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Case Number 332,2013

IN THE SUPREME COURT OF THE STATE OF DELAWARE

GARDA USA, INC., a Delaware corporation and GARDA WORLD SECURITY CORPORATION, a corporation organized under the laws of Canada,	)	
Plaintiffs-Appellees,	)	
v.	)	No. 332, 2013
SPX CORPORATION, a Delaware corporation,	)	On appeal from the Court of Chancery of the State of Delaware, C.A. No. 7115-VCL
Defendant-Appellant.	)	

ANSWERING BRIEF OF PLAINTIFFS-APPELLEES GARDA USA, INC. AND GARDA WORLD SECURITY CORPORATION

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NATURE OF PROCEEDINGS

This case stems from an accounting arbitration following the sale of Vance International ("Vance") by SPX Corporation ("SPX") to Garda USA, Inc. (with Garda World Security Corporation, "Garda") under an Amended Stock Purchase Agreement dated January 13, 2006 (the "Agreement"). The Agreement called for a purchase price adjustment based on Vance's working capital at closing. It directed that a reserve for workers' compensation claims be included in working capital, along with a provision for "incurred but not reported" losses ("IBNR"), to address outstanding claims and the fact that workers' compensation claims tend to worsen over time. SPX did not include IBNR in calculating the Vance workers' compensation reserve.

The parties submitted their working capital dispute to an accounting arbitrator, per the Agreement. The arbitrator adopted SPX's calculation of Vance's working capital, despite SPX's conceded exclusion of IBNR. Garda challenged the award in the Court of Chancery. Master Abigail LeGrow, while viewing Garda's interpretation of the Agreement as correct, felt constrained to defer to the arbitrator. (A-251-4.) Vice Chancellor J. Travis Laster, granted Garda's exceptions to the Master's Report and vacated the arbitration award because the Agreement "clearly and unambiguously requires the inclusion of IBNR. . . ." (A-006-7.)

SUMMARY OF ARGUMENT

1. Denied. The accounting arbitrator in this case faced only one reasonable interpretation of the Agreement and, in any event, was prohibited from interpreting the Agreement even if reasonable alternatives had existed. Section 1.3(a) of the Agreement's Working Capital Schedule mandated that "incurred but nor reported claims"—or IBNR—"shall be included" in the calculation of Vance's workers' compensation reserve, and SPX conceded that it did not include IBNR. The arbitrator could not reasonably construe a command to include IBNR to mean its exact opposite, and even if a rational alternative interpretation existed, the parties and the arbitrator agreed that the arbitrator would have no authority to interpret the Agreement.

2. Denied. In reaching his decision, the only logical conclusion to be drawn from the record in the arbitration and the Award is that the Arbitrator did not include IBNR in formulating the Award.

3. Denied. The Vice Chancellor properly concluded that the question was not whether the Arbitrator had used its judgment in determining the workers' compensation reserves, but whether the Arbitrator failed to follow the express instructions in the Agreement regarding what types of reserves must be considered as part of the workers' compensation reserve. Section 1.3(c) of the Working Capital Schedule does not countermand the specific

direction of § 1.3(a) that IBNR "shall be included" simply because it generally requires the use of historical accounting methodologies. The only reasonable reading that gives meaning to all of the contractual language is that IBNR shall be included, but SPX would calculate it using historical methods, so as to protect Garda against accounting maneuvers that might adversely affect working capital. SPX's reading would render § 1.3(a) of the Agreement a nullity and would violate the principle of contractual interpretation that the specific governs over the general.

4. Denied. The Vice Chancellor properly considered the materials submitted at the arbitration.

5. Denied. The Vice Chancellor gave the Agreement its only logical meaning.

6. Denied. The Vice Chancellor properly concluded that the Arbitrator omitted IBNR as the Arbitrator adopted SPX's calculation of workers' compensation reserves and SPX admitted that its calculation of workers' compensation reserves did not include IBNR.

STATEMENT OF FACTS

A. The Vance Transaction

Garda USA, Inc. is an American subsidiary of Garda World Security Corporation, a Canadian company in the security, cash handling, and investigative services business. (A-0042.) In early 2006, Garda agreed to purchase Vance's stock from SPX for $67.25 million. (A-0164-65.) The terms of this transaction were reflected in the Agreement. (A-0488 *et seq.*)[1]

As in many such transactions, Vance's working capital as of the closing date was a chief concern to Garda because the purchase price was to be adjusted after the closing depending on the amount of working capital Vance had available. (A-0043.) SPX's proper calculation of Vance's working capital was imperative to Garda because an incorrect calculation could result in Garda paying more for Vance than it had bargained. (*See id.*)

One of Vance's most significant liabilities, and thus one of the largest components of the working capital calculation, was Vance's workers' compensation reserve. (A-0046.) SPX did not prepare standalone financial statements for Vance, but instead maintained Vance's workers' compensation reserve on its own books and records. (*Id.*) The result was

[1] Those terms were originally set forth in a Stock Purchase Agreement dated October 20, 2005, (A-0426-87), which Garda and SPX later amended and restated as the Amended Agreement on January 13, 2006. (A-0488.) The parties agree that the Amended Agreement is the operative contract for purposes of their dispute.

that Garda could not review Vance's own books and records to verify the correctness of any of those reserves. (*See id.*)

B. The Agreement and the IBNR Mandate

As a result, the parties conducted detailed negotiations as to how SPX would calculate Vance's reserve for workers' compensation liabilities as part of the working capital calculation. (See A-0046.) In § 1.3(b)(ii)) of the Agreement, the parties agreed that working capital would be calculated in accordance with an attached "Working Capital Schedule." (A-0167.) The Working Capital Schedule specifies that working capital shall mean "current assets minus current liabilities" and goes on to specify which assets and liabilities must be included and excluded in that calculation. (A-556.)

Most notable for this appeal, § 1.3(a) of the Working Capital Schedule provides:

> The calculation of current assets and current liabilities shall exclude the following accounts and balances:
>
> * * *
>
> v. Incurred but not reported claims related to risk management programs, **with the exception of those claims related to workers' compensation liabilities, which shall be included in the calculation of current liabilities;**

(*Id.*; emphasis added.) That is, Section 1.3(a)(v) first sets forth the general rule that SPX did not have to calculate IBNR for any Vance accounting

reserves, with one critical exception: for workers' compensation liabilities, SPX was required to include IBNR. (*See id.*)

Section 1.3(b) then notes that in calculating working capital, SPX "shall not take into account any changes in circumstances or events occurring after" the effective date of the Agreement. (*Id.*) Section 1.3(c) also provides that reserves "shall be calculated using the same methodology in respect of such items" as were used in Vance's interim financial statements, but that "the application of the methodology shall reflect changes in circumstances or events occurring and based on the most current information known to SPX. . . ." (*Id.*) The purpose of these provisions was to prevent SPX from altering its accounting methods "between signing and closing to change the result." (A-0026.)

The inclusion of IBNR in the Vance workers' compensation reserve was a crucial part of the parties' bargain. IBNR reflects the fact that amounts actually paid on workers' compensation claims do not represent the true liability, because there are unasserted claims, and because workers' compensation claims often change and grow over time. (A-1032.).[2]

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[2] Garda submitted to the accounting arbitration several affidavits of François Morissette, a principal at Oliver Wyman and actuary with over twenty years of experience, discussing IBNR and related topics. (A-0870-925; A-1031-45; A-1117-21.) SPX did not submit an affidavit from an actuary or similar expert in support of its own briefing, nor did it offer any substantive discussion of IBNR before the accounting arbitrator.

Workers' compensation claims, by their nature, almost always become more expensive over time because workplace injuries often recur, or worsen, or lead to other injuries stemming from the initial one. (A-0044-45.) Injuries that appear to have been treated often come back or result in future losses not currently anticipated. (*Id.*) Simply looking at amounts paid by insurers does not accurately capture the liability posed by these claims. (*Id.*) Accordingly, actuaries apply IBNR to reserves to capture this concept of "loss development" and to ensure that the reserve gives a true sense of the overall liability.[3] (*Id.*; *see also* A-1031-35.) This was a sufficiently important item to the parties that they singled it out for inclusion in their written contract, even though they agreed that IBNR could be excluded for reserves other than workers' compensation and even though they agreed (in § 1.3(c) of the Working Capital Schedule) that SPX would otherwise be free to use historical accounting methods. (A-556.)

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[3] The actuarial and accounting literature require that IBNR be included in setting a workers' compensation reserve. For example, the Statement of Principles Regarding Property and Casualty Loss and Loss Adjustment Expense Reserves, adopted by the Board of Directors of the Casualty Actuarial Society, states that a loss reserve must include a "[p]rovision for claims incurred but not reported." (A-1037-45.) IBNR often exceeds the actual amount of losses paid by insurers (the "case reserve") at any given point in time because initial payments often grossly understate the total amount required to pay for longer term injuries or recurrences of old injuries. (A-1034.) It is reasonable that IBNR in a case such as this one would reach millions of dollars, and SPX's own actuary established a Vance workers' compensation reserve of $2.7 million largely due to IBNR. (*Id.*)

Nonetheless, when SPX calculated the working capital of Vance, it is undisputed that it did not include any provision for IBNR for workers' compensation claims. (A-0250.) Prior to the closing, however, SPX did not inform Garda that the Vance workers' compensation reserve of approximately $1.366 million did not include any provision for IBNR. (A-0046.) Garda learned only after the closing that in same week that SPX calculated the Vance workers' compensation reserve at $1.366 million, SPX's own actuarial expert (Aon) had informed SPX that the appropriate reserve for Vance was some $1.8 million more than SPX's original calculation after including IBNR. (A-0047.) Moreover, Garda also later learned that SPX signed a post-closing audit representation letter to the Vance auditors, PricewaterhouseCoopers (PwC), that estimated Vance reserves similarly to Aon, at $3 million. (*Id.*) Although Garda was not then aware of why SPX's calculation of $1.366 million was so much lower than what SPX's own actuary estimated, Garda challenged SPX's calculation of Vance's working capital and the accounting arbitration ensued, pursuant to § 1.3(d) of the Agreement. (A-0502.)

C. The Accounting Arbitration

The Agreement provided in § 1.3(d) that working capital disputes would be decided by an "Independent Accountant," defined by the

Agreement to be "a nationally recognized independent accounting firm that has not audited within the past two years Seller or Buyer." (A-0503.) Garda disputed SPX's working capital calculation on May 19, 2006. (A-0831-36.) Protracted discussions among the parties failed to resolve the dispute, and on September 8, 2010, Garda initiated the accounting arbitration to resolve those disputed items, the largest of which by far was the workers' compensation reserve issue that is the subject of this appeal. (A-0048-49.)[4]

The parties subsequently retained Ernst & Young, LLP ("E&Y") to serve as Independent Accountant under a March 15, 2011 "Statement of Work" with the parties which set forth the scope of E&Y's engagement. (A0335-49.) The Statement of Work provided that E&Y "shall not make any legal determinations or otherwise rule upon issues of law in rendering the Award." (A-0338.)

The parties submitted simultaneous opening briefs to E&Y, and it was upon receipt of SPX's opening submission that Garda first realized that SPX had not included any provision for IBNR in the Vance reserve, but had only "utilized the actual reserve balances maintained by Vance's workers' compensation insurance carriers—to calculate the reserve for the Effective Date Balance Sheet . . . ." (A-0932-34.) In other words, SPX simply added

[4] Garda also raised two other issues in the accounting arbitration, but SPX conceded those issues and they are not the subject of this appeal. (*See* A-0362-64.)

up what the insurers had paid to date, without any provision for the possibility of unasserted claims or the fact that claims grow more expensive over time—precisely what IBNR is intended to address. (*Id.*) SPX never addressed its failure to include IBNR in its reserve its submissions to the accounting arbitrator. (A-0929-39; A-1046-58; A-1122-26.) Similarly, SPX never argued—as it does now—that § 1.3(c) of the Working Capital Schedule trumps § 1.3(a)(v); indeed, SPX made no mention at all of IBNR or § 1.3(a)(v) in any of its briefs to E&Y. (*Id.*)

In Garda's reply brief to E&Y, Garda noted SPX's failure to include IBNR in violation of the express requirement of § 1.3(a)(v) of the Working Capital Schedule that it be included. (A-1016-20.) Garda requested that the Independent Accountant apply the proper formula set forth in the Agreement and recalculate the Vance reserve to include IBNR.[5] (*Id.*)

E&Y issued its determination letter to the parties on October 11, 2011. (A-0350-52.) With no explanation, E&Y simply adopted in its entirety SPX's calculation of working capital—including the workers'

[5] Garda also submitted its own actuarial analyses which included IBNR and concluded that the proper workers' compensation reserve should have been in the range of $3.5 to $3.9 million. (A-0870-925; A-1031-45; A-1117-21.) Garda further submitted an affidavit from PwC's audit personnel which made clear that Vance's workers' compensation liability was "substantially all" of the $3 million referenced in SPX's post-closing audit representation letter, and that SPX confirmed this in discussions with PwC. (A-1114-16.)

compensation reserve. (*Id.*) E&Y stated "EY has determined that no adjustment to Closing Date Working Capital is warranted for workers' compensation liabilities as the Buyer has not demonstrated that Seller failed to comply with Section 1.3 of the [Working Capital] Schedule." (A-0351.) E&Y failed to explain how this could be the case given that it was undisputed that SPX did not apply any provision for IBNR as required by § 1.3(a)(v) of the Working Capital Schedule. (*Id.*)[6] On October 13, 2011, counsel for Garda asked E&Y to elaborate on how E&Y could have sustained SPX's calculation when it excluded IBNR, as mandated by the Agreement; E&Y declined to do so. (A-357-58.)

D. Proceedings Before the Court of Chancery

Garda challenged the accounting arbitrator's ruling by commencing an action in the Court of Chancery on December 15, 2011, seeking vacatur pursuant to 10 *Del.* C. § 5714(a)(3). (A-0038-57.) The parties cross-moved for summary judgment, and the matter was assigned to Master LeGrow, who

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[6] SPX now suggests that the arbitration award might have reflected a view by E&Y that IBNR should be zero. (Br. at 6.) This is plainly wrong for several reasons. First, as noted above, SPX made no mention of IBNR in any of its submissions to E&Y, leaving E&Y no basis to calculate IBNR at anything other than what Garda's experts reported. Second, E&Y denied that there was any failure to comply with the Working Capital Schedule, not that there was a failure to comply but it was immaterial. (A-0351.) Finally, SPX's contention makes no sense, as workers' compensation claims are always subject to further loss development. (A-1031-35.) SPX's contention that the Vance workers' compensation claims "reached closure" (Br. at 10) is without citation or support because it is simply untrue.

issued a Final Report on February 7, 2013. (A-0240-60.) Noting that SPX conceded that it had not included IBNR in its calculation of the Vance workers' compensation reserve (A-0243), and finding that E&Y "was cognizant of the contract terms" (A-0250), Master LeGrow agreed with Garda that § 1.3(a)(v) of the Working Capital Schedule "plainly carves out a workers' compensation exception to the general rule that allows for the exclusion of incurred but not reported claims from the calculation of every other reserve." (A-0252.) Although E&Y "applied the contract differently than a Delaware court may have applied it" (A-0253), the Master felt constrained to accept the arbitrator's ruling because she believed the arbitrator was entitled to interpret the contract, and apply a "colorable, if flawed justification" for supporting SPX's argument. (A-0253-54.)

Vice Chancellor Laster disagreed. At a June 4, 2013 hearing, he found the Agreement "clear and unambiguous" and that there was no "colorable reading" that would have permitted E&Y to accept a calculation that excluded IBNR. (A-0024.) Vice Chancellor Laster aptly summarized:

> I think the contract is clear and unambiguous. It's a formula. It's a formula that says include X, exclude Y, include Z. The accountant, for whatever reason, didn't include Z. The accountant can use its judgment as to what Z is. There is another provision of the agreement that says calculate Z according to how it has been calculated historically. But when push comes to shove, there is a specific provision, 1.3(a), that says you must include Z.

(*Id.*)[7]

Vice Chancellor Laster also rejected SPX's argument that the reference to historical methods in § 1.3(c) of the Working Capital Schedule somehow altered the result. As he explained,

> The Workers' Compensation schedule said two things. It said, one, include IBNR. That's 1.3(a). It then said under 1.3(c), don't change your assumptions for doing it, because if you change your projections and things like that, you could affect the methodology. And 1.3(c) doesn't single out IBNR. 1.3(c) says to the extent you've been doing these things historically, do it the same way. Don't try and jigger the numbers between signing and closing to change the result. Then 1.3(a) is the formula that you put those numbers into.

(A-0026.) That is, the Court of Chancery found that § 1.3(a) mandated the inclusion of IBNR and § 1.3(c) did not contradict this, but simply clarified that to the extent that IBNR was calculated historically, that methodology should not be changed. Because the accounting arbitrator ignored the

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[7] Vice Chancellor Laster further noted that the issue was not "whether IBNR had been calculated appropriately . . . ." (A-0032.) Rather, "[t]his is a question of 'Do you add back in the variable Z?. . . .' That's not a judgment call. That's not an accountant call. That's a specific aspect of the formula under this agreement." (A-0033.)

unambiguous mandate of § 1.3(a)(v), the arbitrator exceeded his powers, warranting vacatur under 10 *Del. C.* § 5714(a)(3). (A-0029-30; A-0007.)

That same day, June 4, 2013, the Court of Chancery issued its order granting Garda's motion for summary judgment, denying SPX's cross-motion for summary judgment and vacating the October 11, 2011 accounting arbitrator's award (A-0001-08.) The Order underscored that § 1.3(a) of the Working Capital Schedule is "simply formulaic" and that "Section 1.3.(c) does not alter or inject ambiguity into the formula." (A-0006.) Because the contract provisions were clear and unambiguous, and because the arbitrator clearly had knowledge of them and disregarded them, the award had to be vacated. (A-0007.)

ARGUMENT

I. THE COURT OF CHANCERY CORRECTLY RULED THAT THE ARBITRATOR EXCEEDED HIS AUTHORITY BY IGNORING UNAMBIGUOUS CONTRACTUAL LANGUAGE THAT MANDATED THE INCLUSION OF IBNR.

A. Question Presented.

Did the Court of Chancery err in vacating the accounting arbitrator's award where the arbitrator ignored the unambiguous contractual command that IBNR be included in the calculation of Vance's workers' compensation reserve? (A-0001-08.)

B. Scope of Review.

This Court reviews rulings granting motions for summary judgment *de novo*. *Oakes v. Clark*, 69 A.3d 371 (TABLE), 2013 WL 3147313 (Del. June 18, 2013).

C. Merits of the Argument.

This appeal asks whether an accounting arbitrator, faced with a precise contractual formula dictating what must be included in a calculation of working capital, may disregard that formula and exclude items that the parties explicitly mandated must be included. The Court of Chancery correctly concluded that because the arbitrator disregarded the express contractual directive that gave rise to his authority, his award must be vacated. The Court of Chancery also properly rejected SPX's attempt to

suggest that the plain language of the Agreement means something other than what it says.

1. Section 1.3(a) of the Working Capital Schedule is Unambiguous.

The mandate that IBNR be included in the Vance workers' compensation reserve was a critical part of the parties' bargain, which they carefully and clearly reduced to writing in § 1.3(a)(v) of the Working Capital Schedule. They could not have been clearer in their command that as to "those claims related to workers' compensation liabilities," IBNR "shall be included in the calculation of current liabilities." (A-556.) And it is undisputed that SPX did not include any provision for IBNR in calculating Vance's workers' compensation reserve, nor did it ever advance any argument to the arbitrator concerning IBNR. (A-0250.)

Section 1.3(a)(v) is clear and unambiguous. As this Court has ruled, "[a] contract is not ambiguous 'simply because the parties do not agree upon its proper construction,' but only if it is susceptible to two or more reasonable interpretations." *Norton v. K-Sea Transp. Partners L.P.*, 67 A.3d 354, 360 (Del. 2013) (quoting *AT & T Corp. v. Lillis*, 953 A.2d 241, 252 (Del. 2008)). Section 1.3(a)(v) is not susceptible of any other reasonable interpretation. It says, in sum, include IBNR. The provision is clear on its face and leaves no doubt as to what it requires. One is hard pressed to

imagine any reasonable alternative reading, much less accept the one that SPX and the accounting arbitrator adopted which was to conclude that "IBNR . . . shall be included" somehow meant its exact opposite. (A-556.)

As Vice Chancellor Laster aptly summarized, § 1.3(a) of the Working Capital Schedule is simply a formula, dictating that certain items be included and excluded from the calculation of working capital. (A-0024.) It is a mechanical provision that neither requires nor permits interpretation, but rather lays out the intended algebra for the working capital calculation that the accounting arbitrator was mandated to perform. Section 1.3(a)(v), on its face, is clearly not ambiguous, but provides an unmistakably clear command to the arbitrator that IBNR "shall be included."[8]

[8] The issue here was thus not one of accounting judgment, but of the mechanical application of a clear formula. As the Court of Chancery noted, had there been a dispute about whether IBNR had been calculated appropriately or what IBNR is as a matter of accounting or actuarial science, the accounting arbitrator would have acted within his authority to resolve such a dispute. (A-0032.) But, as the Court of Chancery noted, what happened here was that the arbitrator intentionally omitted a variable from the formula that the parties specified must be included. "This is a question of 'Do you add back in the variable Z?. . . .' That's not a judgment call. That's not an accountant call. That's a specific aspect of the formula under this agreement." (A-0033.) Indeed, inasmuch as SPX never even mentioned IBNR in any of its submissions to E&Y, there is no basis for SPX's current speculation that E&Y implicitly exercised some unexplained judgment to conclude that IBNR should be zero, and somehow neglected to mention this in a report that found no deviation from the Working Capital Schedule. (Br. at 6.)

2. Section 1.3(c) of the Working Capital Schedule Does Not Create Ambiguity.

Although SPX does not contend that the Agreement is ambiguous, it implies that § 1.3(c) of the Working Capital Schedule permits § 1.3(a)(v) to be interpreted in some way other than what its plain language states. SPX contends that because § 1.3(c) makes a general reference to historical accounting methods, this trumps the specific directive in § 1.3(a)(v) that IBNR be included. SPX's contention—which it never advanced to the accounting arbitrator—is unreasonable and unsupported by law.

Section 1.3(c) of the Working Capital Schedule provides:

> In preparing the Effective Date Statement of Working Capital, the respective amounts included in the Effective Date Statement of Working Capital for all reserves (including, but not limited to, accounts receivable reserves and litigation reserves) and for asset valuation allowances (whether or not specified in this sentence) that were valued for the interim September 30, 2005 financial statements by subjective estimates shall be calculated using the same methodology in respect of such items on the interim September 30, 2005 financial statements but the application of the methodology shall reflect changes in circumstances or events occurring and based on the most current information known to SPX, between the date of the interim September 30, 2005 financial statements and the Effective Date.

(A-556.) In other words, when calculating a reserve, SPX will look to the same accounting methodology it previously used for such reserve, but will also include the most current information known to it.

According to SPX, this provision would allow it and the accounting arbitrator to ignore § 1.3(a)(v) and the command to include IBNR. But to read the Agreement SPX's way would be unreasonable and unnecessarily creates conflict among the provisions of the Agreement for several reasons. First, to accept SPX's argument would mean concluding that the very carefully drafted language in Section 1.3(a)(v) was nothing more than a waste of the parties' time and effort; that it was a nullity because IBNR could never be included due to SPX's historical practices. The law prohibits such a conclusion. *See Sonitrol Holding Co. v. Marceau Investissements*, 607 A.2d 1177, 1183 (Del. 1992) ("Under general principles of contract law, a contract should be interpreted in such a way as to not render any of its provisions illusory or meaningless."); s*ee also Matria Healthcare, Inc. v. Coral SR LLC*, 2007 WL 763303, at **6, 9 (Del. Ch. Mar. 1, 2007) ("[W]hen possible, the Court should attempt to give effect to each term of the agreement and to avoid rendering a provision redundant or illusory.").[9]

[9] SPX argued to the Special Master the converse: that reading § 1.3(a)(v) to require the inclusion of IBNR, as the provision plainly requires, renders § 1.3(c) meaningless. (A-0251.) Not so. Because § 1.3(c) is a broad provision that generally covers all reserves of Vance, and not merely workers' compensation, it has effect even though the inclusion of IBNR for workers' compensation is mandated. The Special Master correctly found that SPX had it backwards: "to read subparagraph (c) as allowing SPX to omit from the Vance Reserve an estimate of IBNR for workers' compensation claims renders meaningless" the relevant part of § 1.3(a)(v). (A-0251.)

Second, as this Court has made clear, in interpreting contracts, the specific governs over the general. *Sonitrol Holding Co.*, 607 A.2d at 1184. Section 1.3(a)(v) is extremely specific, and singles out IBNR for inclusion in the working capital formula. Section 1.3(c), by contrast, is general and speaks to reserves overall, not merely workers' compensation reserves or IBNR. Under settled Delaware law, "where there is an inconsistency between general provisions and specific provisions, the specific provisions ordinarily qualify the meaning of the general provisions." *Id.* (quoting *Stasch v. Underwater Works, Inc.*, 158 A.2d 809, 812 (Del Super. 1960) and Restatement (First) of Contracts § 236(c)). That is, SPX must use historical methods of accounting except where specifically directed otherwise, such as the requirement that it include IBNR.

Third, SPX's reading of the Agreement would do violence to the principle that one must read a contract in its entirety and harmonize its provisions. *See DCV Holdings, Inc. v. ConAgra, Inc.*, 889 A.2d 954, 961 (Del. 2005) ("Well-settled rules of contract construction require that a contract be construed as a whole, giving effect to the parties' intentions."); *Brinckherhoff v. Tex. E. Prods. Pipeline Co.*, 986 A.2d 370, 387 (Del. Ch. 2010) ("The two provisions can be read harmoniously together by recognizing that Section 6.1(a) creates a general standard under which the

general partner is authorized to act in its 'sole discretion' when managing the partnership, subject to the requirements of Section 6.6(e) in those specific cases when that provision applies."). SPX's reading of the Agreement needlessly creates an irreconcilable tension between §§ 1.3(a)(v) and 1.3(c). The sole reasonable reading of the Agreement—the one the Court of Chancery endorsed—permits the two to operate together without conflict by letting § 1.3(a)(v) govern IBNR as to workers' compensation specifically, and allowing § 1.3(c) to govern otherwise.

Fourth, SPX's view fundamentally makes no sense. Why would sophisticated parties take the time to include a provision requiring IBNR to be included if they really intended SPX's historical exclusion of IBNR to countermand that? What sense would there have been in discussing IBNR at all if the parties' true intent were that it might be included or excluded as the whims of Vance's accounting history might warrant? One cannot read the Agreement and conclude that in commanding that the Vance workers' compensation reserve include IBNR, these corporate parties meant the exact opposite. SPX's argument leads to an absurd result and should be rejected. *Osborn ex rel. Osborn v. Kemp*, 991 A.2d 1153, 1160 (Del. 2010) (holding that contracts should not be construed to "reach an absurd, unfounded result").

The Court of Chancery found that §§ 1.3(a)(v) and 1.3(c) worked in harmony, and that SPX's interpretation was unreasonable as it posited a needless conflict between the provisions. As Vice Chancellor Laster explained:

> The Workers' Compensation schedule said two things. It said, one, include IBNR. That's 1.3(a). It then said under 1.3(c), don't change your assumptions for doing it, because if you change your projections and things like that, you could affect the methodology. And 1.3(c) doesn't single out IBNR. 1.3(c) says to the extent you've been doing these things historically, do it the same way. Don't try and jigger the numbers between signing and closing to change the result. Then 1.3(a) is the formula that you put those numbers into.

(A-0026.)

The Court of Chancery also correctly observed that the clear purpose of requiring historical methodologies was to protect Garda, not give SPX license to reduce working capital. (*Id.*) SPX's accounting methods were frozen to prevent it from altering the rules of the game to tilt working capital to its advantage. (*Id.*) For SPX now to vaunt that provision into a means to take away a key, bargained-for term that was important to Garda, turns the Agreement on its head.

3. SPX's Newly Minted Argument That The Arbitrator's Decision Was Proper Because It Was Based On Actual Results Has No Merit.

For the first time on appeal, SPX appears to suggest that because the workers' compensation losses it experienced were ultimately comparable to the reserve it previously established, the Court should conclude that no IBNR adjustment was necessary. (Br. at 20.) Because SPX never raised this argument below, it is waived. Supr. Ct. R. 8. Even if the Court considers this argument, it has no merit. The Agreement mandates that IBNR be included, and the Agreement required the calculation of the workers' compensation liability—including IBNR—as of the time of the closing, and not a later time as SPX now appears to argue. In fact, § 1.3(b) of the Working Capital Schedule states that SPX "shall not take into account any changes in circumstances or events occurring after" the date of the Agreement. (A-556.) Moreover, SPX misses the very point of IBNR, which is to address "anticipated liabilities" from workplace injuries that have not yet caused recorded losses—something that is extremely common in the workers' compensation setting where injuries worsen and claims broader. (A-0025.) The amounts that SPX contends it paid to date do not reflect the true liability of the claims.

4. Because the Agreement is Unambiguous, the Accounting Arbitrator's Failure to Apply it Mandates Vacatur.

Section 5714(a)(3) of the Delaware Uniform Arbitration Act empowers the courts to review and vacate an award where an arbitrator "exceeded [his] powers, or so imperfectly executed them that a final and definite award upon the subject matter submitted was not made." The courts of Delaware and elsewhere have held that where an arbitrator disregards controlling contractual language, he or she exceeds his authority and a resulting award may be vacated.

As Chancellor Strine observed in *Pryor v. IAC/InteractiveCorp*, 2012 WL 2046827 (Del. Ch. June 7, 2012), "when the arbitrator acts in 'direct contradiction to the express terms of the agreement' that a court may properly find grounds to vacate." *Id.* at *6 n.61 (quoting *Mansoory v. SC & A Constr., Inc.*, 2009 WL 2140030, at *3 (Del. Ch. July 9, 2009)). Similarly, in *Mansoory v. SC & A Constr., Inc.*, Vice Chancellor Parsons ruled that if an arbitrator's "actions directly contradict the express terms of the agreement of the parties, he has exceeded his authority." 2009 WL 2140030, at *3 (Del. Ch. July 9, 2009), *aff'd*, 988 A.2d 937 (Del. 2010) (TABLE). Vice Chancellor Laster correctly noted in this case that "under Delaware's version of the Uniform Arbitration Act, an arbitration award can be vacated

if the arbitrator acted in manifest disregard of the law and controlling contractual provisions." (A-0029.)[10] SPX offers no argument or authority to the contrary.

This is not a case in which an arbitrator erred in choosing a less advisable interpretation among several that are plausible. Rather, the arbitrator disregarded an express command by the parties. The accounting arbitrator was told by the Agreement to include IBNR. He excluded it. This was a clear disregard of controlling contractual guidance which mandates vacatur of the award.

5. Even if the Agreement Had Been Susceptible of More Than One Reasonable Interpretation, the Accounting Arbitrator Was Not Empowered to Interpret the Agreement.

Significantly, SPX never advanced its incorrect reading of the Agreement to the accounting arbitrator. It never argued that § 1.3(c) trumped § 1.3(a)(v) because the parties specifically agreed, as did E&Y, that

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[10] *See also First Merit Realty Servs., Inc. v. Amberly Square Apartments, L.P.*, 869 N.E.2d 394, 399 (Ill. App. Ct. 2007) (vacating award where arbitrator exceeded authority by ignoring plain language of contract requiring certain calculations to be performed pursuant to precise mathematical models); *Hoteles Condado Beach v. Union De Tronquistas Local 901*, 763 F.2d 34, 41 (1st Cir. 1985) ("The arbitrator is . . . confined to the interpretation and application of the collective bargaining agreement, and although he may construe ambiguous contract language, he is without authority to disregard or modify plain and unambiguous provisions.") (quotations omitted); *InterCity Gas Corp. v. Boise Cascade Corp.*, 845 F.2d 184, 187 (8th Cir. 1988) ("Although the arbitrator may interpret ambiguous language, the arbitrator may not disregard or modify unambiguous contract provisions.").

the accounting arbitrator would not interpret the contract in any way. Thus, even if there had existed more than one reasonable interpretation of the Agreement—and that was not the case—the arbitrator was not given authority to construe the Agreement.

The Agreement gives the accounting arbitrator a limited mandate. Section 1.3(d)(ii) of the Agreement provides that the accounting arbitrator shall not conduct an independent review, but shall examine the dispute submitted by the parties and "report as to the dispute and the resulting computation of the Effective Date Balance Sheet and the adjustment or adjustments provided for in Section 1.3(e) reflected on the Effective Date Balance Sheet . . . ." (A-0502.) The agreement under which the parties engaged E&Y—a March 15, 2011 "Statement of Work" (A0335-49)—is consistent with this. The Statement of Work sets forth the "scope of services" that E&Y would provide, and specifies that E&Y "shall not make any legal determinations or otherwise rule upon issues of law in rendering the Award." (A-0338.)[11]

The parties participated in the accounting arbitration in a manner consistent with this understanding, and did not argue contractual

[11] SPX's counsel further observed during the summary judgment argument before the Court of Chancery that the parties "didn't negotiate an arbitration with AAA rules. They didn't negotiate an arbitration for someone to make a legal determination. They negotiated an accountant's determination, and that's what they got." (A-0021.)

interpretations or ask E&Y to interpret the contract. As SPX's brief concerning the Master's Final Report concedes, during the accounting arbitration, "no law was supplied or considered and indeed, the parties instructed the arbitrator not to make any legal determinations." (A-0311-21.)

Because the parties did not authorize E&Y to interpret the Agreement—if fact, they instructed it not to—and because during the accounting arbitration they did not submit contract interpretation issues to E&Y, E&Y had no authority to engage in contractual interpretation. *See Malekzadeh v. Wyshock*, 611 A.2d 18, 21 (Del. Ch. 1992) (observing that the two sources of an arbitrator's authority are agreement and submission by the parties).[12] E&Y's allotted task was to apply the formula for calculating working capital. It did not sit as plenary arbitrator deciding matters of contract law. Although there was no reasonable interpretation of the Agreement that would have permitted the accounting arbitrator to construe

[12] *See also Avnet, Inc. v. H.I.G. Source, Inc.*, 2010 WL 3787581, at *8 (Del. Ch. Sept. 29, 2010) (holding that parties had agreed only to submit a narrow range of issues to an accountant-arbitrator and that other issues of contractual interpretation were within the purview of the Court); *HDS Inv. Holding Inc. v. Home Depot, Inc.*, 2008 WL 4606262, at *5 (Del. Ch. Oct. 17, 2008) ("When construing narrow arbitration clauses, courts must carefully determine which disputes the parties intended to be decided by arbitration and only send to arbitration those disputes that the parties expressly agreed should be arbitrated.").

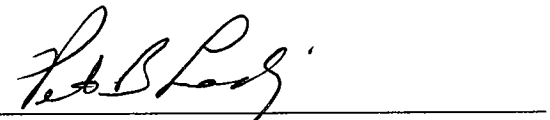
"include IBNR" to mean "exclude IBNR," a mere act of interpretation would have been a transgression of E&Y's bounds of authority.

* * * * *

In sum, this is not a case in which a party challenges an arbitration award as simply ill-advised or erroneous. Rather, this is a case in which the arbitrator did precisely the opposite of what the parties instructed. There is no colorable interpretation of the Agreement that permitted SPX to omit IBNR or for the Independent Accountant to fail to include IBNR in his calculation, nor was the arbitrator even granted authority to interpret the contract if such an interpretation had existed. The public policy in favor of arbitration is not furthered by awards directly at odds with the parties' contractual instructions and expectations. The Court of Chancery correctly vacated the award and its ruling should be affirmed.

CONCLUSION

For the foregoing reasons, summary judgment should be affirmed in favor of the Appellees.



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Dated: September 4, 2013

IN THE SUPREME COURT OF THE STATE OF DELAWARE

SPX CORPORATION, a Delaware corporation, Defendant Below-Appellant, v. GARDA USA, INC., a Delaware corporation and GARDA WORLD SECURITY CORPORATION, a corporation organized under the laws of Canada, Plaintiffs Below-Appellees.	)	No. 332,2013 On appeal from the Court of Chancery of the State of Delaware, C.A. No. 7115-VCL

CERTIFICATE OF ELECTRONIC SERVICE

I, Peter B. Ladig, hereby certify that on this 4th day of September, 2013, a true and correct copy of the following was served on counsel below:

1. Answering Brief of Plaintiffs-Appellees Garda USA, Inc. and Garda World Security Corporation, and

2. this Certificate of Service.

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