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Case No. 4125-



**IN THE COURT OF CHANCERY OF THE STATE OF DELAWARE**

**DELOITTE LLP and DELOITTE & TOUCHE LLP, each a Delaware Limited Liability Partnership,** :

**Plaintiffs,** :

**- against -** :

**THOMAS P. FLANAGAN,** :

**Defendant.** :

**Civil Action No. \_\_\_\_**

**VERIFIED COMPLAINT**

Plaintiffs Deloitte LLP and Deloitte & Touche LLP ("D&T", and, collectively with Deloitte LLP, "Deloitte" or the "Partnerships"), by their undersigned attorneys, as and for their Verified Complaint against defendant Thomas P. Flanagan ("Flanagan") allege, upon knowledge as to their own acts and upon information and belief with respect to all other allegations, as follows:

**NATURE OF ACTION**

1. The Partnerships bring this action to remedy harm they have suffered as a result of the conduct of a faithless fiduciary.
2. Specifically, since at least 2005, Flanagan—who for 30 years was a partner of one or both of the Partnerships or of a predecessor of Deloitte LLP until his abrupt resignation less than two months ago—violated his obligations to Deloitte and betrayed the trust of his partners by willfully violating Deloitte's policies on independence and conflicts of interest and improperly trading in securities of, and relating to, D&T audit clients, including some which Flanagan himself served.
3. Compounding his wrongdoing, Flanagan repeatedly lied to Deloitte about his

clandestine trading activities in annual written certifications, going so far as to conceal the existence of a number of his brokerage accounts to avoid detection of his improper conduct. Indeed, notwithstanding requests since his activities recently came to light, Flanagan still has not disclosed to Deloitte all of the relevant facts about his trading, in further and continuing violation of his obligations to the Partnerships.

4. Flanagan's acts violated the trust and confidence he owed to Deloitte, both under the terms of the Memorandum of Agreement of each of the Partnerships, each of which sets forth the rights and obligations of their respective partners and to which he is a party (collectively, the "MOAs") and as a fiduciary to the Partnerships. These wrongful acts have caused Deloitte substantial injury. By this action, the Partnerships seek to recover for the harm they have suffered as a result of Flanagan's misdeeds and to prevent any further wrongful conduct.

#### **THE PARTIES**

5. Plaintiff Deloitte LLP is a Delaware limited liability partnership that, through its subsidiaries, provides audit, consulting, financial advisory, risk management, and tax services to a variety of clients throughout the United States. Plaintiff D&T is a Delaware limited liability partnership that provides audit and risk management services to a variety of clients throughout the United States.

6. Defendant Flanagan is a former partner of each of the Partnerships and a signatory to the MOAs. Flanagan, a Certified Public Accountant, was a partner of one or both of the Partnerships or of a predecessor of Deloitte LLP for 30 years and, at the time of his resignation from Deloitte, served as an advisory partner in Deloitte's Chicago office for a number of D&T's audit clients. In that role, Flanagan regularly attended meetings of the audit committees of those clients. Flanagan is subject to the jurisdiction of this Court by virtue of

Section 14.05 of the Deloitte LLP MOA and Section 13.05 of the D&T MOA, each of which provides "[e]ach Party hereby irrevocably and unconditionally agrees . . . to be subject to the jurisdiction of the courts of the State of Delaware and of the federal courts sitting in the State of Delaware," which the MOAs establish as the exclusive venues for any disputes relating to the Partnerships or the MOAs.

### **FACTUAL BACKGROUND**

#### The Obligations Imposed on Flanagan by the MOAs

7. Article 9 of each MOA governs the "conduct and rights of parties during and after severing association with the Partnership," and mandated that Flanagan, *inter alia*: (a) "be just and faithful to the Partnership . . . in all actions and in respect of the business and reputation of the Partnership;" (b) "not engage in any conduct or activity . . . contrary or inconsistent with the letter or spirit of [Deloitte's] rules relating to independence and conflicts of interest;" and (c) "submit to the Partnership . . . as requested a written report . . . setting forth such information as the Board may deem appropriate to ascertain compliance by [Flanagan] with the rules relating to independence, outside activities and conflicts of interest."

8. Article 9 of each MOA further obligates Flanagan to continue to comply with Deloitte LLP's rules relating to independence and conflicts of interest even following his departure from the Partnerships.

9. Each MOA provides that any partner who breaches any provision of Article 9 waives the right to receive any amounts payable to him by that Partnership on or after the date of the breach.

#### Deloitte's Independence Policies

10. It is fundamental to the professional practice of the Partnerships that all of their

respective personnel, including their partners, strive to adhere to the highest standards of independence, integrity, and objectivity and to be free from conflicts of interest. To help serve this end, the Partnerships maintain independence policies (the "Policies"), set forth in their Independence Manual, which apply to the partners and the professional and administrative employees of the Partnerships. Flanagan was and is subject to the Policies.

11. At all relevant times, the Policies prohibited partners and employees of the Partnerships from having any "Financial Interest", direct or indirect, in any "Restricted Entity."

12. The Policies defined "Financial Interest" broadly, encompassing, *inter alia*, "the ownership or guarantee of debt or equity securities, options, warrants, long or short security positions, and rights or other commitments to acquire such securities." The Policies also gave broad definition to "Restricted Entity", including within its scope D&T's audit clients.

13. The Policies additionally barred partners and employees of the Partnerships from trading in securities of, and relating to, companies about which they possessed material, non-public information. The Policies also required each partner and employee to notify Deloitte LLP of circumstances in which he had prior notice of a transaction by a client that might affect his interests, such as a Financial Interest held by the partner or employee in a client's proposed acquisition target. Under such circumstances, the Policies further dictated that the partner or employee refrain from taking any action relating to any securities of the companies involved during the time the proposed transaction remained non-public.

14. The Policies required partners and other professional personnel of the respective Partnerships annually to represent to Deloitte LLP that they had complied with the Policies (the "Annual Representation").

15. Flanagan consistently made Annual Representations to Deloitte LLP that, *inter*

*alia*: (a) he was familiar with the Independence Manual and the Policies; (b) he had reviewed the list of Restricted Entities; (c) he had "accurately and completely describe[d] all stocks, debt securities, mutual funds, units investment trusts, 529 plan accounts, and brokerage accounts held by [him], [his] spouse or spousal equivalent, and dependents;" and (d) at no time during the relevant year "did [he], [his] spouse or spousal equivalent, and/or [his] dependents have a financial interest in a Restricted Entity."

16. For at least the years 2005 through 2007, each of Flanagan's Annual Representations was false.

#### Flanagan's Misconduct

17. In August 2008, a regulatory agency asked Deloitte LLP to provide the names and titles of all personnel who constituted the engagement team for a particular D&T audit client between January and July 2007. That client had announced an acquisition of a public company in July 2007. Flanagan was the advisory partner for the D&T audit client and had contact with the client's top executives and the members of its audit committee. Flanagan purchased stock in the client's target approximately one week before the client publicly announced the acquisition. Flanagan did not disclose this trade to Deloitte LLP. This trade, and Flanagan's failure to disclose it, violated the Policies. As it would turn out, this violation of the Policies was only the most recent in a years-long course of improper trading and concealment by Flanagan.

18. Later in August 2008, Deloitte LLP received a further inquiry from the regulatory agency listing a number of companies, asking for which of them D&T acted as an auditor during 2006 and 2007, and further inquiring which of those audit clients Flanagan served. A number of the companies on the list were in fact D&T audit clients, and Flanagan was the advisory partner for a number of those clients.

19. Only after Deloitte LLP had received these inquiries and sought to discuss them with him did Flanagan advise Deloitte not only that he was aware of the regulatory investigation, but also that he had in fact spoken with the regulators, only to break off communication with them and retain counsel after he became uncomfortable with the regulators' questions. Flanagan had not previously disclosed any of this information to Deloitte.

20. Shortly thereafter, on September 5, 2008, Flanagan notified Deloitte that he was resigning, effective immediately.

21. Between January 2005 and June 2008, Flanagan engaged in numerous trades of put and call options with respect to securities of at least 12 of D&T's audit clients, for seven of which Flanagan served as D&T's advisory partner. Flanagan did not disclose these trades to Deloitte LLP in his Annual Representations or otherwise. These trades, and Flanagan's failure to disclose them, violated the Policies.

22. Flanagan also failed to disclose to Deloitte LLP in his Annual Representations or otherwise a number of brokerage accounts maintained in his name, his spouse's name, and his dependents' names, and a trust maintained in his dependents' names. Flanagan's failure to disclose these accounts violated the Policies, and facilitated his ability to continue to make improper trades by making his misconduct virtually impossible for Deloitte to detect.

Deloitte Has Suffered Substantial Harm as a Consequence of Flanagan's Wrongdoing

23. As a result of Flanagan's wrongful actions, Deloitte has suffered and will continue to suffer substantial injury.

24. Beginning with his first breach of the Policies, which occurred no later than 2005, Flanagan waived any right to amounts payable to him by Deloitte. By concealing his wrongdoing, however, Flanagan continued to receive substantial compensation and other sums

from Deloitte to which he was not entitled.

25. Additionally, once Flanagan's misdeeds began to come to light and continuing through the present, Deloitte incurred substantial out-of-pocket costs, including legal fees paid to outside counsel, to address Flanagan's wrongdoing. Moreover, certain of D&T's audit clients that were the subject of Flanagan's improper trading have themselves incurred substantial out-of-pocket costs, including legal fees paid to their outside counsel, to investigate D&T's ability to continue as their independent auditor, and these clients may seek to recover these costs from D&T.

26. Still further, Deloitte personnel reaching to the highest levels of the Partnerships have been forced to devote substantial time and effort, at significant cost to Deloitte, to responding to the revelations of Flanagan's improper actions.

27. The full extent of Flanagan's wrongdoing and its damage to Deloitte is unknown, in part because Flanagan has not disclosed to Deloitte all of the facts about his trading activities.

**COUNT 1 – BREACH OF FIDUCIARY DUTY**

28. Deloitte repeats and realleges each of the allegations contained in paragraphs 1-27.

29. Flanagan owed fiduciary duties to Deloitte under common law, the Delaware Revised Uniform Partnership Act, and the MOAs that required him to act in good faith, loyally, justly and faithfully in all conduct respecting the business and reputation of the Partnerships.

30. Flanagan breached these fiduciary duties by willfully violating his obligations to honor Deloitte's policies on independence and conflicts of interest and then concealing his wrongful conduct by making deliberate misrepresentations to Deloitte.

31. These breaches of fiduciary duty resulted in substantial damage to the Partnerships, including Deloitte's payment of compensation and other sums to Flanagan that he

had waived any right to receive by virtue of his conduct and the substantial costs Deloitte has incurred and will continue to incur in response to Flanagan's actions.

**COUNT 2 – BREACH OF CONTRACT**

32. Deloitte repeats and realleges each of the allegations contained in paragraphs 1-27.

33. The MOAs constitute binding contracts among Flanagan and the other partners of the Partnerships. Flanagan received substantial remuneration in consideration of the obligations he undertook by signing the MOAs.

34. The Partnerships fully performed their respective obligations to Flanagan under the MOAs.

35. Flanagan breached his contracts when he failed to remain "just and faithful to the Partnership[s]" and instead deceived Deloitte about his repeated violations of the Policies.

36. Flanagan also breached his contracts by engaging in stock and options trading that was "contrary or inconsistent with the letter or spirit of [Deloitte's] rules relating to independence and conflicts of interest."

37. Flanagan further breached his contracts by failing to provide the Partnerships with accurate information through which they could ascertain his compliance with "the rules relating to independence, outside activities and conflicts of interest," and instead making misrepresentations to Deloitte LLP in his Annual Representations to conceal his wrongdoing.

38. Deloitte was damaged by each of these breaches of the MOAs, including by paying Flanagan compensation and other sums that he had waived the right to receive by breaching the MOAs and incurring substantial costs in responding to Flanagan's actions.



**COUNT 3 – COMMON LAW FRAUD**

39. Deloitte repeats and realleges each of the allegations contained in paragraphs 1-27.

40. Flanagan falsely and knowingly represented to Deloitte LLP in his Annual Representations that he did not have financial interests in any Restricted Entities and was thus in compliance with Deloitte's policies on independence and conflicts of interest and that he had fully disclosed all brokerage accounts he was required by the Policies to disclose.

41. Flanagan knowingly or willfully induced Deloitte to rely upon those statements.

42. The Partnerships justifiably relied on and were damaged by Flanagan's misrepresentations, including by paying to Flanagan amounts to which he had waived entitlement by engaging in the acts that were the subject of his misrepresentations.

**COUNT 4 – EQUITABLE FRAUD**

43. Deloitte repeats and realleges each of the allegations contained in paragraphs 1-27.

44. Flanagan falsely represented to Deloitte in his Annual Representations that he did not have financial interests in any Restricted Entities and was thus in compliance with Deloitte's policies on independence and conflicts of interest and that he had fully disclosed all brokerage accounts he was required by the Policies to disclose.

45. Flanagan induced Deloitte to rely upon those statements.

46. The Partnerships justifiably relied on and were damaged by Flanagan's misrepresentations, including by paying to Flanagan amounts to which he had waived entitlement by engaging in the acts that were the subject of his misrepresentations.

**REQUEST FOR RELIEF**

WHEREFORE, Deloitte prays for the following relief:

- a. an accounting for and repayment with interest of all monies received by

Flanagan following the first time he was in breach of his fiduciary, contractual, and other duties;

b. a declaration that, pursuant to Article 9 of each MOA, the Partnerships do not owe Flanagan further payments of any nature;

c. an order temporarily, preliminarily, and permanently enjoining Flanagan from committing any further breaches of the MOAs or the fiduciary duties he owes to Deloitte, including requiring him to disclose all relevant facts regarding his trading activities to Deloitte;

d. an award of damages to compensate the Partnerships for all losses resulting from the wrongful actions of Flanagan, including without limitation the legal fees and other costs they have incurred or will incur in responding to his conduct, in an amount to be determined at trial; and

e. such other and further relief as the Court may deem appropriate.

Dated: Wilmington, Delaware  
October 29, 2008

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