outcome would be the same under the laws of all three states.⁴⁷ In analyzing whether deepening insolvency is a valid theory under North Carolina, New York and Delaware law, the court first recognized that the highest courts in all three states—the Delaware Supreme Court, the North Carolina Supreme Court and the New York Court of Appeals—have not ruled on the validity of deepening insolvency as an independent cause of action.⁴⁸

39. *Id.* at 547-48.

40. *See id.* at 548 (discussing deepening insolvency count).

41. *See id.* (same). The court noted that a trustee must specifically “allege that the defendant defrauded the debtor.” *Id.* If the trustee only alleges that the defendant defrauded creditors, the trustee would lack standing to bring a deepening insolvency claim. *See id.* (noting that trustee may only bring cause of action for harms suffered by debtor). Specifically, the trustee

could not bring it under [11 U.S.C.] § 541 because it would not be a claim that the debtor could have brought on its own behalf as of the commencement of the case, nor could he bring it under [11 U.S.C.] § 544 because that section deals only with a trustee’s powers regarding avoidance actions and does not empower him to pursue tort claims.

Id. at 548-49.

42. *Id.*

43. *See id.* (noting requirement of fraud in deepening insolvency causes of action in cases out of District Court for Eastern District of Pennsylvania).

44. 340 B.R. 510 (Bankr. D. Del. 2006).

45. *See id.* at 527 (discussing procedural background of case).

46. *Id.*

47. *See id.* at 528 (discussing choice of law issues).

48. *See id.* at 528 (citing to cases that state that highest court of Delaware, North Carolina and New York have not yet ruled on validity of deepening insol-

While the court noted that the trend seems to be against recognition of deepening insolvency as a valid independent tort, the court ultimately held that Delaware, North Carolina and New York would all recognize it as such.⁴⁹ The court declined to follow the trend because it was bound by “what the Third Circuit would predict the state law was with regard to deepening insolvency as an independent tort.”⁵⁰ In light of *Lafferty*, the court held that Delaware, New York and North Carolina state courts would indeed recognize deepening insolvency as a valid cause of action.⁵¹

Once the court found that deepening insolvency is a valid cause of action, it then had to determine what elements the plaintiff must prove to sustain such a cause of action.⁵² The court noted that most courts within the Third Circuit that have addressed this issue have found that a showing of fraud is required.⁵³ In addition, the *Lafferty* court’s discussion of deepening insolvency was centered on fraud.⁵⁴ Therefore, the court found that a plaintiff is required to prove fraud, and not mere negligence, to sustain a deepening insolvency claim.⁵⁵

2. *Negligence is Sufficient to Sustain a Deepening Insolvency Cause of Action*

Despite the holding in the majority of cases that a plaintiff must allege fraud to maintain a deepening insolvency claim, a few courts have suggested that allegations of negligence are sufficient to support such a claim. For example, in *Tabas v. Greenleaf Ventures, Inc. (In re Flagship Healthcare, Inc.)*,⁵⁶ the court, after discussing the defendants’ alleged negligence, ac-

veny). The court did recognize, however, that several federal courts have attempted to predict how each of these states’ highest courts would come down on the issue. *See id.* (noting that these decisions, however, are “far from uniform”).

49. *See id.* at 528-29. “In the last few years, a growing number of federal courts have issued opinions strongly implying that deepening insolvency ought not be recognized as an independent tort.” *Id.* at 528. The court discussed *In re Global Services* as the case that sparked this trend. *See id.* (discussing *In re Global Services* and listing cases that have followed its reasoning).

50. *Id.* at 530-31.

51. *See id.* at 531 (noting that Delaware, North Carolina and New York “all adhere to the broad remedial themes discussed in *Lafferty*”).

52. *See id.* at 533-34 (noting that *Lafferty* did not determine elements that plaintiff must prove to sustain deepening insolvency cause of action). The court did, however, find that *Lafferty* offered guidance on the issue. *Id.*

53. *See id.* (noting that District Court of Delaware and District Court for Eastern District of Pennsylvania have both held that plaintiff must show fraud to sustain deepening insolvency cause of action).

54. *See id.* at 534 (recognizing defendant’s argument that court in *Lafferty* relied on case that “permitted recovery for mere negligence,” but noting that, “[d]espite this, *Lafferty* talks in terms of fraud”).

55. *See id.* (requiring that fraud, and not negligence, is required for deepening insolvency). The court noted that it is generally agreed that there are five elements of fraud: “‘a representation of material fact, falsity, scienter, reliance and injury.’” *Id.* “Furthermore, the fraudulent conduct must be suffered by the debtor—not merely an individual creditor.” *Id.* The court further noted that “the fraud alleged must be a harm to the corporation.” *Id.*

56. 269 B.R. 721, 728 (Bankr. S.D. Fla. 2001).

knowledge that deepening insolvency may be an independent cause of action.⁵⁷ The court noted that “[t]he financial hardships which possibly resulted from the increased insolvency were not necessarily forthcoming, and if it can be proven that they were a result of the increased insolvency, liability may be found.”⁵⁸ The court cited to *Lafferty* in holding that incurrance of additional debt after the debtor became insolvent “may provide a measure of damages recoverable by the Trustee.”⁵⁹

In *Smith v. Arthur Andersen LLP*,⁶⁰ the plaintiff alleged, among other things, that the defendants misrepresented “(not necessarily intentionally) the firm’s financial condition.”⁶¹ In response, the defendants argued that any harm that resulted from their actions was not an actionable harm to the debtor.⁶² The Ninth Circuit Court of Appeals, however, cited to *Lafferty* for the proposition “that ‘prolonging an insolvent corporation’s life through bad debt may’ dissipate corporate assets and thereby harm the value of corporate property.”⁶³ Thus, the court concluded that the complaint stated a cognizable harm to the debtor in alleging that the defendants artificially prolonged the debtor’s existence.⁶⁴

In *In re LTV Steel Company*,⁶⁵ a group of potential claimants asked the United States Bankruptcy Court for the Northern District of Ohio to grant its motion requesting permission to prosecute its complaint.⁶⁶ The court

57. *Id.* at 728 (granting, in case brought by trustee against financial advisor corporation and employees for negligence in valuing acquired companies, possibility of deepening insolvency as valid cause of action under Florida law).

58. *Id.* The court likened the deepening insolvency of a corporation to a boxer’s situation. In a colorful analogy, the court stated the following:

To utilize judicial/artistic license, the Debtor’s situation was not like an individual who sits in the rain all day and simply cannot get more wet. It is more akin to a boxer with one black eye who, despite being injured, might still persevere and win the fight. If that boxer (the debtor) winds up losing the fight and landing in the hospital (bankruptcy court), a doctor (judge) might find that it was the additional injuries (deepening insolvency) which put him there.

Id. at n.4.

59. *Id.* at 728 (applying rule from *Lafferty* to case before Bankruptcy Court).

60. 421 F.3d 989 (9th Cir. 2005) (recognizing deepening insolvency as valid claim in case involving defendants accused of keeping insolvent corporation afloat for extended period despite knowledge that it rightfully should have declared bankruptcy).

61. *Id.* at 995 (reiterating facts stated in complaint).

62. *See id.* at 1003 (noting defendant’s argument that any harm was harm to debtor’s creditors; therefore, trustee, standing in debtor’s shoes, could not bring cause of action based on this harm).

63. *Id.* at 1004 (quoting Official Comm. of Unsecured Creditors v. R.F. Lafferty & Co., 267 F.3d 340, 350 (3d Cir. 2001)).

64. *See id.* (concluding that corporation is harmed by party who prolongs its existence).

65. 333 B.R. 397 (Bankr. N.D. Ohio 2005) (recognizing deepening insolvency as valid claim in case between corporation’s bankruptcy estate and corporation accused of incurring unnecessary debt and devaluing assets to the detriment of its creditors).

66. *Id.* at 402-03.

granted the group's motion, allowing them to prosecute their complaint, which included one count alleging that,

As a proximate result of the grossly negligent, reckless and/or bad faith prolongation of the Debtor's existence, Defendants' actions caused the Debtor to sink deeper into insolvency by incurring additional liabilities. . . . As a proximate result of the negligent prolongation of the Debtor's existence and deepening insolvency, the value of the Debtor's business that could have been realized had the corporation's existence not been prolonged was lost⁶⁷

Thus, the court appeared to say that a plaintiff can sustain a deepening insolvency claim based on negligence.

B. *Deepening Insolvency as a Measure of Damages*

There are some courts that recognize deepening insolvency as a measure of damages for a separate tort, as opposed to an independent tort in and of itself. For example, in *Kittay v. Atlantic Bank of New York (In re Global Service Group LLC)*,⁶⁸ the United States Bankruptcy Court for the Southern District of New York weighed in on the theory of deepening insolvency. In addressing this theory, the court first noted that some courts have recognized deepening insolvency as an independent tort, while others have recognized it as a theory of damages.⁶⁹ The court also noted that those decisions discussing New York's acceptance of the theory of deepening

67. *Id.* at 421. While all of the cases discussed above deal with whether or not deepening insolvency is a valid independent tort or theory of damages for conduct occurring pre-petition, the *LTV Steel* court addressed the validity of a deepening insolvency claim for conduct occurring post-petition. In addition to the allegations arising from pre-petition conduct, the plaintiff in *LTV Steel* also alleged:

In at least early September 2001, at the latest, LTV Steel's and LTV Corporation's directors and officers appear to have been aware that LTV Steel may soon be unable to pay its post[-]petition debts However, LTV Steel continued to incur additional trade debt which it either knew or should have known it could not pay in full

Id. at 403-04. As such, the plaintiff asserted a deepening insolvency claim for "artificially and wrongfully prolonging the corporation's existence through the incurring of spurious debt from at least September through November 20, 2001." *Id.* at 404. Since LTV Steel was a New Jersey corporation, the court reviewed the Third Circuit's decision in *Lafferty* and the Delaware Bankruptcy Court's decision in *Exide*. *See id.* at 422. Since both the *Lafferty* and *Exide* courts held that deepening insolvency is a valid cause of action, the *LTV Steel* court held that deepening insolvency arguably applies and, therefore, allowed the Plaintiff to pursue its deepening insolvency claim. *See id.* (discussing courts' growing acceptance of deepening insolvency theory).

68. 316 B.R. 451 (Bankr. S.D.N.Y. 2004) (declining to recognize deepening insolvency as independent cause of action under New York law in case between Trustee and lender whose loan to insolvent debtor allowed debtor to fall deeper into insolvency).

69. *See id.* at 457-58 (surveying courts' decisions addressing deepening insolvency).

insolvency regard deepening insolvency as a measure of damages.⁷⁰ The court concluded, however, that

The distinction between “deepening insolvency” as a tort or damage theory may be one unnecessary to make. Prolonging an insolvent corporation’s life, without more, will not result in liability under either approach. Instead, one seeking to recover for “deepening insolvency” must show that the defendant prolonged the company’s life in breach of a separate duty, or committed an actionable tort that contributed to the continued operation of a corporation and its increased debt.⁷¹

The court then noted that extending credit to an insolvent corporation cannot be a tort because, “if it was, most companies in financial distress would be forced to liquidate.”⁷² Along the same lines, the court rejected the notion that “managers of an insolvent limited liability company are under an absolute duty to liquidate the company”⁷³ Therefore, the court concluded that deepening insolvency can be a measure of damages when the plaintiff adequately demonstrates that the defendant committed a separate tort.

In *Official Committee of Unsecured Creditors of VarTec Telecom, Inc. v. Rural Telephone Finance Cooperative (In re VarTec Telecom, Inc.)*,⁷⁴ the court addressed the question of “whether ‘deepening insolvency’ may be pled as a separate cause of action or whether it is treated only as a breach of a separate duty under state tort law or as a theory of damages.”⁷⁵ After acknowledging that other courts have recognized deepening insolvency as a separate cause of action, the court noted that

The words “deepening insolvency” are neither contained in the Bankruptcy Code, nor do they arise from other federal law, so the courts that consider the theory of “deepening insolvency” to

70. See *id.* at 458 (citing to New York deepening insolvency cases).

71. *Id.* (finding that independent cause of action for deepening insolvency, without breach of separate duty, such as fraud, is not supported by case law of New York and other jurisdictions).

72. *Id.* at 459 (finding that type of loan issued in case was issued based on strength of relationship between defendant bank and insider defendants, which “is neither surprising nor improper”).

73. *Id.* The court discussed the fact that “there is no absolute duty under American law to shut down and liquidate an insolvent corporation,” as is the case in some foreign jurisdictions. *Id.* at 460. “In fact, chapter 11 is based on the accepted notion that a business is worth more to everyone alive than dead.” *Id.*

74. 335 B.R. 631 (Bankr. N.D. Tex. 2005) (refusing to recognize independent tort for deepening insolvency under Texas law in case between corporation’s unsecured creditors and secured creditors accused of making loans to debtor corporation, despite debtor’s apparent financial decline).

75. *Id.* at 633 (stating sole issue before court).

be an actionable tort do so by predicting how their respective state courts would rule when adopting a new cause of action.⁷⁶

As such, the court looked to Texas law and, after a long discussion about the origins and development of the theory of deepening insolvency, concluded that the Texas Supreme Court would not recognize deepening insolvency as a separate tort “because the injury caused by the deepening of a corporation’s insolvency is substantially duplicated by torts already established in Texas.”⁷⁷ Although the *VarTec* court refused to recognize deepening insolvency as an independent tort, the court seemed to indicate that deepening insolvency is a valid theory for damages.⁷⁸ Specifically, the court noted that “as the case law in this area has shown, for a plaintiff to assert a valid claim for damages under a theory of ‘deepening insolvency’ the plaintiff must show that the defendant has committed some other tort.”⁷⁹

In *Alberts v. Tuft (In re Greater Southeast Community Hospital Corp. I)*,⁸⁰ the court revisited its earlier opinion finding that a corporation’s deepening insolvency can be harmful.⁸¹ The court, however, rejected the distinction made by some courts between fraud and negligence, noting that it is not “aware of any common law principle holding that an injury sustained as a result of one tort (fraud) is somehow not an injury when it is caused by a different tort (negligence).”⁸² As a result, the court held that “[u]nless and until this court is told differently by a higher court in its own circuit, deepening insolvency will remain a viable theory of damages in this jurisdiction regardless of whether the injury occurred as a result of negligence or fraud.”⁸³

Another case to address deepening insolvency was *Amato v. Southwest Florida Heart Group, P.A. (In re Southwest Florida Heart Group, P.A.)*.⁸⁴ In this case, the court concluded that, with regard to the trustee’s deepening insolvency claim, “such issues will be relevant to the measure of damages only[] and cannot constitute a viable claim in its own right.”⁸⁵

76. *Id.* at 638-39.

77. *Id.* at 644.

78. *See id.* at 645 (explaining potential for recovering damages for deepening insolvency).

79. *Id.* at 644.

80. 353 B.R. 324 (Bankr. D.D.C. 2006) (recognizing deepening insolvency as theory of harm, and not as independent tort, in case involving corporate officers accused of enabling debtor corporation to incur more debt as part of Ponzi scheme).

81. *See id.* at 336 (discussing *CitX*’s potential impact on court’s opinion).

82. *Id.* at 337.

83. *Id.* at 338.

84. 346 B.R. 897, 898 (Bankr. M.D. Fla. 2006) (refusing to recognize independent cause of action for deepening insolvency under Florida law).

85. *Id.* at 898.

C. *Deepening Insolvency – A Legal Fiction*

Recently, there have been a few courts that have outright rejected the concept of deepening insolvency altogether. For example, in *Coroles v. Sabey*,⁸⁶ the Utah Court of Appeals stated, “We decline Plaintiffs’ invitation to recognize ‘deepening insolvency,’ the only theory of damages that Plaintiffs argue on appeal, as sufficient damages. Although deepening insolvency might harm a corporation’s shareholders, it does not, without more, harm the corporation itself.”⁸⁷

In *Bondi v. Bank of America Corporation (In re Parmalat)*,⁸⁸ the United States District Court for the Southern District of New York, analyzing North Carolina law, dismissed the deepening insolvency claim on the basis that it was duplicative.⁸⁹ The court reasoned that the cause of action for breach of fiduciary duties will cover any damages for prolonging the life of an insolvent corporation.⁹⁰

Recently, one of the most influential courts in the country, the Chancery Court in Delaware, weighed in on this issue of deepening insolvency. In *Trenwick American Litigation Trust v. Ernst & Young, L.L.P.*,⁹¹ Vice Chancellor Strine issued a decision concluding that Delaware would not recognize deepening insolvency as a viable cause of action.⁹² This decision is particularly important because so many corporations are incorporated in Delaware, and Delaware law governs the question of whether deepening insolvency is a valid cause of action for corporations incorporated in that state. Vice Chancellor Strine thoughtfully reviewed all of the relevant decisions of other courts and concluded that the well-established body of

86. 79 P.3d 974 (Utah Ct. App. 2003) (rejecting deepening insolvency as theory of damages under Utah law in case involving investors in failed corporation and those who gave them allegedly fraudulent information and financial support during formation of corporation).

87. *Id.* at 983 (affirming trial court’s dismissal of claim).

88. 383 F. Supp. 2d 587 (S.D.N.Y. 2005) (refusing to recognize deepening insolvency as valid claim for damages under North Carolina law in case involving Italian corporation’s Extraordinary Commissioner, analog to American trustee, and lender bank accused of structuring transactions that defrauded corporation and its debtors).

89. *See id.* at 602 (rejecting deepening insolvency as independent cause of action).

90. *See id.* at 601-02 (“If officers and directors can be shown to have breached their fiduciary duties by deepening a corporation’s insolvency, and the resulting injury to the corporation is cognizable . . . , that injury is compensable on a claim for breach of fiduciary duty.”).

91. 906 A.2d 168 (Del. Ch. 2006).

92. *See id.* at 174-75 (rejecting concept of deepening insolvency, court stated that “so long as directors are respectful of the corporation’s obligation to honor the legal rights of its creditors, they should be free to pursue in good faith profit for the corporation’s equity holders”). The court went on to say that “Even when the firm is insolvent, directors are free to pursue value maximizing strategies, while recognizing that the firm’s creditors have become its residual claimants and the advancement of their best interests has become the firm’s principal objective.” *Id.* at 175.

fiduciary responsibility law in Delaware was well-equipped to deal with issues of directors' responsibility.⁹³ Thus, the court reasoned, to adopt the cause of action of deepening insolvency would be inconsistent with the directors' fiduciary duties to pursue value-maximizing strategies, as the existing scope of fiduciary duty law and the business judgment rule make clear that directors are to be insulated from liability for decisions that simply turn out badly.⁹⁴ As the court noted:

If the board of an insolvent corporation, acting with due diligence and good faith, pursues a business strategy that it believes will increase the corporation's value, but that also involves the incurrence of additional debt, it does not become a guarantor of that strategy's success. That the strategy results in continued insolvency and an even more insolvent entity does not in itself give rise to a cause of action. Rather, in such a scenario the directors are protected by the business judgment rule. To conclude otherwise would fundamentally transform Delaware law.⁹⁵

On August 14, 2007, the Delaware Supreme Court affirmed the Delaware Chancery Court's decision in *Trenwick*.⁹⁶ The opinion consisted of the following ruling:

This 14th day of August 2007, the Court, having considered this matter after oral argument and on the briefs and supplemental memoranda filed by the parties, has determined that the final judgment of the Court of Chancery should be affirmed on the basis of and for the reasons assigned by the Court of Chancery in its opinion dated August 10, 2006.⁹⁷

Although the Delaware Court of Chancery and the Delaware Supreme Court have not specifically discussed the concept of deepening insolvency as a measure of damages, it is unlikely that either would accept this concept in light of their *Trenwick* rulings.

In one of the most recent cases to address deepening insolvency, *Schnelling v. Crawford (In re James River Coal Company)*,⁹⁸ the court con-

93. See *id.* at 204-07 (explaining that Delaware law offers alternative avenues of relief for plaintiffs). The court stated that "The rejection of an independent cause of action for deepening insolvency does not absolve directors of insolvent corporations of responsibility. Rather, it remits plaintiffs to the contents of their traditional toolkit, which contains, among other things, causes of action for breach of fiduciary duty and for fraud." *Id.* at 205.

94. See *id.* at 204-05.

95. *Id.* at 205.

96. See *Trenwick Am. Litig. Trust v. Billett*, No. 495, 2006, 2007 Del. LEXIS 357 (Del. Aug. 14, 2007).

97. *Id.* at *1.

98. 360 B.R. 139 (Bankr. E.D. Va. 2007) (rejecting deepening insolvency as independent cause of action under Virginia law in case involving liquidating trust and former directors accused of conducting transactions with shareholders prolonging corporation's apparent insolvency).

cluded that deepening insolvency is not a viable cause of action under Virginia law.⁹⁹ The court first noted that the Virginia Supreme Court has yet to decide whether deepening insolvency is a valid independent tort.¹⁰⁰ As such, the court was required to predict how the Virginia Supreme Court would rule on this issue.¹⁰¹ The court traced the roots of the deepening insolvency theory and noted that some courts have found deepening insolvency to be an independent tort, while others have found it to only be a measure of damages.¹⁰² In rejecting the theory of deepening insolvency altogether, the court cited to *Trenwick* and concluded that to recognize such a theory “would fundamentally transform Virginia law. . . .”¹⁰³

V. *SEITZ v. DETWEILER, HERSHEY AND ASSOCIATES, P.C. (IN RE CITX CORPORATION)*: THE THIRD CIRCUIT SETS STRICT BOUNDARIES FOR DEEPENING INSOLVENCY

The Third Circuit addressed the theory of deepening insolvency for the second time in *Seitz v. Detweiler, Hershey & Associates, P.C. (In re CitX Corporation)*.¹⁰⁴ In *CitX*, the Third Circuit specifically discussed three questions: (1) is deepening insolvency a viable theory of damages for negligence; (2) is negligence sufficient to support a deepening insolvency

99. *See id.* at 179.

100. *See id.* at 178 (analyzing other states' acceptance or rejection of deepening insolvency theory).

101. *See id.* (“When questions of state law which have not been addressed by the highest or intermediate appellate courts of the state are presented to a federal court, the law requires the federal court to forecast what the state supreme court would hold if it were presented with the issue.”).

102. *See id.* at 178-80 (surveying courts that have weighed in on theory of deepening insolvency).

103. *Id.* at 179. In so concluding, the court echoed the sentiment of the Delaware Chancery Court:

No court applying Virginia law has ever recognized an independent cause of action premised solely upon a company's economic decline. Virginia law does not require a financially challenged company to abruptly windup [sic] its business affairs and liquidate its assets. The Board of Directors must remain free to exercise its good faith business judgment that will allow it to pursue strategies the board views as sound to turn the company around.

Id. (footnote omitted).

104. 448 F.3d 672 (3d Cir. 2006). The debtor was an internet company that filed for bankruptcy protection, and it was alleged that it was involved in a Ponzi scheme. *See id.* at 674-76 (discussing background of case). The trustee filed a complaint in bankruptcy court against the Debtor's accounting firm and an individual partner of the accounting firm alleging malpractice, deepening insolvency, breach of fiduciary duty and negligent misrepresentation. *See id.* The reference to the bankruptcy court was withdrawn, and the district court initially granted summary judgment to the defendants on the negligent misrepresentation claim. *See id.* The district court eventually granted the defendants' motion for summary judgment on the negligence and deepening insolvency claims and the Trustee appealed to the Third Circuit. *See id.*

cause of action; and (3) can deepening insolvency be a cause of action under 11 U.S.C. §§ 544 or 541.¹⁰⁵

With regard to the first issue, the court looked to the definition of deepening insolvency set forth in *Lafferty* and found that,

Although we did describe deepening insolvency as a “type of injury,” and a “theory of injury,” we never held that it was a valid theory of damages for an independent cause of action. Those statements in *Lafferty* were in the context of a deepening[]insolvency *cause of action*. They should not be interpreted to create a novel theory of damages for an independent cause of action like malpractice.¹⁰⁶

The court then addressed the issue of whether negligence is sufficient to support a deepening insolvency cause of action. The court was faced with this issue because the trustee brought a cause of action for deepening insolvency but did not provide any support for a claim of fraudulent conduct.¹⁰⁷ “Without fraud, Seitz [Trustee] must fall back on his allegation that [defendant] negligently deepened CitX’s insolvency.”¹⁰⁸ The court then analyzed whether negligence can support a claim for deepening insolvency and noted that *Lafferty* held only that fraudulent conduct, and not negligence, can support a deepening insolvency claim.¹⁰⁹ The court held that “We know no reason to extend the scope of deepening insolvency beyond *Lafferty*’s limited holding. To that end, we hold that a claim of negligence cannot sustain a deepening[]insolvency cause of action.”¹¹⁰

With regard to the third issue, the Third Circuit held that a deepening insolvency claim cannot be brought under 11 U.S.C. § 544: “Because deepening[]insolvency claims are brought on behalf of the debtor corporation, deepening insolvency can only be a claim under Bankruptcy Code § 541 (which deals with property of the debtor’s estate).”¹¹¹ In so finding, the Third Circuit clarified that the cause of action of deepening insolvency does not belong to the creditors of the corporation.¹¹²

105. *See generally id.*

106. *Id.* at 677 (internal citations omitted).

107. *See id.* at 680 (determining whether allegation of negligence can sustain deepening insolvency claim).

108. *Id.* (stating issue after having dismissed possibility of Trustee alleging fraud on part of defendants).

109. *See id.* at 681 (limiting *Lafferty* holding to fraudulent conduct).

110. *Id.* (refusing to find claim of negligence sufficient to sustain cause of action for deepening insolvency, given limit of *Lafferty*).

111. *Id.* at 676 n.6. (internal citations omitted).

112. *Id.* (explaining that Section 544 only implicates trustee’s avoidance powers for benefit of creditors and purchasers).

VI. IMPACT: THE FUTURE OF DEEPENING INSOLVENCY OUTSIDE OF THE THIRD CIRCUIT

Just as the Third Circuit's opinion in *Lafferty* influenced courts across the country in answering the question of whether to embrace the concept of deepening insolvency, *CitX* will now have a similar, albeit opposite, impact. Courts that previously followed the reasoning of *Lafferty* and accepted the theory of deepening insolvency as a broad theory are now likely to revisit their positions when faced with a deepening insolvency case. Likewise, courts that were previously skeptical to follow the broad reasoning of *Lafferty* will welcome the *CitX* court's narrowing of the deepening insolvency theory and now cite to *CitX* for support in their dismissal or narrow acceptance of this theory. These conservative courts will likely find that, at the very least, a showing of fraud is required to sustain a cause of action under the theory of deepening insolvency.

The writing on the wall is clear: the trend of courts refusing to recognize deepening insolvency as a cause of action or as a measure of damages is the correct one and one that the supreme courts of the states within the Third Circuit—specifically Pennsylvania and New Jersey—are likely to eventually adopt. The Third Circuit started a chain reaction that will eventually eliminate any and all acceptance of deepening insolvency by recognizing, through its holding in *CitX*, that its holding in *Lafferty* was flawed.

Delaware has already eliminated deepening insolvency as an independent cause of action. As discussed above, the preliminary writing on the wall in Delaware came from the Delaware Court of Chancery, an influential court in the corporate world, which had refused to recognize deepening insolvency. Then, on August 14, 2007, the Delaware Supreme Court affirmed the Delaware Court of Chancery's *Trenwick* decision and permanently eliminated deepening insolvency as an independent cause of action in that state.¹¹³ The inevitable impact of the Delaware Supreme Court's ruling cannot be overstated. Because courts around the country dealing with corporate and bankruptcy law issues most often look to Delaware case law for guidance, courts will become even more skeptical of the deepening insolvency theory and refuse to adopt it or, at the very least, reevaluate their positions.

The impact of *Citx* and *Trenwick* has already become apparent in Pennsylvania. On September 20, 2007, the Common Pleas Court of Philadelphia, Pennsylvania issued a decision in which, among other things, it dismissed the trustee's count for deepening insolvency.¹¹⁴ In *Miller*, the plaintiffs argued that Pennsylvania law applied and the defendants argued that Delaware law applied to the question of whether the plaintiffs could

113. See *Trenwick Am. Litig. Trust v. Billett*, No. 495, 2006, 2007 Del. LEXIS 357 (Del. Aug. 14, 2007) (affirming decision of Court of Chancery against claim of deepening insolvency as independent cause of action).

114. *Miller v. Santilli*, No. 1225, 2007 Phila. C.P. LEXIS 252, at *10-13 (Phila. C.P. Sept. 20, 2007).

sustain a cause of action for deepening insolvency.¹¹⁵ The court, however, stated that there was no actual conflict of law since “neither state recognizes a cause of action for deepening insolvency.”¹¹⁶ In so noting, the court cited to the Chancery Court’s holding in *Trenwick* that there is no cause of action for deepening insolvency in Delaware.¹¹⁷ With regard to Pennsylvania, the court first noted that “no Pennsylvania state court has ever recognized a cause of action for deepening insolvency.”¹¹⁸ The court then cited to *CitX* and its narrowing of the *Lafferty* holding in finding that a plaintiff must demonstrate that the defendant engaged in fraudulent conduct to sustain a cause of action for deepening insolvency.¹¹⁹ After noting that it was not bound by a federal court’s interpretation of state law, the court ultimately went a step farther and held that “once the ultimate harm from an unrestrained deepening insolvency has been suffered and bankruptcy has occurred, traditional claims for fraud and breach of fiduciary duty, which ‘have been carefully shaped by generations of experience,’ are sufficient to recover for any wrongdoing.”¹²⁰

CitX and *Trenwick* are two of the most recent cases adding fuel to the flame that is engulfing the deepening insolvency theory and eliminating it altogether. These decisions from the Third Circuit and the Delaware Chancery and Supreme Courts have greatly influenced courts’ approaches to the theory. Because the Third Circuit helped shape and define deepening insolvency, and because the Delaware Chancery and Supreme Courts are perhaps the most influential courts in the country on corporate law issues, the fact that these courts have narrowed the acceptance of this theory is monumental. Furthermore, these courts are recognizing that directors and officers should be encouraged to take reasoned, calculated risks, regardless of the outcome, without fear of retribution in hindsight. The economy thrives and advances only in an environment where companies have an opportunity to explore means of greater success, which, in turn, provides a greater benefit to shareholders and/or creditors.

VII. CONCLUSION

It is clear that the debate among the courts and bankruptcy practitioners about the validity of deepening insolvency as a theory in general, and as a cause of action or measure of damages in particular, is still in the early stages. At least for the near future, however, practitioners in the Third Circuit have a relatively established framework within which to work. Specifically, when bringing a cause of action for deepening insolvency under Pennsylvania law, practitioners need to demonstrate that the

115. *Id.* at *10.

116. *Id.*

117. *See id.* at *11-12.

118. *Id.* at *12.

119. *See id.*

120. *Id.* at *13.

defendant(s) committed fraud that led to the artificial prolongation of the corporation's life; alleging mere negligence is not enough.¹²¹

Because deepening insolvency is a state law issue, practitioners who are working under Delaware law cannot bring a cause of action for deepening insolvency in light of the Delaware Supreme Court's affirming of the Delaware Chancery Court's *Trenwick* decision, which eliminated deepening insolvency as a cause of action in Delaware. As a result, the relief in the boardroom is that directors and officers may return to the business of advancing their companies' interests, rather than looking over their shoulders for the next lawsuit.

121. See *Stanziale v. Pepper Hamilton LLP (In re Student Fin. Corp.)*, 335 B.R. 539 (D. Del. 2005).