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Re: *Fuhlendorf v. Isilon Systems, Inc.*
C.A. No. 5772-VCN
Date Submitted: June 11, 2011

Dear Counsel:

Plaintiff Stuart W. Fuhlendorf entered into an agreement with Defendant Isilon Systems, Inc. ("Isilon"), under which he is entitled to advancement of expenses incurred in defending several actions arising out of his employment with Isilon (the "Indemnification Agreement"). Mr. Fuhlendorf filed a motion for summary judgment on October 4, 2010 (the "Summary Judgment Motion"). Because the parties agreed that he was entitled to summary judgment as to his right

to advancement,¹ the issue raised at that juncture related only to whether a review of the reasonableness of the amounts sought by Mr. Fuhlendorf pursuant to Isilon's advancement obligation was appropriate at that time.

In his opening brief in support of the Summary Judgment Motion, Mr. Fuhlendorf took issue with Isilon's position that it could elect to advance only 50% of the submitted amounts and that it could seek a reasonableness review of any disputed expenses. In addition, Mr. Fuhlendorf also argued that he was entitled to an award of fees on fees and pre-judgment interest because of Isilon's refusal to advance all of his expenses.

In response, Isilon, while recognizing Mr. Fuhlendorf's entitlement to advancement, argued that the fees and expenses must be reasonable according to both Delaware law and the Indemnification Agreement. For that reason, Isilon set forth that it had proposed a reasonableness review process to Mr. Fuhlendorf that was analogous to the procedures ordered in *Duthie v. CorSolutions Medical, Inc.*²

¹ See *Fuhlendorf v. Isilon Sys., Inc.*, 2010 WL 4570225, at *1 n.1 (Del. Ch. Nov. 9, 2010) (the "Letter Opinion").

² 2008 WL 4173850 (Del. Ch. Sept. 10, 2008).

There, the parties were to divide equally the costs of the special master selected to resolve the disputed amounts under the advancement obligation, the exception being that the entire cost of the special master was to be borne by the objecting party if those objections were determined to have been made without good cause.³

In his reply letter in support of the Summary Judgment Motion, Mr. Fuhlendorf reiterated his contention that referral of any disputed amounts to a special master for reasonableness review was contrary to the requirements of Delaware law. Absent evidence of bad faith or clear abuse—which Mr. Fuhlendorf argued had not been presented—he asserted that a reasonableness review was not proper and, at the very least, should be deferred to avoid prejudicing his defense in the underlying proceedings. Mr. Fuhlendorf characterized Isilon’s position as another attempt to delay complying with its advancement obligations.

The Court, recognizing that the value of advancement would be impaired if payment was not promptly made, nevertheless observed that the fees and expenses

³ *Id.* at *2.

sought by way of advancement must be reasonable.⁴ Accordingly, the Court, employing the procedures of *Duthie*, prescribed a series of steps for the parties to follow; most significantly, if, after following certain steps, a dispute remained as to the reasonableness of the fees and expenses submitted by Mr. Fuhlendorf, those disputed amounts were to be presented to a special master.⁵ Consistent with *Duthie*, the Court directed that the costs of the Special Master were to be equally divided between the parties, “except that the entire cost of the Special Master [was to] be borne by Isilon if it turn[ed] out that its objections to payment of the fees for which advancement ha[d] been sought [were] made without good cause.”⁶

⁴ *Fuhlendorf*, 2010 WL 4570225, at *1.

⁵ *Id.* In the Letter Opinion, the Court stated as follows: “*Duthie* sets forth an appropriate procedure to be followed: (1) Plaintiff’s counsel, if they have not already done so, shall certify in good faith that the fees and expenses for which advancement has been sought were incurred reasonably as a matter of sound professional judgment; (2) Isilon shall identify those fees which it asserts fall outside the standard of Delaware law for advancement; its counsel shall certify their good faith belief that the advancement of such fees is not appropriate; (3) The fees as to which there is no dispute shall be promptly paid; (4) The fees as to which any dispute remains shall be submitted to a Special Master; and (5) The costs of the Special Master will be divided equally between the parties, except that the entire cost of the Special Master will be borne by Isilon if it turns out that its objections to payment of the fees for which advancement has been sought have been made without good cause.” *Id.* (citation omitted).

⁶ *Id.*

In accordance with the Letter Opinion, the Special Master—finding that Isilon had sufficient good cause to resist the payments requested by Mr. Fuhlendorf—recommended that his fees be allocated equally between the parties.⁷ Thereafter, Mr. Fuhlendorf filed an exception under Court of Chancery Rule 144 challenging that recommendation and arguing that an equal allocation of the Special Master’s fees contradicts Isilon’s obligations under the Indemnification Agreement. Instead, Isilon must bear the costs of the Special Master, according to Mr. Fuhlendorf, because those fees fall under the covered “Expenses” set forth in the Agreement.

A reading of Sections 2(e), 9, and 13(d) of the Indemnification Agreement shows that Mr. Fuhlendorf correctly contends that the Special Master’s fees are “Expenses,” as defined in the Agreement. As a result, Isilon alone is obligated to bear the costs of the Special Master under the Agreement.⁸ The Letter Opinion,

⁷ Final Report Concerning Special Master Fees Through February 2011, at 2.

⁸ Section 13(d) of the Indemnification Agreement provides that the intent of the parties is to prevent Mr. Fuhlendorf from “incur[ring] legal fees or other Expenses associated with the interpretation, enforcement or defense” of his rights under the Agreement “because the cost and expense thereof would substantially detract from the benefits intended to be extended” to Mr. Fuhlendorf. That section further provides that Isilon “shall indemnify [Mr. Fuhlendorf] against any and all Expenses Section 2(e) defines “Expenses” to include court costs and other

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employing the *Duthie* procedures, is noticeably inconsistent with the terms of the parties' contractual arrangement. Although the doctrine of the law of the case generally precludes reconsideration of matters that have been previously ruled upon, the Court may revisit its interlocutory ruling in the Letter Opinion.⁹ Delaware case law suggests, however, that the Court should refrain from doing so, unless a compelling reason exists to disturb that ruling.¹⁰

Whether the Special Master's fees fall within the definition of "Expenses" under the Indemnification Agreement was not at issue in the Summary Judgment Motion. Although the parties' submissions on the Summary Judgment Motion

expenses incurred, "for purposes of Section 13(d) only, . . . in connection with the interpretation, enforcement or defense of [Mr. Fuhlendorf's] rights under [the Indemnification] Agreement, by litigation or otherwise."

⁹ See *In re CNX Gas Corp. S'holders Litig.*, 2010 WL 2705147, at *2 (Del. Ch. July 5, 2010) (quoting *Siegman v. Columbia Pictures Entm't, Inc.*, 1993 WL 10969, at *3 (Del. Ch. Jan. 15, 1993)). This case is unlike *Dr Pepper Bottling Co. of Texas*, because in that appraisal action the Court was called upon to reconsider its valuation analysis after a form of judgment had been implemented. See *Crescent/Mach I P'ship, L.P. v. Dr Pepper Bottling Co. of Tex.*, 2008 WL 2440303 (Del. Ch. June 4, 2008), *rev'd sub nom. Crescent/Mach I Partners, L.P. v. Dr Pepper Bottling Co. of Tex.*, 962 A.2d 205 (Del. 2008). Here, no final judgment has yet been entered.

¹⁰ *CNX Gas Corp.*, 2010 WL 2705147, at *2; see also *Zirn v. VLI Corp.*, 1994 WL 548938, at *2 (Del. Ch. Sept. 23, 1994) ("Once a matter has been addressed in a procedurally appropriate way by a court, it is generally held to be the law of that case and will not be disturbed by that court unless compelling reason to do so appears.").

may have tangentially related to that question, the Court did not consider that matter in crafting the Letter Opinion. Rather, it simply drew upon the procedures set forth in *Duthie* for a reasonableness review methodology—an arrangement that the Court, with the benefit of a more comprehensive understanding of the Indemnification Agreement, concludes is partly incompatible with the provisions of that agreement.¹¹ Moreover, a review of the transcript of the argument on the Summary Judgment Motion reveals no discussion as to what the proper division of a special master's fees should have been in the event the Court was inclined to allow a reasonableness review. For that reason, although the Court arguably ruled on that issue in the Letter Opinion, it was never squarely raised at any point during the Summary Judgment Motion and was not necessary for the Court to have addressed in the Letter Opinion.

To the extent a compelling reason is necessary for the Court to revisit its earlier interlocutory ruling contained in the Letter Opinion, a sufficient basis to do so exists in this instance. Although the Court could articulate reasons for

¹¹ The language used in the Indemnification Agreement makes clear that the intent of the parties was to provide substantial protection to Mr. Fuhlendorf and, thus, it is distinctly employee-friendly.

concluding that the Letter Opinion is the law of the case and should not be disturbed,¹² the better course of action here is to reassess that ruling because of the Court's obligation "to give meaning and substance to the words that the parties have freely chosen" in the Indemnification Agreement.¹³ Moreover, the Court is mindful that the Delaware General Corporation Law "is intentionally designed to provide directors and stockholders with flexible authority, permitting great discretion for private ordering and adaptation."¹⁴ That preference for private ordering extends, at least to some extent, to indemnification and advancement rights under 8 *Del. C.* § 145.¹⁵

¹² The primary reason counseling against revisiting the allocation of the Special Master's fees is the significant delay by Mr. Fuhlendorf in raising this issue. He had ample opportunity to object to or to seek reconsideration under Court of Chancery Rule 59(f) of the Court's guidelines pertaining to the Special Master's fees after the Letter Opinion was issued on November 9, 2010. Nonetheless, Mr. Fuhlendorf made no such effort in this Court until he filed his notice of exception on March 21, 2011. By that time, the Special Master had already issued the final report on the reasonableness of the fees requested by Mr. Fuhlendorf under the Indemnification Agreement and the final report concerning the allocation of the Special Master's fees.

¹³ See *CorVel Enter. Comp, Inc. v. Schaffer*, 2010 WL 2091212, at *4 (Del. Ch. May 19, 2010). The Court's decision to reconsider the Letter Opinion is predominantly guided by a concern for giving meaning to the Indemnification Agreement.

¹⁴ *Hollinger Int'l, Inc. v. Black*, 844 A.2d 1022, 1078 (Del. Ch. 2004)

¹⁵ See *Perconti v. Thornton Oil Corp.*, 2002 WL 982419, at *9-*10 (Del. Ch. May 3, 2002).

Thus, in accordance with the terms of the Indemnification Agreement, Isilon is solely responsible for any fees arising from a reasonableness review conducted by a special master. For that reason, the Special Master's fees of approximately \$45,000 incurred through February 2011 are to be paid by Isilon,¹⁶ along with any future amounts arising from similar proceedings before the Special Master.¹⁷

IT IS SO ORDERED.

Very truly yours,

/s/ John W. Noble

JWN/cap
cc: Register in Chancery-K

¹⁶ The Special Master's fees incurred through February 2011 (and presumably any additional fees incurred after that date) are negligible when compared to the approximately \$5.53 million advancement obligation of Isilon. It had previously advanced roughly \$4 million and, after his review, the Special Master recommended that the Court order the prompt payment by Isilon of roughly an additional \$1.5 million, a recommendation to which no exception was taken.

¹⁷ Although this issue is raised procedurally as an exception to the Special Master's final report on fees, Mr. Fuhlendorf's request ultimately seeks a reexamination of the Letter Opinion, which set forth the procedures for the Special Master to follow in deciding how his fees were to be allocated between the parties. The Special Master correctly implemented the Court's earlier directives. Now, however, the Court is modifying its own earlier ruling, which was the basis upon which the Special Master had recommended his fee allocation.