IN THE SUPREME COURT OF THE STATE OF NEVADA

ROBERT CHUR; STEVE FOGG; MARK GARBER; CAROL HARTER; ROBERT HURLBUT; BARBARA LUMPKIN; JEFF MARSHALL; AND ERIC STICKELS, Petitioners, *vs.* THE EIGHTH JUDICIAL DISTRICT COURT OF THE STATE OF NEVADA, IN AND FOR THE COUNTY OF CLARK; AND THE HONORABLE NANCY L. ALLF, DISTRICT JUDGE, Respondents, and COMMISSIONER OF INSURANCE FOR THE STATE OF NEVADA AS RECEIVER OF LEWIS AND CLARK LTC RISK RETENTION GROUP, INC., Real Party in Interest.	Supreme Court Case No.: 78301 District Court Case No.: A-14-711535-C **REAL PARTY IN INTEREST'S PETITION FOR REHEARING**

Nature of Proceeding: Petition for Writ of Mandamus
Court Below: Eighth Judicial District Court, Department XXVII
The Honorable Nancy Allf

Brenoch Wirthlin, Esq. – NV Bar No. 10282
Traci L. Cassity, Esq. – NV Bar No. 9648
HUTCHISON & STEFFEN
10080 W. Alta Dr., Suite 200
Las Vegas, Nevada 89145
702-385-2500 (Telephone) – 702-385-2086 (Facsimile)
Email: *bwirthlin@hutchlegal.com*
Attorneys for Real Party in Interest

Real Party in Interest, Commissioner of Insurance for the State of Nevada as Receiver of Lewis and Clark LTC Risk Retention Group, Inc. (the "Commissioner"), hereby files this petition for rehearing pursuant to NRAP 40.

I. INTRODUCTION

On February 27, 2020, the Court issued its Opinion and Writ ("Opinion") in this matter, instructing the Honorable Judge Allf to vacate the order denying Motion for Judgment on the Pleadings and enter a new order granting that Motion. *See* Opinion (20-07840). In rendering its Opinion, the Court applied the Business Judgment Rule ("BJR") to all allegations against the Directors[1] in the Third Amended Complaint ("TAC"). Rehearing is warranted because the Court misapplied the BJR with respect to allegations of Directors failing in their duty to be informed, abdicating their duties, and failing to make a business decision which would implicate the BJR.

Specifically, in the TAC, the Commissioner provided allegations and facts of non-business decisions, or inaction not constituting a decision, which are not protected by the BJR. The Court has overlooked the plain language of NRS 78.138, as well as its prior decisions, regarding the scope of the BJR, its applications as to non-statutory business decisions, and as to the duty of care and to be informed. As

[1] "Directors" shall refer to the Petitioners: Robert Chur, Steve Fogg, Mark Garber, Carol Harter, Robert Hurlbut, Barbara Lumpkin, Jeff Marshall and Eric Stickels.

a result of the misapplication of Nevada law, the Opinion has inappropriately broadened the scope of NRS 78.138, eradicated the duty of care and any claim for harm based on failure to make a business decision, and has created a standard incentivizing willful ignorance of Nevada corporations' directors and officers.

II. PETITION FOR REHEARING STANDARD

Under NRAP 40(c)(2), the Court may consider rehearing when "the court has overlooked or misapprehended a material fact in the record or a material question of law in the case," or "the court has overlooked, misapplied or failed to consider a statute, procedural rule, regulation or decision directly controlling a dispositive issue in the case." NRAP 40(c)(2); *see also Lavi v. Eighth Judicial Dist. Court*, 325 P.3d 1265, 1267 (Nev. 2014). Here, rehearing is warranted because the Opinion misapplied the BJR and overlooked controlling Nevada case law, including *In re Amerco Derivative Litig.*, 127 Nev. 196, 252 P.3d 681 (2011).

III. ANALYSIS

A. The Opinion misapplies the BJR and overlooks controlling law.

In issuing the Opinion, this Court cited NRS 78.138(3) indicating: "[t]he business judgment rule states that 'directors and officers, ***in deciding upon matters of business***, are presumed to act in good faith, on an ***informed*** basis and with a view to the interests of the corporation.'" *See* Opinion (20-07840), at pg. 7 (emphasis added). Further, this Court recognized that "[i]n Nevada, directors and officers owe

the fiduciary duties of care and loyalty to the corporation." *See* Opinion at p. 7. Yet, the Court then "disavow[ed] *Shoen* to the extent it implied a bifurcated approach to duty-of-care and duty-of-loyalty claims", concluding that "NRS 78.138(7) provides the **sole avenue** to hold directors and officers individually liable for damages arising from **official conduct**." *Id*. at p. 8 (emphasis added). Further, this Court stated that "in order to state a claim against the Directors individually, the Commissioner must allege facts that when taken as true (1) rebut the business judgment rule, and (2) constitute a breach of fiduciary duty involving 'intentional misconduct, fraud or a knowing violation of the law.'" *Id*. at p. 9.

What the Opinion overlooks is situations in which directors and officers **did not "decid[e] upon matters of business" but should have**. Did the Court intend to eradicate all liability for directors and officers that are so egregiously uninformed they are completely ignorant of the need to make a business decision? That is different than making a business decision to take no action. How can the BJR – which this Court specifically recognized protects directors and officers "***in deciding upon matters of business***" – protect directors *who did not decide upon matters of business*, despite the fiduciary duty of care requiring that they should have done so? Should the law in Nevada be so one-sided that it protects such an appalling violation of the fiduciary duty of care? Contrary to the Opinion, binding Nevada precedent says no.

In *In re Amerco Derivative Litig*., 127 Nev. 196, 222, n. 10, 252 P.3d 681, 700 (2011), this Court made that clear:

> Respondents contend that this court should affirm the district court's order because appellants have not overcome the presumption that respondents acted in good faith. Pursuant to Nevada's business judgment rule set forth in NRS 78.138, directors and officers benefit from the " 'presumption that in making a business decision [they] ... acted on an informed basis, in good faith and in the honest belief that the action taken was in the best interests of the company.' " *Shoen*, 122 Nev. at 632, 137 P.3d at 1178–79 (quoting Aronson, 473 A.2d at 812). ***However, the business judgment rule cannot be invoked by directors, where, as alleged here, they were not asked to consider the issue***, … ***nor can respondents rely on the business judgment rule as to directors Bayer, Carty, and Dodds when the board was not asked to consider the SAC entity transactions***.

127 Nev. at 222 (emphasis added, internal citation omitted); *see also Wynn Resorts, Ltd.*, 133 Nev. at 375 (recognizing the BJR only applies in the context of directors or officers "making a business decision"). Thus, based on Nevada law and controlling case law, the BJR is not invoked, and does not shield a director or officer from personal liability, if the director or officer does not "decide upon matters of business" when the situation warranted it. This includes the factual allegations set forth in the TAC in which the Directors abdicated their responsibilities or were not asked to consider issues that should have been considered, and otherwise breached their fiduciary duty of care due to ignorance, willful or otherwise. *See* NRS 78.138(3); *In re Amerco Derivative Litig.*, 127 Nev. at 222.

Stated another way, despite Nevada law being clear on this issue – that

directors and officers cannot hide behind the BJR when they failed to act due to improper ignorance or abdication – not because they made a business decision, but because they were so egregiously uninformed about the facts warranting a proper business decision – the Court misapplied it in the Opinion as to the TAC. *See* Opinion (20-07840), at pg. 12-13. This dismissed all claims against the Directors despite voluminous allegations relating to the Directors abdicating their duties, remaining willfully ignorant, and failing to make decisions when they should have, which cannot invoke the protections of the BJR.[2] As alleged in the TAC, no business decision could have been made by the Directors when they did not meet or consider an issue when they should have, did not inform themselves as required under NRS 78.138, or abdicated their duties:[3]

> 146. Even with the bad financial news in early October, 2011, the Board was indifferent to its legal obligations and did not meet again until December 20, 2011, over two and a half months later. …
>
> 155. Notwithstanding the dire financial issues, the Board remained indifferent to its legal obligations and did not meet again until April 30, 2012, almost three (3) months later. …
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> 158. On information and belief, the Board did not meet for another two and a half (2 ½) months regarding the financial conditions of L&C.

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[2] *See* TAC at ¶¶ 34, 57, 58, 59, 96, 97, 98, 99, 100, 105, 108, 112, 113, 117, 121, 122, 124, 125, 126, 129, 131, 134, 145, 146, 147, 148, 150, 153, 154, 155, 156, 158, 159, 163, 164, 170, 188, 189, 192, 193, 194, 219, 220, 221, 227, 228, 229, 231, 232, 236 and 238 of the Amended Complaint. *See* Petitioner's Appendix Vol. 1, at APP00037-84.

[3] *Id*.

> The Board met telephonically on June 6, 2012, the Minutes for which are attached hereto as Exhibit 30, but the only business noted was the approval of reinsurance. There is no entry regarding a discussion of the financial status of L&C.
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> 236. The Board's inaction severely prolonged the insurance actions of L&C that led to its initial insolvency and that then also increased its insolvency.

In such instances, under *Amerco*, the Directors are not protected from personal liability by the BJR, **because no business decision was made which could invoke the BJR**. The Directors should have acted in those instances, but due to their ignorance, failure to inform themselves and/or abdication of their duties, they did not. Yet, the Opinion would seem to suggest that such utter failures of the duty of care cannot be actionable on their own. Such a result overlooks the controlling authority referenced in *Amerco* which makes clear that the protections of the BJR are only implicated when directors "decided on matters of business", not when they made no decision but should have.

Thus, it was a misapplication of NRS 78.138 and controlling case law to dismiss the TAC as to all liability against the Directors. Accordingly, the Court should grant rehearing and reinstate the Commissioner's complaint against the Directors.

B. The Opinion incentivizes willful ignorance and eradicates the duty of care.

The Opinion relies upon the 10th Circuit Court's opinion in *In re ZAGG Inc.*

S'holder Derivative Action, 826 F.3d 1222 (10th Cir. 2016). Preliminarily, it should be noted by adopting this new standard from the 10th Circuit, the Court appears to have overlooked NRS 78.102(3) which holds that "[t]he plain meaning of the laws enacted by the Legislature in this title, including, without limitation, the fiduciary duties and liability of the directors and officers of a domestic corporation set forth in NRS 78.138 and 78.139, must not be supplanted or modified by laws or judicial decisions from any other jurisdiction."

Further, this Court cited NRS 78.138, indicating "the 'director's [sic] or officer's act or failure to act' must constitute "a breach of his or her *fiduciary duties*," and that breach must further involve "intentional misconduct, fraud or a knowing violation of the law." *See* Opinion (20-07840), at pg. 7 (citation omitted). This Court additionally mandated that the Commissioner "must establish that the director or officer had knowledge that the alleged conduct was wrongful". *Id*. at pg. 11-12.

Based on the foregoing, this Court's Opinion appears to have the unintended consequence of incentivizing directors and officers to remain willfully ignorant, as the Opinion appears to set up ignorance – willful or otherwise – as a complete defense to liability for a breach of the duty of care. Under the Opinion, directors and officers will argue that all directors or officers must prove is that they were so ignorant of the law, their duties, or the state of affairs of the company, that they had no idea what they were doing was wrong. Despite no business decision having been

made due to ignorance and abdication, under the Opinion requiring a "two-step analysis" and allegations of "intentional misconduct, fraud, or a knowing violation of the law", directors or officers will assert that all they need to prove to avoid liability for a breach of the duty of care is that they were so egregiously ignorant, they did not know they needed to act. In such a situation, directors and officers will argue that even willful ignorance would appear to be a complete defense to any liability under the Opinion.

This would effectively eradicate the duty of care. To be sure, the duty of care would still "exist", but in name only. If a plaintiff must plead and prove that – in addition to breaching the duty of care through abdication and willful ignorance – the director **also** committed "intentional misconduct, fraud or a knowing violation of the law", then effectively a breach of the duty of care, no matter how wrongful, is not actionable. Under that scenario, a director or officer would be free to be as egregiously uninformed and derelict in her duties of care as she wanted to be, secure in the knowledge that, so long as her conduct did not involve a "intentional misconduct, fraud or a knowing violation of the law", she could not be held personally liable.

The problem with this outcome is clear. The duty of care, by definition, is the "duty to act on an **informed** basis." *Shoen*, 137 P.3d at 1178. Thus, if a director is not acting "on an informed basis", his or her actions will necessarily not include the

scienter necessary to prove "intentional misconduct, fraud or a knowing violation of the law". But, that is the point. It is logically inconsistent for the Opinion to require that a plaintiff plead and prove a director or officer had the *scienter* required to prove their conduct involved "intentional misconduct, fraud, or a knowing violation of the law" in order to prove a breach of the duty of care which occurred through abdication and ignorance, as such an allegation will necessarily not include the *scienter* required for intentional conduct. Therefore, a breach of the duty of care would not be actionable absent a concurrent breach of the duty of loyalty.

Moreover, if a director or officer can only held liable if they willfully commit a wrongful act, they are incentivized to remain flagrantly uninformed in their capacity as director or officer—in violation of the duty of care—as this will ensure they did not "knowingly" commit a wrongful act. Thus, despite acknowledging the duty of care[4], by collapsing of the duty of care into the duty of loyalty, the Opinion permits a director or officer to avoid liability through reckless ignorance and total abdication of duties. Under the Opinion, knowledge can only bring liability. It certainly gives a new meaning to the phrase "ignorance is bliss."

Here, the TAC makes clear that in many instances the Directors were willfully

[4] This issue and the confusion created by it are further compounded by the fact NRS 78.138 creates a presumption that directors, in making business decisions, are presumed to act "on an informed basis." *See Wynn Resorts, Ltd.*, 399 P.3d at 342-43; and NRS 78.138(3).

ignorant and uniformed as to their duties, applicable legal requirements, and information relevant to board decisions; yet, in so doing, they will argue they are protected under the Opinion because that same willful ignorance affords them the assurance they do not have the *scienter* to have "knowingly" breached their fiduciary duty of care. Specifically, the Directors are alleged to have breached their duty of care and remained egregiously uninformed.[5] Such conduct is improper and a violation of the Directors' duty of care. However, the Opinion would seem to protect the Directors from these blatant, uninformed breaches of the duty of care.

The Opinion also fails to differentiate between reckless and willful ignorance. The Court should also clarify that willful ignorance rises to the level of *scienter* required under the new standard adopted in the Court's Opinion. The facts alleged in the TAC regarding the Directors' failure to act on an informed basis constitute willful ignorance on the part of the Board.[6] As such, the Court should grant the petition for rehearing.

IV. CONCLUSION

For the foregoing reasons, the Commissioner respectfully requests the Court grant the petition for rehearing in this case, vacate the Opinion and Writ entered on

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[5] *See* TAC at ¶¶ 99, 105, 117, and 145. *See* Petitioner's Appendix Vol. 1, at APP00037-84.

[6] *See* TAC at ¶¶ 59, 99, 105, 108, 113, 117, 122, 126, 134, 139, 145, 153, 154, 164, 165 and 170. *See* Petitioner's Appendix Vol. 1, at APP00037-84.

February 27, 2020, and grant such other and further relief as the Court deems proper.

DATED: *April 29, 2020*.

HUTCHISON & STEFFEN

By: */s/ Brenoch Wirthlin, Esq.*

Brenoch Wirthlin, Esq.
NV Bar No. 10282
Traci L. Cassity, Esq. – NV
NV Bar No. 9648
10080 W. Alta Dr., Suite 200
Las Vegas, Nevada 89145
Attorneys for Real Party in Interest

CERTIFICATE OF COMPLIANCE

I hereby certify that this Petition for Rehearing complies with the formatting requirements of NRAP 32(a)(4), the typeface requirements of NRAP 32(a)(5), and the type style requirements of NRAP 32(a)(6) because: It has been prepared in proportionally spaced typeface using Microsoft Word in 14-point Times New Roman font.

I further certify that this Petition complies with the length limitations NRAP 40(b)(3) because it does not exceed more than 4,667 words.

DATED: *April 29, 2020*.

HUTCHISON & STEFFEN

By: */s/ Brenoch Wirthlin, Esq.*
Brenoch Wirthlin, Esq.
NV Bar No. 10282
10080 W. Alta Dr., Suite 200
Las Vegas, Nevada 89145
Attorneys for Real Party in Interest

CERTIFICATE OF SERVICE

I, the undersigned, hereby certify that I electronically filed **Real Party in Interest's Petition for Rehearing** with the Clerk of Court for the Supreme Court of Nevada by using the Supreme Court of Nevada's E-filing system on *April 29, 2020*. Electronic service shall be made in accordance with the following service list:

J. Stephen Peek, Esq.
Jessica Whelan, Esq.
Ryan Semerad, Esq.
Holland & Hart, LLP
9555 Hillwood Dr., 2nd Floor
Las Vegas, Nevada 89134

Joseph P. Garin, Esq.
Angela T. Nakamura Ochoa, Esq.
Lipson Neilson, P.C.
9900 Covington Cross Dr., Suite 120
Las Vegas, Nevada 89144
Phone No.: (702) 382-1500
Attorneys for Appellants

A hard copy of **Real Party in Interest's Petition for Rehearing** has also been mailed to the following:

The Honorable Nancy L. Allf
District Court, Dept. 27
Regional Justice Center
200 Lewis Ave.
Las Vegas, Nevada 89155
Respondent

/s/ Danielle Kelley
An employee of
Hutchison & Steffen