2006 ABA ANNUAL MEETING

SECTION OF BUSINESS LAW

Important Case Law Developments for Partnerships
and Limited Liability Companies

2005-2006 SUPPLEMENT TO

CUMULATIVE SURVEY OF DELAWARE CASE LAW

RELATING TO

ALTERNATIVE ENTITIES*

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* The entire Cumulative Survey is available on the Morris Nichols website at www.MNAT.com under Publications/Legal Periodicals and Seminar Papers/Partnerships and Limited Liability Companies.

II. LIMITED PARTNERSHIPS

A. Fiduciary Duties

1. *Duties of General Partners*

a. *Anglo American Security Fund, L.P. v. S.R. Global International Fund, L.P.*, C.A. No. 20066-N (Del. Ch. May 24, 2006)

Plaintiffs were limited partners ("LPs") in a Delaware limited partnership operating as a hedge fund (the "Fund") and brought suit against the Fund, its general partner ("GP") and its independent auditors for breach of contract, breach of fiduciary duty and negligence. Both the plaintiffs and defendants moved for summary judgment, and the court granted the defendants' motion. At the center of the dispute were provisions of the limited partnership agreement relating to the deduction, crediting and withdrawal of the GP's incentive fee. The partnership agreement provided that the GP was entitled to a 15% incentive fee on the LPs' net profits, such incentive fee to be deducted from each LP's capital account and credited to the GP's capital account as of the end of the fiscal year. The GP had the right to withdraw funds from its capital account as of the last day of any month. The books and records of the Fund were to be audited by an independent certified accountant as of the end of each fiscal year, and the Fund was to provide copies of the audited financial statements to the LPs after the end of each fiscal year. On December 31, 1999, the incentive fee was deducted from the LPs' capital accounts and credited to the GP's capital account (the "Allocation"). After the close of business on the same day, the incentive fee was withdrawn from the GP's capital account (the "Withdrawal"). The Allocation was reported to the LPs in February of 2000 in the Fund's 1999 fourth quarter financial statement, but the Withdrawal was not. Instead, the Withdrawal was reported in May in the Fund's first quarter statement for the year 2000. Based on the Fund's fourth quarter statement received in February, the plaintiffs withdrew part of their investment, but without regard to whether or not the GP kept its 1999 incentive fee invested in the Fund. After the Withdrawal was disclosed in May, the plaintiffs continued to remain invested in the Fund.

The plaintiffs alleged that the GP breached its fiduciary duties by misstating that it had retained the incentive fee in its capital account when it had actually withdrawn nearly all of it, by not disclosing the Withdrawal as a subsequent event and by not disclosing that the Withdrawal was contrary to the terms of the limited partnership agreement. The court held that the plaintiffs had not established that they relied upon the omitted disclosure of the Withdrawal in the 1999 fourth quarter financial statements. Thus the court refused to consider whether the 1999 statement should have disclosed the Withdrawal or whether the Withdrawal should have been reported in the Subsequent Event footnote of those financials. In so holding, the court rejected the plaintiffs' reliance on federal precedents under Section 10(b) of the Securities Exchange Act of 1934. Specifically, the court reiterated that Delaware does not recognize the "fraud on the market" theory recognized in the federal courts. In breach of fiduciary duty cases based on omissions, reliance may only be presumed when shareholder or partner action is requested. As such action was not requested in the present case, the plaintiffs were required to prove reliance, which they failed to do.

With regard to plaintiffs' disclosure claim, the court emphasized that if the language of a contract is unambiguous, its plain meaning would dictate the outcome, and held that the unambiguous language of the partnership agreement

did not impose a duty of disclosure on the defendants in the present circumstances.

The plaintiffs' negligence claim was rejected for several reasons. First, the limited partnership agreement exculpated the defendants from liability for negligent conduct. Second, Section 17-407 of the Delaware Revised Uniform Limited Partnership Act ("DRULPA") shields a general partner from liability when it relies in good faith upon those charged with properly preparing and presenting financial records. Because the GP had relied on the Fund's administrator and independent auditors, Section 17-407 protected it from liability. Finally, the court rejected the plaintiffs' negligence claim because they failed to prove reliance.

Because the plaintiffs failed to prove reliance and failed to prove a breach of fiduciary duty, their claims against the independent auditors for negligent misrepresentation and aiding and abetting a breach of fiduciary duty also failed.

b. *McGovern v. General Holding, Inc.*, C.A. No. 1296-N (Del. Ch. May 18, 2006)

Plaintiffs were limited partners in KX Industries, L.P., a Delaware limited partnership ("KXI"). Defendant Evan Koslow was chief inventor and CEO of KXI and controlled the general partner and owned 90% of KXI's equity. The plaintiffs sued Evan, the general partner and other instrumentalities of Evan for breach of fiduciary duty and breach of the limited partnership agreement.

KXI had developed numerous new technologies that had the potential for lucrative sales over the next several years. As the company's future began to look bright, Evan attempted to squeeze out plaintiffs by claiming that most of the patents for the new technologies were actually owned by one of his wholly-owned companies, Koslow Technologies Corporation ("KT"). He contemplated selling KXI's already established business, cashing out plaintiffs and moving forward to reap the financial rewards of the new technologies on his own.

The court found that Evan breached both the partnership agreement and his fiduciary duties by appropriating the company's valuable technology. It rejected Evan's primary defense which was based on a 1989 License Agreement between KXI and KT that Evan asserted made KT the owner of the new technologies. This license agreement was formed when KXI was a joint venture between Evan and a subsidiary of Exxon, and disagreements as to its scope and validity were part of the reason Exxon left the partnership. The court held that the license agreement did not excuse Evan's behavior for several reasons.

First, the court found that the license agreement was of dubious validity because the limited partnership agreement between Evan and the Exxon subsidiary required that Exxon give prior written consent to any contracts between KXI and KT, and there was no such written consent. Second, the court found that the license was moribund. After Exxon had left the partnership, Evan largely abandoned KT as an operating company and converted it into, what was by all appearances, a patent holding company for KXI. No work was done by KT as an operating company, and it had no employees. The plaintiffs were all led by Evan to believe that KT was merely a patent holding company for KXI and that the new technologies belonged to KXI. KXI had born all the risks and costs of researching and developing the new technologies. Having treated the license as inoperative for nearly 16 years, the court found that Evan could not conveniently assert that it compelled him to appropriate KXI's valuable technology.

The court also held that even if the license agreement were operative, which it was not, Evan breached his fiduciary duties by having KXI pursue costly research from which it could gain no economic value but would instead enrich Evan personally. The court also found that Evan breached the limited partnership agreement which contained clauses stipulating that all property acquired by the partnership was deemed to be owned by the partnership and that the resources of the partnership could be used for partnership purposes only and not for the personal benefit of any of the partners.

Finally, the court held that even if the license agreement were operative, Evan interpreted it in an implausible and inconsistent manner. At most, the license agreement covered improvements that were based upon an older technology and did not cover the broad range of new developments and technologies that KXI had pursued at Evan's behest.

Using its broad equitable powers to grant appropriate relief, the court ordered that KT transfer the patent rights to KXI without payment, that KXI be dissolved, Evan removed as general partner and a receiver be appointed to sell KXI and an affiliate company. It also ordered that Evan be precluded from bidding for KXI and that he be prohibited from competing with KXI for a period of three years. Finally, the court held that Evan's behavior precluded the company from indemnifying him for his litigation expenses (and that he was required to return funds he had received as an advance), and held that because the litigation obviously benefited KXI, the plaintiffs would have their reasonable litigation costs and expenses reimbursed by the company.

c. *Albert v. Alex. Brown Mgmt. Servs., Inc.*, C.A. Nos. 762-N, 763-N (Del. Ch. Aug. 26, 2005)

In a further decision in this case brought by limited partners of two Delaware limited partnerships (*see* Sections II.J.1 and II.J.4 for summaries of prior decisions), the court addressed several issues raised by defendants' motion to dismiss that remained unresolved following an earlier decision, including issues relating to plaintiffs' disclosure claims, plaintiffs' breach of fiduciary duty and contract claims, whether plaintiffs' claims were direct or derivative in nature and whether the court had personal jurisdiction over certain defendants.

With respect to plaintiffs' disclosure claims, the court stated that to survive the motion to dismiss, the court must find that the allegations supported a reasonable inference of materiality. The standard to be applied was whether there existed a substantial likelihood that a reasonable investor would have considered the disclosure of the omitted fact to significantly alter the total mix of information. The court determined that the managers' failure to disclose (i) that hedging, which was believed by the managers to be in the best interests of the funds, was impractical because of the funds' liquidity situation, (ii) information regarding the funds' liquidity problems and (iii) the funds' defaults under credit arrangements were material. The court made clear that there is no independent duty of disclosure, but rather that the disclosure allegations must be tied to a fiduciary or contractual duty to disclose, and, in this case, plaintiffs claimed both.

The court then turned to plaintiffs' breach of fiduciary duty claims, the first of which related to the managers' failure to provide financial statements. The court held that, while financial statements were required to be provided as a contractual matter under the partnership agreements, the failure to provide such financial statements did not amount to a fiduciary duty claim. Similarly, the

managers' permitting limited partners to withdraw and redeem their interests pursuant to the partnership agreements did not constitute a breach of fiduciary duty, as there was no personal benefit to the managers to support a breach of the duty of loyalty and there was no gross negligence (which the court stated would require allegations that the managers acted on a "recklessly uninformed" basis or acted "outside the bounds of reason") to support a breach of the duty of care. The partnership agreements' grant of sole discretion to the managers to deny a limited partner's limited contractual right of redemption did not impart a positive duty to exercise such power, regardless of the liquidity issues faced by the funds. Finally, while the court disposed of the related allegations as to the qualifications of the managers, it determined that plaintiffs' allegations regarding the time and attention the managers devoted to the funds and the alleged disclosure violations did state breach of duty of care claims. In this regard, the court explained that adequate management is a fact-intensive question and the answer varies depending on the type of fund and complexity of the issues faced.

With respect to plaintiffs' breach of contract claims, the court set forth the standard to survive a motion to dismiss, which requires proof of (i) the existence of a contract, (ii) breach of a duty imposed by such contract and (iii) damages to plaintiff from such breach. In contrast to the dismissal of the corresponding breach of fiduciary claim, the court found that the failure to provide financial statements did constitute a breach of contract claim. However, plaintiffs' allegations as to the limited partner withdrawals and redemptions were not sufficient to sustain a breach of contract claim. Finally, the court found the managers' failure to provide information due to limited partners under the partnership agreements in good faith and without material misinformation created a breach of contract claim, in addition to the breach of fiduciary duty claim discussed above.

Apart from whether plaintiffs' claims were factually supported, defendants argued that several counts of the complaint were derivative claims for which demand was neither made nor excused. The court first cited the demand requirement in the limited partnership context, as codified in DRULPA Section 17-1001, and observed the substantial similarity to Delaware corporate law, under which the Delaware Supreme Court in *Tooley v. Donaldson, Lufkin & Jenrette, Inc., 845 A.2d 1031 (Del. 2004)*, set forth a revised test for determining whether a suit is derivative or direct. Under the revised test, the only factors are (i) who suffered the harm and (ii) who would receive the benefit of any recovery or other remedy, in each case looking at the corporation or partnership, as applicable, versus the stockholders or interest holders, as applicable. In this case, the court found that the fiduciary duty and contract claims based on alleged failures to disclose were direct claims (for which demand was not required). The harm was to the interest holders, in their loss of the ability to withdraw or redeem their interests in response to the information that would have been gained, and the remedy, which, at this stage, may be monetary damages, would go to such holders. In contrast, the fiduciary duty claims based on gross negligence and inadequate management were derivative claims. Mismanagement is, according to the court, the paradigm of the derivative claim, as the managers' actions caused losses to the funds and any recovery would go to the funds. While the failure of demand, and absence of allegations as to why demand was excused, forced the court to dismiss these claims, plaintiffs were given leave to replead.

The final issue addressed by the court was a challenge to personal jurisdiction over certain defendants. Two individual defendants, who were the owners and

managers of a Tennessee limited liability company that was the general partner of one of the funds, argued that they were residents of Tennessee who performed their duties from such state and had not solicited business from, engaged in regular conduct with, or even traveled to, Delaware. The court explained that upon such a challenge, the burden was on plaintiffs to show the basis for personal jurisdiction, which will then requires the court to determine (i) whether service of process on the nonresident defendant was authorized by the Delaware long-arm statute and (ii) whether the exercise of jurisdiction is consistent with due process. After stating that the Delaware long-arm statute had been interpreted to allow jurisdiction to the fullest extent permitted by the due process clause, the court observed that the funds were formed as Delaware limited partnerships governed by Delaware law and that the entity in which these defendants were managing members and owners was responsible for the day-to-day management of both funds (in its capacity as sub-advisor of each fund, in addition to being the general partner of one fund). The conclusion that the contacts of these defendants constituted "transacting business" within the meaning of the long-arm statute was supported by the facts that the entity that these defendants served (i) participated in the formation of, (ii) was primarily responsible for the management of and (iii) received fees from, the funds. The court then considered whether "minimum contacts" between the nonresident defendants and the state existed -- that is, whether these defendants deliberately engaged in conduct that created obligations between themselves and the state, including the protection of the state's laws, such that these defendants should reasonably anticipate action in Delaware courts. In addition to the facts cited with respect to the long-arm statute, these defendants enjoyed the benefits of Delaware law, including limited liability. Further, Delaware's important interest in regulating entities that choose its laws warrants its exercise of jurisdiction over those who manage such entities and avail themselves of the laws of the state that empower them to act. The claims at issue in this case involved corporate power and fiduciary obligations, which are at the heart of the internal affairs and governance issues of special concern for the state, making the exercise of personal jurisdiction over these defendants appropriate.

C. Removal of General Partners

1. *Hillman v. Hillman*, 2006 WL 2434231 (August 23, 2006)

The plaintiff was general partner of Venhill Limited Partnership L.P., a Delaware limited partnership ("Venhill"). Two trusts served as the limited partners of Venhill. The plaintiff, in his capacity as general partner, invested 1% of the initial capital and each of the trusts contributed 49.5% of the initial capital. The limited partners challenged the plaintiff's actions in causing Venhill to invest a substantial amount of Venhill's assets in Auto-trol ("Auto-trol"), a company founded and controlled by the plaintiff. Unable to resolve the dispute over Venhill's investment in Auto-trol, the limited partners removed the plaintiff as general partner.

The plaintiff filed suit seeking declaratory judgment that upon his removal he had converted his general partner interest into a limited partner interest in Venhill. The suit also alleged that the limited partners breached fiduciary duties owed to him as a limited partner by the actions they took following his removal. The court concluded that Venhill's limited partnership agreement (the "Agreement") did not provide a general partner the right to "elect" to become a limited partner when removed by the limited partners and thus dismissed his claim for a declaratory judgment that he was a limited partner. The court then discussed what rights the plaintiff possessed following his removal.

The court first noted that the Agreement did not provide what a removed general partner would receive in consideration of its interest upon removal. It then reviewed the DRULPA provisions and related legislative history governing the withdrawal of a general partner. Under Section 17-604, a "withdrawing partner" upon withdrawal will be entitled to receive any distribution to which it was entitled under the partnership agreement and if not otherwise provided for in the partnership agreement, the partner shall be entitled to receive the fair value of its partnership interest. The plaintiff argued that Section 17-604 applied to all types of withdrawals by a general partner, while the defendants argued that Section 17-604 was intended to apply only to *voluntary* withdrawals made pursuant to Sections 17-602 and 17-603. The court agreed with the defendants and concluded that the narrower reading of Section 17-604 presented fewer conflicts and was "more consistent with the structure and language of the statute and the legislative history." Thus, Section 17-604 did not apply to the plaintiff because he did not voluntarily withdrawal under Section 17-602.

Having concluded that Section 17-604 did not apply to the plaintiff, the court sought to determine what effect the plaintiff's involuntary withdrawal would have on his economic stake in the partnership. The court noted that under Section 17-1105, if DRULPA is silent on an issue, "an applicable provision of the Delaware Uniform Partnership Law in effect on July 11, 1999 (the "DUPL") and the rules of law and equity… shall govern." Although the court specifically recognized that the DUPL applied to fill the gaps under the DRULPA, it nonetheless referred to the provisions of the Delaware Revised Uniform Partnership Act, 6 Del. C. §§ 15-101 et seq. (the "DRUPA"), rather than the provisions of the DUPL and noted that under the DRUPA a general partner can be dissociated from the partnership upon "the partner's expulsion pursuant to the partnership agreement" and that upon such expulsion, the partnership must cause the dissociated partner's interest to be purchased at an amount equal to the fair value of such partner's economic interest as of the date of dissociation based on such partner's right to share in distributions from the partnership. Thus, the court concluded that under DRULPA, the plaintiff was entitled to receive an amount equal to the fair value of his partnership interest which, the court noted, was comparable to what a withdrawing partner is entitled to under DRULPA Section 17-604. (It should also be noted that under DUPL Section 1542, a partner that is expelled from a partnership the business of which is continued by the remaining partners is entitled to an amount equal to his interest in the partnership.) In addition, the court further noted that because "equity abhors a forfeiture," in the event the general partnership statute did not provide compensation to the plaintiff, he would have a right in equity to seek protection of his economic interest.

Finally, because the plaintiff was removed as a general partner and all of the plaintiff's other claims related to the partnership's conduct following his removal, the plaintiff lacked standing and his other claims for breach of fiduciary and contractual duties were also dismissed.

2. *McGovern v. General Holding, Inc.*, C.A. No. 1296-N (Del. Ch. May 18, 2006)

Plaintiffs were limited partners in KX Industries, L.P., a Delaware limited partnership ("KXI"). Defendant Evan Koslow was chief inventor and CEO of KXI and controlled the general partner and owned 90% of KXI's equity. The plaintiffs sued Evan, the general partner and other instrumentalities of Evan for breach of fiduciary duty and breach of the limited partnership agreement.

KXI had developed numerous new technologies that had the potential for lucrative sales over the next several years. As the company's future began to look bright, Evan attempted to squeeze out plaintiffs by claiming that most of the patents for the new technologies were actually owned by one of his wholly-owned companies, Koslow Technologies Corporation ("KT"). He contemplated selling KXI's already established

business, cashing out plaintiffs and moving forward to reap the financial rewards of the new technologies on his own.

The court found that Evan breached both the partnership agreement and his fiduciary duties by appropriating the company's valuable technology. It rejected Evan's primary defense which was based on a 1989 License Agreement between KXI and KT that Evan asserted made KT the owner of the new technologies. This license agreement was formed when KXI was a joint venture between Evan and a subsidiary of Exxon, and disagreements as to its scope and validity were part of the reason Exxon left the partnership. The court held that the license agreement did not excuse Evan's behavior for several reasons.

First, the court found that the license agreement was of dubious validity because the limited partnership agreement between Evan and the Exxon subsidiary required that Exxon give prior written consent to any contracts between KXI and KT, and there was no such written consent. Second, the court found that the license was moribund. After Exxon had left the partnership, Evan largely abandoned KT as an operating company and converted it into, what was by all appearances, a patent holding company for KXI. No work was done by KT as an operating company, and it had no employees. The plaintiffs were all led by Evan to believe that KT was merely a patent holding company for KXI and that the new technologies belonged to KXI. KXI had born all the risks and costs of researching and developing the new technologies. Having treated the license as inoperative for nearly 16 years, the court found that Evan could not conveniently assert that it compelled him to appropriate KXI's valuable technology.

The court also held that even if the license agreement were operative, which it was not, Evan breached his fiduciary duties by having KXI pursue costly research from which it could gain no economic value but would instead enrich Evan personally. The court also found that Evan breached the limited partnership agreement which contained clauses stipulating that all property acquired by the partnership was deemed to be owned by the partnership and that the resources of the partnership could be used for partnership purposes only and not for the personal benefit of any of the partners.

Finally, the court held that even if the license agreement were operative, Evan interpreted it in an implausible and inconsistent manner. At most, the license agreement covered improvements that were based upon an older technology and did not cover the broad range of new developments and technologies that KXI had pursued at Evan's behest.

Using its broad equitable powers to grant appropriate relief, the court ordered that Evan would be removed as general partner pursuant to the KXI partnership agreement which provided for removal of the general partner for "fraud which is material and detrimental to the Partnership or gross negligence." In ordering removal, the court held that it was "clear that Evan's conduct was in bad faith, worse than grossly negligent, and purposely misleading." It therefore held that the removal provision was easily satisfied. As further relief, the court ordered that KXI be dissolved and a receiver appointed to sell KXI and an affiliated company.

E. Indemnification

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In addition to other relief, the court held that Evan's behavior precluded the company from indemnifying him for his litigation expenses (and that he was required to return funds he had received as an advance), and held that because the litigation obviously benefited KXI, the plaintiffs would have their reasonable litigation costs and expenses reimbursed by the company.

G. Dissolution

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H. Derivative Actions

2. *Demand Requirements*

a. *Albert v. Alex. Brown Mgmt. Servs., Inc.*, C.A. Nos. 762-N, 763-N (Del. Ch. Aug. 26, 2005)

In a further decision in this case brought by limited partners of two Delaware limited partnerships (*see* Sections II.J.1 and II.J.4 for summaries of prior decisions), the court addressed several issues raised by defendants' motion to dismiss that remained unresolved following an earlier decision, including issues relating to plaintiffs' disclosure claims, plaintiffs' breach of fiduciary duty and contract claims, whether plaintiffs' claims were direct or derivative in nature and whether the court had personal jurisdiction over certain defendants.

With respect to plaintiffs' disclosure claims, the court stated that to survive the motion to dismiss, the court must find that the allegations supported a reasonable inference of materiality. The standard to be applied was whether there existed a substantial likelihood that a reasonable investor would have considered the disclosure of the omitted fact to significantly alter the total mix

of information. The court determined that the managers' failure to disclose (i) that hedging, which was believed by the managers to be in the best interests of the funds, was impractical because of the funds' liquidity situation, (ii) information regarding the funds' liquidity problems and (iii) the funds' defaults under credit arrangements were material. The court made clear that there is no independent duty of disclosure, but rather that the disclosure allegations must be tied to a fiduciary or contractual duty to disclose, and, in this case, plaintiffs claimed both.

The court then turned to plaintiffs' breach of fiduciary duty claims, the first of which related to the managers' failure to provide financial statements. The court held that, while financial statements were required to be provided as a contractual matter under the partnership agreements, the failure to provide such financial statements did not amount to a fiduciary duty claim. Similarly, the managers' permitting limited partners to withdraw and redeem their interests pursuant to the partnership agreements did not constitute a breach of fiduciary duty, as there was no personal benefit to the managers to support a breach of the duty of loyalty and there was no gross negligence (which the court stated would require allegations that the managers acted on a "recklessly uninformed" basis or acted "outside the bounds of reason") to support a breach of the duty of care. The partnership agreements' grant of sole discretion to the managers to deny a limited partner's limited contractual right of redemption did not impart a positive duty to exercise such power, regardless of the liquidity issues faced by the funds. Finally, while the court disposed of the related allegations as to the qualifications of the managers, it determined that plaintiffs' allegations regarding the time and attention the managers devoted to the funds and the alleged disclosure violations did state breach of duty of care claims. In this regard, the court explained that adequate management is a fact-intensive question and the answer varies depending on the type of fund and complexity of the issues faced.

With respect to plaintiffs' breach of contract claims, the court set forth the standard to survive a motion to dismiss, which requires proof of (i) the existence of a contract, (ii) breach of a duty imposed by such contract and (iii) damages to plaintiff from such breach. In contrast to the dismissal of the corresponding breach of fiduciary claim, the court found that the failure to provide financial statements did constitute a breach of contract claim. However, plaintiffs' allegations as to the limited partner withdrawals and redemptions were not sufficient to sustain a breach of contract claim. Finally, the court found the managers' failure to provide information due to limited partners under the partnership agreements in good faith and without material misinformation created a breach of contract claim, in addition to the breach of fiduciary duty claim discussed above.

Apart from whether plaintiffs' claims were factually supported, defendants argued that several counts of the complaint were derivative claims for which demand was neither made nor excused. The court first cited the demand requirement in the limited partnership context, as codified in DRULPA Section 17-1001, and observed the substantial similarity to Delaware corporate law, under which the Delaware Supreme Court in *Tooley v. Donaldson, Lufkin & Jenrette, Inc., 845 A.2d 1031 (Del. 2004)*, set forth a revised test for determining whether a suit is derivative or direct. Under the revised test, the only factors are (i) who suffered the harm and (ii) who would receive the benefit of any recovery or other remedy, in each case looking at the corporation or partnership, as applicable, versus the stockholders or interest holders, as applicable. In this case, the court found that the fiduciary duty and contract claims based on alleged

failures to disclose were direct claims (for which demand was not required). The harm was to the interest holders, in their loss of the ability to withdraw or redeem their interests in response to the information that would have been gained, and the remedy, which, at this stage, may be monetary damages, would go to such holders. In contrast, the fiduciary duty claims based on gross negligence and inadequate management were derivative claims. Mismanagement is, according to the court, the paradigm of the derivative claim, as the managers' actions caused losses to the funds and any recovery would go to the funds. While the failure of demand, and absence of allegations as to why demand was excused, forced the court to dismiss these claims, plaintiffs were given leave to replead.

The final issue addressed by the court was a challenge to personal jurisdiction over certain defendants. Two individual defendants, who were the owners and managers of a Tennessee limited liability company that was the general partner of one of the funds, argued that they were residents of Tennessee who performed their duties from such state and had not solicited business from, engaged in regular conduct with, or even traveled to, Delaware. The court explained that upon such a challenge, the burden was on plaintiffs to show the basis for personal jurisdiction, which will then requires the court to determine (i) whether service of process on the nonresident defendant was authorized by the Delaware long-arm statute and (ii) whether the exercise of jurisdiction is consistent with due process. After stating that the Delaware long-arm statute had been interpreted to allow jurisdiction to the fullest extent permitted by the due process clause, the court observed that the funds were formed as Delaware limited partnerships governed by Delaware law and that the entity in which these defendants were managing members and owners was responsible for the day-to-day management of both funds (in its capacity as sub-advisor of each fund, in addition to being the general partner of one fund). The conclusion that the contacts of these defendants constituted "transacting business" within the meaning of the long-arm statute was supported by the facts that the entity that these defendants served (i) participated in the formation of, (ii) was primarily responsible for the management of and (iii) received fees from, the funds. The court then considered whether "minimum contacts" between the nonresident defendants and the state existed -- that is, whether these defendants deliberately engaged in conduct that created obligations between themselves and the state, including the protection of the state's laws, such that these defendants should reasonably anticipate action in Delaware courts. In addition to the facts cited with respect to the long-arm statute, these defendants enjoyed the benefits of Delaware law, including limited liability. Further, Delaware's important interest in regulating entities that choose its laws warrants its exercise of jurisdiction over those who manage such entities and avail themselves of the laws of the state that empower them to act. The claims at issue in this case involved corporate power and fiduciary obligations, which are at the heart of the internal affairs and governance issues of special concern for the state, making the exercise of personal jurisdiction over these defendants appropriate.

I. Disclosures

1. *Anglo American Security Fund, L.P. v. S.R. Global International Fund, L.P.*, C.A. No. 20066-N (Del. Ch. May 24, 2006)

Plaintiffs were limited partners ("LPs") in a Delaware limited partnership operating as a hedge fund (the "Fund") and brought suit against the Fund, its general partner ("GP") and its independent auditors for breach of contract, breach of fiduciary duty and negligence. Both the plaintiffs and defendants moved for summary judgment, and the court granted

the defendants' motion. At the center of the dispute were provisions of the limited partnership agreement relating to the deduction, crediting and withdrawal of the GP's incentive fee. The partnership agreement provided that the GP was entitled to a 15% incentive fee on the LPs' net profits, such incentive fee to be deducted from each LP's capital account and credited to the GP's capital account as of the end of the fiscal year. The GP had the right to withdraw funds from its capital account as of the last day of any month. The books and records of the Fund were to be audited by an independent certified accountant as of the end of each fiscal year, and the Fund was to provide copies of the audited financial statements to the LPs after the end of each fiscal year. On December 31, 1999, the incentive fee was deducted from the LPs' capital accounts and credited to the GP's capital account (the "Allocation"). After the close of business on the same day, the incentive fee was withdrawn from the GP's capital account (the "Withdrawal"). The Allocation was reported to the LPs in February of 2000 in the Fund's 1999 fourth quarter financial statement, but the Withdrawal was not. Instead, the Withdrawal was reported in May in the Fund's first quarter statement for the year 2000. Based on the Fund's fourth quarter statement received in February, the plaintiffs withdrew part of their investment, but without regard to whether or not the GP kept its 1999 incentive fee invested in the Fund. After the Withdrawal was disclosed in May, the plaintiffs continued to remain invested in the Fund.

The plaintiffs alleged that the GP breached its fiduciary duties by misstating that it had retained the incentive fee in its capital account when it had actually withdrawn nearly all of it, by not disclosing the Withdrawal as a subsequent event and by not disclosing that the Withdrawal was contrary to the terms of the limited partnership agreement. The court held that the plaintiffs had not established that they relied upon the omitted disclosure of the Withdrawal in the 1999 fourth quarter financial statements. Thus the court refused to consider whether the 1999 statement should have disclosed the Withdrawal or whether the Withdrawal should have been reported in the Subsequent Event footnote of those financials. In so holding, the court rejected the plaintiffs' reliance on federal precedents under Section 10(b) of the Securities Exchange Act of 1934. Specifically, the court reiterated that Delaware does not recognize the "fraud on the market" theory recognized in the federal courts. In breach of fiduciary duty cases based on omissions, reliance may only be presumed when shareholder or partner action is requested. As such action was not requested in the present case, the plaintiffs were required to prove reliance, which they failed to do. With regard to plaintiffs' disclosure claim, the court emphasized that if the language of a contract is unambiguous, its plain meaning would dictate the outcome, and held that the unambiguous language of the partnership agreement did not impose a duty of disclosure on the defendants in the present circumstances.

2. *Albert v. Alex. Brown Mgmt. Servs., Inc.*, C.A. Nos. 762-N, 763-N (Del. Ch. Aug. 26, 2005)

In a further decision in this case brought by limited partners of two Delaware limited partnerships (*see* Sections II.J.1 and II.J.4 for summaries of prior decisions), the court addressed several issues raised by defendants' motion to dismiss that remained unresolved following an earlier decision, including issues relating to plaintiffs' disclosure claims, plaintiffs' breach of fiduciary duty and contract claims, whether plaintiffs' claims were direct or derivative in nature and whether the court had personal jurisdiction over certain defendants.

With respect to plaintiffs' disclosure claims, the court stated that to survive the motion to dismiss, the court must find that the allegations supported a reasonable inference of materiality. The standard to be applied was whether there existed a substantial likelihood that a reasonable investor would have considered the disclosure of the omitted fact to significantly alter the total mix of information. The court determined that the managers' failure to disclose (i) that hedging, which was believed by the managers to be in the best

interests of the funds, was impractical because of the funds' liquidity situation, (ii) information regarding the funds' liquidity problems and (iii) the funds' defaults under credit arrangements were material. The court made clear that there is no independent duty of disclosure, but rather that the disclosure allegations must be tied to a fiduciary or contractual duty to disclose, and, in this case, plaintiffs claimed both.

The court then turned to plaintiffs' breach of fiduciary duty claims, the first of which related to the managers' failure to provide financial statements. The court held that, while financial statements were required to be provided as a contractual matter under the partnership agreements, the failure to provide such financial statements did not amount to a fiduciary duty claim. Similarly, the managers' permitting limited partners to withdraw and redeem their interests pursuant to the partnership agreements did not constitute a breach of fiduciary duty, as there was no personal benefit to the managers to support a breach of the duty of loyalty and there was no gross negligence (which the court stated would require allegations that the managers acted on a "recklessly uninformed" basis or acted "outside the bounds of reason") to support a breach of the duty of care. The partnership agreements' grant of sole discretion to the managers to deny a limited partner's limited contractual right of redemption did not impart a positive duty to exercise such power, regardless of the liquidity issues faced by the funds. Finally, while the court disposed of the related allegations as to the qualifications of the managers, it determined that plaintiffs' allegations regarding the time and attention the managers devoted to the funds and the alleged disclosure violations did state breach of duty of care claims. In this regard, the court explained that adequate management is a fact-intensive question and the answer varies depending on the type of fund and complexity of the issues faced.

With respect to plaintiffs' breach of contract claims, the court set forth the standard to survive a motion to dismiss, which requires proof of (i) the existence of a contract, (ii) breach of a duty imposed by such contract and (iii) damages to plaintiff from such breach. In contrast to the dismissal of the corresponding breach of fiduciary claim, the court found that the failure to provide financial statements did constitute a breach of contract claim. However, plaintiffs' allegations as to the limited partner withdrawals and redemptions were not sufficient to sustain a breach of contract claim. Finally, the court found the managers' failure to provide information due to limited partners under the partnership agreements in good faith and without material misinformation created a breach of contract claim, in addition to the breach of fiduciary duty claim discussed above.

Apart from whether plaintiffs' claims were factually supported, defendants argued that several counts of the complaint were derivative claims for which demand was neither made nor excused. The court first cited the demand requirement in the limited partnership context, as codified in DRULPA Section 17-1001, and observed the substantial similarity to Delaware corporate law, under which the Delaware Supreme Court in *Tooley v. Donaldson, Lufkin & Jenrette, Inc., 845 A.2d 1031 (Del. 2004)*, set forth a revised test for determining whether a suit is derivative or direct. Under the revised test, the only factors are (i) who suffered the harm and (ii) who would receive the benefit of any recovery or other remedy, in each case looking at the corporation or partnership, as applicable, versus the stockholders or interest holders, as applicable. In this case, the court found that the fiduciary duty and contract claims based on alleged failures to disclose were direct claims (for which demand was not required). The harm was to the interest holders, in their loss of the ability to withdraw or redeem their interests in response to the information that would have been gained, and the remedy, which, at this stage, may be monetary damages, would go to such holders. In contrast, the fiduciary duty claims based on gross negligence and inadequate management were derivative claims. Mismanagement is, according to the court, the paradigm of the derivative claim, as the managers' actions caused losses to the funds and any recovery would go to the funds. While the failure of demand, and absence of allegations as to why

demand was excused, forced the court to dismiss these claims, plaintiffs were given leave to replead.

The final issue addressed by the court was a challenge to personal jurisdiction over certain defendants. Two individual defendants, who were the owners and managers of a Tennessee limited liability company that was the general partner of one of the funds, argued that they were residents of Tennessee who performed their duties from such state and had not solicited business from, engaged in regular conduct with, or even traveled to, Delaware. The court explained that upon such a challenge, the burden was on plaintiffs to show the basis for personal jurisdiction, which will then requires the court to determine (i) whether service of process on the nonresident defendant was authorized by the Delaware long-arm statute and (ii) whether the exercise of jurisdiction is consistent with due process. After stating that the Delaware long-arm statute had been interpreted to allow jurisdiction to the fullest extent permitted by the due process clause, the court observed that the funds were formed as Delaware limited partnerships governed by Delaware law and that the entity in which these defendants were managing members and owners was responsible for the day-to-day management of both funds (in its capacity as sub-advisor of each fund, in addition to being the general partner of one fund). The conclusion that the contacts of these defendants constituted "transacting business" within the meaning of the long-arm statute was supported by the facts that the entity that these defendants served (i) participated in the formation of, (ii) was primarily responsible for the management of and (iii) received fees from, the funds. The court then considered whether "minimum contacts" between the nonresident defendants and the state existed -- that is, whether these defendants deliberately engaged in conduct that created obligations between themselves and the state, including the protection of the state's laws, such that these defendants should reasonably anticipate action in Delaware courts. In addition to the facts cited with respect to the long-arm statute, these defendants enjoyed the benefits of Delaware law, including limited liability. Further, Delaware's important interest in regulating entities that choose its laws warrants its exercise of jurisdiction over those who manage such entities and avail themselves of the laws of the state that empower them to act. The claims at issue in this case involved corporate power and fiduciary obligations, which are at the heart of the internal affairs and governance issues of special concern for the state, making the exercise of personal jurisdiction over these defendants appropriate.

J. Procedural Issues

2. *Personal Jurisdiction*

a. *Albert v. Alex. Brown Mgmt. Servs., Inc.*, C.A. Nos. 762-N, 763-N (Del. Ch. Aug. 26, 2005)

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10. *Expedited Proceedings*

a. *Madison Real Estate Immobbilien-Anlagegesellschaft beschränkt haftende KG v. GENO One Financial Place L.P.*, (Del. Ch. Feb. 22, 2006)

This case arose from an unregulated tender offer for a portion of the limited partnership interests of a Delaware limited partnership. After some partnership interests had been tendered to plaintiff, another company, Meridian 10, made a competing, and more attractive, offer. Because of provisions in the partnership agreement, the general partner took the position that it could not consent to the plaintiff's admission to the limited partnership until January 1 of the following

year, unless the plaintiff obtained new transfer agreements from those who had already tendered. The plaintiffs sought an expedited hearing for consideration of their motion for a preliminary injunction to prevent the general partner from consenting to the transfer of partnership interests to Meridian 10 and compelling the general partner to consent to the transfers to itself.

The court denied the plaintiff's motion for expedited proceedings. It held that the plaintiffs had not made a sufficiently colorable claim, nor shown a sufficient possibility of a threatened irreparable injury, to justify the additional burden and expense, on both the defendants and the public, of expedited proceedings. The plaintiff's claim was not sufficiently colorable because the partnership agreement gave the general partner the broad duty to investigate any substituted limited partner before consenting to a transfer of partnership interests, and the general partner would probably be justified in refusing to make special accommodations (such as giving retroactive consent) to facilitate the plaintiff's lower priced tender offer. The plaintiff had not shown irreparable injury because it was in control of its own, unregulated, offer. Because the tender offer materials used by the plaintiff were not in the record, the court was unable to determine the exact effect of the general partner's consent on plaintiff's ability to complete the purchase of the tendered partnership interests. However, if the right to purchase the tendered shares was not conditioned on the general partner's consent, it could purchase without irreparable injury. If its right to purchase was dependent on the general partner's consent, the court would not exercise its equitable powers to correct plaintiff's own flawed contract.

11. *Standing*

a. *Hillman v. Hillman*, 2006 WL 2434231 (August 23, 2006)

The plaintiff was general partner of Venhill Limited Partnership L.P., a Delaware limited partnership ("Venhill"). Two trusts served as the limited partners of Venhill. The plaintiff, in his capacity as general partner, invested 1% of the initial capital and each of the trusts contributed 49.5% of the initial capital. The limited partners challenged the plaintiff's actions in causing Venhill to invest a substantial amount of Venhill's assets in Auto-trol ("Auto-trol"), a company founded and controlled by the plaintiff. Unable to resolve the dispute over Venhill's investment in Auto-trol, the limited partners removed the plaintiff as general partner.

The plaintiff filed suit seeking declaratory judgment that upon his removal he had converted his general partner interest into a limited partner interest in Venhill. The suit also alleged that the limited partners breached fiduciary duties owed to him as a limited partner by the actions they took following his removal. The court concluded that Venhill's limited partnership agreement (the "Agreement") did not provide a general partner the right to "elect" to become a limited partner when removed by the limited partners and thus dismissed his claim for a declaratory judgment that he was a limited partner. The court concluded that the plaintiff was entitled to the fair value of his interest in the partnership but also held that because the plaintiff was removed as a general partner and all of the plaintiff's other claims related to the partnership's conduct following his removal, the plaintiff lacked standing and his other claims for breach of fiduciary and contractual duties were also dismissed.

O. Mergers

1. *Fair Value of Interests*

a. *Ramunno v. Capano*, C.A. No. 18798-NC (Del. Ch. Feb. 10, 2006)

Plaintiff, in his capacity as the trustee of four trusts that together held 12.1% of a limited partnership, brought this action to determine the fair value of the trusts' minority interests in connection with a merger of the limited partnership into a new limited partnership and the consequent extinction of the trusts' interests. At the time of the merger, a majority of the equity interests in the original limited partnership was controlled by two brothers, each of whom was a limited partner. A corporation controlled by one of the brothers served as general partner of the original limited partnership. The new limited partnership resulting from the merger was controlled by the two brothers who had held the majority interest in the old limited partnership, and in such capacity, had caused the merger that squeezed out the trusts. The two brothers, each of whom was a defendant (as was the corporate general partner), had placed a $268,889 value on the interests of the trusts at the time of the merger.

The original limited partnership had been formed by the two defendant brothers, plus a third brother. The third brother had transferred a portion of his interest in the original limited partnership to plaintiff as trustee of the trusts, which were for the benefit of his children. Defendants claimed that no fiduciary duties were owed to plaintiff because the trusts were assignees of limited partner interests and never attained limited partner status. Under the terms of the partnership agreement of the original limited partnership, the general prohibition on transfers without consent did not extend to inter-family transfers (including transfers to trusts for the benefit of children of the transferee). Defendants, however, cited plaintiff's failure to comply with the requirement under the partnership agreement that the transferee execute a counterpart of the partnership agreement. The court found that defendants' past treatment of the transferees, the ability to freely assign interests to family members and the defendants' failure to raise the issue previously amounted to a waiver of the ability to challenge plaintiff's status as a limited partner.

In its consideration of the fair value of the interests held by plaintiff, the court focused on (i) the fair value of the property owned by the original limited partnership; (ii) the rate of interest to be applied against the failure of the third brother to meet a capital call (prior to the transfer of his limited partner interest); and (iii) the proper treatment of a loan made to the original limited partnership by a corporation owned by the defendant brothers. As to the value of the property, the court adopted an appraisal commissioned by an independent third party near the time of the most recent leasing of the property, as increased by inflation, but not, as urged by plaintiff, increased by the value of potential expansion of the property, which the court found to be speculative. As to the second consideration, the court determined that the uncured shortfall in the third brother's capital account allocable to the portion of the third brother's interest transferred to the trusts must be taken into account in determining the fair value of the trusts' interests. The court rejected plaintiff's argument that the interest rate to be applied to the shortfall amount was the rate set in the partnership agreement of the original limited partnership for loans made by the partnership to its limited partners. Such a rate would not adequately account for the venture risk to which the assets were subject and would be fundamentally unfair to those partners whose funds were at risk. Instead, the discount rate set by the above-mentioned appraiser for the risk and cost of capital was used. A third

consideration was a loan from a corporation controlled by the defendant brothers to the original limited partnership, which, while not evidenced by a note, was found by the court to be an obligation of the partnership. The loan was reflected on the books the original limited partnership for several years but was removed from the books at the time that the defendant brothers decided to take a bad debt deduction on their personal income tax returns. After the merger, however, the loan appeared on the books of the new limited partnership and defendants argued that it should be included as a partnership debt in the calculation of the value of the trusts' interests. Plaintiff countered that reentering the loan on the partnership's books constituted a self-interested act in breach of defendants' fiduciary duties and, in addition, that collection of the debt was time-barred and that waiver of the statute of limitations defense by defendants on behalf of the original limited partnership would be a breach of duties. The court determined that neither the lack of payments on the debt, nor the fact that the loan did not appear on the lending corporation's books as a collectible or on the partnership's books as an obligation, meant that the debt had been released. The court stated, however, that the statute of limitations (which was shorter because the debt was not evidenced by a negotiable instrument) could be a viable defense if this issue was viewed as a debt collection matter. In the opinion of the court, however, this should not be viewed as a debt collection. Instead of treating the debt as an obligation of the partnership, the court determined that, despite the fact that the defendant brothers wrote off the loan for their personal benefit, the amount of the loan should be treated as a capital contribution of the defendant brothers for purposes of determining the fair value of the trusts' interests. According to the court, under regular accounting expectations, a related party loan that is written off should be treated as a capital contribution, even if it was questionable whether equitable principles should save the defendant brothers from the consequences of their self-interested actions. If it were treated otherwise, plaintiff would have received a windfall. In addition to the foregoing, the court included the original limited partnership's cash and cash equivalents, prepaid expenses, accounts payable, accrued expenses and outstanding mortgage on the property in determining the fair value of the trusts' interests. On the basis of these considerations, the court held that the fair value of the trusts' interest was $586,665.

P. Forfeiture of Interests

1. *Hillman v. Hillman*, 2006 WL 2434231 (August 23, 2006)

The plaintiff was general partner of Venhill Limited Partnership L.P., a Delaware limited partnership ("Venhill"). Two trusts served as the limited partners of Venhill. The plaintiff, in his capacity as general partner, invested 1% of the initial capital and each of the trusts contributed 49.5% of the initial capital. The limited partners challenged the plaintiff's actions in causing Venhill to invest a substantial amount of Venhill's assets in Auto-trol ("Auto-trol"), a company founded and controlled by the plaintiff. Unable to resolve the dispute over Venhill's investment in Auto-trol, the limited partners removed the plaintiff as general partner.

The plaintiff filed suit seeking declaratory judgment that upon his removal he had converted his general partner interest into a limited partner interest in Venhill. The suit also alleged that the limited partners breached fiduciary duties owed to him as a limited partner by the actions they took following his removal. The court concluded that Venhill's limited partnership agreement (the "Agreement") did not provide a general partner the right to "elect" to become a limited partner when removed by the limited partners and thus dismissed his claim for a declaratory judgment that he was a limited

partner. The court then discussed what rights the plaintiff possessed following his removal.

The court first noted that the Agreement did not provide what a removed general partner would receive in consideration of its interest upon removal. It then reviewed the DRULPA provisions and related legislative history and concluded that the DRULPA did not address what a general partner received upon removal. The court, therefore, looked to the general partnership law and concluded that it provided that upon expulsion a general partner would receive the fair value of such partner's economic interest. Significantly, the court noted that even if the general partnership law did not provide compensation to the plaintiff, he would have a right in equity to seek protection of his economic interest because "equity abhors a forfeiture." (It should be noted that the Agreement did not, by its terms, purport to cause the forfeiture of the general partner's interest upon his removal which the court might have concluded was permissible under DRULPA Sections17-306 and 17-502(c)).

III. LIMITED LIABILITY COMPANIES

A. Fiduciary Duties

1. *Bakerman v. Sidney Frank Importing Co., Inc.*, C.A. No. 1844-N (Del. Ch. Oct. 10, 2006)

Plaintiff was chief legal counsel to Sidney Frank Importing Co., Inc. ("SFIC") and individually owned a membership interest in a subsidiary of SFIC, Grey Goose LLC (the "LLC"). SFIC and the LLC conducted the Grey Goose vodka business. Despite plaintiff's position as chief legal counsel, management of SFIC and the LLC negotiated a sale of the vodka business without the knowledge of plaintiff. Shortly before the scheduled public announcement of the sale, management of the LLC advised plaintiff of the sale and requested plaintiff's consent to the sale in his capacity as a member of the LLC, which was required under the LLC's operating agreement. Of the $2.25 billion dollar cash purchase price, less than 0.49% was proposed to be allocated to the LLC, and on this basis plaintiff initially refused to give his consent. After management threatened to sue plaintiff and terminate his employment, plaintiff consented to the sale. Plaintiff then brought this action, which alleged several derivative and direct claims. In this decision, the court addressed defendants' motion to dismiss.

The court first addressed defendants' motion to dismiss plaintiff's derivative claims for failure to make a proper demand. The court stated that the standard for alleging demand futility in Delaware (as established in *Aronson v. Lewis*, 473 A.2d 805 (Del. 1984)) requires the pleading of particularized facts raising a reasonable doubt that (i) management is disinterested and independent or (ii) the contested transaction was otherwise the result of a valid exercise of business judgment. As to the first element of the first prong, the court stated that "disinterested" means that a manager is not on both sides of the transaction and is not due to receive a benefit from the transaction that is not shared by the company or other interest holders. In this case, the court determined that the substantial benefit that the managers of the LLC received in their capacity as shareholders of SFIC, at the expense of the LLC, satisfied this element of demand-futility. As to the second element of the first prong, the court stated that the independence of a manager is sufficiently compromised for the purposes of demand-futility when the manager is beholden to a controlling person or so under the influence of a controlling person that the manager's discretion is effectively sterilized. In this case, the control that SFIC and Sidney Frank, who was the founder, chairman, chief executive officer and majority shareholder of SFIC, exerted with respect to the LLC and the sale transaction created a reasonable doubt as to the independence of the managers of the LLC. Despite concluding that demand was excused under the first prong, the court went on to analyze the second prong of the demand-futility test. The court stated that

managers of an LLC are presumed to have acted on an informed basis and in the honest belief that their decisions were in furtherance of the LLC and its members. The court stated that, in determining whether such a presumption is overcome by the facts, which typically requires a showing tantamount to corporate waste, both the substance of the transaction and the process by which it was adopted are reviewed. As to the substance of the transaction, the court found that under the facts presented it could not be reasonably concluded that the allocation of the purchase price between SFIC and the LLC was appropriate. As to process, plaintiff alleged that defendants failed to utilize mechanisms typically employed to produce a fair process, such as obtaining an independent appraisal of the assets or appointing a special committee to assess the fairness of the transaction. The court thus held that plaintiff had met his burden of demonstrating demand futility.

Defendants also alleged that plaintiff was an inadequate derivative representative of the LLC because (i) at the time of the sale he was SFIC's chief legal counsel, (ii) he allegedly violated New York's attorney disciplinary rules by accepting an interest in the LLC while serving as SFIC's legal counsel and (iii) the lawsuit was not supported by other members of the LLC. The court found that plaintiff's position as legal counsel to SFIC did not preclude him from bringing a derivative suit because, as defendants excluded him from the negotiations regarding the sale, he never served as legal advisor on the transaction, and thus his representation of SFIC did not involve issues that were "substantially related" to the derivative claims. In addition, the court found that the derivative claims may be maintained without the support of the other members of the LLC, stating that a derivative representative is assessed by his ability to advance the interest of similarly situated interest holders (even if there is only one interest holder with such interest), regardless of the support of other interest holders.

Turning to the substance of plaintiff's derivative claims, the court first addressed plaintiff's claim of breach of fiduciary duty based on the alleged coercion that led plaintiff to consent to the sale. The court disagreed with plaintiff's assertion that the inequitable coercion doctrine, which is the doctrine Delaware courts have applied in the context of proxy voting by diffuse shareholders of public corporations, was applicable in this case. The court found that this doctrine was not applicable to a member of a closely held LLC, which, unlike diffuse shareholders, is not hampered by the difficulties of collective action. Instead, the court applied the standards relating to coercion and duress in bilateral contract negotiations, stating that a party alleging coercion or duress must plead (i) a wrongful act, (ii) which overcomes the will of the aggrieved part and (iii) that he has no adequate legal remedy to protect himself. The court determined that the application of these standards in this context by the fact that the managers of the LLC, in their position as fiduciaries, had a duty to disclose to plaintiff any information that carried a substantial likelihood that a reasonable interest holder would view as significantly changing the total mix of information bearing on the decision. The court concluded that the threats of litigation and loss of employment, combined with the brief time period in which plaintiff was forced to make a decision without the assistance of counsel, coerced his consent, and thus the court refused to dismiss these claims.

The court then examined defendants' allegations that plaintiff's direct claims were in fact derivative in nature. The court stated that the classification of a claim as derivative or direct turns on (i) who suffered the harm (the company or the suing interest holder individually) and (ii) who would receive the benefit of the remedy (the company or the interest holder individually). Based on this test, plaintiff's breach of contract and breach of good faith and fair dealing claims were judged to be direct because plaintiff suffered the unique harm of the deprivation of his voting rights under the LLC's operating agreement through the defendants' economic coercion and the remedy for such harm would be due solely to plaintiff. The court thus concluded that these claims were direct claims and determined that plaintiff's pleadings with respect to these claims were sufficient to survive defendants' motion to dismiss.

2. *Blackmore Partners, L.P. v. Link Energy LLC*, C.A. No. 454-N (Del. Ch. Oct. 14, 2005)

Following the court's denial of the defendants' motion to dismiss referred to below, the defendants moved for summary judgment at the conclusion of discovery and this opinion was the court's decision with respect to such motion.

The plaintiff first alleged that the court should apply enhanced scrutiny to the challenged transaction in which the proceeds of the sale of substantially all of the LLC's assets were used to repay the debt of the LLC and to pay holders of unsecured notes a payment for covenant waiver thus rendering the LLC's units worthless. The plaintiff claimed the board of directors of the LLC deprived the unit holders of consideration that they would have received if the board had not agreed to the demands of the note holders. The court rejected the plaintiff's reliance on the court's decision in *Orban v. Field* which held that "when a board approves a transaction that favors one corporate constituency over another, they lose, at least as an initial matter, the cloak of business judgment protection," and the board must demonstrate that it acted reasonably and in good faith. The court in the instant case distinguished *Orban* by finding that the "defendants did not act 'solely or primarily for the express purpose of depriving a shareholder of effective enjoyment of a right conferred by law.'" Importantly, the LLC's operating agreement empowered the board of directors to authorize a sale of all or substantially all of the LLC's assets without a vote of the unit holders thus precluding any need for measures by the board to prevent the unit holder's approval or vote. The court also found that even if *Orban* applied to the instant case, the defendants met the enhanced scrutiny standard since the company was insolvent and no better transaction was available.

The court next addressed the plaintiff's claim that the defendants breached their fiduciary duties to the unit holders by focusing on the creditors' interests over the interests of the unit holders. The plaintiff conceded that the company was insolvent at the time of the disputed transaction, and the court stated that "the board of directors of an insolvent company may take into account the interests of creditors at the apparent expense of stockholders if, in doing so, the board meets its fiduciary duties to all relevant constituencies."

The court then analyzed whether the directors met their fiduciary duties with respect to the unit holders. The plaintiff claimed that the board's decisions regarding the transaction were tainted by the involvement of J. Robert Chambers ("Chambers"), a director who was a managing director of Lehman Brothers, a holder of an equal percentage of notes and units of the LLC. The court referred to its decision in *Cooke v. Oolie* which involved defendants who were both shareholders and creditors of a corporation considering an acquisition proposal. The *Cooke* court held that "plaintiffs bore the burden of showing that an actual conflict existed, and that the deal chosen by the defendants offered superior terms for creditors and inferior terms for the plaintiff shareholders compared to other proposals available to the defendant corporation." Unlike the defendants in *Cooke*, the defendants in the instant case owed fiduciary duties to creditors because the company was insolvent. Even if Chambers' membership on the board created a potential conflict, there were no better alternatives for the unit holders other than the transaction approved by the board. The court also noted that even if Chambers were conflicted, the board would still receive the protections of the business judgment rule because such protections only require that a majority of the directors approving the transaction remain disinterested, and the plaintiff made no claims that other directors were interested.

The court also rejected the plaintiff's argument that the Special Committee of independent directors formed by the board to consider potential transactions was tainted by the presence of the CEO of the LLC and Chambers at the meetings of the Special Committee. Since the plaintiff failed to present evidence that the CEO or Chambers

influenced the Special Committee or acted "as anything more than necessary sources of information," the court found the Special Committee operated with "sufficient independence to merit the cloak of business judgment protection."

Next, the plaintiff argued that the defendants breached their duty of care by approving the transaction without sufficient expert information and by failing to use the leverage from a potential bankruptcy filing against the note holders to negotiate a better settlement for the unit holders. The court found that the plaintiff's claims based on breach of the duty of care were precluded by the LLC's operating agreement exculpating directors for all awards of damages for violations of the duty of due care. Nonetheless, the court addressed the plaintiff's claims regarding the duty of due care finding that the directors did not violate such duty. The court stated that the defendants did not act with gross negligence since the record showed that the Special Committee met "repeatedly over months to address the issue of the company's impending insolvency and to consider alternatives." Additionally, the note holders had the ability to veto any proposed transaction thus limiting any leverage power the company had against the note holders. Moreover, the court noted that "the choices made in formulating a negotiating strategy are within the core of what is protected by the business judgment rule," and the evidence failed to support the plaintiff's claimed violation of due care.

Finally, the court rejected the plaintiff's claim that the defendants acted in bad faith in approving the transaction finding that "the fact that unit holders were left with nothing at the end, given a context in which the chief alternative substantiated by evidence was an equally barren bankruptcy proceeding, does not suffice to rebut the presumption that the directors were acting in the good faith exercise of their fiduciary duties, or to establish a claim of waste." The court granted the defendants' motion for summary judgment.

C. Indemnification and Advancement

1. *Citrin v. Int'l Airport Centers, LLC*, C.A. No. 2005-N (Del. Ch. Sept. 7, 2006)

This decision of the Court of Chancery followed a ruling by a federal appeals court (see *Int'l Airport Centers, LLC v. Citrin*, 455 F.3d 749 (7th Cir. 2006)) that a claim for advancement may be litigated outside of the lawsuit giving rise to such claim, which allowed this action in the Court of Chancery to proceed. Having previously determined in a judgment on the pleadings that the underlying lawsuit implicated plaintiff's right to advancement under the operative limited liability company agreement, the remaining issue addressed by the court in this opinion was whether plaintiff was entitled to pre-judgment interest on the amounts for which plaintiff was entitled to advancement. The court stated that when a plaintiff has a contractual right to advancement, as in this case, the time at which the defendant unjustifiably refuses to pay the amount due is the starting point for the accrual of interest, noting that the requirement to pay interest is to ensure that a plaintiff to whom payment was owed does not suffer injury by the defendant's unjustified delay in making such payment. The court acknowledged that in prior cases the time at which interest began to accrue was the time as which the specific amount of fees and expenses incurred was submitted to the defendant. In this case, however, defendant refused to identify to plaintiff to whom plaintiff should submit his invoices, which precluded plaintiff's submission of invoices specifying his fees and expenses. The court estimated that had defendant identified a person to whom fees and expenses should be sent as requested in plaintiff's demands for advancement, plaintiff would have delivered the invoices within ten days thereafter and thus determined that this was the appropriate date from which interest would accrue on expenses incurred before the date of his first demand and that interest would accrue on all later expenses from the date on which they were paid by plaintiff.

2. *Delucca v. KKAT Mgmt., L.L.C.,* C.A. No. 1384-N (Del. Ch. Jan. 23, 2006)

Plaintiff moved for a judgment on the pleadings seeking from defendants advancement of her legal fees and expenses in connection with a lawsuit brought against plaintiff by affiliates of the defendants. Plaintiff was a former employee and Managing Member of Katonah Capital, L.L.C ("Katonah") and a member of each of the defendant limited liability companies (the "KKAT Companies"). The KKAT Companies, affiliates of Kohlberg Capital, L.L.C. ("Kohlberg"), were formed by plaintiff and Kohlberg to invest in certain investment funds (the "Funds") of which Katonah served as the investment manager and plaintiff was the key money manager. During the course of plaintiff's employment with Katonah, many disputes arose including plaintiff's failure to hire another money manager when Kohlberg sought an additional manager to help manage the funds, plaintiff's alleged interference with meetings between Katonah employees and prospective buyers of Katonah during a proposed sale of Katonah and plaintiff's alleged formation of a competing venture and supposed sharing of confidential and proprietary information of Katonah with third parties. Plaintiff's alleged violations of fiduciary and contractual duties prompted Katonah and Kohlberg to bring an action against plaintiff (the "New York Action") and plaintiff sought advancement of her legal fees and expenses in connection with the New York Action from the KKAT Companies.

In relevant part, the Operating Agreement for each KKAT Company provided that "the Company shall, to the full extent permitted by applicable laws, indemnify and hold harmless each of the Indemnified Persons from and against any and all Losses to which such Indemnified Person may become subject…in connection with or arising out of or related to…the operations or affairs of the [KKAT Company] or the [Katonah Funds]." The Operating Agreement further provided that the KKAT Company would advance the legal and other expenses of "any Indemnified Person involved in any capacity in any action, proceeding or investigation in connection with any matter that may result in the indemnification." The court emphasized the importance of analyzing the plain language of the Operating Agreement as "advancement cases are particularly appropriate for resolution on a paper record, as they principally involve the question of whether claims pled in a complaint against a party…trigger a right to advancement under the terms of a corporate instrument."

The court first addressed whether plaintiff was an "Indemnified Person" under the Operating Agreement, which included any employee of an Affiliate of Kohlberg. Under the Operating Agreement, the term "Affiliate" included any "Person directly or indirectly…controlled by" Kohlberg. The court found Katonah to be an "Affiliate" of Kohlberg because Kohlberg was a majority stockholder in Katonah. Plaintiff, a former portfolio manager and managing principal of Katonah, was an "employee of an Affiliate" of Kohlberg and thus, an "Indemnified Person."

The next question for the court was whether plaintiff had "Losses" in order to seek advancement. Defendants asserted that plaintiff's company, not plaintiff, paid her legal fees thereby cutting off plaintiff's right to seek advancement of the fees. The court found defendants' argument to be inconsistent with the policy underlying Delaware law stating that defendant's argument "would encourage indemnitors to use the leverage of a denial of advancement to deprive indemnitees of appropriate legal advice, putting them under pressure to settle disputes not because of the merits, but because of doubts about whether they could obtain competent defense counsel."

The court next addressed whether the legal claims under the New York Action fell under the language of the advancement provision in the Operating Agreement. Noting that the language of the advancement provision was extremely broad using terms and phrases such as "to the full extent permitted by law," "in connection with or arising out of or related to," "operations" and "affairs," the court found that advancement could result

from Losses connected with, arising out of or relating to either the operations or affairs of either the KKAT Companies or the Funds.

In trying to negate the broad provisions of the Operating Agreement, defendants first argued that allowing plaintiff to recover for advancement for defending claims such as stealing information and the tortious interference with the sale of Katonah would be a "startling proposition." The court rejected defendants' argument citing the Delaware Supreme Court in *Homestore, Inc. v. Tafeen* and noting that advancement rights were particularly critical "when a business official is accused of serious wrongdoing."

Defendants next sought an implicit requirement that the "Losses" in the advancement provision result from a claim of either the Funds or KKAT Companies, "or by their stockholders or members, acting as plaintiffs in that precise capacity." The court again focused on the precise language of the Operating Agreement stating that the Operating Agreement could have easily limited advancement to situations where plaintiff was causing an injury to the KKAT Companies or the Funds. The language of the advancement provision, however, was drafted broadly to include acts of Indemnified Persons relating to or in connection with the KKAT Companies or the Funds including "through their employment with an Affiliate of Kohlberg, such as Katonah." Finding that the advancement provision in the Operating Agreement was, "by its plain terms, expansively written and mandatory," the court held it would enforce the Operating Agreement as written. The complaints alleged in the New York Action included plaintiff's breach of confidentiality agreements with Katonah and the KKAT Companies, breach of contractual duties with Katonah by creating a competing company, breach of fiduciary duties owed to Katonah and Kohlberg, misappropriation of trade secrets, tortious interference with the sale of Katonah and tortious interference of the relationship among Katonah, Kohlberg and investors of the Funds, all of which the court found to relate to the affairs of the Funds.

Defendants' also argued that because the Operating Agreement provided for liability exclusion of Indemnified Persons in another section of the Operating Agreement, plaintiff could only receive indemnification and advancement if the claims against her fell within the liability exclusion provision. The court stated that there did not appear to be any dependence between the two sections other than the reliance of the indemnification and advancement provision on the definition of "Losses" in the liability exclusion provision. Again, the court stated that if the drafters intended to make indemnity and advancement rights dependent on liability immunity rights granted in the liability exclusion provision, they could have done so.

The court also found that plaintiff was not required to seek advancement from the Funds before seeking such advancement from the defendants even though the Operating Agreement stated that "to the extent that any Indemnified Persons may be entitled to indemnification…such Indemnified Person first shall be required to seek indemnification…from [Katonah Funds]." The court distinguished indemnification and advancement, stating that the Operating Agreement did not clearly combine the rights of advancement and indemnification.

Finally, the court awarded plaintiff the legal fees and expenses associated with the action to enforce the advancement provision ("fees on fees") because of her success on the claim. Citing the Delaware Supreme Court in *Stifel Financial Corp. v. Cochran*, the court noted that "the only way out of the *Stifel* 'fees on fees' award was for the KKAT Companies 'to tailor their indemnification…to exclude 'fees on fees' if that was a desirable goal,'" and the KKAT Companies failed to do so. Additionally, the Operating Agreements permitted indemnification "to the full extent permitted by applicable laws" thus including the rule established by *Stifel*, which the court stated applied to both corporations and LLCs. The court also ruled that an award of fees on fees did not depend

on the outcome of the New York Action because the award of fees on fees focused on whether plaintiff succeeded in an action for advancement, not whether she succeeded in the New York Action.

E. Removal of Managing Member

1. *Child Care of Irvine, L.L.C. v. Facchina*, C.A. No. 16227 (Del. Ch. July 15, 1998); *Facchina v. Malley*, C.A. No. 783-N (Del. Ch. July 12, 2006)

Plaintiffs moved for summary judgment on their claim that they validly removed the defendant as the managing member of a Delaware limited liability company. Defendant, in turn, also moved for summary judgment, asserting that the plaintiffs did not have the authority to remove him as managing member. The individual plaintiffs and the defendant had organized a California corporation and entered into a shareholder agreement that appointed the defendant "to manage the corporation in a professional and efficient manner." When the California corporation was unable to obtain "S" corporation status, the plaintiffs and defendant agreed to convert the corporation to a Delaware LLC through a merger solely for the tax benefits. The shareholders of the corporation entered into a shareholder consent in which they approved the merger and a merger agreement, which stated that the LLC would be governed by the LLC agreement in effect immediately prior to the merger, and authorized the defendant to take the actions necessary to effectuate the merger of the California corporation into the Delaware LLC. The defendant formed the Delaware LLC but the plaintiffs and defendant never executed an LLC agreement. The defendant then effected the merger and managed the business of the LLC. The plaintiffs became dissatisfied with the management of the defendant and purported to remove him as manager through the delivery of two resolutions signed by the individual plaintiffs.

The issue before the court was whether a majority of the members of the LLC had the authority to remove the defendant as the managing member. The plaintiffs argued that the parties orally agreed that the provisions of the shareholder agreement would govern the LLC and that the manager could thus be removed if he acted "unprofessionally" or "inefficiently." In the alternative, the plaintiffs argued that there was no LLC agreement and that, under Section 18-402 of the LLC Act, the management of the LLC was vested in the members and, therefore, a majority of the members could remove the defendant. The defendant argued that the plaintiffs had accepted a draft LLC agreement he claimed to have circulated that appointed himself manager and contained no provision for removing the manager. He claimed that under Section 18-402 of the LLC Act, a manager may only be removed as specified in the LLC agreement and, absent a provision for removal, a manager is unable to be removed except through judicial dissolution of the LLC. In the alternative, the defendant argued that the merger agreement, which appointed himself as manager and did not include a removal provision, was the operative LLC agreement. Because facts necessary to resolve the issue were in dispute, the court denied the cross-motions for summary judgment. The court also noted that either of the agreements proffered by the parties as the rightful LLC agreement would require arbitration of the dispute and encouraged the parties to seek arbitration rather than to litigate the case further to determine the rightful LLC agreement and then have the court direct the parties to arbitrate the dispute in accordance with such agreement.

In a related subsequent proceeding, Facchina, the defendant in the prior proceeding, acting in unison with certain other members of the LLC, removed the then current managing member and installed Facchina in that capacity and also caused the LLC to merge with another Delaware LLC. Each of these actions was challenged by plaintiffs on several grounds. However, the court held that since Facchina and those acting in concert with him owned more than a majority of the membership interests in the LLC, pursuant to Section 18-402 of the LLC Act, they could designate Facchina as the managing member.

F. Removal of Members and Forfeitures of Interests

1. *Eureka VII LLC v. Niagara Falls Holdings LLC*, C.A. No. 1203-N (Del. Ch. June 6, 2006)

Plaintiff, who held 50% of the voting and economic interests in a Delaware LLC, brought an action against defendant, who held the remaining 50% of the voting and economic interests, alleging several material breaches of the LLC agreement. Defendant's alleged breaches resulted in a creditor of a trust that controlled defendant gaining voting control, as well as legal and beneficial ownership, of defendant in violation of several anti-transfer provisions in the LLC agreement designed to prevent such an occurrence.

Plaintiff filed a motion for summary judgment seeking a declaration that defendant had relinquished its membership interest and retained only its economic rights in the LLC. The LLC agreement was silent as to the remedy for breach and thus plaintiff called upon the court to exercise its equitable powers to provide the requested declaration. Plaintiff drew support for its motion from Section 18-702(b)(3) of the LLC Act, which provides that "[a] member ceases to be a member and to have the power to exercise any rights of powers of a member upon assignment of all of the member's limited liability company interest." Although the court found that the statute does not directly apply to the facts of this case, the court agreed with plaintiff that it addressed a situation analogous to the one in this case and therefore provided a foundation for the remedy sought by plaintiff. Further, the court held that defendant's breaches of the LLC agreement ultimately had the same effect as a complete assignment for the benefit of creditors, which is the type of assignment that typically results in the statutory divestiture of a membership interest under Section 18-304 of the LLC Act. The court held that these statutory expressions of policy clearly support the right of a member of an LLC to craft provisions mandating that its fellow member either retain certain characteristics or lose its membership. Therefore, unless defendant was deprived of its membership rights, plaintiff would be denied its own contractual expectations. As a result, the court granted plaintiff's motion, noting that it was entirely fitting and proportionate for defendant, by virtue of the breaches committed in this case, to be declared as having lost its status as a member of the LLC and to be limited to the rights of an assignee as set forth in the LLC Act.

Defendant admitted breaching the LLC Agreement but asserted a counterclaim against plaintiff arguing that that plaintiff's own breach of the LLC agreement should bar plaintiff from asserting such breaches against defendant and depriving defendant of its status as a member. Defendant claimed plaintiff breached the buy/sell provision of the LLC agreement when plaintiff failed to close on the purchase of defendant's interest in the LLC following defendant's invocation of the buy/sell.

The court dismissed defendant's counterclaims on the basis that defendant's first material breach of the LLC agreement predated its attempt to invoke the buy/sell provision and, therefore, defendant was in no equitable position to claim it was entitled to invoke the buy/sell provision when it did so. Further, the court found that defendant lacked the financial capacity to close on the terms of the buy/sell provision when it invoked the buy/sell. The court also dismissed defendant's claim for dissolution. The court found that defendant's only plausible argument for dissolution was that plaintiff and the party now controlling defendant's interest did not get along and that the continuation of the LLC was therefore impracticable. However, having held that defendant's rights in the LLC were restricted to that of an assignee, the court held that plaintiff had the authority to act as the sole member of the LLC and, therefore, no impasse could exist that would support an action for dissolution.

G. Dissolution

1. *Willie Gary LLC v. James & Jackson LLC*, C.A. No. 1781 (Del. Ch. Jan. 10, 2006) and *Willie Gary LLC v. James & Jackson LLC*, C.A. No. 1781 (Del. Mar. 14, 2006), *aff'g*, (Del. Ch. Jan. 10, 2006)

   Plaintiff and defendant were co-owners of a Delaware LLC that was in need of a significant infusion of capital to succeed. Plaintiff negotiated an agreement with a third-party investor who was willing to provide capital, but the defendant refused to agree to a pro rata reduction of its interest in order to generate the equity needed to compensate the investor. As a result, plaintiff could not consummate the agreement and the parties became deadlocked with respect to the business of the LLC.

   Plaintiff filed a suit in the Court of Chancery seeking a mandatory injunction and specific performance or, in the alternative, judicial dissolution of the LLC. Defendant filed a motion to dismiss the complaint, arguing that plaintiff's claims were required to be arbitrated pursuant to the terms of the LLC agreement. Prior to determining the issue of arbitrability, the court first had to determine whether the arbitrability of the claims should be decided by the court or an arbitrator. Following United States Supreme Court and Delaware Supreme Court precedent, the court held that, as a general rule, the issue of substantive arbitrability required judicial resolution unless there was clear and unmistakable evidence that the parties intended otherwise. In determining that the issue was properly before the court, the court held that the mere reference to the rules of the American Arbitration Association (the "AAA Rules") in the arbitration clause of the LLC Agreement did not provide clear and unmistakable evidence that the issue of substantive arbitrability was to be decided by an arbitrator.

   Upon determining that the court should decide the issue of arbitrability, the court denied defendant's motion to dismiss the complaint, finding that none of plaintiff's claims were subject to the mandatory arbitration clause in the LLC agreement. To the contrary, the court held that the LLC agreement itself expressly authorized members of the LLC to apply to courts for the remedies of injunctive relief and specific performance. Further, with respect to plaintiff's claim for judicial dissolution, the court distinguished the dissolution clause in this case from that examined in *Terex Corp. v. STV USA, Inc.* (*see* Section III.K) and held that the provisions in the LLC agreement relating to judicial dissolution under the LLC Act explicitly contemplated judicial involvement in the dissolution process.

   In a subsequent decision in this case, the Delaware Supreme Court affirmed the Chancery Court's decision that the plaintiff's claims were not required to be arbitrated. With respect to the issue of substantive arbitrability, however, the Supreme Court did not totally agree with the Chancery Court's analysis regarding the significance of a reference to the AAA Rules in the arbitration clause. As a matter of policy, the Delaware Supreme Court held that Delaware follows the majority federal view that references to the AAA Rules in an arbitration agreement are clear and unmistakable evidence that the parties intended to arbitrate issues of substantive arbitrability. The Supreme Court stated that the majority view, however, does not require that arbitrators decide the arbitrability of all cases where an arbitration clause incorporates the AAA Rules. Instead, it only applies where the arbitration clause generally provides for arbitration of all disputes and also incorporates a set of arbitration rules that empower arbitrators to decide arbitrability. Thus, since the arbitration provision in the LLC agreement did not subject all disputes to arbitration, the Supreme Court held that the Chancery Court was correct in not applying the federal majority rule in this case.

2. *Terex Corp. v. STV USA, Inc.*, C.A. No. 1614-N (Del. Ch. Oct. 20, 2005)

In an action seeking judicial dissolution of a Delaware LLC, defendant filed this motion to dismiss the complaint pursuant to a broad mandatory arbitration clause in the LLC Agreement. In construing the scope of the arbitration clause, which unequivocally required all disputes arising out of or relating to the LLC Agreement to be resolved through arbitration, the court stated that the broad scope of the arbitration mandate would only be limited where a plain reading of the text specifically indicated such a limitation. The court held that a clause requiring members of the LLC to take appropriate steps required by law following the entry of a judicial dissolution under the LLC Act did not carve out judicial dissolution from the reach of the arbitration clause, stating that dissolution could be entered in accordance with, and following, dissolution proceedings before an arbitrator. The court therefore granted defendant's motion to dismiss.

3. *In re Silver Leaf, L.L.C.*, C.A. No. 20611 (Del. Ch. Aug. 18, 2005)

In a further decision in this case relating to a dispute among three members of a Delaware LLC formed for the purpose of acquiring a license to sell, market, sublease and distribute vending machines (*see* Sections III.K.3 and III.K.8 for summaries of the prior decision), the court addressed plaintiff's motion for judicial dissolution of the LLC. Plaintiff moved for judicial dissolution following the termination of a sales and marketing agreement between the LLC and the manufacturer of the vending machines, which was the LLC's primary asset. In addition, due to a provision in the LLC Agreement requiring the vote of a majority of interests in order for any member to take certain key business actions on behalf of the LLC, plaintiff and defendants, who each collectively owned 50% of the LLC, were deadlocked with respect to the future operations of the LLC. The court granted plaintiff's motion to judicially dissolved the LLC pursuant to Section 18-802 of the LLC Act, finding that the LLC was no longer reasonably practicable to carry on its business in a reasonably practicable manner. The defendants also asserted various counterclaims against plaintiff but, having determined that the business in which the LLC was involved was nothing more than a penny stock fraud, the court applied the doctrine of unclean hands to bar all other claims among the parties arising out of the LLC, including petitions by both parties for the appointment of a receiver.

H. Derivative Actions

1. *Bakerman v. Sidney Frank Importing Co., Inc.*, C.A. No. 1844-N (Del. Ch. Oct. 10, 2006)

Plaintiff was chief legal counsel to Sidney Frank Importing Co., Inc. ("SFIC") and individually owned a membership interest in a subsidiary of SFIC, Grey Goose LLC (the "LLC"). SFIC and the LLC conducted the Grey Goose vodka business. Despite plaintiff's position as chief legal counsel, management of SFIC and the LLC negotiated a sale of the vodka business without the knowledge of plaintiff. Shortly before the scheduled public announcement of the sale, management of the LLC advised plaintiff of the sale and requested plaintiff's consent to the sale in his capacity as a member of the LLC, which was required under the LLC's operating agreement. Of the $2.25 billion dollar cash purchase price, less than 0.49% was proposed to be allocated to the LLC, and on this basis plaintiff initially refused to give his consent. After management threatened to sue plaintiff and terminate his employment, plaintiff consented to the sale. Plaintiff then brought this action, which alleged several derivative and direct claims. In this decision, the court addressed defendants' motion to dismiss.

The court first addressed defendants' motion to dismiss plaintiff's derivative claims for failure to make a proper demand. The court stated that the standard for alleging demand futility in Delaware (as established in *Aronson v. Lewis*, 473 A.2d 805 (Del. 1984)) requires the pleading of particularized facts raising a reasonable doubt that (i)

management is disinterested and independent or (ii) the contested transaction was otherwise the result of a valid exercise of business judgment. As to the first element of the first prong, the court stated that "disinterested" means that a manager is not on both sides of the transaction and is not due to receive a benefit from the transaction that is not shared by the company or other interest holders. In this case, the court determined that the substantial benefit that the managers of the LLC received in their capacity as shareholders of SFIC, at the expense of the LLC, satisfied this element of demand-futility. As to the second element of the first prong, the court stated that the independence of a manager is sufficiently compromised for the purposes of demand-futility when the manager is beholden to a controlling person or so under the influence of a controlling person that the manager's discretion is effectively sterilized. In this case, the control that SFIC and Sidney Frank, who was the founder, chairman, chief executive officer and majority shareholder of SFIC, exerted with respect to the LLC and the sale transaction created a reasonable doubt as to the independence of the managers of the LLC. Despite concluding that demand was excused under the first prong, the court went on to analyze the second prong of the demand-futility test. The court stated that managers of an LLC are presumed to have acted on an informed basis and in the honest belief that their decisions were in furtherance of the LLC and its members. The court stated that, in determining whether such a presumption is overcome by the facts, which typically requires a showing tantamount to corporate waste, both the substance of the transaction and the process by which it was adopted are reviewed. As to the substance of the transaction, the court found that under the facts presented it could not be reasonably concluded that the allocation of the purchase price between SFIC and the LLC was appropriate. As to process, plaintiff alleged that defendants failed to utilize mechanisms typically employed to produce a fair process, such as obtaining an independent appraisal of the assets or appointing a special committee to assess the fairness of the transaction. The court thus held that plaintiff had met his burden of demonstrating demand futility.

Defendants also alleged that plaintiff was an inadequate derivative representative of the LLC because (i) at the time of the sale he was SFIC's chief legal counsel, (ii) he allegedly violated New York's attorney disciplinary rules by accepting an interest in the LLC while serving as SFIC's legal counsel and (iii) the lawsuit was not supported by other members of the LLC. The court found that plaintiff's position as legal counsel to SFIC did not preclude him from bringing a derivative suit because, as defendants excluded him from the negotiations regarding the sale, he never served as legal advisor on the transaction, and thus his representation of SFIC did not involve issues that were "substantially related" to the derivative claims. In addition, the court found that the derivative claims may be maintained without the support of the other members of the LLC, stating that a derivative representative is assessed by his ability to advance the interest of similarly situated interest holders (even if there is only one interest holder with such interest), regardless of the support of other interest holders.

Turning to the substance of plaintiff's derivative claims, the court first addressed plaintiff's claim of breach of fiduciary duty based on the alleged coercion that led plaintiff to consent to the sale. The court disagreed with plaintiff's assertion that the inequitable coercion doctrine, which is the doctrine Delaware courts have applied in the context of proxy voting by diffuse shareholders of public corporations, was applicable in this case. The court found that this doctrine was not applicable to a member of a closely held LLC, which, unlike diffuse shareholders, is not hampered by the difficulties of collective action. Instead, the court applied the standards relating to coercion and duress in bilateral contract negotiations, stating that a party alleging coercion or duress must plead (i) a wrongful act, (ii) which overcomes the will of the aggrieved part and (iii) that he has no adequate legal remedy to protect himself. The court determined that the application of these standards in this context by the fact that the managers of the LLC, in their position as fiduciaries, had a duty to disclose to plaintiff any information that carried a substantial likelihood that a reasonable interest holder would view as significantly

changing the total mix of information bearing on the decision. The court concluded that the threats of litigation and loss of employment, combined with the brief time period in which plaintiff was forced to make a decision without the assistance of counsel, coerced his consent, and thus the court refused to dismiss these claims.

The court then examined defendants' allegations that plaintiff's direct claims were in fact derivative in nature. The court stated that the classification of a claim as derivative or direct turns on (i) who suffered the harm (the company or the suing interest holder individually) and (ii) who would receive the benefit of the remedy (the company or the interest holder individually). Based on this test, plaintiff's breach of contract and breach of good faith and fair dealing claims were judged to be direct because plaintiff suffered the unique harm of the deprivation of his voting rights under the LLC's operating agreement through the defendants' economic coercion and the remedy for such harm would be due solely to plaintiff. The court thus concluded that these claims were direct claims and determined that plaintiff's pleadings with respect to these claims were sufficient to survive defendants' motion to dismiss.

2. *Ishimaru v. Fung*, C.A. No. 929 (Del. Ch. Oct. 26, 2005)

The plaintiff and one of the defendants, Fung, formed a Delaware LLC for the purposes of managing and marketing hedge funds to Japanese investors. The LLC formed a joint venture with a subsidiary of defendant Ivy Asset Management ("Ivy") which had experience and products that would compliment the LLC's business. After Ivy was bought by a third-party bank, it began to market non-J.V. products to the Japanese market in competition with the LLC and in contravention of the amended joint venture agreement.

The complaint alleged that Ivy breached the amended joint venture agreement by failing to adhere to the terms on which Ivy would market certain investment funds in Japan. However, rather than plead facts showing that the plaintiff was entitled to proceed on behalf of the LLC, the complaint instead alleged that Fung, the managing member, breached his fiduciary duties by refusing to bring suit against Ivy. The court found that in essence, the case was a derivative suit against Ivy and to clarify matters, ordered the plaintiff to seek judgment on the pleadings as to whether she could proceed derivatively. The court then held that demand was excused and that the plaintiff could proceed on behalf of the LLC.

The court held that demand was excused because Fung had waived any argument that the plaintiff could not sue derivatively. Fung had argued that the suit against Ivy should be adjudicated before the suit against him, and he twice lead the court and plaintiff to believe he was not objecting to the plaintiff's purported derivative action. Additionally, the court applied precedent from the corporate context and held that demand was excused because the plaintiff articulated particularized facts that, if true, demonstrated that Fung was incapable of disinterestingly determining whether to cause the LLC to sue Ivy. According to the complaint, Fung was planning to leave the LLC and to begin marketing in Europe products substantively identical to the joint venture's. These actions probably violated provisions of the amended joint venture agreement and the LLC agreement, but Fung was allegedly willing to trade away the LLC's claims against Ivy in exchange for Ivy's concessions allowing him to conduct his European marketing. However, the court dismissed the plaintiff's complaint, holding that the LLC would have to arbitrate its claims in accordance with an arbitration provision contained in the joint venture agreement (*see* Section II.K.1).

I. Disclosures

1. *Bakerman v. Sidney Frank Importing Co., Inc.*, C.A. No. 1844-N (Del. Ch. Oct. 10, 2006)

Plaintiff was chief legal counsel to Sidney Frank Importing Co., Inc. ("SFIC") and individually owned a membership interest in a subsidiary of SFIC, Grey Goose LLC (the "LLC"). SFIC and the LLC conducted the Grey Goose vodka business. Despite plaintiff's position as chief legal counsel, management of SFIC and the LLC negotiated a sale of the vodka business without the knowledge of plaintiff. Shortly before the scheduled public announcement of the sale, management of the LLC advised plaintiff of the sale and requested plaintiff's consent to the sale in his capacity as a member of the LLC, which was required under the LLC's operating agreement. Of the $2.25 billion dollar cash purchase price, less than 0.49% was proposed to be allocated to the LLC, and on this basis plaintiff initially refused to give his consent. After management threatened to sue plaintiff and terminate his employment, plaintiff consented to the sale. Plaintiff then brought this action, which alleged several derivative and direct claims. In this decision, the court addressed defendants' motion to dismiss.

The court first addressed defendants' motion to dismiss plaintiff's derivative claims for failure to make a proper demand. The court stated that the standard for alleging demand futility in Delaware (as established in *Aronson v. Lewis*, 473 A.2d 805 (Del. 1984)) requires the pleading of particularized facts raising a reasonable doubt that (i) management is disinterested and independent or (ii) the contested transaction was otherwise the result of a valid exercise of business judgment. As to the first element of the first prong, the court stated that "disinterested" means that a manager is not on both sides of the transaction and is not due to receive a benefit from the transaction that is not shared by the company or other interest holders. In this case, the court determined that the substantial benefit that the managers of the LLC received in their capacity as shareholders of SFIC, at the expense of the LLC, satisfied this element of demand-futility. As to the second element of the first prong, the court stated that the independence of a manager is sufficiently compromised for the purposes of demand-futility when the manager is beholden to a controlling person or so under the influence of a controlling person that the manager's discretion is effectively sterilized. In this case, the control that SFIC and Sidney Frank, who was the founder, chairman, chief executive officer and majority shareholder of SFIC, exerted with respect to the LLC and the sale transaction created a reasonable doubt as to the independence of the managers of the LLC. Despite concluding that demand was excused under the first prong, the court went on to analyze the second prong of the demand-futility test. The court stated that managers of an LLC are presumed to have acted on an informed basis and in the honest belief that their decisions were in furtherance of the LLC and its members. The court stated that, in determining whether such a presumption is overcome by the facts, which typically requires a showing tantamount to corporate waste, both the substance of the transaction and the process by which it was adopted are reviewed. As to the substance of the transaction, the court found that under the facts presented it could not be reasonably concluded that the allocation of the purchase price between SFIC and the LLC was appropriate. As to process, plaintiff alleged that defendants failed to utilize mechanisms typically employed to produce a fair process, such as obtaining an independent appraisal of the assets or appointing a special committee to assess the fairness of the transaction. The court thus held that plaintiff had met his burden of demonstrating demand futility.

Defendants also alleged that plaintiff was an inadequate derivative representative of the LLC because (i) at the time of the sale he was SFIC's chief legal counsel, (ii) he allegedly violated New York's attorney disciplinary rules by accepting an interest in the LLC while serving as SFIC's legal counsel and (iii) the lawsuit was not supported by other members of the LLC. The court found that plaintiff's position as legal counsel to SFIC did not preclude him from bringing a derivative suit because, as defendants excluded him from

the negotiations regarding the sale, he never served as legal advisor on the transaction, and thus his representation of SFIC did not involve issues that were "substantially related" to the derivative claims. In addition, the court found that the derivative claims may be maintained without the support of the other members of the LLC, stating that a derivative representative is assessed by his ability to advance the interest of similarly situated interest holders (even if there is only one interest holder with such interest), regardless of the support of other interest holders.

Turning to the substance of plaintiff's derivative claims, the court first addressed plaintiff's claim of breach of fiduciary duty based on the alleged coercion that led plaintiff to consent to the sale. The court disagreed with plaintiff's assertion that the inequitable coercion doctrine, which is the doctrine Delaware courts have applied in the context of proxy voting by diffuse shareholders of public corporations, was applicable in this case. The court found that this doctrine was not applicable to a member of a closely held LLC, which, unlike diffuse shareholders, is not hampered by the difficulties of collective action. Instead, the court applied the standards relating to coercion and duress in bilateral contract negotiations, stating that a party alleging coercion or duress must plead (i) a wrongful act, (ii) which overcomes the will of the aggrieved part and (iii) that he has no adequate legal remedy to protect himself. The court determined that the application of these standards in this context by the fact that the managers of the LLC, in their position as fiduciaries, had a duty to disclose to plaintiff any information that carried a substantial likelihood that a reasonable interest holder would view as significantly changing the total mix of information bearing on the decision. The court concluded that the threats of litigation and loss of employment, combined with the brief time period in which plaintiff was forced to make a decision without the assistance of counsel, coerced his consent, and thus the court refused to dismiss these claims.

The court then examined defendants' allegations that plaintiff's direct claims were in fact derivative in nature. The court stated that the classification of a claim as derivative or direct turns on (i) who suffered the harm (the company or the suing interest holder individually) and (ii) who would receive the benefit of the remedy (the company or the interest holder individually). Based on this test, plaintiff's breach of contract and breach of good faith and fair dealing claims were judged to be direct because plaintiff suffered the unique harm of the deprivation of his voting rights under the LLC's operating agreement through the defendants' economic coercion and the remedy for such harm would be due solely to plaintiff. The court thus concluded that these claims were direct claims and determined that plaintiff's pleadings with respect to these claims were sufficient to survive defendants' motion to dismiss.

J. Liability of Members

1. *Thomas v. Hobbs*, C.A. No. 04C-02-010-RFS (Del. Super. Ct. Apr. 27, 2005)

The plaintiff brought a breach of contract action against the defendant, the sole member of a limited liability company, Tara Venture, LLC ("Tara Venture"), based on a written construction contract between the plaintiff and Tara Venture. The defendant filed a motion for summary judgment claiming that the plaintiff did not have a cause of action against her personally, but only had a cause of action against Tara Venture. This opinion was the court's decision with respect to such motion.

The court stated that similar to a corporation, "a member of a limited liability company may not be held liable for the debts, obligations and liabilities of the company" unless the member signed a contract on her own behalf, rather than for the company or the member agreed to be obligated personally for the obligations and liabilities of the company. Additionally, the Delaware Superior Court has no jurisdiction to pierce the corporate veil of a limited liability company.

The court found that the defendant, who signed the contract as a member of Tara Venture, was not personally liable for the obligations of Tara Venture under the contract. The contract clearly stated that it was between the plaintiff and "Taraventures L.L.C. c/o Debra A. Hobbs," as the Contractor and that it was signed with "Taraventure LLC" listed as the Contractor, by the defendant, as the member of Tara Venture. (While there was a dispute surrounding the name of Tara Venture since the contract stated that the contract was between the plaintiff and "Taraventures L.L.C.," the contract was signed by the defendant as the member of "Taraventure LLC" and the company was formed under the name "Tara Venture, LLC," it was clear to the court that the mistakes in the contract were clerical errors and Tara Venture, Taraventures and Taraventure were all the same company.) The body of the contract also referred to the "Contractor" rather than the defendant in her individual capacity. Additionally, there was no evidence of a limited liability company agreement clause in which the defendant agreed to be personally obligated for the obligations and liabilities of the company. The plaintiff asserted that the defendant orally agreed to be personally responsible for the obligations of the contract, however the court considered such statements as extrinsic evidence barred under the parol evidence rule since the contract was fully integrated and no exceptions to the parol evidence rule applied. The court granted the defendant's motion for summary judgment and dismissed the defendant from the case.

K. Procedural Issues

1. *Arbitration*

a. *Douzinas v. Am. Bureau of Shipping, Inc.*, 888 A.2d 1146 (Del. Ch. 2006)

Plaintiffs, who were minority members of a Delaware LLC, brought this action against the managing member asserting claims for breach of fiduciary duty. Plaintiffs also asserted various claims against affiliates of the managing member arising from the same course of conduct by the managing member.

Defendants argued that plaintiffs' claims against the managing member were required to be arbitrated pursuant to broad language in the LLC agreement that made arbitration the exclusive method for resolving any dispute arising under or relating to the LLC agreement. In so arguing, defendants' relied heavily on the Delaware Supreme Court's decision in *Elf Atochem North America, Inc. Jaffari* (*see* Section III.K.1), in which the Supreme Court indicated that a broad arbitration provision in an LLC Agreement could encompass fiduciary duty claims raised by a member. Plaintiffs disagreed, arguing that their fiduciary duty claims did not require reference to the LLC agreement and, therefore, were not subject to mandatory arbitration thereunder. In support of this contention, plaintiffs argued for the application of the Supreme Court's teaching in *Parfi Holding AB v. Mirror Image Internet Inc., 817 A.2d 149 (Del. 2002)*, rather than *Elf Atochem*.

The court first addressed the choice of law provision in the LLC agreement, which provided that "except to the extent any provision hereof is mandatorily required to be governed by the [LLC Act], this agreement is governed by and shall be construed in accordance with the law of the state of Texas." The court found, and the parties agreed, that there were no material differences between Texas law and Delaware law regarding the issues raised in this case. The court thus primarily looked to Delaware precedent in rendering this decision but cited Texas precedent, where relevant, to demonstrate the consistency of Texas law with its decision.

With regard to plaintiffs' claims against the managing member, the court found that the facts of this case were more analogous to those in *Elf Atochem* than *Parfi Holding* and, thus held that the parties were required to arbitrate the claims in accordance with the LLC agreement. Significant to the court's finding was the fact that the arbitration clause at issue here, as in *Elf Atochem*, was contained in an LLC agreement, which was the basic contract that gave rise to the fiduciary relationship. The court rejected plaintiff's contention that *Parfi Holding* was applicable precedent in large part because the arbitration provision at issue in that case was not in the company's basic governing document but rather in an underwriting agreement that bore no relation to the parties' fiduciary duties. As a result, the court held, as in *Elf Atochem*, that the scope of the arbitration clause encompassed claims for breach of fiduciary duty. Further, unlike *Parfi Holding,* this case and *Elf Atochem* arose in the alternative entity context, in which the governing statutes, such as the LLC Act, permit contracting parties to expand or restrict fiduciary duties in their governing contract. As a result, the court concluded that no fiduciary duty claim could be decided in the alternative entity context without a close examination of the governing document because as any person adjudicating the claims would be required to interpret various provisions in the governing document in order to determine the breadth and nature of the fiduciary duties thereunder, if any.

With respect to plaintiffs' claims against the affiliates of the managing member, plaintiffs argued that those claims were not subject to mandatory arbitration under the LLC agreement because the affiliates were not members of the LLC and thus not subject to the LLC agreement. The court rejected plaintiffs' argument and ordered arbitration of all such claims based on a theory of equitable estoppel. The court cited *MS Dealer Serv. Corp. v. Franklin, 177 F.3d 942 (11thCir. 1999)*, for the proposition that where a signatory to a contract containing an arbitration clause raises allegations of substantially interdependent and concerted misconduct by both the non-signatory and one or more of the signatories to the contract, equitable estoppel frequently warrants arbitration of all claims because a refusal to do so would render the arbitration clause meaningless and thwart state and federal policy favoring arbitration.

b. *Willie Gary LLC v. James & Jackson LLC*, C.A. No. 1781 (Del. Ch. Jan. 10, 2006) and *Willie Gary LLC v. James & Jackson LLC*, C.A. No. 1781 (Del. Mar. 14, 2006), *aff'g*, (Del. Ch. Jan. 10, 2006)

Plaintiff and defendant were co-owners of a Delaware LLC that was in need of a significant infusion of capital to succeed. Plaintiff negotiated an agreement with a third-party investor who was willing to provide capital, but the defendant refused to agree to a pro rata reduction of its interest in order to generate the equity needed to compensate the investor. As a result, plaintiff could not consummate the agreement and the parties became deadlocked with respect to the business of the LLC.

Plaintiff filed a suit in the Court of Chancery seeking a mandatory injunction and specific performance or, in the alternative, judicial dissolution of the LLC. Defendant filed a motion to dismiss the complaint, arguing that plaintiff's claims were required to be arbitrated pursuant to the terms of the LLC agreement. Prior to determining the issue of arbitrability, the court first had to determine whether the arbitrability of the claims should be decided by the court or an arbitrator. Following United States Supreme Court and Delaware Supreme Court precedent, the court held that, as a general rule, the issue of substantive arbitrability required judicial resolution unless there was clear and unmistakable evidence that the parties intended otherwise. In determining that the issue was

properly before the court, the court held that the mere reference to the rules of the American Arbitration Association (the "AAA Rules") in the arbitration clause of the LLC Agreement did not provide clear and unmistakable evidence that the issue of substantive arbitrability was to be decided by an arbitrator.

Upon determining that the court should decide the issue of arbitrability, the court denied defendant's motion to dismiss the complaint, finding that none of plaintiff's claims were subject to the mandatory arbitration clause in the LLC agreement. To the contrary, the court held that the LLC agreement itself expressly authorized members of the LLC to apply to courts for the remedies of injunctive relief and specific performance. Further, with respect to plaintiff's claim for judicial dissolution, the court distinguished the dissolution clause in this case from that examined in *Terex Corp. v. STV USA, Inc.* (*see* Section III.K) and held that the provisions in the LLC agreement relating to judicial dissolution under the LLC Act explicitly contemplated judicial involvement in the dissolution process.

In a subsequent decision in this case, the Delaware Supreme Court affirmed the Chancery Court's decision that the plaintiff's claims were not required to be arbitrated. With respect to the issue of substantive arbitrability, however, the Supreme Court did not totally agree with the Chancery Court's analysis regarding the significance of a reference to the AAA Rules in the arbitration clause. As a matter of policy, the Delaware Supreme Court held that Delaware follows the majority federal view that references to the AAA Rules in an arbitration agreement are clear and unmistakable evidence that the parties intended to arbitrate issues of substantive arbitrability. The Supreme Court stated that the majority view, however, does not require that arbitrators decide the arbitrability of all cases where an arbitration clause incorporates the AAA Rules. Instead, it only applies where the arbitration clause generally provides for arbitration of all disputes and also incorporates a set of arbitration rules that empower arbitrators to decide arbitrability. Thus, since the arbitration provision in the LLC agreement did not subject all disputes to arbitration, the Supreme Court held that the Chancery Court was correct in not applying the federal majority rule in this case.

c. *Ishimaru v. Fung*, C.A. No. 929 (Del. Ch. Oct. 26, 2005)

The plaintiff and one of the defendants, Fung, formed a Delaware LLC for the purposes of managing and marketing hedge funds to Japanese investors. The LLC formed a joint venture with a subsidiary of defendant Ivy Asset Management ("Ivy") which had experience and products that would compliment the LLC's business. After Ivy was bought by a third-party bank, it began to market non-J.V. products to the Japanese market in competition with the LLC and in contravention of the amended joint venture agreement.

After holding that the plaintiff could sue derivatively on behalf of the Company and that demand was excused (*see* Section II.H), the court dismissed the plaintiff's complaint holding that the LLC would have to arbitrate its claims in accordance with an arbitration provision contained in the joint venture agreement. In doing so, the court relied upon Delaware and federal public policy which requires that doubts be resolved in favor of arbitration when that conclusion is a reasonable interpretation of the parties contract. Although Ivy Asset was not, by its literal terms, bound by the arbitration clause, the court nonetheless held that the dispute was subject to arbitration. The LLC was bound by the arbitration clause, and the plaintiff's allegations effectively argued that Ivy Asset signed a contract fundamentally amending the terms of the Joint

Venture Agreement and then breached that amendment. The court, therefore, found that the claims plaintiffs sought to bring derivatively were contingent upon the proposition that Ivy Asset was effectively admitted as a party to the joint venture agreement, altered the formal terms of that agreement and thereafter breached the altered joint venture agreement. Hence, the plaintiff was equitably estopped from denying Ivy Asset's demand to arbitrate in accordance with the joint venture agreement.

d. *Terex Corp. v. STV USA, Inc.*, C.A. No. 1614-N (Del. Ch. Oct. 20, 2005)

In an action seeking judicial dissolution of a Delaware LLC, defendant filed this motion to dismiss the complaint pursuant to a broad mandatory arbitration clause in the LLC Agreement. In construing the scope of the arbitration clause, which unequivocally required all disputes arising out of or relating to the LLC Agreement to be resolved through arbitration, the court stated that the broad scope of the arbitration mandate would only be limited where a plain reading of the text specifically indicated such a limitation. The court held that a clause requiring members of the LLC to take appropriate steps required by law following the entry of a judicial dissolution under the LLC Act did not carve out judicial dissolution from the reach of the arbitration clause, stating that dissolution could be entered in accordance with, and following, dissolution proceedings before an arbitrator. The court therefore granted defendant's motion to dismiss.

e. *Flight Options Int'l, Inc. v. Flight Options, LLC*, C.A. No. 1459-N (Del. Ch. July 11, 2005).

The plaintiff, a member of the defendant limited liability company (the "Company"), sought a preliminary injunction to enjoin the Company from implementing a Purchase Agreement with Raytheon Travel Air Company ("RTA"), another member of the Company, pending arbitration of their disputes. The plaintiff alleged that the Purchase Agreement, which would reduce the plaintiff's equity interest in the Company from 31% to 1%, violated the LLC agreement of the Company and that the managers breached their fiduciary duties and obligations under the LLC agreement.

The Company had been in constant indebtedness which has been mainly supported by Raytheon Company ("Raytheon"), the parent company of RTA, and its affiliates. From 2004 to 2005, the Company received reports from two consulting firms as to the poor financial outlook of the Company and an appraisal of the Company's common equity units from Standard & Poor's. In May 2005, RTA submitted a term sheet for its purchase of new equity which included the issuance of $50 million of common units of the Company, valued at $0.01 per unit, to RTA and any other equity holder who chose to exercise its preemptive rights. Despite opposition from the managers of the Company who represented the plaintiff, the Company executed the Purchase Agreement with Raytheon on June 9, 2005. While the Company sought investments from external investors, none of their negotiations were successful before July 11, 2005, the date the Purchase Agreement was to be implemented. Despite efforts by the Company to enhance the terms of the Purchase Agreement, Raytheon only agreed to a "fiduciary out" and following execution of the Purchase Agreement, all eligible equity holders, including the plaintiff, were sent a preemptive rights notice. The plaintiff did not exercise its preemptive rights.

The plaintiff sought a preliminary injunction to enjoin the Company from implementing the Purchase Agreement. For a preliminary injunction, the

plaintiff must prove 1) a reasonable probability of success on the merits at trial; 2) that it will suffer imminent, irreparable harm if its application is denied; and 3) that the harm to the plaintiff, if relief is denied, outweighs the harm to the defendant if relief is granted. In this case, the preliminary injunction was sought in aid of arbitration thus requiring the plaintiff to show in connection with success on the merits, its entitlement to arbitration and the merits of its arbitration claims. The court stated that where the right to arbitrate is clear, the party seeking the preliminary injunction need only "establish a reasonable probability that its arbitration position is sound." In other words, the plaintiff must "persuade the court that the arbitration panel could find in its favor and that there is a reasonable possibility of such a result."

With respect to the first prong regarding the probability of success on the merits, the court found that the conduct of the RTA Managers was to be evaluated by an "arm's length" standard under the LLC Agreement rather than the entire fairness standard. The LLC Agreement provided that for transactions between the Company and its affiliates, the general fiduciary duties of managers were limited to requiring that the transaction be on "arm's length terms and conditions" and carried out in good faith and through fair dealing. The plaintiff questioned the process by which the RTA Managers valued the common units by asserting that the Company did not retain an investment adviser and failed to receive a formal opinion from either of the consulting firms from which it received reports as to the company's outlook. The court agreed with the plaintiff's position and placed importance on the lack of formal opinions from the consulting firms in presenting their conclusions as well as the lack of coordination and process for reading market perception. The court stated that "the process chosen [to value the equity] was so informal as to undermine substantially the ability of the RTA Managers to show that the price is the equivalent of an arm's length transaction's result, at least within the projected views of an arbitration panel." The court found that the plaintiff met its burden with respect to the first prong of the test for a preliminary injunction.

The court next addressed whether irreparable harm would result if the preliminary injunction was denied. Even though a severe dilution of a party's equity interest in a company had been found to constitute irreparable harm, the court stated that the determination was a case-by-case analysis in which the potential consequences of the dilution must be considered. The defendants argued that no irreparable harm would result since Raytheon would receive the benefits of the dilution, and rescission of the agreement was a possibility. The defendants also asserted that the value of the plaintiff's interest before and after the issuance of the new equity could be fairly measured and that dilution of the plaintiff's equity interest would not impair its right to designate two members of the board of the Company. The court, however, concluded that the dilution of the plaintiff's equity interest in the Company could be characterized as irreparable harm since rescission could be impeded by Raytheon's sale of its interests and calculating the damages would be a "daunting task."

In balancing the equities between the Company and the plaintiff, the court found that restoring the plaintiff's equity position following a dilution of its equity interest would be "problematic." With respect to harm to the Company, the court found that even though Raytheon could act in its discretion to cause harm to the Company if the injunction were granted, the court found such actions to be unlikely since Raytheon owned 69% of the Company's equity and would be similarly harmed by such actions. Therefore, the court concluded that the balance of equities tipped slightly in favor of the plaintiff.

Finding all of the requirements for a preliminary injunction satisfied, the court granted the preliminary injunction enjoining implementation of the Purchase Agreement pending commencement of the arbitration proceedings, but, noting that the LLC Agreement specifically authorized the parties to pursue interim relief through arbitration, the court's order provided that the injunction would expire in 30 days during which period plaintiff could take its claims to arbitration and seek interim relief there.

3. *Jurisdiction*

a. *Shamrock Holdings of California, Inc. v. Arenson*, C.A. No. 04-1339-SLR (D. Del. Mar. 14, 2006)

The parties to this action were either members, investors or class representatives on the Supervisory Board of ALH Holdings, LLC ("ALH"), a Delaware limited liability company. Of the six named defendants, three were Delaware entities. In December 1998, members of ALH's Supervisory Board formed a Delaware corporate subsidiary, ALH II, Inc. ("ALH II") to serve as the parent company of all of ALH's operating subsidiaries. In 2004, plaintiffs filed a declaratory judgment action against defendants. Defendants sought to dismiss plaintiffs' declaratory judgment action asserting that the United States District Court for the District of Delaware lacked personal jurisdiction over defendants. Additionally, Abraham Arenson ("Arenson"), a class B representative on ALH's Supervisory Board, sought to dismiss plaintiffs' declaratory judgment against him for failing to allege "that a case or controversy of sufficient immediacy exist[ed] between Arenson and plaintiffs."

The court first addressed defendants' motion to dismiss for lack of personal jurisdiction. In such a motion, the court stated that "once a jurisdictional defense has been raised, the plaintiff bears the burden of establishing with reasonable particularity that sufficient minimum contacts have occurred between the defendant and the forum state to support jurisdiction." The plaintiff must allege facts to satisfy the forum state's long arm statute as well as the constitutional requirements for jurisdiction. Delaware's long-arm statute provides that a Delaware court may "exercise personal jurisdiction over any nonresident, or a personal representative, who in person or through an agent transacts any business or performs any character of work or services in the State [of Delaware]." Citing the Delaware Chancery Court in *Cairns v. Gelmon*, the court stated that "a single act of incorporation in Delaware will suffice to confer personal jurisdiction over a nonresident defendant if such purposeful activity in Delaware is an integral component of the total transaction to which plaintiff's cause of action relates."

The court found that the causes of action in the suit brought by plaintiffs related to the formation and incorporation of ALH and ALH II, respectively, and that the defendants' involvement in the formation and incorporation of these Delaware entities satisfied the requirements for jurisdiction under Delaware's long-arm statute. The court went on to state that defendants along with other ALH members created ALH II in order to obtain debt financing and hold stock in ALH's subsidiaries, thus "purposely avail[ing] themselves of the privilege of conducting activities in Delaware." Based on the foregoing reasons, the court denied defendants' motion to dismiss based on lack of personal jurisdiction.

The court next addressed Arenson's motion to dismiss. In a declaratory judgment action, "a plaintiff must demonstrate the existence of an actual controversy in which the parties have adverse legal interests, and which is of

sufficient immediacy to warrant a declaration of rights." The court dismissed plaintiffs' arguments that Arenson might assert that he was "wrongfully deprived of a meaningful role in the ALH Supervisory Board's decision-making process" (finding that the class B members, not Arenson, would suffer a harm if Arenson could not participate in the ALH Supervisory Board) and that Arenson's interests were adverse to plaintiffs because he was an indirect holder of class B equity interests (holding that plaintiffs had no foundation for "the position that a financial interest in a company is enough to require a party to defend a declaratory judgment action") -- but the court accepted plaintiffs' argument that Arenson had the authority as a class B representative on ALH's Supervisory Board to advance plaintiffs' legal fees and expenses and had tried to interfere with the indemnification and advancement rights of plaintiffs finding that there was a factual issue with regard to Arenson's "role in the Supervisory Board decision-making process" and thus denied Arenson's motion to dismiss.

L. General Construction and Application of Limited Liability Company Agreements

1. *Minnesota Invco of RSA #7, Inc. v. Midwest Wireless Holdings LLC*, C.A. No. 1887-N (Del. Ch. June 7, 2006).

The plaintiffs, minority interest holders in Midwest Wireless Communications LLC, a Delaware limited liability company ("Communications"), sought specific performance of a right of first refusal under Communications' operating agreement (the "1995 LLC Agreement") to prohibit the sale of Midwest Wireless Holdings LLC ("Holdings"), the majority interest holder in Communications, without first offering plaintiffs the right to purchase Holdings' interest in Communications.

In 1999, Communications and plaintiffs entered into a restructuring whereby Holdings was formed to purchase certain assets in Iowa and Wisconsin. To facilitate the restructuring, plaintiffs, Communications and Holdings executed an agreement (the "1999 Agreement") which provided that if there were a proposed sale of all or substantially all of the assets of Holdings, plaintiffs had a right to "tag along" by exchanging their interests in Communications for interests in Holdings. The 1999 Agreement further provided that if the plaintiffs failed to exercise their "tag along rights," Holdings could compel plaintiffs to transfer their interests in Communications by exercising its "drag along rights." As a result of the restructuring, Holdings owned an 86% interest in Communications. The 1999 Agreement did not refer to plaintiffs' right of first refusal under the 1995 LLC Agreement and contained a broad integration clause as well as a conflict provision stating that the terms of the 1999 Agreement would govern in the event of a conflict with the 1995 LLC Agreement.

In 2005, Holdings sought potential bidders to purchase the company. The plaintiffs did not initially assert that a sale of Holdings would trigger their right of first refusal. In order to receive the highest price from bidders, the boards of managers of Holdings and Communications amended their respective LLC agreements on November 11, 2005 to eliminate all members' rights of first refusal. Plaintiffs were notified of the amendments and did not object. On November 17, 2005, Holdings announced its agreement with Alltel Corporation ("Alltel") pursuant to which Alltel would acquire all of Holdings by merger (the "Alltel Transaction"). Plaintiffs met with Holdings on December 14, 2005 to discuss their rights regarding the Alltel Transaction and asserted its right of first refusal for the first time. Holdings then requested plaintiffs to exercise its tag along rights, indicating otherwise Holdings would exercise its drag along rights.

The court first addressed whether plaintiffs had a right of first refusal with respect to the units of Communications in the Alltel Transaction. The court found that the 1999 Agreement clearly governed the Alltel Transaction based on its tag-along and drag-along provisions in the event of a proposed sale of all or substantially all of Holdings' assets

and its broad integration clause. Since the 1999 Agreement was fully integrated and failed to provide for any right of first refusal, the court stated that a plain reading of the integration clause indicated that there was no right of first refusal in connection with the Alltel Transaction. Additionally, the court found that Holdings' drag along rights were in direct conflict with the plaintiffs' right of first refusal since plaintiffs' ability to exercise a right of first refusal would eliminate Holdings' drag along rights. Since the 1999 Agreement expressly stated that its terms would govern in the event of a conflict with the 1995 LLC Agreement, Holdings' drag along rights prevailed over plaintiffs' right of first refusal.

The plaintiffs also argued that the November 2005 amendment in which Holdings voted its 86% interest in favor of eliminating the members' right of first refusal was invalid since the 1995 LLC Agreement contained an "acquiring person" provision which prevented any member owning more than a 30% interest in Communications from exercising majority voting power. The court rejected plaintiffs' argument stating that "treating Holdings as an 'acquiring person'…runs counter to the very structure and purpose of the 1999 transaction to act as the parent of Communications." Additionally, Holdings had previously exercised its majority voting power without objection in all other Communications matters.

Finally, the court also rejected plaintiff's argument that the Communications board members breached their fiduciary duty of care when they approved the amendment to the 1995 LLC Agreement. The court found that the board members were fully informed and approved the amendments based on the advice of counsel and Bear Stearns and in the good faith belief that the amendments would maximize the sale price of Holdings and get the best possible value for its unit holders and for plaintiffs. Based on the foregoing, the court held that the plaintiffs did not have a right of first refusal with respect to the Alltel Transaction and Holdings could assert its drag along rights.

O. Change of Control Transactions

1. *Blackmore Partners, L.P. v. Link Energy LLC*, C.A. No. 454-N (Del. Ch. Oct. 14, 2005)

Following the court's denial of the defendants' motion to dismiss referred to below, the defendants moved for summary judgment at the conclusion of discovery and this opinion was the court's decision with respect to such motion.

The plaintiff first alleged that the court should apply enhanced scrutiny to the challenged transaction in which the proceeds of the sale of substantially all of the LLC's assets were used to repay the debt of the LLC and to pay holders of unsecured notes a payment for covenant waiver thus rendering the LLC's units worthless. The plaintiff claimed the board of directors of the LLC deprived the unit holders of consideration that they would have received if the board had not agreed to the demands of the note holders. The court rejected the plaintiff's reliance on the court's decision in *Orban v. Field* which held that "when a board approves a transaction that favors one corporate constituency over another, they lose, at least as an initial matter, the cloak of business judgment protection," and the board must demonstrate that it acted reasonably and in good faith. The court in the instant case distinguished *Orban* by finding that the "defendants did not act 'solely or primarily for the express purpose of depriving a shareholder of effective enjoyment of a right conferred by law.'" Importantly, the LLC's operating agreement empowered the board of directors to authorize a sale of all or substantially all of the LLC's assets without a vote of the unit holders thus precluding any need for measures by the board to prevent the unit holder's approval or vote. The court also found that even if *Orban* applied to the instant case, the defendants met the enhanced scrutiny standard since the company was insolvent and no better transaction was available.

The court next addressed the plaintiff's claim that the defendants breached their fiduciary duties to the unit holders by focusing on the creditors' interests over the interests of the unit holders. The plaintiff conceded that the company was insolvent at the time of the disputed transaction, and the court stated that "the board of directors of an insolvent company may take into account the interests of creditors at the apparent expense of stockholders if, in doing so, the board meets its fiduciary duties to all relevant constituencies."

The court then analyzed whether the directors met their fiduciary duties with respect to the unit holders. The plaintiff claimed that the board's decisions regarding the transaction were tainted by the involvement of J. Robert Chambers ("Chambers"), a director who was a managing director of Lehman Brothers, a holder of an equal percentage of notes and units of the LLC. The court referred to its decision in *Cooke v. Oolie* which involved defendants who were both shareholders and creditors of a corporation considering an acquisition proposal. The *Cooke* court held that "plaintiffs bore the burden of showing that an actual conflict existed, and that the deal chosen by the defendants offered superior terms for creditors and inferior terms for the plaintiff shareholders compared to other proposals available to the defendant corporation." Unlike the defendants in *Cooke*, the defendants in the instant case owed fiduciary duties to creditors because the company was insolvent. Even if Chambers' membership on the board created a potential conflict, there were no better alternatives for the unit holders other than the transaction approved by the board. The court also noted that even if Chambers were conflicted, the board would still receive the protections of the business judgment rule because such protections only require that a majority of the directors approving the transaction remain disinterested, and the plaintiff made no claims that other directors were interested.

The court also rejected the plaintiff's argument that the Special Committee of independent directors formed by the board to consider potential transactions was tainted by the presence of the CEO of the LLC and Chambers at the meetings of the Special Committee. Since the plaintiff failed to present evidence that the CEO or Chambers influenced the Special Committee or acted "as anything more than necessary sources of information," the court found the Special Committee operated with "sufficient independence to merit the cloak of business judgment protection."

Next, the plaintiff argued that the defendants breached their duty of care by approving the transaction without sufficient expert information and by failing to use the leverage from a potential bankruptcy filing against the note holders to negotiate a better settlement for the unit holders. The court found that the plaintiff's claims based on breach of the duty of care were precluded by the LLC's operating agreement exculpating directors for all awards of damages for violations of the duty of due care. Nonetheless, the court addressed the plaintiff's claims regarding the duty of due care finding that the directors did not violate such duty. The court stated that the defendants did not act with gross negligence since the record showed that the Special Committee met "repeatedly over months to address the issue of the company's impending insolvency and to consider alternatives." Additionally, the note holders had the ability to veto any proposed transaction thus limiting any leverage power the company had against the note holders. Moreover, the court noted that "the choices made in formulating a negotiating strategy are within the core of what is protected by the business judgment rule," and the evidence failed to support the plaintiff's claimed violation of due care.

Finally, the court rejected the plaintiff's claim that the defendants acted in bad faith in approving the transaction finding that "the fact that unit holders were left with nothing at the end, given a context in which the chief alternative substantiated by evidence was an equally barren bankruptcy proceeding, does not suffice to rebut the presumption that the

directors were acting in the good faith exercise of their fiduciary duties, or to establish a claim of waste." The court granted the defendants' motion for summary judgment.

P. Membership

1. *In re Grupo Dos Chiles, LLC*, C.A. No. 1447-N (Del. Ch. Mar. 10, 2006)

The petitioner, Shriver, and one of the respondents, Martinez, formed a Delaware LLC. The LLC's certificate of formation ("Certificate") named Martinez's son as the "initial" member, and the one page LLC Agreement named Shriver and Martinez as the "Managing Partners." Grupo eventually lost its good standing with the State of Delaware because it did not pay its Delaware taxes. Shriver sought reformation of the LLC Agreement to reflect accurately the true membership of the LLC and also sought a finding that Martinez's unilateral payment of back taxes on behalf of the company did not return Grupo to good standing with the State of Delaware.

In its letter opinion, the court emphasized that it considered the underlying facts and course of dealing among the parties to be at least as important as formalities. The court first held that both Shriver and Martinez were members of the LLC. Significantly, the court said in this regard that the LLC Agreement superceded the Certificate, and the LLC Agreement made it clear that both Shriver and Martinez were members of the LLC. In so holding, the court indicated that it did not think it important that the LLC Agreement referred to the parties as "Managing Partners," rather than as members. Moreover, the documentary evidence (letters, loan documents, etc.) made it clear that Shriver and Martinez were members of the LLC. The court also noted that, because the LLC Act does not require that members of an LLC be set forth in a certificate of formation, there did not appear to be a continuing obligation to amend a certificate of formation every time membership in an LLC changed.

The court declined to decide whether restoring the good standing of an LLC that had had its good standing cancelled for failure to pay taxes was a "ministerial" act that any member or manager could take, or whether such action required a vote of the members. Instead, the court narrowed its holding to the facts of the case and held that if an LLC lost its good standing for nonpayment of taxes, a member who represented less than a majority of the voting power, and who knew that there is a dispute as to whether the company should continue because another co-equal member has initiated litigation to dissolve the company, could not unilaterally restore the LLC to good standing by paying the taxes due. Thus, the court voided the Delaware Secretary of State's restoration of the LLC to good standing.

Q. Management

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R. Limited Liability Company Agreement

1. *Facchina v. Malley*, C.A. No. 783-N (Del. Ch. July 12, 2006)

This case is one in a long running dispute involving several related Delaware limited liability companies. The disputes generally involve control over the LLCs. In this opinion, the court found that there was no limited liability company agreement but, nonetheless, still found that there was a limited liability company and that it had members each owning a set, identifiable interest in the LLC, notwithstanding the fact that the LLC Act would seem to require an LLC agreement for various purposes including the determination of the members (*see* Section 18-301 of the LLC Act). The court held in the absence of an LLC agreement, the LLC Act would provide the governing framework for the LLC and that under Section 18-402 of the LLC Act, management of an LLC is vested in the members owning a majority percentage interest in the LLC.

S. Formation

1. *Ramone v. Lang,* C.A. No. 1592-N (Del. Ch. Apr. 3, 2006)

Plaintiff brought this action under theories of breach of contract, breach of fiduciary duty and promissory estoppel based on six months of discussions between plaintiff and defendant that failed to result in the contemplated formalization of their arrangement in an LLC agreement.

Before plaintiff's involvement with defendant, defendant had already signed a purchase agreement to buy property on which plaintiff had considered opening a public swim and fitness center. For months, plaintiff and defendant discussed varying deal terms but were unable to reach a final agreement. While negotiations were ongoing, plaintiff and defendant worked together to have the property rezoned, defendant represented to the press and his financing bank that plaintiff was involved in the project and plaintiff solicited members for a swim team at the property. Ultimately, defendant, frustrated by his inability to reach a final accord with plaintiff, entered into an LLC agreement with three other parties. Plaintiff then filed this action.

The court found that no binding contractual relationship existed between the parties. Plaintiff claimed that, through their e-mail exchanges, the parties established a final, binding agreement as to their respective rights and obligations in an LLC and as to the property. The court cited the general principle of contract formation in Delaware, which does not look to a party's subjective intent but rather requires an "overt" "manifestation of mutual assent to the exchange and consideration." For a party's assent to constitute an acceptance that would form a contract, it must include an expression of commitment that (i) is not conditional on any further act by either party and (ii) is on the terms proposed in the offer without the slightest variation. To be enforceable, a contract must contain all material terms and a court will not order specific performance if, as in this case, it would be required to supply essential terms. In this case, the language used in, and the negotiations that occurred after, the e-mail cited by plaintiff as constituting a final, binding agreement evidenced that a contract had not been formed.

The court then considered the theory of de facto partnership and concluded that a partnership relationship had not been created. Separate from the contractual duties that the court disposed of as discussed above, plaintiff claimed that the parties had become partners and that defendant was in breach of his fiduciary duties. The court stated that under DRUPA Section 15-202 a partnership exists where, regardless of the intent of the parties, two or more persons associate themselves to carry on a business for profit. The level of proof required to establish this type of association is higher in a suit between the alleged partners (as opposed to a suit by a third party). Under Delaware law, "there is no singularly dispositive consideration that determines whether or not a partnership existed," but a court must find a mutual obligation to share profits and losses and may consider the conduct of the parties. In this case, the court, while acknowledging that the lack of written agreement is not necessarily conclusive of the existence of a partnership, found that the absence of such an agreement left it without terms to enforce. In addition, the fact that the fiduciary relationship contemplated by the parties was as members of a limited liability company counseled against finding that they had created a general partnership. DRUPA Section 15-502 specifically provides that associations formed under other chapters of the Delaware Code are not partnerships and, in the opinion of the court, it would be an odd result that a failed attempt at creating an LLC would place the parties in a partnership. Even given this, however, the court posited that in a situation in which the parties had reached agreement on material terms and one side simply balked on the documentation of the LLC, it might be possible to find that a general partnership had been created. This, however, was not the situation in this case.

The court did find the doctrine of promissory estoppel to be available to plaintiff, as defendant had disappointed the expectation of plaintiff's participation in the property, on which plaintiff had reasonably relied. The court set forth the elements of promissory estoppel under Delaware law, which are clear and convincing evidence of (i) a promise; (ii) the reasonable expectation, from an objective viewpoint, of the promissor to induce action or forebearance by the promissee; (iii) the promissee's actual, reasonable reliance on the promise and action to his detriment and (iv) the binding effect of the promise because without enforcement there would be an injustice. The court espoused its view that the normal failure of parties to reach a binding contract is not grounds for invoking the doctrine and that promissory estoppel should be used in the relatively narrow circumstances in which the legitimate expectations of a party made vulnerable by promises in the negotiation process need to be protected. In this case, the court accepted plaintiff's argument that, even if the parties had not agreed on a final deal structure, the understanding throughout the process was that defendant would make the pool facilities at the property available for plaintiff's use and that plaintiff relied on this promise with the knowledge of defendant.

IV. GENERAL PARTNERSHIPS & JOINT VENTURES

A. Formation

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