IN THE COURT OF CHANCERY OF THE STATE OF DELAWARE
IN AND FOR NEW CASTLE COUNTY

GREGORY BRADY, Plaintiff, v. i2 TECHNOLOGIES INC., a Delaware corporation, Defendant and Counterclaim Plaintiff.	)	Civil Action No. 1543-N

MEMORANDUM OPINION

Date Submitted: October 4, 2005
Date Decided: December 14, 2005

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CHANDLER, Chancellor

A former executive and director of a Delaware corporation seeks advancement of his expenses in connection with the defense of certain proceedings, including a civil enforcement action filed against him by the Securities and Exchange Commission. This case requires me to interpret the effect of a severance agreement and its indemnification provision on advancement rights granted in an earlier agreement between the same parties. In particular, when the later severance agreement includes an integration clause affirming that such agreement expresses the entire agreement with respect to its subject matter, do the advancement rights survive integration, or are they superseded by the newer severance agreement? As explained below, I conclude that the advancement rights have survived and remain in full force and effect.

I. FACTUAL BACKGROUND

Defendant i2 Technologies, Inc. ("i2" or the "Company") provides enterprise supply management solutions, including various supply chain software and service offerings. In 1996, i2 presciently entered into an Indemnification Agreement (the "1996 Agreement") with plaintiff Gregory Brady, then President of Field Operations, in order to induce Brady to continue to serve as an officer or director

of the Company.[1] Relevant provisions of the 1996 Agreement beyond general indemnification obligations include the continuation of the Company's obligations after the termination of Brady's employment[2] and the advancement by the Company of reasonable expenses incurred in defending against any action brought against Brady arising from his position with i2.[3] Further, any amendment or termination of the 1996 Agreement would not be effective unless in writing signed by both parties.[4]

In May 2001, Brady became i2's CEO and a member of its Board of Directors, but his tenure was short lived. Following communications from an ex-officer containing allegations related to revenue recognition and financial reporting, i2's Board of Directors directed its Audit Committee to conduct an internal investigation.[5] During this investigation, in early April 2002, Brady resigned as CEO of the Company. Robert Donohoo, i2's General Counsel, drafted and negotiated Brady's severance agreement (the "2002 Agreement") to address

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[1] Ex. B to Plaintiff's Answering Brief in Response to Defendant's Summary Judgment Motion (hereafter "PX __") at recitals.
[2] *Id*. at § 5.
[3] *Id*. at § 7.
[4] *Id*. at § 15.
[5] Ex. L to Affidavit of Michael W. McDermott, Esquire, submitted in support of Movants' Opening Brief of Defendant and Counterclaim Plaintiff i2 Technologies, Inc. in Support of Its Motion for Summary Judgment (hereafter "McDermott Exhibit __") at ¶ 6.

the numerous issues left open by Brady's resignation.[6] The 2002 Agreement ultimately included, among other things, a $500,000 consulting fee and the allocations of a BMW Z-8, a leased Porsche, and expenses associated with the use of Brady's yacht for "Company related business matters."[7] Additionally, the 2002 Agreement provided for the Company's indemnification of Brady against any proceeding arising by reason of Brady's employment at the Company.[8] The 2002 Agreement concludes with an integration clause stating that the 2002 Agreement, along with certain other agreements, constitute "an integrated, written contract, expressing the entire agreement between the Company and [Brady] with respect to the subject matter hereof."[9]

In 2003 during the course of its investigation, the Audit Committee advised certain former officers, including Brady, to retain counsel before the Committee's planned interviews of each such officer. Brady's newly retained counsel requested the advancement of legal fees, and i2 responded by proposing a new advancement agreement between i2 and Brady (the "2003 Agreement"). In the proposed 2003 Agreement, the Company agreed to advance Brady reasonable attorney's fees and

[6] *Id*. at ¶ 18.
[7] PX D at 2-3.
[8] *Id*. at 2.
[9] *Id*. at 3.

expenses; the Company could discontinue such payments at will.[10] Unfamiliar with all of Brady's earlier agreements with i2, Brady's counsel was careful to negotiate a savings clause that protects the rights granted in the 2002 Agreement "or that otherwise might exist" from any diminishment.[11] After these negotiations, Brady executed the 2003 Agreement.

Inevitably, as litigation defense costs mounted, i2 examined how to shore up its profits[12] and, on July 28, 2005, i2 informed Brady that the Board of Directors determined to discontinue the advancement of attorney's fees and expenses to Brady.[13] Brady brought this action seeking enforcement of his alleged right to advancement of attorney's fees and other expenses incurred and to be incurred in connection with certain underlying proceedings. In addition, Brady seeks reimbursement of the attorney's fees and other expenses incurred and to be incurred in prosecuting this action – so-called "fees on fees." i2 has moved for summary judgment as to all claims.

[10] McDermott Exhibit B.
[11] *See Id.*, PX F.
[12] *See* McDermott Exhibit N at 24-25.
[13] *See* Ex. E to Def.'s Answer and Counterclaim.

II. STANDARD OF REVIEW

Court of Chancery Rule 56(c) permits summary judgment "if the pleadings, depositions, answers to interrogatories and admissions on file, together with the affidavits, if any, show that there is no genuine issue as to any material fact and that the moving party is entitled to a judgment as a matter of law."[14] "When a party moves for summary judgment, the court may award summary judgment to the other party, regardless of whether the other party moves for summary judgment, when the undisputed material facts of record show that the other party is clearly entitled to such relief."[15]

Summary judgment is an effective vehicle for resolving advancement disputes in particular because "the relevant question turns on the application of the terms of the corporate instruments setting forth the purported right to advancement and the pleadings in the proceedings for which advancement is sought."[16]

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[14] CT. CH. R. 56(c).
[15] *Telstra Corp. v. Dynegy, Inc.*, 2003 WL 1016984, at *5 (Del. Ch. 2003).
[16] *Morgan v. Grace*, 2003 Del. Ch. LEXIS 113, at *35 (Del. Ch. Oct. 29, 2003) quoting *Weinstock v. Lazard Debt Recovery GP, LLC*, 2003 Del. Ch. LEXIS 83, at *6 (Del. Ch. Aug. l, 2003).

III. ANALYSIS

The substantive interpretation of Brady's indemnification and advancement rights is governed by Delaware law.[17] The interpretation of the 2002 Agreement and the effect of its integration clause is governed by Texas law, as that is the place of contracting and the state with the most significant relationship to Brady's severance from i2.[18]

A. The 2002 Agreement's Integration Clause did not Abrogate Brady's Advancement Rights

Texas courts apply an objective theory of contract interpretation, under which the court looks to the words of the agreement and the objective circumstances, not subjective or uncommunicated intentions.[19] Terms are given

[17] The 1996 Agreement specifically states that Delaware law applies to its interpretation and enforcement. PX B at ¶ 13.

[18] *See Hurst v. Gen. Dynamics Corp.*, 583 A.2d 1334, 1338 n.5 (Del. Ch. 1990) (noting that Delaware choice of law rules are "governed either by a place of formation test … or a most significant relationship test"); *Wilmington Trust Co. v. Penn. Co.*, 172 A.2d 63, 66-67 (Del. 1961).

[19] *See Derr Construction Co. v. City of Houston*, 846 S.W.2d 854, 861 (Tex. App. 1992) (noting that "objective, not subjective, intent controls" questions of contract interpretation and that "the question is not what the parties meant to say, but what they did say"); *Zurich American Ins. Co. v. Hunt Petroleum (AEC), Inc.*, 157 S.W.3d 462, 465 (Tex. App. 2004); *Heritage Resources, Inc. v. NationsBank*, 939 S.W.2d 118, 121 (Tex. 1996); *Hewlett-Packard Co. v. Benchmark Electronics, Inc.*, 142 S.W.3d 554, 561 (Tex. App. 2004). Delaware applies a similar approach. *See US WEST, Inc. v. Time Warner Inc.*, 1996 WL 307445, at *9-10 (Del. Ch.).

their plain, ordinary, and generally accepted meaning unless the contract shows the parties used them in a technical or different sense.[20]

In determining whether a contract is ambiguous, Texas courts look to the contract as a whole, in light of the circumstances present when the contract was executed.[21] In construing a particular contract provision, the court may ascertain the intention of the parties so that their purpose may be effectuated, but it is the objective intent, not the subjective intent that is relevant. That is, "it is the intent expressed or apparent in the writing that controls."[22] Indeed, "[t]he terms of the contract must be the conclusive factor because such terms may have a meaning different from that which either party contemplated."[23]

The question therefore posed is this: what is the plain and ordinary meaning of the "subject matter" found in the integration clause of the 2002 Agreement? I conclude that the plain and ordinary meaning of "subject matter" is sufficiently narrow in its scope so as not to conflate the meaning of advancement and

[20] *Heritage Resources*, 939 S.W.2d at 121.
[21] *Sun Oil Co. (Del.) v. Madeley,* 626 S.W.2d 726, 731 (Tex. 1981); *see also Hewlett-Packard,* 142 S.W.3d at 561 ("We construe a contract from a utilitarian standpoint, bearing in mind the particular business activity sought to be served.").
[22] *Meyerland Cmty. Improvement Ass'n v. Temple*, 700 S.W.2d 263, 267 (Tex. App 1985) citing *City of Pinehurst v. Spooner Addition Water Co.*, 432 S.W.2d 515, 518 (Tex. 1968).
[23] *Id.*

indemnification. Advancement and indemnification are distinct concepts in plain and ordinary language.

Ordinarily and plainly, the advancement contemplated by the 1996 Agreement is wholly different from the indemnity payment contemplated by the 2002 Agreement. Advancement is an option to borrow, triggered upon the initiation of a lawsuit or proceeding; its value lies in the cheap (usually free) access to capital required to maintain a rigorous defense, in a situation where the officer or director's cost of capital has increased under the threat of enormous liabilities and insolvency.[24] Indemnities are insurance policies that pay out upon the realization of those enormous liabilities. Advancement can exist even if indemnification is eventually determined not to apply (in which case the advanced fees would have to be repaid to the company), and indemnification can exist without any initial rights to advancement.[25] Advancement and indemnification are separate and distinct legal actions, and the summary nature of advancement proceedings make it impractical (if not impossible) for litigating indemnification during the

[24] *See Homestore, Inc. v. Tafeen*, 2005 WL 3091887, at *6 (Del. 2005) ("Advancement provides corporate officials with immediate interim relief from the personal out-of-pocket financial burden of paying the significant on-going expenses inevitably involved with investigations and legal proceedings.")

[25] *See Homestore*, 2005 WL 3091887, at *8 ("The right to advancement is not dependent on the right to indemnification."); *Citadel Holding Corp. v. Roven*, 602 A.2d 818, 822 (Del. 1992).

advancement proceedings.[26] Accordingly, the general inclusion of these distinct concepts together in the same contracts (including the 1996 Agreement) does not make them of the same subject matter.

The 2002 Agreement is unambiguous that the integration clause did not preclude advancement. The clear distinction between advancement and indemnification make them different subjects, leaving the advancement provision of the 1996 Agreement unaffected by the 2002 Agreement's integration clause. i2 nonetheless maintains that if the "subject matter" of the 2002 Agreement was shown to be ambiguous, certain extrinsic evidence would resolve the ambiguity and show that "subject matter" was intended by the contracting parties to include advancement rights at the time of contracting. Under both Texas and Delaware law and the doctrine of *contra preferentum*, however, any ambiguity in the 2002 Agreement is construed against i2, the drafter of the agreement.[27]

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[26] *See Homestore*, 2005 WL 3091887, at *8; *Kaung v. Cole Nat'l Corp.*, 884 A.2d 500, 2005 WL 1635200, at *6-7.

[27] *See GTE Mobilnet of South Texas L.P. v. Telecell Cellular, Inc.*, 955 S.W.2d 286, 291 (Tex. App. 1997) ("The principle of construing a contract against its drafter is part of the 'rule *contra preferentum*,' which is a rule applied by courts when construing a contract as a matter of law."); *Kaiser Aluminum Corp. v. Matheson*, 681 A.2d 392, 398-99 (Del. 1996) (applying principle of *contra preferentum*); *Greco v. Columbia/HCA Healthcare Corp.*, 1999 WL 1261446, at *13 (in advancement case, construing ambiguous language against corporation and in favor of the claimant).

Further, assume "subject matter" was ambiguous and that defendant could (1) present sufficient extrinsic evidence at trial to overcome the doctrine of *contra preferentum*, and (2) demonstrate that advancement rights were intended to be the same "subject matter" integrated by the 2002 Agreement. Even assuming defendant could make such a showing at trial, integration would still not terminate Brady's advancement rights, for the reasons described below.

B. The 2002 Agreement does not supersede the 1996 Agreement's advancement provisions.

A written merger clause (such as the one in the 2002 Agreement) is essentially a memorialization of the merger doctrine.[28] Merger occurs where parties have concluded a valid integrated agreement dealing with the subject matter of an earlier agreement between them; merger's corollary, the parol evidence rule, will prevent enforcement of the earlier agreement that is inconsistent with the integrated agreement.[29] This bar, however, does not preclude enforcement of earlier agreements that are collateral to, are not inconsistent with, and do not vary or contradict the express or implied terms or obligations of the integrated

[28] *See Fish v. Tandy Corp.*, 948 S.W.2d 886, 899 (Tex. App. 1997).
[29] *Springs Window Fashions Div., Inc. v. The Blind Maker, Inc.*, 2005 WL 1787440, at *20 (Tex. App. 2005); *Fish*, 948 S.W.2d at 898; *Leon Ltd. v. Albuquerque Commons Partnership*, 862 S.W.2d 693, 700; *see also Texas A & M University-Kingsville v. Lawson*, 127 S.W.3d 866, 872.

agreement.[30] To be collateral, the earlier agreement must be one that the parties might naturally make separately or the integrated agreement merely modifies the earlier agreement in some respect.[31]

In this case, even assuming that the advancement provision of the 1996 Agreement is the same subject matter as the indemnification rights provision under the 2002 Agreement, the advancement provision of the 1996 Agreement nonetheless constitutes its own agreement that is collateral to and consistent with the terms of the 2002 Agreement. Nor does the 1996 Agreement's advancement provision contradict the express or implied terms of the 2002 Agreement. Furthermore, the 1996 Agreement's separability provision states that each provision is a distinct agreement, independent of the others;[32] the advancement provision thereby constitutes its own independent agreement. Advancement agreements and indemnification agreements are often made separately, and are therefore collateral to one another in this case. One need not look far for proof: the 2003 Agreement grants Brady advancement rights separate from the 2002 Agreement containing his indemnification rights. Finally, the 1996 Agreement's

[30] *Hubacek v. Ennis State Bank*, 317 S.W.2d 30, 32 (Tex. 1958).
[31] *Leon*, 862 S.W.2d at 700-01.
[32] PX B at ¶ 12.

advancement provision is not inconsistent with, and does not vary, the terms of the 2002 Agreement. Therefore, the integration clause of the 2002 Agreement does not preclude enforcement of the 1996 Agreement's advancement provision.

C. Brady is entitled to receive the expenses incurred in prosecuting the advancement action and pre-judgment interest.

In *Stifel Financial Corp. v. Cochran*, the Delaware Supreme Court held that corporations are authorized to indemnify for expenses incurred in successfully prosecuting actions under 8 *Del. C.* §145 ("Section 145").[33] "Without an award of attorney's fees for the indemnification suit itself, indemnification would be incomplete."[34] This is so because "the corporation itself is responsible for putting the director through the process of litigation."[35] Further, the Court noted that "giving full effect to Section 145 prevents a corporation from using its 'deep pockets' to wear down a former director, with a valid claim to indemnification, through expensive litigation."[36] Although the Court noted that a corporation may tailor its indemnification bylaws to exclude "fees on fees,"[37] i2 took no such steps. For these reasons, I conclude that Brady is entitled to receive reasonable expenses

[33] 809 A. 2d 555, 561 (Del. 2002).
[34] *Id*.
[35] *Id*.
[36] *Id*.
[37] *Id*.

incurred in prosecuting the advancement action.[38] If counsel are unable to reach agreement on the expenses incurred in prosecuting this action, application may be made to the Court.

Finally, under settled Delaware law, "prejudgment interest is awarded as a matter of right."[39] Brady is entitled to interest computed from the date of demand.[40] The rate of prejudgment interest is 5% over the Federal Reserve discount rate as of the time of the injury.[41] Accordingly, the rate of prejudgment interest on amounts to be advanced to Brady's legal and accounting advisors is 8.5% until September 20, 2005, and 8.75% from then until the date of judgment.

IV. CONCLUSION

Because Brady's advancement rights remain in full force and effect, summary judgment is hereby entered in favor of Brady on both counts.

Counsel shall confer and submit an Order implementing this decision within ten days.

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[38] *Homestore*, 2005 WL 3091887, at *12-13 ("[A]ll contracts providing for the advancement of expenses are implicitly limited to those that are reasonably incurred.")
[39] *Citadel*, 603 A.2d at 826.
[40] *Id*.
[41] *See* 6 *Del. C.* § 2301(a).