2017 SPRING MEETING
OF
ABA BUSINESS LAW SECTION

2017 Review of LLC Case Law Developments

2017 SUMMARY OF DELAWARE CASE LAW

RELATING TO

ALTERNATIVE ENTITIES[1]

Louis G. Hering
David A. Harris
Morris, Nichols, Arsht & Tunnell LLP
Wilmington, Delaware

February 2, 2017

© Copyright 2017, Morris, Nichols, Arsht & Tunnell LLP
All rights reserved.

[1] Morris Nichols maintains a Cumulative Survey of Delaware case law relating to alternative entities which is updated annually, organized by subject area and includes most cases that address significant alternative entity issues. The entire Cumulative Survey and annual updates are available on the Morris Nichols website at www.mnat.com/practices/commercial under EPublications.

TABLE OF CONTENTS

1. *Merinoff v. Empire Merchants, LLC*, C.A. No. 12920–VCS (Del. Ch. Feb. 2, 2017) (V.C. Slights) 1

2. *CelestialRX Investments, LLC v. Krivulka*, C.A. No. 11733-VCG (Del. Ch. Jan. 31, 2017) (V.C. Glasscock) 2

3. *Dieckman v. Regency GP LP*, No. 208, 2016 (Del. Jan. 20, 2017) (J. Seitz) 4

4. *El Paso Pipeline GP Company, L.L.C. v. Brinckerhoff*, No. 103, 2016 (Del. Dec. 20, 2016) (en banc) 5

5. *Employees Retirement System of the City of St. Louis v. TC Pipelines GP, Inc.*, C.A. No. 291, 2016 (Del. Dec. 19, 2016) (ORDER) 7

6. *In re Arctic Ease, LLC*, C.A. No. 8932–VCMR (Del. Ch. Dec. 9, 2016) (V.C. Montgomery-Reeves) 7

7. *Gomes v. Karnell*, C.A. No. 11814–VCMR (Del. Ch. Nov. 30, 2016) (V.C. Montgomery-Reeves) 9

8. *Trascent Mgmt. Consulting, LLC v. Bouri*, C.A. No. 10915-VCM (Del. Nov. 28, 2016) (*en banc*) 9

9. *Abelmann v. Granum*, C.A. No. 12041–VCMR (Del. Ch. Nov. 15, 2016) (V.C. Montgomery-Reeves) 10

10. *Finger Lakes Capital Partners, LLC v. Honeoye Lake Acquisition, LLC*, C.A. No. 9742-VCL (Del. Ch. Oct. 26, 2015), *aff'd in part, rev'd in part* No. 42, 2016 (Del. Nov. 14, 2016) (*en banc*) 10

11. *Grand Acquisition, LLC v. Passco Indian Springs DST*, C.A. No. 12003–VCMR (Del. Ch. Sept. 7, 2016) (V.C. Montgomery-Reeves) 12

12. *Bizzari v. Suburban Waste Servs., Inc.*, C.A. No. 10709-JL (Del. Ch. Aug. 30, 2016) (J. LeGrow) 14

13. *Obeid v. Hogan*, C.A. No. 11900-VCL (Del. Ch. June 10, 2016) (V.C. Laster) 15

14. *Angus v. Ajio, LLC*, C.A. No. 11895-VCG (Del. Ch. May 13, 2016) (V.C. Glasscock) 16

15. *Employees Retirement System of the City of St. Louis v. TC Pipelines GP, Inc.*, C.A. No. 11603-VCG (Del. Ch. May 11, 2016) (V.C. Glasscock) 17

16. *Brinckerhoff v. Enbridge Energy Company, Inc.*, C.A. No. 11314-VCS (Del. Ch. April 29, 2016) (V.C. Slights) 18

17. *The Joseph Penar Family Trust v. Adams*, C.A. No. 10441-VCG (Del. Ch. April 28, 2016) (V.C. Glasscock)....................19

18. *Hyatt v. Al Jazeera America Holdings II, LLC*, C.A. No. 11465-VCG (Del. Ch. Mar. 31, 2016) (V.C. Glasscock)....................20

19. *Dieckman v. Regency GP LP*, C.A. No. 11130-CB (Del. Ch. Mar. 29, 2016) (C. Bouchard)....................21

20. *CIM Urban Lending GP, LLC v. Cantor Commercial Real Estate Sponsor, L.P.*, C.A. No. 11060-VCN (Del. Ch. Feb. 26, 2016) (V.C. Noble)....................22

1. *Merinoff v. Empire Merchants, LLC*, C.A. No. 12920–VCS (Del. Ch. Feb. 2, 2017) (V.C. Slights)

Plaintiffs Charles Merinoff and Gregory Baird brought an action for advancement of legal fees they claimed were owed to them by defendant, Empire Merchants, LLC, a Delaware limited liability company (the "Company"), in connection with their defense of a lawsuit brought against them by defendant in New York federal court for running a cross-border alcohol bootlegging scheme. Defendant moved for dismissal under Court of Chancery Rule 12(b)(3) for improper venue, arguing that the forum selection clause in Section 12.6 of the Company's Amended and Restated Limited Liability Company Agreement (the "LLC Agreement") designated New York as the proper venue for the action. Section 12.6 stated, in relevant part, that any "suit, action or other legal proceeding arising out of [the LLC Agreement would] be brought" in New York. Arguing against dismissal, plaintiffs relied on a carve-out in the same provision specifying that "notwithstanding the foregoing, any legal proceeding arising out of the LLC Agreement which, under [the Delaware LLC] Act or, to the extent made applicable to the Company pursuant to the [LLC] Agreement, the DGCL, is required to be brought in the Delaware Court of Chancery may only be brought in the Delaware Court of Chancery and the parties hereto hereby consent to the jurisdiction of the Delaware Court of Chancery under such circumstances."

Although plaintiffs acknowledged that the Delaware LLC Act does not mandate the venue in which an advancement action must be brought, plaintiffs argued that the carve-out nonetheless applied. Plaintiffs contended that because the advancement section of the LLC Agreement referenced the DGCL three times, the parties must have intended to make the DGCL apply to contractual advancement rights. Consequently, plaintiffs argued that because the DGCL expressly designates the Court of Chancery as the exclusive Delaware venue for advancement actions, venue was not only proper in the Court of Chancery but was also required pursuant to the carve-out, thereby overriding the New York forum selection clause.

The court began its analysis with a general overview of Delaware judicial deference to forum selection clauses that are mutually contracted for by parties to an agreement. The court stated that the rule of interpretation of such clauses gives language its plain and ordinary meaning in an attempt to effectuate the parties' intent. Applying that interpretive method to the LLC Agreement, the court noted that in order for the carve-out to override the forum selection clause, the DGCL must (i) have been made applicable to the advancement provision and (ii) require that advancement actions be brought in the Court of Chancery. The court determined that the LLC Agreement had not made the DGCL applicable to the advancement provision, noting that the references to the DGCL were meant to define the fiduciary duties of managers and officers of the Company and to clarify the type of conduct that could give rise to indemnification rights. The court stated that "[n]o reasonable interpretation of [the advancement provision] would suggest that the parties intended to incorporate the DGCL to define or address in any manner the contractual right to advancement." Therefore, the court concluded that the DGCL was inapplicable by the LLC Agreement's own terms and that the carve-out did not override the New York forum selection clause. The court went on to note that even if the DGCL

had been made applicable by the LLC Agreement, the DGCL does not require that advancement actions be brought in the Court of Chancery; rather, the DGCL simply states that the Court of Chancery has exclusive jurisdiction among the Delaware courts over such actions. Indeed, the court recognized that advancement actions involving Delaware entities are "regularly brought and adjudicated" outside Delaware. In the court's view, plaintiffs' reading of the carve-out was an attempt to twist its unambiguous language into an overbroad provision that would nullify the forum selection clause any time a DGCL section (made applicable by the LLC Agreement) conferred exclusive jurisdiction on the Court of Chancery. The court therefore upheld the forum selection clause and granted defendant's motion to dismiss for improper venue.

2. *CelestialRX Investments, LLC v. Krivulka*, C.A. No. 11733-VCG (Del. Ch. Jan. 31, 2017) (V.C. Glasscock)

Plaintiff, CelestialRX, LLC ("CelestialRX"), which is wholly owned by non-party Steve Laumas ("Laumas"), is a member of Akrimax Pharmaceuticals, LLC (the "Company"). CelestialRX and Krittika Life Sciences, LLC brought this claim against, among others, the two other members of the Company, Joseph J. Krivulka ("Krivulka") and Leonard Mazur ("Mazur" and together with CelestialRX and Krivulka, the "Members") for improper self-dealing transactions. Plaintiffs alleged that Krivulka improperly inserted entities that he controlled or had an investment in as middlemen (the "Middlemen Entities") between the Company and other companies with whom the Company did business. By acting as middlemen, the Middlemen Entities received a percentage of the sales and marketing revenue of the Company. In 2013, certain of the Middlemen Entities informed the Company that the Company's rights to sell and distribute certain drugs were being terminated under various agreements between the Middlemen Entities and the Company, which caused a dispute to arise among the Members. After CelestialRX and Mazur threatened to bring suit against Krivulka and the Middlemen Entities, the parties entered into a settlement agreement (the "Settlement Agreement") in which the Middlemen Entities agreed not to terminate the Company's rights to sell and distribute certain drugs in exchange for additional royalty fees. Additionally, a release agreement (the "Release Agreement") was signed in connection with the Settlement Agreement that included a general release in which Laumas released all of his claims against Krivulka and Mazur. In addition to the Settlement Agreement, the Members entered into an amendment (the "Amendment") to the LLC Agreement of the Company (the "Company Agreement") that amended the applicable fiduciary duty standard and also named Krivulka the manager of the Company. Subsequently, the Company defaulted on its payment obligations under the Settlement Agreement and, as a result, the Company's rights to sell and distribute drugs reverted back to the Middlemen Entities.

In this opinion, the court addressed defendants' motion for partial summary judgement. First, defendants asserted that the Release Agreement, which was signed by Laumas in his individual capacity, released the claims that CelestialRX brought in this action because Laumas was the sole member of CelestialRX. The "Parties" in the Release Agreement were defined as Krivulka, Laumas and Mazur. The Release Agreement defined the "Releasing Parties" as Krivulka, Laumas and Mazur "and their past, present and future agents, employees, representatives, attorneys, estates, and assigns . . . ." The

court held that CelestialRX was not a Releasing Party under the terms of the Release Agreement and thus denied defendants' request for summary judgment that CelestialRX's claims were released in the Release Agreement.

The court then examined the fiduciary duty standard applicable to conflicted transactions under the Company Agreement, as modified by the Amendment. Defendants argued that the Amendment eliminated all fiduciary duties. Alternatively, defendants argued that Sections 8.01 and 8.02 of the Company Agreement expressly provided for contractual standards that supplanted any fiduciary duties that might apply with respect to conflicted transactions and corporate opportunities. The court began its review of the applicable fiduciary duty standard by examining the effect of the Amendment. The court noted that under the Delaware LLC Act, a manager has implied fiduciary duties unless otherwise provided in the limited liability company agreement. The court continued by stating that to waive fiduciary duties in a limited liability company agreement, the waiver must be clear and unambiguous. The Amendment amended Section 4.01(h) of the Company Agreement to provide that the Manager and the members of the Board of the Directors of the Company did not have any fiduciary duties to the Company or the Members and would not be personally liable for any breach "that [did] not involve (i) an act or omission not in good faith or which involve[d] intentional misconduct or a knowing violation of law; or (ii) a transaction from which such Manager, a member of the Board of Directors, or Member derived an improper personal benefit." The court held that the plain language of Section 4.01(h) eliminated fiduciary duties except for "intentional or illegal misconduct and other bad faith actions, as well as for improper self-dealing." The court noted that the alleged conflicted transactions must be examined in light of Sections 8.01 and 8.02 of the Company Agreement because those provisions provided contractual standards specifically governing conflicted transactions and corporate opportunities.

Section 8.02 of the Company Agreement eliminated the corporate opportunity doctrine and allowed conflicted interests to be held by directors and the Members. Section 8.01(a) of the Company Agreement provided that unless entered into in bad faith, a conflicted party was not liable to the Company or any other person as a result of a conflicted transaction involving the Company and its Members or any "Indemnified Party" if the transaction was entered into in absence of bad faith and the Manager, in good faith, determined that the transaction was fair and reasonable to the Company. "Indemnified Party" was defined to include officers and affiliates. Section 8.01(b) set forth an alternative safe harbor for the same types of transactions described in Section 8.01(a) if the terms of the transaction were fair and reasonable to the Company or any Member and the conflicted party did not enter into the transaction in bad faith. In seeking a safe harbor under Section 8.01(b), the conflicted party must "resolve such conflict of interest, taking such action or providing such terms, considering in each case the relative interest of each party (including its own interest) to such conflict, agreement, transaction or situation and the benefits and burdens relating to such interests, any customary or acceptable industry practices, and any applicable generally acceptable accounting practices or principles." The court, after construing Section 4.01(h) and Sections 8.01 and 8.02 together, held that parties that entered into conflicted transactions that did not comply with the safe harbor requirements under Sections 8.01 and 8.02 may be shown to have derived an improper personal benefit under Section 4.01(h)(ii). Because the parties

did not argue that the Section 8.01(a) safe harbor applied, the court concluded that the challenged transactions entered into after the date of the Amendment should be evaluated under the following standard: "Defendants will be found not to have breached a duty under Section 4.01(h)(ii), and are insulated from liability under Section 8.01(b), where the conflicted transaction was (1) entered in good faith and (2) where the particular Defendant subjectively determined that the transaction was fair and reasonable to the Company and Members after the required good-faith balancing of interests."

3. *Dieckman v. Regency GP LP*, No. 208, 2016 (Del. Jan. 20, 2017) (J. Seitz)

Appeal was taken by plaintiffs below to the Court of Chancery's dismissal of plaintiff's complaint challenging a unit-for-unit merger between Regency Energy Partners LP ("Regency"), a Delaware MLP, and an affiliated MLP. Plaintiff, a Regency unitholder, argued below that Regency's general partner breached the good faith requirement of the Regency limited partnership agreement (the "Regency LPA") by favoring the interests of the general partner's affiliates to the detriment of Regency's unaffiliated unitholders by approving the merger while the trading price of Regency's common units was artificially depressed. Defendants below moved to dismiss plaintiff's complaint and argued that the affiliate merger was safeguarded from judicial review by operation of two safe harbor provisions set forth in the Regency LPA. The first safe harbor would be satisfied if a potentially conflicted transaction was approved by a majority of unaffiliated common units (the "Unaffiliated Unitholder Vote" safe harbor). The second safe harbor would be satisfied if a potentially conflicted transaction was approved by a conflicts committee (the "Special Approval" safe harbor). Plaintiff alleged that the Special Approval safe harbor was not satisfied because one member of the conflicts committee served on the board of an affiliate entity while serving on the conflicts committee. Plaintiff further alleged that the Unaffiliated Unitholder Vote safe harbor was not satisfied because a proxy statement issued by the general partner to the unitholders contained false and misleading statements relating to the independence of the conflicts committee. The Court of Chancery ruled in favor of defendants and reasoned that the affiliate merger was shielded from judicial review by operation of the Unaffiliated Unitholder Vote safe harbor because the Regency LPA waived all fiduciary duties and that the general partner of Regency complied with the express disclosure requirements of the Regency LPA (which merely required the disclosure of the merger agreement). The Court of Chancery did not address whether the affiliate merger was shielded by the Special Approval safe harbor because it found that the affiliate merger was protected by the Unaffiliated Unitholder Vote safe harbor.

The Delaware Supreme Court began its analysis by noting that when fiduciary duties are waived in a partnership agreement, investors must rely on the express language of a partnership agreement in order to determine the parties' rights and obligations. However, the court further noted that despite such a waiver of fiduciary duties, investors nevertheless have some protections. Among these protections, the court explained, included the doctrine of *contra proferentem* and the implied contractual covenant of good faith and fair dealing. The court further explained that the express terms of an MLP's partnership agreement may, in some circumstances, "be reasonably read to imply certain other conditions, or leave a gap, that would prescribe certain conduct" in order to uphold

the apparent intentions and reasonable expectations of the parties at the time of contracting.

Turning to the affiliate merger, the court held that the Court of Chancery should have focused on the reasonable meaning of the safe harbor provisions, rather than narrowly focusing on whether the disclosure provisions of the Regency LPA displaced the implied covenant. The court found that both safe harbor provisions contained an implicit requirement that the general partner of Regency not undermine the protections afforded unitholders in the safe harbor process. The court reasoned that drafters of a partnership agreement would not include "obvious and provocative" conditions in such an agreement (like "the General Partner will not mislead unitholders when seeking Unaffiliated Unitholder Approval" and "the General Partner will not subvert the Special Approval process by appointing conflicted members to the Conflicts Committee"). The court explained that such terms are implied because the parties must have intended them and excluded them only because they were too obvious to expressly include in the partnership agreement.

The court further noted that its use of the implied covenant was based on the language of the Regency LPA and not the waived fiduciary duties. The court held that once the general partner went beyond the express requirements of the Regency LPA by issuing a proxy statement, along with the merger agreement, in order to induce the unitholder approval, there was an implied obligation in the Unaffiliated Unitholder Vote safe harbor not to mislead the unitholders with false or misleading statements. Likewise, the court held that the Special Approval safe harbor contained an implicit condition that (i) the members of the conflicts committee must be genuinely unaffiliated and independent and (ii) the general partner must not use deceptive conduct to create the false appearance of an unaffiliated and independent conflicts committee. Accordingly, the court found that plaintiff pled facts raising sufficient doubt about the general partner's ability to use the safe harbor provisions and reversed the judgment of the Court of Chancery that dismissed Counts I and II of plaintiff's complaint.

4. *El Paso Pipeline GP Company, L.L.C. v. Brinckerhoff*, No. 103, 2016 (Del. Dec. 20, 2016) (en banc)

The Court of Chancery below found that the sole general partner (the "General Partner") of El Paso Pipeline Partners, L.P. (the "MLP") was liable for over $171 million for a dropdown transaction referred to by the court as the "Fall Dropdown". After plaintiff won at trial, the MLP was acquired in a merger. The Court of Chancery held that the plaintiff did not lose his standing to pursue his claim after the consummation of the merger, characterizing his claims either as derivative for purposes of claim initiation and as direct for purposes of claim termination or (if forced to choose a single characterization) as direct because the plaintiff proved that the General Partner breached a contract--the limited partnership agreement--to which the plaintiff was a party and the plaintiff was entitled to enforce the terms of that contract. The plaintiff appealed to the Supreme Court and the Supreme Court reversed, finding that the plaintiff's claims were not dual-natured or direct but rather that his claims "were and remain derivative in

nature" and thus his standing to pursue those claims was extinguished by the consummation of the merger.

In its opinion, the Supreme Court analyzed the two principal conclusions that the Court of Chancery formed (noted above) in the context of the ultimate question—whether plaintiff had standing to pursue his claims after the consummation of the merger.

In supporting its decision below, the Chancery Court distinguished this case from *Tooley v. Donaldson, Lufkin & Jenrette, Inc.*, 845 A.2d 1031 (Del. 2004), noting by reference to *NAF Holdings LLC v. Li & Fung (Trading) Ltd.*, 118 A.3d 175 (Del. 2015), that *Tooley* does not apply to contract rights and that limited partners can sue directly to enforce contractual provisions of limited partnership agreements. The Supreme Court stated that the Chancery Court interpreted the *NAF Holdings* case too broadly. The Supreme Court noted that "*NAF Holdings* does not support the proposition that any claim sounding in contract is direct by default, irrespective of *Tooley*" because such a reading would essentially abrogate *Tooley* for cases involving alternative entities, which are "creatures of contract."

Because plaintiff's claims sounded in breach of a contractual duty owed to the MLP, the Supreme Court proceeded to apply the two prongs of *Tooley* – specifically, (1) who suffered the alleged harm and (2) who would receive the benefit of the recovery or other remedy? With respect to the first prong, the Supreme Court noted that plaintiff's complaint alleged that the MLP was injured because the MLP paid too much in the Fall Dropdown and that such a claim is typically viewed as causing harm to the entity itself and therefore is regarded as derivative in nature. The Supreme Court also noted that plaintiff presented evidence of harm only to the MLP, not to the individual unitholders. The Supreme Court found the analysis in *Gerber v. EPE Holdings, LLC*, 2013 WL 209568 (Del. Ch. Jan. 18, 2013), persuasive, stating that the plaintiff in this case, like in *Gerber*, asserted an overpayment claim that resulted in harm to the partnership in the form of loss in the entity's overall value. The *Gerber* court declined to distinguish *Tooley* even though the plaintiff in *Gerber* had contractual claims, noting that such claims would be considered direct if the limited partners' contractual rights were "independent" of the partnership's rights. The Supreme Court found that the contract right that plaintiff asserted in this case "was not separate and distinct from the rights of the entity. The 'best interests of the Partnership' standard provided 'no separation' between the Partnership's contractual rights and any rights of the limited partners." The Supreme Court refused to expand the "universe of claims" that a plaintiff may assert dually and found that, under the first prong of *Tooley*, plaintiff's claim was derivative.

In applying the second prong of *Tooley*, the Supreme Court found that the benefit of recovery flowed to the MLP, which the Chancery Court recognized in its opinions below and which was evidenced by the necessity of the *pro rata* recovery that the Chancery Court awarded to unitholders of the MLP. The Supreme Court was unpersuaded by the Chancery Court's reliance on cases involving insider stock transfers and stock dilution because plaintiff did not claim that the Fall Dropdown either affected his voting rights or the parent's control of the MLP. Thus, under the second prong of *Tooley*, plaintiff's claim was derivative.

The Supreme Court applied the continuous ownership requirement set forth in *Lewis v. Anderson*, 477 A.2d 1040 (Del. 1984), and found that plaintiff's claims were an asset of the MLP that passed by operation of law to the surviving entity in the merger, thus extinguishing plaintiff's standing to assert his claims. The Supreme Court also dismissed plaintiff's cross-appeal challenging the so-called "Spring Dropdown", noting that the same reasoning outlined in this opinion applied.

Chief Justice Strine authored a concurring opinion to express his view that *Gentile v. Rossette*, 906 A.2d 91 (Del. 2006), a "dual-natured claims" case, should be overruled.

5. *Employees Retirement System of the City of St. Louis v. TC Pipelines GP, Inc.*, C.A. No. 291, 2016 (Del. Dec. 19, 2016) (ORDER).

   The appellants challenged the Chancery Court's May 11, 2016 decision, wherein the Chancery Court found that the existence of special approval precluded judicial scrutiny of the substance of the challenged drop-down transaction. The Supreme Court agreed that the appellant "could not escape the conclusive effect given to Conflicts Committee approval solely by attacking the fairness of the underlying transaction" and in this order affirmed the judgment of the Chancery Court.

6. *In re Arctic Ease, LLC*, C.A. No. 8932–VCMR (Del. Ch. Dec. 9, 2016) (V.C. Montgomery-Reeves)

   In a dissolution action, certain limited liability company members filed third-party complaints against another limited liability company member and some of its owners and affiliates which alleged breach of fiduciary duty, misrepresentation, fraud, and related claims. The allegations contained in the third-party complaint focused on the conduct of William Cohen. Cohen was a member of the Board of Directors of Summetria, LLC, a Delaware limited liability company ("Summetria"), and a member of Costar Partners, LLC, a New Jersey limited liability company ("Costar"), which owned 20 percent of Summetria's equity. Forden Holdings, Inc., WCFOTM, Inc., BC Parent, LLC, and Arctic Advisors, LLC (collectively, the "Forden Entities") owned 60 percent of the equity of Summetria and Bruce Heck, Eileen Nigro, Eileen Slawek, and Joseph Slawek (collectively, the "Heck Parties") together owned the remaining 20 percent of Summetria's equity. Summetria owned 100 percent of Arctic Ease, LLC, a Delaware limited liability company ("Arctic Ease").

   In 2012, Cohen provided a $1 million loan to Summetria (the "Cohen Note"), and shortly thereafter agreed to provide an additional $250,000 of principal to Summetria. In early 2013, Arctic Ease remained in need of capital and Cohen allegedly negotiated bridge financing for Arctic Ease through CSG Re Partners, LLC ("CSG"). However, Cohen ultimately would not agree to the bridge financing through CSG after they insisted that Cohen guarantee any bridge financing that they would arrange. Later in 2013, Cohen resigned from the Summetria board of directors and notified Summetria of its default on the Cohen Note. Summetria and Arctic Ease then defaulted on other secured loans and their assets were purchased at a foreclosure sale by Gawi, LLC, a New Jersey limited liability company controlled by Cohen ("Gawi"). In relation to these transactions, the

Forden Entities and the Heck Parties asserted claims against Cohen for breach of fiduciary duty, fraud, misrepresentation and other related claims. Cohen moved to dismiss the complaint for lack of personal jurisdiction. The Heck Parties and Forden Entities opposed the motion and alleged that the court had personal jurisdiction over Cohen under the Delaware Limited Liability Company Act (the "LLC Act").

The court looked to the LLC Act's implied consent provision in 6 *Del. C.* § 18-109 to determine whether the court could exercise personal jurisdiction over Cohen. Section 18-109 allows a Delaware court to exercise personal jurisdiction over parties who manage Delaware limited liability companies in actions "involving or relating to the business" of the company. The court noted that Section 18-109(a) describes two different types of "managers" for personal jurisdiction purposes under the statute: (i) managers as defined in the operative limited liability company agreement and (ii) parties who "participate materially in the management" of a Delaware limited liability company. The court held that a Delaware court could not exercise personal jurisdiction over Cohen under Section 18-109(a) because he was not a manager of Summetria under either definition provided in the statute.

The Forden Entities and the Heck Parties argued that Cohen was a manager of Summetria under Section 18-109(a)(i) because, as a member of the Summetria board of directors, he possessed voting power. The court rejected this argument based on the specific terms of the Summetria LLC Agreement, which made clear that Forden was the sole manager of Summetria and did not grant any management authority to the board of directors, other than the authority to set board members' compensation. The court held that under the terms of the Summetria LLC Agreement, Cohen could not be considered a manager under Section 18-109(a)(i) because Forden exclusively, and not the Summetria board of directors as a whole, had the authority to manage the business and affairs of Summetria.

The Forden Entities and Heck Parties also argued that a Delaware court could exercise personal jurisdiction over Cohen under Section 18-109(a)(ii) because Cohen materially participated in the management of Summetria. In support, the third-party plaintiffs provided evidence that Cohen negotiated a distribution agreement for Arctic Ease, conveyed information to Summetria members about Summetria's finances, attempted to arrange bridge financing for Arctic Ease and discussed Arctic Ease products with potential medical distributers in Indonesia, Japan, and Korea. The court held that these activities did not show a "control or decision-making role" which the court in *Wakely Ltd. v. Ensotran, LLC*, 2014 WL 1116968, at *5 (D. Del. Mar. 18, 2014) held was required for material participation under Section 18-109(a)(ii). The court found Cohen's conduct to be similar to that alleged in *Wakely*, and because Cohen's power was subject to Forden's authority under the Summetria LLC Agreement, he lacked the requisite control or decision-making role required to show material participation in the management of Summetria under Section 18-109(a)(ii).

7. *Gomes v. Karnell*, C.A. No. 11814–VCMR (Del. Ch. Nov. 30, 2016) (V.C. Montgomery-Reeves)

Plaintiff and defendants were members of two Delaware limited liability companies, PTT Capital, LLC ("PTT") and Montext, LLC ("Montext"). Plaintiff sued defendants for breach of fiduciary duty, breach of the PTT LLC Agreement, waste and aiding and abetting a breach of fiduciary duty. Plaintiff also sought judicial dissolution of PTT and the appointment of a liquidating trustee of PTT for purpose of selling PTT's assets. Defendants moved to dismiss plaintiff's claims for lack of subject matter jurisdiction, contending that the parties had agreed to arbitrate the matters at issue.

The court held that the agreement among the parties to arbitrate their disputes was enforceable and granted defendants' motion to dismiss the fiduciary duty, breach of PTT LLC Agreement, waste and aiding and abetting claims. With respect to the claims for judicial dissolution and appointment of a liquidating trustee, defendants agreed with plaintiff that the court should make the ultimate determination on those claims and therefore the court stayed those claims pending the results of the arbitration.

In the course of its analysis, the court rejected plaintiff's claim that the arbitration agreement must be incorporated by reference into the PTT LLC Agreement, or the PTT LLC Agreement must be incorporated by reference into the arbitration agreement, in order for the arbitration agreement to be binding with respect to disputes under the PTT LLC Agreement. The court noted that the PTT LLC Agreement did not mention arbitration and the PTT LLC Agreement was in existence long before the arbitration agreement was allegedly executed and thus held that the PTT LLC Agreement did not prohibit the parties from entering into the arbitration agreement to govern their disputes.

8. *Trascent Mgmt. Consulting, LLC v. Bouri*, C.A. No. 10915-VCM (Del. Nov. 28, 2016) (*en banc*)

The defendant in a Court of Chancery summary proceeding, Trascent Management Consulting, LLC ("Trascent"), appealed to the Delaware Supreme Court following the Court of Chancery's ruling granting a request by the plaintiff, George Bouri ("Bouri"), for indemnification advancement. Bouri, who was a former executive officer and manager of Trascent, sought advancement in accordance with the plain terms of both his employment agreement and Trascent's LLC agreement. Trascent argued that the Court of Chancery erred in enforcing the plain language of the agreements without first adjudicating Trascent's claim that the agreements were induced by fraud and, therefore, unenforceable.

Relying on authority that included *Homestore v. Tafeen* and *De Lucca v. KKAT Mgmt.*, the Court of Chancery based its decision on the plain language of the agreements and refused to examine Trascent's fraud claim on the basis that it was "identical to what is properly a plenary claim and beyond the narrow scope of a summary advancement proceeding." The Court of Chancery reasoned that sanctioning a defense of this nature would undermine the purpose for providing a summary proceeding for advancement cases by allowing entities to employ key officers and directors under a promise of

advancement, and then seek to escape or delay that obligation by injecting into the summary proceeding a plenary claim that the underlying contract was induced by fraud. The court also noted its concern that permitting this defense would subsequently "encourage any employer offering advancement at the outset of the employment relationship to turn around and add a fraud in the inducement claim to a dispute" to avoid its obligation and deny a party's right to advancement at the very time it is needed most. Accordingly, the Court of Chancery held that Trascent's allegations regarding Bouri's conduct were not properly raised in the summary proceeding and, although they could be raised in a separate plenary action, they would not be considered in the summary proceeding. On appeal, the Supreme Court upheld the Court of Chancery's decision, asserting that the determination not to delay enforcing the plain language of the agreements was well reasoned and wholly consistent with Delaware's public policy in favor of indemnification and advancement.

9. *Abelmann v. Granum*, C.A. No. 12041–VCMR (Del. Ch. Nov. 15, 2016) (V.C. Montgomery-Reeves)

Plaintiffs, who were members and managers of NAP Partners, LLC (the "Company"), filed a petition for judicial dissolution under LLC Act Section 18-802 on the grounds that the Company was deadlocked and unable to fulfill its defined purpose. Defendants agreed that the Company should be judicially dissolved but requested that the court use its equitable powers to delay dissolution to avoid a potentially prejudicial effect on pending California civil litigation involving the Company. Defendants' primary concern was that dissolution of the Company could give rise to issues of standing and mootness in the California action. In an attempt to alleviate defendants' fear of such prejudice, plaintiffs submitted that they would agree to a dissolution order that prohibited plaintiffs from using the dissolution of the Company as a defense or as a means of challenging defendants' standing in the California litigation. Defendants agreed they would not use the dissolution as a sword in the California action. The court granted the petition for judicial dissolution, subject to the limitations agreed to by the parties.

10. *Finger Lakes Capital Partners, LLC v. Honeoye Lake Acquisition, LLC*, C.A. No. 9742-VCL (Del. Ch. Oct. 26, 2015), *aff'd in part, rev'd in part* No. 42, 2016 (Del. Nov. 14, 2016) (*en banc*)

This case involved whether a special purpose entity's operating agreement superseded prior agreements between the parties. Zubin Mehta ("Mehta") and Gregory Shalov ("Shalov") created an asset management firm in 2003 called Finger Lakes Capital Partners, LLC ("Finger Lakes"). Finger Lakes' main capital provider was Lyrical Partners, L.P. ("Lyrical") through defendant Lyrical Opportunity Partners, L.P. After Finger Lakes' portfolio companies performed poorly, Lyrical exercised its contractual rights to take control of the portfolio companies. Subsequently, one of the portfolio companies, Revolabs, Inc. ("Revolabs"), was successfully sold. Finger Lakes and Lyrical bickered over how to distribute the proceeds. As a result of this dispute, Finger Lakes filed this action to compel Lyrical to distribute the Revolabs sale proceeds in accordance with Revolabs' Operating Agreement (the "Operating Agreement").

In addition to the Operating Agreement, Finger Lakes' and Lyrical's relationship was also governed by a term sheet between the principal of Lyrical, Jeffrey Keswin, Mehta and Shalov (the "Term Sheet") and a clawback agreement between Lyrical and Finger Lakes (the "Clawback Agreement"). The Term Sheet provided that Lyrical had a 25% interest in Finger Lakes and a right to a portion of the management fees earned by Finger Lakes. The Clawback Agreement provided that Lyrical would recoup any losses from its investments in Finger Lakes' portfolio companies before Mehta and Shalov received their appropriate distribution. The main issue in this case was whether the Operating Agreement superseded the Term Sheet and the Clawback Agreement. Finger Lakes argued that as a result of the Operating Agreement's integration clause, the Operating Agreement superseded the Term Sheet and the Clawback Agreement—thus Finger Lakes was not bound by the Term Sheet and the Clawback Agreement. The integration clause stated that the agreement superseded all prior agreements "with respect to the subject matter hereof." The court held that the "subject matter hereof" was the investment in Revolabs and that "[a]s with all of the special purpose vehicles, the scope of the governing agreement did not extend to the ongoing business relationship between Finger Lakes and Lyrical." With respect to the Term Sheet, the court noted that Mehta and Shalov abided by the Term Sheet in their interactions with Lyrical. In addition, the court stated that it was never the intent of Mehta and Shalov to supersede the Term Sheet because Finger Lakes obtained its capital from Lyrical through the Term Sheet and superseding the Term Sheet would have gone against their own interest. In regard to the Clawback Agreement, the court noted that the Operating Agreement only discussed how to distribute proceeds to the members of Revolabs. Therefore, the court held that the Operating Agreement did not supersede the Term Sheet and the Clawback Agreement.

As a secondary issue, Finger Lakes attempted to recover all fees and expenses incurred in litigating this matter before the proceeds of the sale were distributed. Pursuant to the Operating Agreement, Revolabs would indemnify Finger Lakes for all fees and expenses incurred in matters it became involved in because it was a member of Revolabs. The court noted that Finger Lakes was entitled to indemnification even though it is a plaintiff because there was no restriction in the Operating Agreement limiting indemnification to defendants. However, the court restricted the amount that Finger Lakes received to the legal fees and expenses incurred for the "portion of the action [that] involved Finger Lakes' status as a member and its efforts to compel a distribution in that capacity." For the part of the case that pertained to the "implications of the Term Sheet and the Clawback Agreement," the court denied Finger Lakes request for indemnification because "[t]hose agreements did not govern Finger Lakes' rights as a member of Revolabs."

Finger Lakes appealed the Court of Chancery's post-trial decision to the Delaware Supreme Court, arguing that the Operating Agreement superseded the Term Sheet and the Clawback Agreement and that even if the Clawback Agreement was not superseded, the Court of Chancery applied it incorrectly. In addition, Finger Lakes argued that Lyrical could not recover its unpaid management fees through setoff or recoupment and that the Court of Chancery improperly limited Finger Lakes' indemnification to expenses incurred until Finger Lakes was awarded a partial judgment on the pleadings rather than awarding indemnification for all expenses related to those proceedings. The Supreme

Court affirmed the Court of Chancery's holding that the Operating Agreement did not supersede the Term Sheet or the Clawback Agreement and affirmed the Court of Chancery's holding denying Finger Lakes indemnification for the part of the case that pertained to the implications of the Term Sheet and the Clawback Agreement.

The Supreme Court, however, reversed the Court of Chancery's holding that Lyrical could use the doctrine of setoff or recoupment to recover time-barred management fees from amounts otherwise payable to Finger Lakes. In the Chancery Court action, Lyrical had filed a counterclaim seeking its share of management fees, including those that were due more than three years before the filing of the claim and therefore barred by the statute of limitations. The Court of Chancery rejected Finger Lakes' argument that laches barred recovery of these earlier amounts, holding that the statute of limitations did not apply to the affirmative defenses of recoupment and setoff. The Supreme Court held that 10 *Del. C.* § 8120 precluded setoff for amounts owed outside the statute of limitations and that Lyrical could not assert its time-barred claims by way of recoupment because the defensive claims did not arise from the same transaction as Finger Lakes' claims. The Supreme Court stated that while setoff is clearly subject to a three year statute of limitations, time-barred claims can be considered for recoupment when they arise out of the same factually-related transaction as plaintiff's claim. The court found that Lyrical's claims to use the earlier amounts owed to it arising from the management of multiple portfolio companies as a defense to Finger Lakes' claim for a distribution of the proceeds from the sale of Revolabs were not factually related and therefore could not be considered for recoupment.

11. *Grand Acquisition, LLC v. Passco Indian Springs DST*, C.A. No. 12003–VCMR (Del. Ch. Sept. 7, 2016) (V.C. Montgomery-Reeves)

Plaintiff, Grand Acquisition LLC, a beneficial owner of Passco Indian Springs DST, a Delaware statutory trust ("Passco"), sought to inspect certain of Passco's books and records. Plaintiff sent Passco a letter demanding to inspect and make copies of the current list of Passco's beneficial owners, their contact information, and their respective ownership interests in the Trust. Plaintiff brought its request under both Section 5.3(c) of Passco's trust agreement (the "Trust Agreement") and Section 3819 of the Delaware Statutory Trust Act (the "DTA"). Section 5.3 of the Trust Agreement expressly entitled the owners to "inspect, examine and copy the Trust's books and records," subject only to the condition that such inspection, examination, and copying be done "during normal business hours." Passco denied plaintiff's request on the basis that Section 3819 of the DTA required plaintiff to provide a reasonable basis for the release of that information and plaintiff had not done so.

The issue before the court was whether the owners' contractual right to Passco's books and records under Section 5.3(c) of the Trust Agreement was subject to Section 3819's preconditions and defenses. Passco argued that the Trust Agreement must affirmatively disavow Section 3819's preconditions and defenses for them not to apply, and since the Trust Agreement was silent, Section 3819 must still apply to plaintiff's books and records demand. Plaintiff argued that the Trust Agreement's books and records provision

eliminated the statutory "reasonable basis" requirement regarding a books and records demand under Section 3819.

Plaintiff and defendant asserted cross-motions for summary judgment. The court granted plaintiff's motion for summary judgment and found that plaintiff was entitled to the requested information under Section 5.3(c) of the Trust Agreement. Specifically, the court held that a beneficial owner's contractual right to Passco's books and records under Section 5.3(c) was not subject to Section 3819's preconditions and defenses. The court applied case law involving limited liability companies and limited partnerships to the Delaware statutory trust context. This case law indicated that providing an entity's owners with an unconditional contractual right to inspect that entity's books and records has the impact of rendering the relevant statutory preconditions and defenses inapplicable to that independent contractual right. The court found that because Section 5.3(c) expressly entitled the owners to "inspect, examine and copy the Trust's books and records," subject only to the condition that such inspection, examination, and copying be done "during normal business hours," the Trust Agreement therefore granted the owners an unconditional right to inspect Passco's books and records because Section 5.3(c) did not expressly include Section 3819's preconditions and defenses.

Passco argued that even if Section 3819 did not apply, plaintiff was still not entitled to the requested information because it did not constitute "books and records" under Section 5.3(c) of Passco's trust agreement. The court held that plaintiff's contractual inspection right under the trust agreement included the requested information. Section 5.3(c) provided that "books and records" should be defined by their "customary meaning." The court found that a Delaware statutory trust's customary books and records include the requested information, referencing Section 3819's express inclusion in the list of books and records to which a beneficial owner is entitled of "[a] current list of the name and last known business, residence or mailing address of each beneficial owner and trustee."

In addition, Passco argued that the "improper purpose defense" developed in limited liability company and limited partnership case law regarding contractual inspection rights should apply with respect to statutory trusts and that, by reason of such defense, plaintiff's inspection request should be denied. The court declined to decide whether the "improper purpose defense" applies in this case, but held that even if it did, Passco would not have prevailed. The court stated that to apply the "improper purpose defense," Passco would have to prove that no provision in the Trust Agreement explicitly negated the proper purpose requirement, that plaintiff sough the requested information for a personal purpose and that granting plaintiff the right to inspect the requested information actually would be adverse to Passco's interests. Passco alleged that plaintiff was seeking the requested information for the purpose of being disruptive and causing stress in order to make financial gains at the expense of others. The court held that Passco failed to prove by a preponderance of the evidence that plaintiff's inspection request would adversely affect Passco in an economic sense.

12. *Bizzari v. Suburban Waste Servs., Inc.*, C.A. No. 10709-JL (Del. Ch. Aug. 30, 2016) (J. LeGrow)

Plaintiff was the founder of Suburban Waste Services of Delaware, Inc., a Delaware corporation ("Suburban Waste of DE") and Felt Properties, LLC, a Delaware limited liability company ("Felt" and together with Suburban Waste of DE, "Suburban Waste"), both of which operated in the waste management industry. Plaintiff owned one-third of Suburban Waste, with the other two-thirds being owned by plaintiff's wife and plaintiff's business partner. Plaintiff was also a manager of Felt and director of Suburban Waste of DE. After a falling out with the management and staff of Suburban Waste and discovering that his wife and business partner were having an affair, plaintiff began working for his father's waste management company, which directly competed with Suburban Waste. Plaintiff subsequently sent a letter to Suburban Waste demanding inspection of the companies' books and records. Plaintiff indicated the purpose of the inspection demand was, among other reasons, to value his interest in each company and investigate possible wrongdoing and mismanagement. When the companies resisted, plaintiff brought the instant books and records action. After post-trial briefing and argument, the court issued a memorandum opinion granting plaintiff limited inspection rights but denying the majority of his requested relief.

The court began its analysis by noting that the standard governing inspection rights depended on plaintiff's capacity. Thus, the court analyzed plaintiff's inspection rights as a stockholder/member separately from his inspection rights as a director/manager. The court began its stockholder/member analysis by noting that it would not draw any distinction between plaintiff's inspection rights as a stockholder as opposed to his rights as a member, given that the parties had not drawn any distinction between the inspection rights plaintiff may have as a stockholder as opposed to a member and that the court has treated Section 220 of the DGCL and the cases interpreting it as the corporate analogue for Section 18-305 of the LLC Act. Accordingly, the court recited the corporate rule that a stockholder may inspect books and records if the demand complies with the statutory form and manner requirements and the stockholder states a proper purpose. The court then addressed plaintiff's two purported purposes for demanding inspection as a member/stockholder: (i) to investigate potential mismanagement or wrongdoing and (ii) to value his interest in Suburban Waste.

Regarding the first purported purpose, the court noted that plaintiff did not state a proper purpose by simply reciting "mismanagement and wrongdoing" without more detail. The court noted that a stockholder must proffer some evidence to suggest a credible basis from which the court may infer that possible mismanagement, waste or wrongdoing has occurred. The court disagreed with plaintiff's contention that he met the credible basis standard by introducing evidence that (i) the other two principals sought to remove him as director and manager, (ii) the other two principals sold company assets despite needing his consent and (iii) the companies' accounts payable increased substantially in the past year, thus inferring potential mismanagement. The court noted that in regard to the first two allegations, plaintiff filed a separate action for breach of fiduciary duty that was still pending in the Court of Chancery (the "Plenary Action"). Accordingly, the court held that the availability of discovery in the Plenary Action undermined plaintiff's need to

investigate mismanagement through an inspection demand. The court then held that the remaining allegation, the increase in accounts payable, was not by itself sufficient evidence from which the court may infer possible mismanagement or wrongdoing. Thus, the court concluded that plaintiff failed to meet the credible basis burden to investigate possible mismanagement or wrongdoing.

Regarding the second purported purpose, the court noted that minority stockholders of privately held corporations face unique risks because they do not receive mandated, periodic disclosures associated with a publicly held corporation. The court also noted that defendants conceded that plaintiff's valuation purpose was proper and that plaintiff was entitled to inspect books and records to value his interest in Suburban Waste. Thus, the court held that plaintiff established the need to inspect various high-level financial documents. However, the court refused to grant plaintiff access to detailed financial data because plaintiff failed to articulate why he needed that information to value his interests. Furthermore, the court noted that evidence of plaintiff's conflicting motives and past conduct left the court with serious doubts regarding whether plaintiff sought inspection rights to value his interests or "to further his vendetta" against his wife and former business partner. Accordingly, the court conditioned plaintiff's limited inspection rights on his agreement to abide by a court-ordered confidentiality order.

The court then turned its analysis to plaintiff's inspection rights in his capacity as a director/manager of Suburban Waste. The court noted that there is a strong presumption under Delaware law that a director is entitled to "unfettered access" to the books and records of the corporation to which he is a fiduciary. Accordingly, the court noted that Suburban Waste had the burden of establishing an improper motive for plaintiff's inspection as a director/manager of Suburban Waste. The court noted that based on the testimony presented at trial, plaintiff demonstrated a willingness to compete directly with Suburban Waste as a result of his "extreme anger and resentment" toward his wife and former business partner. Concluding that plaintiff's real purpose was to either damage Suburban Waste or hold Suburban Waste hostage in order to leverage a desirable settlement regarding the companies' future, the court held that permitting inspection would enable plaintiff to breach his fiduciary duties, rather than uphold them. Accordingly, the court held that Suburban Waste carried its burden in showing that plaintiff's purpose for inspecting the companies' books and records, other than its high-level financial information, was not reasonably related to his interests as a director/manager.

13. *Obeid v. Hogan*, C.A. No. 11900-VCL (Del. Ch. June 10, 2016) (V.C. Laster)

Plaintiff, a member and manager of two Delaware limited liability companies (the "LLCs"), Gemini Equity Partners, LLC (the "Corporate LLC") and Gemini Real Estate Advisors, LLC (the "Manager LLC"), sought a declaratory judgment that only a manager of an LLC could serve on a special litigation committee formed to assert control over derivative litigation brought on behalf of the LLCs.

Each LLC had three members, plaintiff and two of the individual defendants ("Defendants"). The members also acted as directors and managers for the LLCs. The

Corporate LLC's operating agreement contained governance provisions paralleling that of a corporation, e.g., a board of directors. The Manager LLC's operating agreement provided that the Manager LLC was managed by the managers.

As a result of a disagreement among the members, plaintiff and Defendants filed lawsuits against each other in multiple jurisdictions. In one of the actions, plaintiff sued Defendants directly and derivatively on behalf of the LLCs. While litigation was ongoing, plaintiff called a special meeting of the directors and managers of each LLC. At the meeting, Defendants voted in favor of creating a special litigation committee comprised solely of a retired judge, but no formal resolutions were adopted. Defendants proceeded to cause the LLCs to hire a retired judge to serve as the sole member of the special litigation committee. At a subsequent special meeting, Defendants voted in favor of removing plaintiff as a director of the Corporate LLC.

The court was asked to determine whether a non-director or non-manager could serve on the special litigation committee. Because the Corporate LLC substantially re-created the governance structure of a Delaware corporation, the court looked to corporate law analogies in making its determination. The court analyzed the special litigation committee question in the context of *Zapata v. Maldonado*, which held that a properly empowered committee of a corporate board can assert control over a derivative action. The court did not find any corporate precedent where a non-director served on a litigation committee and although Section 18-407 of the Delaware Limited Liability Company Act (the "Act") permits managers to delegate their power to non-managers, unless provided otherwise in the operating agreement, the court held that Sections 18-1001 and 18-1003 of the Act imply that only managers (or, if member-managed, members) are authorized to take control of a derivative action, consistent with the holding of *Zapata*. The court also found that the Corporate LLC's governance structure was sufficient evidence that the operating agreement "provided otherwise" for purposes of Section 18-407 delegation and therefore a non-director could not serve on the special litigation committee. The court came to the same result for the Manager LLC as follows. The court held that the Manager LLC's operating agreement provided the managers with a more limited set of powers, and therefore, the operating agreement "provided otherwise" for purposes of Section 18-407, meaning only a manager of the Manager LLC could serve on the special litigation committee. In addition, the court suggested that the Manager LLC, which was governed by the managers of the LLC, was enough of a corporate governance structure for Zapata to apply.

14. *Angus v. Ajio, LLC*, C.A. No. 11895-VCG (Del. Ch. May 13, 2016) (V.C. Glasscock)

This matter related to whether defendants, who were members of MoGo Sport, LLC (the "Company"), could rescind their vote to sell the Company after learning that plaintiff officers of the Company allegedly took an investment opportunity from the Company in violation of the Company's Operating Agreement (the "Operating Agreement"). Prior to this action, defendants filed a demand for arbitration pursuant to an arbitration provision in the Operating Agreement (the "Arbitration Provision"). The Arbitration Provision stated that "[a]ll disputes among Members or Former Members over the provisions of [the Operating Agreement] . . . shall be submitted to binding arbitration under the

guidelines of the American Arbitration Association." Defendants claimed in the arbitration demand that plaintiffs breached their fiduciary duties, committed fraud and violated the Operating Agreement. Plaintiffs filed a motion in the Court of Chancery to enjoin the arbitration, arguing that (i) three of the officers did not consent to arbitration because they are not parties to the Operating Agreement and (ii) the claims against Bruce Angus, a party to the Operating Agreement, did not fall under the scope of the Arbitration Provision.

The court enjoined the arbitration as it related to the three officers that were not signatories to the Operating Agreement because as non-signatories, they were not bound to arbitration. In regards to Angus, the court applied the Willie Gary test of arbitrability. Pursuant to *James & Jackson, LLC v. Willie Gary, LLC*, 906 A.2d 76 (Del. 2006), the court will presume that parties agreed to arbitrate issues of arbitrability if there is "clear and unmistakable evidence" of intent to arbitrate arbitrability. Such evidence exists when there is "(1) an arbitration clause that generally provides for arbitration of all disputes; and (2) a reference to a set of arbitration rules that empower arbitrators to decide arbitrability, such as the American Arbitration Association Rules." In *McLaughlin v. McCann*, 942 A.2d 616 (Del. Ch. 2008), the court stated that in addition to satisfying the two Willie Gary factors, the party desiring arbitration must have a "non-frivolous argument about substantive arbitrability to make before the arbitrator." The court held that there "was clear and unmistakable evidence" of the intent to arbitrate because the Arbitration Provision provided that all applicable disputes should be submitted to binding arbitration and such arbitration was subject to the American Arbitration Association Rules. Then, with respect to the additional McLaughlin factor, the court held that defendants raised at least one non-frivolous claim about substantive arbitrability. Plaintiffs claimed that defendants lacked standing to bring their claims because claims arising under the Operating Agreement must be pursued by the Company—not by members. The court rejected this argument, reasoning that "issues of standing by signatories to a contract to enforce breaches of that contract do not strike me as the kind of frivolous issues in regard to which the parties' agreement in favor of arbitration should be overridden." As a result, the court did not examine defendants' other arguments because defendants had presented at least one non-frivolous argument regarding substantive arbitrability. Therefore, the court denied plaintiffs' request to enjoin the arbitration with respect to the claims against Angus.

15. *Employees Retirement System of the City of St. Louis v. TC Pipelines GP, Inc.*, C.A. No. 11603-VCG (Del. Ch. May 11, 2016) (V.C. Glasscock)

Plaintiff, a unitholder in a master limited partnership (the "MLP"), challenged a conflicted dropdown transaction in which the parent of the MLP's general partner sold a pipeline asset to the MLP on grounds that the dropdown was not "fair and reasonable" to the MLP, which was the standard articulated in the MLP's limited partnership agreement (the "Partnership Agreement"). The Partnership Agreement provided that a conflicted transaction was conclusively deemed fair and reasonable if special approval (defined in the Partnership Agreement as approval by a majority of the members of the conflicts committee) was obtained and the material facts known to the general partner and its affiliates regarding the dropdown were disclosed to the conflicts committee.

The conflicts committee approved the dropdown and the plaintiff did not allege defects in the approval (i.e., a majority was lacking or material facts were not disclosed). Therefore, the court, applying the holding of the Delaware Supreme Court in *The Haynes Family Trust v. Kinder Morgan G.P., Inc.*, 2016 WL 912184 (Del. Mar. 10, 2016) (ORDER), found that the existence of special approval precluded judicial scrutiny of the substance of the transaction.

Plaintiff also alleged that the implied covenant required the conflicts committee to determine, in good faith, whether the dropdown was in the best interests of the MLP. The court refused to recognize a gap in the LPA that the implied covenant should fill – the LPA provided a specific standard (fair and reasonable to the MLP) and a way to satisfy that standard (special approval by a conflicts committee to whom material facts were disclosed). Therefore, the court did not need to look to the implied covenant to supply further terms to the LPA's contractual standard.

16. *Brinckerhoff v. Enbridge Energy Company, Inc.*, C.A. No. 11314-VCS (Del. Ch. April 29, 2016) (V.C. Slights)

Plaintiff, a unitholder in a master limited partnership (the "MLP"), challenged a conflicted transaction in which the parent ("Enbridge") of the MLP's general partner (the "GP") sold to the MLP Enbridge's interest in a pipeline joint venture, which Enbridge had acquired six years earlier from the MLP at a lower price, on grounds that the transaction was not "fair and reasonable" to the MLP, which was the standard articulated in the MLP's limited partnership agreement (the "Partnership Agreement"). The Partnership Agreement provided that the GP was authorized to approve a conflicted transaction if it determined that the transaction was fair and reasonable to the MLP, and in doing so, the GP was to consider comparable transactions to ensure that the terms were no less favorable than those available from unrelated third parties. Also the GP was only required to consider the interests of the MLP. The Partnership Agreement also limited the liability of the GP and its affiliates to decisions made in bad faith and provided a conclusive presumption of good faith when decisions were made in reliance on an advisor.

Plaintiff alleged that the transaction was unfair because (i) the interest was being resold to the MLP for $200 million more than the MLP had received for the interest six years earlier, (ii) Enbridge retained from the interest a valuable pipeline expansion right and (iii) as part of the transaction, the Partnership Agreement was amended to impose a special tax allocation on the unitholders, relieving Enbridge of a significant tax obligation. The court noted that had plaintiff's claims been analyzed under traditional fiduciary duty standards, they may have survived this motion to dismiss. The Partnership Agreement, however, was clear in its modification of fiduciary duties and in only permitting liability upon a showing of bad faith. Plaintiff failed to allege facts allowing an inference that defendants acted in bad faith when they approved the transaction and failed to rebut the conclusive presumption of good faith imparted by the Partnership Agreement.

Plaintiff also alleged that defendants breached the Partnership Agreement and the implied covenant of good faith and fair dealing when they permitted the special tax allocation and the corresponding amendment to the Partnership Agreement. The Partnership Agreement authorized the GP to issue additional units and fix allocations of items of income with respect to any new units. Plaintiff averred that the special tax allocation was actually a special allocation for federal income tax purposes governed by a separate provision of the Partnership Agreement that could not be accomplished if it would have a material adverse effect on unitholders. In rejecting this argument, the court found that if viewed in isolation the claim would have merit, but since the special tax allocation was an integral piece of the transaction and was considered by the financial advisor in giving its fairness opinion, the good faith standard applied. In order to be successful, plaintiff would have needed to plead not only a breach of the Partnership Agreement provisions relating to the issuance of new units and allocation of income but also that such breaches were committed in bad faith.

Finally, the court held that the comprehensive governance and approval scheme in the Partnership Agreement did not leave any gap to be filled and therefore dismissed all of plaintiff's implied covenant claims.

17. *The Joseph Penar Family Trust v. Adams*, C.A. No. 10441-VCG (Del. Ch. April 28, 2016) (V.C. Glasscock)

Plaintiffs were members of a Delaware limited liability company (the "LLC") that was created as a result of bankruptcy proceedings concerning two affiliated companies. Plaintiffs were former creditors of the bankrupt companies who became members of the LLC pursuant to a plan of reorganization approved by the bankruptcy court. The LLC was intended to be a liquidating entity that would manage the remaining assets and distribute proceeds from those assets to the LLC's members. Plaintiffs derivatively and directly challenged a transaction by which defendants, who were members of the board of managers of the LLC, allegedly transferred the LLC's assets to themselves or to affiliates for a manifestly inadequate price, which plaintiffs alleged constituted a breach of defendants' contractual duty to act in good faith. Defendants moved to dismiss plaintiffs' complaint for failure to state a claim.

The court granted defendants' motion to dismiss, holding that plaintiffs' complaint failed to allege sufficient facts to support their conclusory allegation that the disputed transaction was a breach of defendants' contractual duty to act in good faith. The facts that supported plaintiffs' allegations arose from voluntary disclosures made by defendants in the course of settlement negotiations. Plaintiffs did not include those facts in their complaint, contending at oral argument that they could not include those facts in the complaint because they had a professional responsibility not to use or otherwise disclose those facts because they were disclosed in aid of settlement. Referring to those unpled facts as the "Phantom Facts," the court noted that plaintiffs could have sought documents under Section 18-305 of the Delaware Limited Liability Company Act, which would have entitled them, as members of the LLC, to books and records relating to the disputed transaction, to develop facts for this type of litigation. Plaintiffs failed to seek information under Section 18-305, and the court found that there were insufficient facts

to support their direct and derivative claims against defendants. Accordingly, the court dismissed plaintiffs' complaint but suggested that another plaintiff could attempt to establish a sufficient factual basis for litigation on behalf of the members of the LLC.

18. *Hyatt v. Al Jazeera America Holdings II, LLC*, C.A. No. 11465-VCG (Del. Ch. Mar. 31, 2016) (V.C. Glasscock)

Plaintiffs, former officers and directors of Current Media, LLC, a Delaware limited liability company ("Current"), sought advancement of expenses from defendant, who acquired Current in a merger transaction and, in connection therewith, agreed to indemnify former officers and directors of Current for six years following the closing of the merger to the extent such individuals would have been entitled to indemnification under Current's LLC agreement.

Plaintiffs' advancement request arose in an unusual way—in an underlying action, they sued defendant in their capacities as members of Current and as the members' representative under the merger agreement seeking release of funds in an escrow account established by the merger agreement. Defendant counterclaimed, arguing that one plaintiff (the members' representative under the merger agreement) breached the merger agreement by denying release of the funds in the escrow account to indemnify defendant against alleged breaches of representations and warranties contained in the merger agreement. Defendant's allegations of breaches of representations and warranties under the merger agreement arose mainly from defendant's contention that plaintiffs—in their capacity as directors and officers of Current—breached various "most favored nations" provisions in Current's contracts and that Current represented in the merger agreement that it was in compliance with these "most favored nations" provisions. Plaintiffs desired to defend their actions as former directors and officers of Current to ensure that the funds in the escrow account were released to them. Thus, the question before the court was whether plaintiffs were entitled to advancement of expenses they incurred in defending themselves against defendant's counterclaims and in bringing this suit to enforce their alleged right to advancement under Current's LLC agreement (which obligations were assumed by defendant in the merger agreement).

Plaintiffs and defendant moved for summary judgment on the issue of whether plaintiffs were entitled to, and defendant was liable for, advancement. The parties requested that the court address only the issue of liability, and the court assented.

The merger agreement included both fee-shifting (which applied in the event of a challenge to a claim on funds from the escrow account), which the court interpreted as providing indemnification but not advancement, and indemnification of past and present officers and directors of Current to the same extent such persons were entitled to indemnification under the Current LLC agreement (which provided for both indemnification and advancement). Defendant asserted that, with respect to disputes regarding the escrow account—which it viewed this dispute as—only the fee-shifting and indemnification provisions under the merger agreement applied and, therefore, plaintiffs were not entitled to advancement. The court disagreed, noting that the application of

those provisions would depend on the capacity in which the person making the claim for indemnification or advancement was acting.

In analyzing the merger agreement's indemnification provision, the court reviewed the relevant provisions of Current's LLC agreement, which provided former officers and directors who were, are or threatened to be made a defendant to a proceeding the right to advancement "by reason of the fact" that such person was a director or officer of Current. The court determined based on the facts of this case that the parties intended that the interpretation of Section 145 of the DGCL, which uses the same "by reason of the fact" language, be applied to the interpretation of that language in Current's LLC agreement. The court stated that "by reason of the fact" meant that "a 'nexus or causal connection' existed between the underlying proceedings and the defendant's 'official corporate capacity'."

The court then turned to defendant's counterclaims and analyzed each in light of the "by reason of the fact" standard, finding that plaintiffs were entitled to advancement for expenses incurred in defending against four of the six counterclaims because the resolution of those counterclaims would mostly likely require plaintiffs to defend their actions as former officers and directors of Current.

19. *Dieckman v. Regency GP LP*, C.A. No. 11130-CB (Del. Ch. Mar. 29, 2016) (C. Bouchard)

This case involved a disputed unit-for-unit merger between a Delaware limited partnership and an affiliated entity. Regency Energy Partners LP ("Regency") was a publicly traded Delaware limited partnership in the natural gas business. The Regency limited partnership agreement (the "LPA") replaced all default fiduciary duties owed by the general partner with a contractual governance scheme that merely required the general partner to act in good faith. The LPA established four safe harbors for potentially conflicted transaction that, if satisfied, would cause the transaction to be deemed to be approved by all of Regency's limited partners and not a breach of the LPA or a breach of any express or implied duty in law or equity. The first relevant safe harbor would be satisfied if a potentially conflicted transaction was approved by a majority of unaffiliated common units. The second relevant safe harbor would be satisfied if a potentially conflicted transaction was approved by a conflicts committee. In this case, the affiliate merger was approved by a majority of Regency's unaffiliated common units. Plaintiff, a Regency unitholder, filed suit challenging the merger and alleged that Regency's general partner breached the LPA's good faith requirement by favoring the interests of the general partner's affiliates to the detriment of Regency's unaffiliated unitholders by approving the merger while the trading price of Regency's common units was artificially depressed. Defendants moved to dismiss plaintiff's complaint for failure to state a claim and argued that the merger was shielded from judicial review by operation of the two aforementioned safe harbor provisions in the LPA.

The Court of Chancery focused its analysis on the unitholder approval safe harbor, which it found to be dispositive in this case. The court noted that the language of the unitholder approval safe harbor provided that a conflicted transaction was shielded from judicial

review if the transaction was "approved by the vote of a majority of the Common Units (excluding Common Units owned by the General Partner and its Affiliates)." The court stated that because a majority of the unaffiliated common units approved the merger, the only remaining question was whether the shareholder vote was somehow ineffective. Plaintiff argued that vote was ineffective because the proxy statement failed to adequately disclose that one member of the conflicts committee was a board member of an affiliated entity or that two members of the conflicts committee would join an affiliated entity's board after the merger closed. The court rejected plaintiff's argument, finding that because the LPA eliminated all fiduciary duties, it would be inappropriate to include any common law duty of disclosure requirements as a condition to triggering the unitholder approval safe harbor. Rather, the court noted it was required to look only to the terms of the LPA to find what, if any, disclosure duties were contractually mandated. The court found the only disclosure requirement provided by the LPA was that a copy or summary of the merger agreement was to be enclosed with a notice of a special meeting or written consent. The court also found that the implied covenant of good faith and fair dealing did not create any additional disclosure obligations. The court stated that the LPA's express waiver of fiduciary duties and its clearly articulated single disclosure requirement prevented the implied covenant from adding additional disclosure obligations because doing so would contradict the explicit arrangements set forth in the LPA. Because the unitholder approval safe harbor was satisfied, the court reasoned that the merger was deemed approved by all of the limited partners, including plaintiff, and thus was shielded from a breach of contract claim by the LPA's own terms. The court noted that while its ruling "may seem harsh," it cautioned investors to carefully read alternative entity agreements to understand the limitations on their rights contained therein.

The court then addressed plaintiff's claim for breach of the implied covenant based on plaintiff's claims that two members of the conflicts committee were not independent. The court noted that to bring a claim for breach of the implied covenant, plaintiff would be required to show damages. Given that the unitholder approval safe harbor provided an independent basis to conclude that the merger did not constitute a breach of the LPA or any duty stated therein or implied by law or equity, the court ruled that plaintiff did not adequately allege an injury to sustain a claim for breach of the implied covenant relating to the conflicts committee safe harbor. Hence, the court dismissed plaintiff's claim for breach of the implied covenant.

The court also dismissed plaintiff's two remaining claims for aiding and abetting and tortious interference, reasoning that both claims failed due to the failure of the underlying breach of contract claims.

20. *CIM Urban Lending GP, LLC v. Cantor Commercial Real Estate Sponsor, L.P.*, C.A. No. 11060-VCN (Del. Ch. Feb. 26, 2016) (V.C. Noble)

This case involved a dispute between the limited partners and a general partner of Cantor Commercial Real Estate Company, L.P., a Delaware limited partnership (the "Partnership"). The Partnership was formed for the purpose of originating, purchasing and securitizing mortgage loans. The Second Amended and Restated Agreement of Limited Partnership of the Partnership (the "LPA") provided that Cantor Commercial

Real Estate Sponsor, L.P. (the "CF General Partner"), one of the Partnership's general partners, was authorized to retain its affiliates to provide, among other things, securities underwriting services to the Partnership, provided that compensation for such services must be at "competitive market rates charged by first-class unaffiliated service providers." The CF General Partner contracted with an affiliate to provide underwriting services to the Partnership at rates later characterized by plaintiffs as "blatantly improper." Plaintiffs filed suit individually and derivatively on behalf of the Partnership and alleged that defendant CF General Partner caused the Partnership to overpay its underwriting affiliate in violation of the LPA. In addition to the breach of contract claim, plaintiffs claimed (i) breaches of fiduciary duty by the CF General Partner, (ii) aiding and abetting such fiduciary breaches by the underwriting affiliates and (iii) unjust enrichment against the underwriting affiliates. This opinion addressed defendants motion to dismiss the latter three claims.

The court first analyzed plaintiffs' unjust enrichment claim. The court found that the unjust enrichment claim was based upon the same conduct as the breach of contract claim. The court noted that Delaware courts regularly reject claims for unjust enrichment arising from contractual relationships if the underlying conduct is the same. Moreover, the court reasoned that because there was a contractual standard involved, contractual remedies were the exclusive remedy, even though the underwriting affiliates were not parties to the LPA. Thus, the court dismissed the unjust enrichment claim against the underwriting affiliates.

The court then addressed the claims for breaches of fiduciary duty and aiding and abetting such breaches. Citing an earlier ruling in *Grayson v. Imagination Station, Inc.*, 2010 WL 3221951 (Del. Ch. Aug. 16, 2010), the court noted that generally, under Delaware law, allowing a fiduciary claim that is duplicative of a contract claim undermines the primacy of contract law over fiduciary law in matters involving contractual disputes. The court reasoned that Delaware law allows a duplicative fiduciary duty claim to proceed only if there is an independent basis for the fiduciary claim apart from the parallel contract claim. The court found that plaintiffs' fiduciary duty claims failed because the relief which they would obtain would be identical under the contract claim, and thus dismissed such claims as being duplicative of the breach of contract claim. Consequently, the court also dismissed plaintiffs' claims for aiding and abetting such fiduciary duty breaches because there could be no claim for aiding and abetting if there were no such breaches. Thus, the court granted defendants' motion to dismiss the aiding and abetting claim.

*   *   *

10831863.1