



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

SCOTT THOMPSON,)
)
 Plaintiff,)
)
 v.) C.A. No. 2716-VCS
)
 THE WILLIAMS COMPANIES, INC. and)
 WILLIAMS POWER COMPANY, f/k/a)
 WILLIAMS ENERGY MARKETING)
 AND TRADING,)
)
 Defendants.)

MEMORANDUM OPINION

Date Submitted: June 21, 2007
Date Decided: July 31, 2007

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STRINE, Vice Chancellor.

Plaintiff Scott Thompson seeks advancement from defendant Williams Power Company (“Power”), a wholly-owned indirect subsidiary of defendant The Williams Companies, Inc. (“Williams”).¹ Thompson is a former, non-officer, non-director employee of Power, who worked at the company’s natural gas trading desk from April 1999 to March 2001. During his time with Power, Thompson is alleged to have participated in a conspiracy to manipulate the price of natural gas and to commit wire fraud by providing false trading information to industry publications. Thompson first came under investigation in February 2003, and he was indicted in September 2006.

Thompson has incurred approximately \$500,000 in legal fees and expenses, which, he says, he is entitled to have reimbursed (in addition to having his future legal fees and expenses paid) under an advancement article in the Power bylaws. The applicable Power “Advancement Bylaw” states:

Expenses Payable in Advance. Expenses incurred by an officer or Director in defending a civil or criminal action, suit or proceeding may be paid by the Company in advance of the final disposition of such action, suit or proceeding upon the receipt of an undertaking by or on behalf of the Director or officer to repay such amount if it shall ultimately be determined that such person is not entitled to be indemnified by the Company as authorized in this Article VI. *Such expenses incurred by other employees and agents shall be*

¹ Thompson’s first request for advancement was not directed at Power. Rather, he petitioned Williams for advancement in November 2006, even though he never worked directly for that entity. That request was denied on January 26, 2007. Shortly thereafter, on February 6, Thompson filed this action, indicating that he believed the bylaws of Power also applied. Thompson now acknowledges that the Power bylaws are the only bylaws applicable to his advancement request. Joint Pretrial Order (June 18, 2007) at ¶ 4. He has therefore effectively dropped his claim against Williams.

*paid upon such terms and conditions, if any, as the Board of Directors deems appropriate.*²

The related “Indemnification Bylaw” provides, in relevant part:

Power to Indemnify in Actions, Suits or Proceedings Other Than Those by or in the Right of the Company. . . . [T]he Company shall indemnify any person who was or is a party or is threatened to be made a party to any threatened, pending or completed action, suit or proceeding, whether civil, criminal, administrative or investigative . . . by reason of the fact that such person is or was a[n] . . . employee . . . of the Company . . . *if such person acted in good faith and in a manner such person reasonably believed to be in or not opposed to the best interests of the Company, and, with respect to any criminal action or proceeding, had no reasonable cause to believe the conduct was unlawful.* . . .³

On March 26, the Power board of directors considered Thompson’s advancement request and resolved to grant advancement to Thompson on the condition that he execute a fully-secured undertaking. That decision was communicated to Thompson, along with the “Secured Undertaking” approved by the board, in a letter dated April 4, 2007. The April 4 letter stated:

Although Defendants, including [Power], believe that Mr. Thompson is not entitled to any advancement under any bylaws, the Board of Directors of [Power] has resolved to grant advancement of legal expenses incurred in the Criminal Case (but not the investigations) subject to terms and conditions. Mr. Thompson’s execution of (and compliance with) the secured undertaking enclosed with this letter would satisfy those terms and conditions.⁴

² Joint Exhibit (“JX”) 1 at § 6.6 (emphasis added). The Power bylaws were amended and restated in August 2003, but no change was made to the Advancement Bylaw. JX 2 at § 6.6.

³ JX 1 at § 6.1 (emphasis added); *see also* JX 2 at § 6.1 (using same language).

⁴ JX 11.

The Secured Undertaking set the following conditions on advancement. First, it required that Thompson represent to the board his personal belief that he met the standard for indemnification set forth in the Indemnification Bylaw. That is, Power sought representations that Thompson “acted at all times as an employee . . . of [Power] in good faith and for a purpose that [he] reasonably believed to be in the best interests of [Power] and/or any related entities, including [Williams],” and that he “ha[s] no reasonable cause to believe [his] conduct was unlawful at any time.”⁵ Next, the Undertaking stipulated that only legal expenses incurred after the indictment would be advanced. Finally, it required that Thompson provide, at his own cost, “adequate security to secure fully [his] obligation . . . to repay [Power] any and all amounts advanced by [Power] should it be determined that [he was] not entitled to indemnification” in one of three forms: (i) an irrevocable letter of credit issued by a bank acceptable to Power; (ii) a bond in a form, and from a surety, acceptable to Power; or (iii) other security acceptable to Power in its discretion.⁶ The Secured Undertaking also clarified that additional security could be demanded after the initial Undertaking was signed if Thompson’s expenses increased, stating: “At all times that [Power] is obligated to advance expenses hereunder, the amount of such security shall exceed the total amount of all expenses then requested and all expenses previously advanced.”⁷

⁵ *Id.*

⁶ *Id.*

⁷ *Id.*

Thompson rejected those terms, made no counteroffer to Power that proposed alternative terms or forms of security, and refused to sign the Secured Undertaking that the board provided. Instead, he presses claims in this court asserting that the conditions imposed by the Power board are so onerous that they violate principles of good faith and fair dealing. He also argues that the dollar-for-dollar security demanded by the Power board would be impossible for him to meet, and therefore would, in his opinion, eviscerate the advancement right for which he says he contracted. For those reasons, Thompson seeks a judicial order granting him unconditional, unsecured advancement from Power for all of his expenses incurred during the investigation and judicial proceedings related to his allegedly criminal actions while employed by Power.

In this post-trial opinion, I reject Thompson's claims. The plain language of the Advancement Bylaw vests the Power board of directors with the ability to place reasonable conditions on the credit it advanced to Thompson as a former employee. Thus, Thompson was never promised the unconditional, unsecured advancement he now seeks. Further, I find that the Power board used its contractual discretion rationally and in good faith, particularly in light of Thompson's admission that he lacks the financial wherewithal to obtain dollar-for-dollar security, much less repay Power if it is determined that he is not entitled to indemnification in the future, and his refusal to represent his personal belief that his conduct met the required standard for indemnification. The Power board was entitled to protect the legitimate interests of Power. Although the board could not condition Thompson's right to advancement on arbitrary terms not rationally related to a proper corporate interest, the board was well within its contractual discretion

to require Thompson to establish his ability to repay the loan and to represent that his conduct as an employee was consistent with an ultimate right of indemnification.

In reaching these conclusions, I begin by recognizing that the Delaware General Corporation Law allows, but does not require, corporations to advance the litigation costs and expenses of their directors, officers, key employees and agents.⁸ This court has long recognized that “advancement is not mandatory absent a clearly worded by-law or contract making it mandatory.”⁹ As a corollary to that principle, it is also settled that advancement bylaws are strictly construed according to their terms.¹⁰

There is only one aspect of the Advancement Bylaw that aids Thompson and it does so weakly. As Power admits, any ambiguity in the Advancement Bylaw must be read against it, as the drafter.¹¹ A reading of the Advancement Bylaw as a whole suggests that it was likely that the drafters infelicitously used the word “shall” in the sentence addressing “other employees and agents.” I say this because it strikes me as odd that an Advancement Bylaw, which gives Power’s board the discretion — by use of the term “may” — to deny advancement to a director or officer, was nonetheless intended to mandate that Power’s board offer advancement to other employees and agents. More probable is that the sentence of the Advancement Bylaw that states, “Such expenses incurred by other employees and agents shall be paid upon such terms and conditions, if any, as the Board of Directors deems appropriate,” was intended to reflect another

⁸ 8 *Del. C.* § 145(e); see also *Citadel Holding Corp. v. Roven*, 603 A.2d 818, 823 (Del. 1992).

⁹ *Havens v. Attar*, 1997 WL 695579, at *3 (Del. Ch. 1997).

¹⁰ E.g., *Gentile v. SinglePoint Financial, Inc.*, 788 A.2d 111, 113 (Del. 2001).

¹¹ E.g., *Greco v. Columbia/HCA Healthcare Corp.*, 1999 WL 1261446, at *13 (Del. Ch. 1999).

category involving total discretion on the part of the Power board. Nonetheless, Power concedes that the use of the word “shall” creates ambiguity, and that the last sentence may be read as requiring that “other employees and agents” be offered advancement but subject to terms and conditions unilaterally established by the Power board.

Indeed, it is the very conditionality of the language that renders the word “shall” so inutile for Thompson. In its key respect, the Advancement Bylaw is entirely clear. Power contracted to advance expenses incurred by its employees in defending a civil or criminal action, suit, or proceeding only “upon such terms and conditions, if any, as the Board of Directors deems appropriate.”¹² It did not promise to grant them unconditional, unsecured credit.¹³ Rather, even assuming that the use of the word “shall” required the Power board to offer advancement to Thompson, the remainder of the bylaw makes clear that the board retained substantial leeway to protect Power’s legitimate interests because the board had the discretion to tie Thompson’s access to advancement to his compliance with “terms and conditions” the board unilaterally determined to be “appropriate.”¹⁴

Thompson’s arguments against this conclusion are unpersuasive. First, Thompson’s claim that he is entitled to a broader advancement right than the one provided in the Advancement Bylaw on account of Delaware’s public policy favoring advancement fails because that policy preference “does not trump basic principles of

¹² JX 1 at § 6.6.

¹³ See *Advanced Mining Systems, Inc. v. Fricke*, 623 A.2d 82, 84 (Del. Ch. 1992) (explaining that a board’s decision to grant advancement is essentially a decision to advance credit).

¹⁴ See *West Center City Neighborhood Ass’n v. West Center City Neighborhood Planning Advisory Comm., Inc.*, 2003 WL 241356, at *6 (Del. Ch. 2003) (“Bylaws ‘should be read as a whole and, if possible, interpreted to reconcile all of the provisions of the document.’”) (quoting *Kaiser Aluminum Corp. v. Matheson*, 681 A.2d 392, 395 (Del. 1996)).

contract interpretation.”¹⁵ To the contrary, our law is clear: “any agreement on the part of a corporation to provide advancement rights should be construed according to its terms.”¹⁶

Thompson’s second argument — that the Advancement Bylaw, by not specifying any specific conditions, must therefore provide for advancement to the fullest extent statutorily permissible — ignores the express reservation of rights in the Advancement Bylaw. Unlike the advancement provisions at issue in the *Reddy*¹⁷ and *Tafeen*¹⁸ decisions on which Thompson relies for the proposition that conditions must be spelled out, the Power bylaws did not purport to grant an unfettered right to advancement. Just the opposite, the Advancement Bylaw expressly sets forth the right of the board to impose terms and conditions, and it gives fair notice to anyone hoping to rely on that provision that prerequisites to a grant of advancement might be demanded.

The key question, then, is whether the terms and conditions set by the Power board were “appropriate,” within the meaning of the Advancement Bylaw. Although the Advancement Bylaw does not purport to define the precise boundaries of propriety, the chosen term is best understood as enabling the board to condition a grant of advancement on terms and conditions that rational directors might believe necessary to protect Power’s legitimate interests. So long as the terms and conditions meet that standard, i.e., as an exercise in business judgment by the Power board, someone in Thompson’s position has

¹⁵ *Majkowski v. American Imaging Mgmt. Services, LLC*, 913 A.2d 572, 592-93 (Del. Ch. 2006).

¹⁶ *Gentile*, 788 A.2d at 113.

¹⁷ *Reddy v. Electronic Data Systems Corp.*, 2002 WL 1358761 (Del. Ch. 2002).

¹⁸ *Homestore, Inc. v. Tafeen*, 888 A.2d 204 (Del. 2005).

no contractual basis to complain.¹⁹ That interpretation also comports with the implied covenant of good faith and fair dealing inherent in all contracts, including advancement and indemnification agreements.²⁰ As the Delaware Supreme Court recently explained, “[T]he implied covenant requires a party in a contractual relationship to refrain from arbitrary or unreasonable conduct which has the effect of preventing the other party to the contract from receiving the fruits of the bargain.”²¹ Because terms and conditions must be rationally related to Power’s legitimate interests, Thompson is protected by the implied covenant against any pretextual terms and conditions designed merely to deny him advancement.

With that interpretation in mind, I examine Thompson’s two primary reasons for contending that the terms of the Secured Undertaking were inappropriate. First, he says that it will be impossible for him to provide the dollar-for-dollar security mandated by the Undertaking. Second, Thompson asserts that the terms and conditions imposed on him are more arduous than those the board has levied against the other employees alleged to have been involved in the same activities that formed the basis of his indictment.

¹⁹ Cf. *Advanced Mining*, 623 A.2d at 84 (“Section 145(e) leaves to the business judgment of the board the task of determining whether the undertaking proffered in all of the circumstances, is sufficient to protect the corporation’s interest in repayment and whether, ultimately, advancement of expenses would on balance be likely to promote the corporation’s interests.”).

²⁰ E.g., *Radiancy, Inc. v. Azar*, 2006 WL 224059, at *1 (Del. Ch. 2006) (“[C]orporations that voluntarily extend to their officers and directors the right to indemnification and advancement under 8 *Del. C.* § 145 have a duty to fulfill their obligations under such provisions with good faith and dispatch.”).

²¹ *Dunlap v. State Farm Fire and Casualty Co.*, 878 A.2d 434, 442 (Del. 2005) (internal citations and quotations omitted).

The difficulty for Thompson is that he misconceives Power's duty to him. He sees Power as having a duty to offer him terms and conditions that permit him to receive advancement. But that is not what the Advancement Bylaw says. As long as the terms and conditions Power imposes are "appropriate" — i.e., rationally related to a proper corporate interest — Thompson must adhere to them as a condition of receiving advancement. Simply because Thompson lacks personal assets sufficient to provide adequate security to protect Power's ability to secure repayment in the event that Thompson is ultimately found not to be entitled to indemnification, it does not follow that Power breached any contractual duty to him by demanding such security.

The Power board rationally determined that extending credit to Thompson was a risky proposition; indeed, Thompson's own arguments admit as much. Most of Thompson's assets are co-owned with his wife, and therefore effectively insulated from the reach of his creditors. Thompson, if convicted, faces a prison sentence on conspiracy charges, during which he would presumably be without income. Plus, at the time the board considered his request for advancement, Thompson refused to divulge his personal financial situation to give the board confidence that advances made to him would be repaid if he was ultimately determined not to be entitled to indemnification.²²

Despite that, the Power directors did not deny Thompson's advancement request. They merely conditioned it on a showing of adequate security to cover the advancements he would receive. That Thompson did not have the wherewithal to make such a showing

²² Thompson has admitted that he "provided no financial information to Williams, Power or either of their agents prior to filing this lawsuit." Joint Pretrial Order (June 18, 2007) at ¶ 12.

is irrelevant. The Power board's request for security was rationally tied to the amount of credit the company was advancing and the legitimate purpose of managing the company's exposure to that credit risk. At oral argument, Thompson's counsel tried to pluck the court's equitable heartstrings by pointing out the difficult straits Thompson finds himself in, as a person making a salary in the low six figures, and facing a federal white collar crime prosecution. But, however sympathetic one personally might be to Thompson's circumstances,²³ one cannot reasonably read Power's Advancement Bylaw as granting Thompson a right to credit in circumstances in which he admits that he will not be able to repay Power if Power becomes entitled to repayment. Many corporate advancement provisions do put corporations at such a mandatory, unsecured risk of non-repayment. By clear contrast to such provisions, the Power Advancement Bylaw gave the Power board the discretion to protect the company by conditioning advancement on the provision of security sufficient to guarantee that the corporation would be repaid.

In fact, the Power board decision very much resembles the credit criteria of other lending institutions, which demand at least (and often more than) dollar-for-dollar security on mortgages and other loans as well as covenants regarding the future use of the pledged funds and property. Like any secured loan, a secured grant of advancement can

²³ In noting Thompson's predicament, it is important to keep in mind that he hardly occupies that fate alone. A multitude of non-wealthy criminal defendants face very serious charges and must come up with funds for their defense or rely upon public defenders as their counsel. The court cannot distort contracts and impose on particular parties, such as Power, a duty to provide defense funds in response to a plea based on the assertion that society ought to do more than it is currently doing to assist criminal defendants in defending themselves. That argument provides no legitimate basis for a judge to tax Power so as to provide Thompson with defense funds. Such a fiat would be rooted in sentiments that might legitimately move legislators to enact legislation but that should not motivate a judge interpreting an advancement contract.

be economically beneficial to the recipient because it permits the recipient to use borrowed funds — in this case, at no interest — to meet his obligations. The mere fact that Power was not willing to extend Thompson an interest-free loan without assurance that he could repay the loan if he was convicted does not evidence any contractual breach; rather, it exemplifies exactly the sort of condition one might expect Power reasonably to demand of someone in Thompson's position.

One can envision arbitrary conditions that would evidence contractual bad faith, such as a requirement that Thompson walk a tight-rope between skyscrapers as a condition to receiving advancement, or a demand that Thompson post security worth five times the amount advanced. Conditions such as those would be improper because they would simply act as a bar to Thompson's ability to receive advancement without rationally protecting any legitimate corporate interest. But a demand that Thompson provide sufficient security to ensure that he will be able to repay Power if he is ultimately not entitled to indemnity is very different than those examples, because even if Thompson is unable to comply with the condition, the condition is obviously and reasonably related to protecting Power's legitimate interests as a creditor.

Likewise, Power's demand that Thompson certify that he acted in a manner that was consistent with his ultimate entitlement to indemnification was also appropriate. By that means, Power simply demanded that Thompson evidence his personal belief that he had acted in a manner entitling him to indemnification under the plain terms of the Indemnification Bylaw. The Power board knew that the federal authorities had procured an indictment charging Thompson with having engaged in conduct that cannot be

indemnified; it simply wanted Thompson to certify that he believes himself to have acted lawfully and faithfully. That may seem useless to those of a cynical bent, but I do not believe it inappropriate for the Power board to desire an attestation of good faith from a former employee facing serious criminal charges before extending him hundreds of thousands of dollars in interest-free credit.

Thompson's alternate challenge under the implied covenant relates to the board's decision to offer him credit at different terms than his co-workers. To this point, Thompson offered evidence that twelve other current and former employees of Williams or Power had been advanced legal expenses, that none were required to post security or divulge financial information, and that two were not even required to sign undertakings. Furthermore, drawing on the experience of three of these employees who had their advancement rights terminated when Williams determined that they would not ultimately be entitled to indemnity, Thompson worries that a trap is being set for him whereby Power will lay claim to all of his assets via the security he has been asked to provide and then cut off his advancement because he cannot provide additional security or because the board determines later that his representations regarding his good faith belief in the lawfulness of his conduct were false. All in all, Thompson believes that he is being singled out and offered an illusory advancement right.

As an initial matter, it is critical to note that nothing in the Advancement Bylaw requires that all employees receive the same advancement package. This is not a case in which unconditional and mandatory advancement was guaranteed by the Power bylaws. Power was free to demand different terms and conditions from different employees. So

long as the terms and conditions asked of Thompson were not arbitrary in the sense previously discussed, Thompson has no claim. This court should not read 14th Amendment-like protections against unequal treatment into discretionary advancement contracts governing the relationship of corporations and their executives.

Further, as Power points out, Thompson was differently situated than the other employees to whom he now compares himself.²⁴ Although Thompson sought advances in the context of defending a criminal proceeding (and its foregoing investigation), the other twelve did not. They were witnesses that Williams and Power wanted to induce to cooperate with internal and government investigations by providing them with funds to obtain independent counsel under a different bylaw.²⁵ In fact, when three of the twelve were named as targets or defendants in the investigation, their advancement was stopped. Thus, Thompson is actually being treated more charitably than those three employees because Power has represented that it will not terminate his advancement before the legality of his conduct (and thereby his right to indemnification) is determined in court.²⁶

Relatedly, Power's representation is consistent with how I read the conditions imposed on Thompson by the Secured Undertaking. That is, I do not read the condition that Thompson certify that he believes his past behavior as an employee of Power entitles him to ultimate indemnification as giving Power a license to deny him further advancement if it concludes he lied before his criminal prosecution is concluded. Rather,

²⁴ Trial Transcript ("Tr.") at 42-47.

²⁵ See Tr. at 43 (citing § 6.7 of the bylaws); JX 1 at § 6.7 (permitting advancement and indemnification in circumstances other than those expressly set forth in the bylaws).

²⁶ Tr. at 45-46.

I read it as manifesting the board's demand for an affirmative representation by Thompson of his own belief in the good faith and legality of his actions while an employee as a reassuring prerequisite to advancing him company funds.

For the foregoing reasons, judgment is entered in favor of Williams and Power, and all of Thompson's counts are dismissed.²⁷ The parties shall bear their own costs. IT IS SO ORDERED.

²⁷ Because Thompson refused to meet the terms and conditions required for him to receive any advancement at all, the subsidiary issue involving the question of whether the Advancement Bylaw covers the costs of responding to a criminal investigation before an indictment issues need not be addressed.