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Re: *Miller v. Palladium Industries, Inc.*
C.A. No. 7475-VCN
Date Submitted: September 14, 2012

Dear Counsel:

This is an action, under 8 *Del. C.* § 145(e), for advancement of legal fees and expenses.

Plaintiff David F. Miller, III (“Miller”) served as President, Chief Executive Officer, and Director of Defendant Palladium Industries, Inc. (“Palladium”), its operating subsidiary VisionAid, Inc. (“VisionAid”), and their predecessors from 1983 to 2011.¹ In 2011, VisionAid sued Miller in this Court for breach of

¹ There is some dispute as to when Miller was removed as a director. That dispute is not germane to these proceedings.

fiduciary duty as an officer and director of VisionAid and Palladium, as well as for misappropriation, waste, and conversion (the “Underlying Action”).²

In December 2002, the Palladium board amended its bylaws to provide for advancement. Article X reads in pertinent part:

Section 1. Each person who was or is made a party or is threatened to be made a party to or is involved in any action, suit or proceeding, whether civil, criminal, administrative or investigative (hereinafter a “proceeding”), by reason of the fact that he or she, ..., is or was a director or officer, of the corporation or is or was serving at the request of the corporation as a director, officer, employee, fiduciary, or agent of another corporation ..., shall be indemnified and held harmless by the corporation to the fullest extent which it is empowered to do so unless prohibited from doing so by the General Corporation Law of the State of Delaware, as the same exists or may hereafter be amended (but, in the case of any such amendment, only to the extent that such amendment permits the corporation to provide broader indemnification rights than said law permitted the corporation to provide prior to such amendment) against all expense, liability and loss (including attorneys’ fees actually and reasonably incurred by such person in connection with such proceeding) The right to indemnification conferred in this Article X shall be a contract right and, **subject to Sections 2 and 5 hereof, shall include the right to be paid by the corporation the expenses incurred in defending any such proceeding in advance of its final disposition....**

² *VisionAid, Inc. v. Miller*, C.A. No. 7083-VCN. The amended verified complaint in the Underlying Action appears at Verified Compl. Ex. 1.

Section 2. Any indemnification of a director or officer of the corporation under Section 1 of this Article X or advance of expenses under Section 5 of this Article X shall be made promptly, and in any event within thirty days, upon the written request of the director or officer.... If the corporation denies a written request for indemnification or advancing of expenses, in whole or in part, or if payment in full pursuant to such request is not made within thirty days, the right to indemnification or advances as granted by this Article X shall be enforceable by the director or officer in any court of competent jurisdiction. Such person's costs and expenses incurred in connection with successfully establishing his or her right to indemnification, in whole or in part, in any such action shall also be indemnified by the corporation....

Section 5. Expenses incurred by any person described in Section 1 of this Article X in defending a proceeding ***shall be paid by the corporation in advance of such proceeding's final disposition unless otherwise determined by the Board of Directors in the specific case*** upon receipt of an undertaking by or on behalf of the director or officer to repay such amount if it shall ultimately be determined that he or she is not entitled to be indemnified by the corporation....³

³ Verified Compl. ¶ 7 (quoting Palladium's Bylaws, Art. X) (emphasis revised in part). The complete text of Article X of Palladium's Bylaws may be found at David F. Miller III's Answering Brief in Opposition to Defendant's Motion for Judgment on the Pleadings, Ex. 1.

On March 19, 2012, Miller sought advancement from Palladium⁴ for the fees and expenses incurred in defending the Underlying Action.⁵ Palladium's board rejected Miller's request for advancement and set forth its reasons:

The Palladium board has considered Mr. Miller's request for advancement of fees. In a duly noticed special meeting of the directors, held on April 17, 2012, the board has voted to deny the request as not being in the Company's best interest. The board based this decision on multiple independent reasons. In the board's view, each reason standing alone merits denial of the request. Those reasons include, without limitation:

1. Were the board to advance fees and expenses, Palladium and VisionAid would not have funds adequate to meet operating expenses and their own litigation expenses;

2. The company's impaired financial condition and lack of sufficient funds is due in large part to Mr. Miller's conduct at issue in the litigation;

3. In light of the facts known to Palladium, the likelihood that Mr. Miller would be required to repay any advanced funds is high;

⁴ Both Palladium and VisionAid are Delaware corporations. Verified Compl. ¶ 1.

⁵ Verified Compl. Ex. 2.

4. The likelihood Mr. Miller would be able to perform his repayment obligation is low. Despite Palladium's request, Mr. Miller has not offered to provide collateral that would be sufficient to secure his repayment obligation nor has he provided evidence of his ability to satisfy both the expected judgment and his repayment obligation;

5. It is not in the company's interest to finance an opposition to the company's claims, especially when the would-be recipient of such financing has no demonstrated ability to repay any funds advanced.⁶

When his request was denied, Miller brought this action.

* * *

Palladium has moved for judgment on the pleadings. Its motion presents a narrow issue. Palladium's Bylaws provide that defense expenses "shall be paid . . . in advance of . . . final disposition."⁷ That sounds like mandatory advancement.⁸ The bylaws, however, go on to provide that advancement will be paid "unless otherwise determined by the Board of Directors in the specific case"⁹ The question presented, thus, is straightforward. Does the language following "unless" convert what otherwise seems to be a mandatory right to advancement provision

⁶ Verified Compl. Ex. 3 (Letter of Kenneth R. Berman, Esq. to Jay Flynn, Esq., dated April 18, 2012).

⁷ Palladium's Bylaws, Art. X, § 5 (quoted in Verified Comp. ¶ 7).

⁸ *Schoon v. Troy Corp.*, 948 A.2d 1157, 1169 (Del. Ch. 2008).

⁹ Palladium's Bylaws, Art. X, § 5.

("[e]xpenses . . . shall be paid . . .") into one that, nevertheless, remains subject to the board's taking action specifically to reject the advancement request.

* * *

Court of Chancery Rule 12(c) governs a motion for judgment on the pleadings which may appropriately be granted when no material facts are in dispute and the moving party is entitled to judgment as a matter of law. The Court must accept the facts well-pleaded by the non-moving party and draw its reasonable inferences from those facts in the "light most favorable" to the non-moving party.¹⁰

* * *

Whether applying a bylaw or a contract, the Court uses a reasonable third-party's reading of the pertinent terms.¹¹ A few fundamental precepts of contract law guide the Court in this instance. The words of the bylaw will be given their plain and ordinary meaning. The bylaws, as with a contract, will be construed in

¹⁰ *Desert Equities, Inc. v. Morgan Stanley Leveraged Equity Fund II, L.P.*, 624 A.2d 1199, 1205 (Del. 1993).

¹¹ *Matria Healthcare, Inc. v. Coral SR LLC*, 2007 WL 763303, at *6 & n.20 (Del. Ch. Mar. 1, 2007).

an effort to give meaning to all of its provisions.¹² A contract is ambiguous when the provisions in debate are “reasonably or fairly susceptible of different interpretations or may have two or more different meanings.”¹³ If there is no ambiguity and the meaning can be ascertained from the words themselves, reference to extrinsic evidence is neither necessary nor permitted.¹⁴

* * *

The Delaware General Corporation Law allows for, but does not require, advancement. By 8 *Del. C.* § 145(e), “[e]xpenses . . . incurred by an officer or a director . . . in defending any . . . action . . . may be paid by the corporation in advance of the final disposition of such action” Indeed, a corporation may provide for mandatory advancement.¹⁵ Delaware policy favors indemnification and advancement as a means of attracting qualified individuals to serve in important corporate capacities.¹⁶ That policy supports the approach of resolving

¹² *O’Brien v. Progressive N. Ins. Co.*, 785 A.2d 281, 287 (Del. 2001).

¹³ *Rhone-Poulenc Basic Chems. Co. v. Am. Motorists, Ins. Co.*, 616 A.2d 1192, 1196 (Del. 1992).

¹⁴ *Eagle Indus., Inc. v. DeVilbiss Health Care, Inc.*, 702 A.2d 1228, 1232 (Del. 1997).

¹⁵ See *Reddy v. Electronic Data Sys. Corp.*, 2002 WL 1358761, at *3-4 (Del. Ch. June 18, 2002).

¹⁶ See, e.g., *Homestore, Inc. v. Tafeen*, 888 A.2d 204, 218 (Del. 2005).

ambiguity in favor of indemnification and advancement.¹⁷ However, absent a bylaw or contractual provision that makes advancement mandatory, Delaware law leaves the decision to advance expenses to the business judgment of the board.¹⁸

Palladium's Bylaws do, however, provide for advancement that, at least in some instances, amounts to mandatory advancement. The only reading of Palladium's advancement provision is that advancement shall be paid (*i.e.*, up to this point, it is mandatory) unless Palladium's board specifically determines not to pay a specific advancement. In other words, Palladium must advance legal fees and expenses if the board does not adopt a contrary directive. This is the only fair reading of the pertinent provision (Art. X) of Palladium's Bylaws.¹⁹ Failure of the board to act in a specified time after receipt of a request for advancement will leave the request as a mandatory one. Here, the board acted in a timely fashion—within roughly thirty days from the date of Miller's demand.

¹⁷ *Sun-Times Media Group, Inc. v. Black*, 954 A.2d 380, 404 (Del. Ch. 2008).

¹⁸ *Bernstein v. TractManager, Inc.*, 953 A.2d 1003, 1008 (Del. Ch. 2007).

¹⁹ Because Palladium's advancement bylaw is not ambiguous, there is no reason to consider extrinsic evidence or the *contra proferentum* doctrine.

Palladium's board, as it was authorized to do, adopted an advancement regime which assured its covered officers, directors, and employees of advancement unless the board acted to deny the right in a particular case. That is what the board did in this specific instance and that is why, as a matter of undisputed fact, Miller's case for advancement must be dismissed as a matter of law.

* * *

Miller relies upon *Stockman v. Heartland Industrial Partners, L.P.*²⁰ *Stockman* is an example of how to apply the principles that a contract must be read as a whole and that all provisions, if possible, should be ascribed meaning. Two separate sentences from the advancement provision of the bylaws in *Stockman* framed the debate:

Expenses reasonably incurred by an Indemnitee in defense or settlement of any claim that may be subject to a right of indemnification hereunder shall be advanced by the Partnership prior to the final disposition thereof upon receipt of an undertaking by or on behalf of the Indemnitee to repay such amount to the extent that it shall be determined ultimately that such Indemnitee is not entitled to be indemnified hereunder.

²⁰ 2009 WL 2096213 (Del. Ch. July 14, 2009).

No advances shall be made by the Partnership under this Section 4.4(b)(i) without the prior written approval of the General Partner or (ii) in connection with an action brought against an Indemnatee by a Majority in Interest of the Limited Partners.²¹

The corporation in *Stockman* sought to avoid advancement by relying upon the “prior written approval of the General Partner.” In other words, the General Partner, in his discretion, could render the first sentence effectively meaningless. The Court, however, concluded that the second sentence authorized the General Partner to determine that the form of the request for advancement was proper and that the request complied with various technical requirements, such as the delivery of an undertaking to repay the sums advanced if that became necessary.²²

In Palladium’s Bylaws, there is no way to isolate the “unless” provision from the advancement grant provision. There is no way to give separate and independent meaning to the “unless” clause except as Palladium has interpreted it. Section 1 of Article X of Palladium’s Bylaws is expressly made subject to Section 5. The “unless” language is an integral part of Section 5. Ultimately, the

²¹ *Id.* at *3 (italics omitted).

²² *Id.* at *5-8.

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difference between Miller's claim and *Stockman's* claim is that Miller has not conjured up a way to give meaning to the "unless" phrase.²³

* * *

Accordingly, for the foregoing reasons, the Palladium board, by acting in accordance with the plain meaning of Palladium's Bylaws, effectively rejected Miller's request for advancement. Accordingly, Palladium is entitled to judgment on the pleadings. Therefore, judgment is entered in favor of Palladium and against Miller. This action is dismissed. The parties shall bear their own costs.

IT IS SO ORDERED.

Very truly yours,

/s/ John W. Noble

JWN/cap
cc: Register in Chancery-K

²³ Miller also contends that the Palladium board had wrongfully sought to impose additional conditions on his right to advancement. These additional conditions include providing financial information and identification of collateral to secure any future repayment. The Court's conclusion that Miller's request for advancement was properly rejected obviates the need to address this argument.