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OPTION AGREEMENT TRUMPS EMPLOYMENT AGREEMENT

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"The court concluded that even assuming that the executive and Chevron reached an express employment agreement . . . permitting exercise later than the three month deadline under the LTIP, . . . the option grants effectively modified the original employment agreement . . . ."

Disputes about the late exercise of options are a dime a dozen. But a recent unreported case caught our eye because of a twist we found interesting. The case is *Porkert v. Chevron Corp.*, 2012 U.S. App. LEXIS 710 (4th Cir. 2012).

In *Porkert*, an executive asserted that the final version of his employment agreement included a provision permitting him to exercise stock options for 10 years from the date he received the options, even if he terminated employment earlier. The federal appeals court (the Fourth Circuit) assumed the executive's assertion as to the employment agreement was accurate even though the executive did not have a copy of the agreement he described. The court did so because it was reviewing a summary judgment award (in favor of the executive's employer, Chevron), and was therefore required to resolve factual disputes in the executive's favor. Of perhaps some note, stock options the executive received as a signing bonus did, in fact, permit exercise for the remainder of their 10 year term following termination of employment. Those options were, however, not the subject of the dispute.

The grants for the executive's options in dispute indicated that they were subject to Chevron's Long-Term Incentive Plan ("LTIP") and its rules. The executive acknowledged that he understood the LTIP and its rules were incorporated into the option grants, and that the LTIP and its rules were available upon request. The executive did not, however, "have time" to read those documents.

The executive probably wished he had read the documents, because they explained that on termination prior to age 65 (the executive retired when he was 64), the options were exercisable for only three months following termination. The executive missed this deadline. When the executive retired, almost 72,000 of his 110,000 stock options were vested, but he did not attempt to exercise any of those options until more than two years following his retirement. Chevron said that was too late.

The plaintiff had received annual stock option grants from 1999 through 2004. For the years 1999 through 2001, the executive accepted and signed each stock option grant, as required by the terms of those grants. He also accepted annual grants from 2002 until 2004, though those grants did not require his signature.

The court concluded that even assuming that the executive and Chevron reached an express employment agreement as described by the executive (permitting exercise later than the three month deadline under the LTIP), the

option grants effectively modified the original employment agreement because the executive agreed to the terms of the LTIP incorporated into each grant. The executive argued that the grants could not have modified his employment agreement because a modification of that agreement would have required a "meeting of the minds" and "new consideration."

The appeals court rejected the executive's arguments that the option grants did not modify any conflicting terms in the executive's employment agreement. In doing so, the court applied California law to determine the rules for a valid modification of a written contract.

The court said under California law an offer of stock options constitutes an offer for a unilateral contract, which is accepted if the employee continues in employment after the offer. Specifically, "[c]onsideration is inherent where stock options are granted to employees and the employee continues employment knowing of the options." Although in some circumstances the adequacy of consideration may be a question of fact for a jury, where the facts underlying the purported consideration are uncontested, a court is permitted to find consideration adequate as a matter of law, which the court of appeals did.

The court rejected the executive's argument that the parties did not reach a meeting of the minds concerning the particular LTIP term restricting exercise after termination to a three month period. That was because the executive unequivocally accepted each grant on an annual basis and did so knowing that each grant was expressly governed by the LTIP terms and rules.

The court also found no merit in the executive's argument that the grants were not "new consideration" sufficient to support a modification of his employment contract. In doing so, the court reiterated that the rule in California is that consideration is inherent when stock options are granted to an employee who continues in that employment with knowledge of the option grant. Since the executive continued his employment with Chevron after unambiguously accepting the grants for specific and substantial numbers of options knowing they were governed by the LTIP, he could not argue that the grants lacked the consideration necessary to modify his prior employment agreement.

All of this led the court to conclude that the option grants modified any prior agreement to the contrary. This meant the executive was required to exercise his stock options within three months of his retirement date, which he failed to do.

Lesson. Although an unpublished decision, we think *Porkert* is of considerable interest. The lesson for employers is that having executives sign grant awards, and expressly acknowledge that the grants are subject to the terms of the LTIP or omnibus plan under which they are issued, may prove helpful should an executive later assert that the terms of the plan or grant conflict with one-off terms included in a prior employment agreement. The companion lesson is that if the parties' intention is that special terms in an employment agreement differ from the default terms in an option plan, those special provisions applicable to the executive should be expressly reflected in any awards issued (in a fashion consistent with the granting committee's power to vary from the plan's default terms).

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