

IN THE COURT OF CHANCERY OF THE STATE OF DELAWARE

R&R CAPITAL, LLC, a New York limited liability company, and FTP CAPITAL, LLC, a New York limited liability company,

Petitioners,

v.

Civil Action No. 3803-CC

BUCK & DOE RUN VALLEY FARMS, LLC, a Delaware limited liability company, GRAYS FERRY PROPERTIES, LLC, a Delaware limited liability company, HOPE LAND, LLC, a Delaware limited liability company, MERRITT LAND, LLC, a Delaware limited liability company, UNIONVILLE LAND, LLC, a Delaware limited liability company, MOORE STREET, LLC, a Delaware limited liability company, PDF PROPERTIES, LLC, a Delaware limited liability company, PANDORA FARMS, LLC, a Delaware limited liability company, and PANDORA RACING, LLC, a Delaware limited liability company,

Respondents.

MEMORANDUM OPINION

Date Submitted: August 7, 2008

Date Decided: August 19, 2008

Richard P. Rollo and Scott W. Perkins, of RICHARDS, LAYTON & FINGER, P.A., Wilmington, DE; OF COUNSEL: Paul Sweeney, of HOGAN & HARTSON LLP, New York, New York, Attorneys for Petitioners.

John C. Phillips, Jr., Brian E. Farnan, and David A. Bilson, of PHILLIPS, GOLDMAN & SPENCE, P.A., Wilmington, Delaware, Attorneys for Respondents.

CHANDLER, Chancellor

For Shakespeare, it may have been the play, but for a Delaware limited liability company, *the contract's the thing*.¹ Ultimately, it is the contract that compels the Court's decision in this case because it is the contract that "defines the scope, structure, and personality of limited liability companies."² On June 2, 2008, two New York LLCs filed a petition with this Court seeking dissolution of nine separate Delaware LLCs. The respondent Delaware LLCs, some of which have had their certificates of formation canceled by the state pursuant to 6 *Del. C.* § 18-1108 for failure to pay their annual taxes, have moved to dismiss the petition. That motion is based primarily on two arguments. First, with respect to two of the respondent entities, the petitioners lack standing to seek dissolution because they are neither members nor managers. For reasons explained more fully below, I conclude that this argument is meritorious, but incomplete. Consequently, I grant respondent's motion to dismiss the claims against Pandora Farms, LLC and Pandora Racing, LLC pursuant to 6 *Del. C.* §§ 18-802 and 18-803, but cannot dismiss the claim pursuant to 6 *Del. C.* § 18-805. Second, with respect to the other respondent entities, of which the petitioners are members, the respondents argue that petitioners have waived their right to seek dissolution in the respective LLC Agreements. Again, for reasons explained at length below, I conclude that this

¹ Compare WILLIAM SHAKESPEARE, *HAMLET* act 1, sc. 2, ln. 604 ("the play's the thing"), with *TravelCenters of Am., LLC v. Brog*, C.A. No. 3516-CC, 2008 WL 1746987, at *1 (Del. Ch. Apr. 3, 2008) ("Limited Liability Companies are creatures of contract").

² *Fisk Ventures, LLC v. Segal*, C.A. No. 3017-CC, 2008 WL 1961156, at *1 (Del. Ch. May 7, 2008).

argument is meritorious and that Delaware's strong policy in favor of freedom of contract in the LLC Agreements requires such a result.

I. BACKGROUND

The factual background of this dispute is somewhat predictable; the procedural background, however, is a veritable nightmare. Generally, the respondent entities were formed years ago with capital contributions from the Russet brothers (presumably the Rs in R&R Capital) and Linda Merritt. The bulk of the capital (over \$9.7 million) was provided by the petitioners, but Merritt had the sole and exclusive power to manage the entities.³ These respondent entities own land and race horses. Unfortunately, the relationship between the financiers, the Russets, and their appointed manager, Merritt, has deteriorated, and, perhaps predictably,⁴ the parties have turned to the courts.

The courts the parties have turned to, however, seemingly span the eastern seaboard. In addition to the present case, there are related proceedings in the state court in Chester County, Pennsylvania, in the federal district court in the Eastern District of Pennsylvania in Philadelphia, and in the Civil Division of the New York County Supreme Court in New York. The procedural details of those other cases are irrelevant to the pending motion to dismiss, but the existence of those other

³ Petition at ¶ 1.

⁴ Justice Charles E. Ramos, before whom many of these parties are presently litigating in New York, sagely noted that race horses are a “[g]reat way to lose money.” See Transcript of Oral Argument at 6, *R&R Capital v. Merritt*, No. 604080 (N.Y. Sup. Ct. July 29, 2008).

cases has made this action a minefield in terms of comity and concerns of issue and claim preclusion.

The June 2 petition for dissolution seeks, in the alternative, the winding up and dissolution of the respondent entities or the appointment of a receiver. The petitioners allege that most of the respondent entities have had their certificates of formation canceled for failing to designate a registered agent, for failing to pay annual taxes, or for both. They further allege that Merritt’s attempts to revive the cancelled certificates are ineffective as a matter of law,⁵ that Merritt has refused to provide an accounting of the canceled entities,⁶ and that Merritt—along with her “longtime boyfriend” Leonard Pelullo—has defrauded the entities and orchestrated self-dealing transactions.⁷ Neither Merritt nor Pelullo, however, is a party to this action.

On June 12, 2008, shortly after the petition was filed, the Court entered a status quo order to preserve the respondents’ assets in case the Court ultimately ordered dissolution. Since that time, each side has sought modification of the status quo order, and the respondents have moved to dismiss the petition. Briefing on the motion to dismiss was completed on August 4, 2008, and the Court held a status conference with counsel on August 7, 2008, at which the Court announced it

⁵ Petition at ¶¶ 17–18.

⁶ *Id.* at ¶ 20.

⁷ *Id.*

would grant the motion to dismiss in part. This is the Court’s written opinion explaining that decision.

II. ANALYSIS

Rule 12(b)(6) directs the Court to dismiss a case when the complaint or petition fails “to state a claim upon which relief can be granted.”⁸ When reviewing a motion under this rule, the Court ““must determine whether it appears with reasonable certainty that, under any set of facts that could be proven to support the claims asserted, the plaintiffs would not be entitled to relief.””⁹ That inquiry is limited to the facts alleged in the petition, which the Court must assume are true when making its determination.¹⁰ However, the Court may also “consider the unambiguous terms of documents incorporated by reference in the complaint when the documents are integral to the plaintiff’s claims.”¹¹ Consequently, because the petition explicitly references and relies on the respondent entities’ various LLC Agreements, the Court may consider the unambiguous terms of those contracts without converting this motion to dismiss into a motion for summary judgment.¹²

⁸ Ct. Ch. R. 12(b)(6).

⁹ *VLIW Tech., LLC v. Hewlett-Packard Co.*, 840 A.2d 606, 610–11 (Del. 2003) (quoting *McMullin v. Beran*, 765 A.2d 910, 916 (Del. 2000)).

¹⁰ *Id.* But see *In re Coca-Cola Enters.*, C.A. No. 1927-CC, 2007 WL 3122370, at *3–4 (Del. Ch. Oct. 17, 2007) (noting that the Court will not give “any credence to conclusory allegations” and noting that “[a]n allegation is conclusory when it merely states a generalized conclusion with no supporting facts”), *aff’d sub nom. Int’l Bhd. of Teamsters v. Coca-Cola Co.*, No. 601, 2007, 2008 WL 2484587 (Del. June 20, 2008).

¹¹ *E.g., Encite v. Soni*, C.A. No. 2476-CC, 2008 WL 2973015, at *5 (Del. Ch. Aug. 1, 2008).

¹² See *In re Santa Fe Pacific Corp. S’holder Litig.*, 669 A.2d 59, 69–70 (Del. 1995).

A. The Pandora Entities

Before the Court need look to any contractual language, however, it must consider the argument of Pandora Racing, LLC and Pandora Farms, LLC (collectively, the “Pandora Entities”), which contend that the claims against them must be dismissed on account of standing. Specifically, the Pandora Entities dispute petitioners’ ability to seek dissolution or winding up under 6 *Del. C.* §§ 18-802 or 18-803. Under section 18-802, “[o]n application *by or for a member or manager*, the Court of Chancery may decree dissolution of a limited liability company whenever it is not reasonably practicable to carry on the business in conformity with a limited liability company agreement.” Similarly, under section 18-803, only managers or members have standing to wind up a limited liability company’s affairs.¹³

The petitioners, however, are neither members nor managers of the Pandora Entities. The sole member of the two Pandora Entities is PDF Properties, LLC. There is no authority for the proposition that a member of an LLC which is itself a

¹³ 6 *Del. C.* § 18-803 (“Unless otherwise provided in a limited liability company agreement, a manager who has not wrongfully dissolved a limited liability company or, if none, the members or a person approved by the members or, if there is more than 1 class or group of members, then by each class or group of members, in either case, by members who own more than 50 percent of the then current percentage or other interest in the profits of the limited liability company owned by all of the members or by the members in each class or group, as appropriate, may wind up the limited liability company’s affairs; but the Court of Chancery, upon cause shown, may wind up the limited liability company’s affairs upon application of any member or manager, the member’s or manager’s personal representative or assignee, and in connection therewith, may appoint a liquidating trustee.”).

member of another LLC can seek dissolution or the winding up of the latter LLC. Under the plain language of the LLC Act, the petition to dissolve or wind up the affairs of the Pandora Entities must be dismissed.

The petition, however, also seeks the appointment of a receiver for the Pandora Entities pursuant to 6 *Del. C.* § 18-805. Section 18-805 permits any “creditor, member or manager of the Limited liability company, or any other person who shows good cause” to present an application for the appointment of a receiver. The Pandora Entities do not challenge petitioners’ ability to seek relief pursuant to section 18-805 and, therefore, that claim survives this motion.¹⁴

B. The Waiver Entities

Petitioners are members of the other seven respondent entities, and there is no question, therefore, that they have statutory standing to seek relief under sections 18-802, 18-803, and 18-805. Nevertheless, Buck & Doe Run Valley Farms, LLC, Grays Ferry Properties, LLC, Hope Land, LLC, Merritt Land, LLC, Unionville Land, LLC, Moore Street, LLC, and PDF Properties, LLC (collectively, the “Waiver Entities”) contend that the petitioners cannot pursue this action because they have waived their rights to seek dissolution or the appointment of a liquidator. Specifically, the Waiver Entities point to provisions of their respective

¹⁴ See Respondents’ Reply Br. at 16 n.10 (“Respondents are at a loss as to why Petitioners expended so much effort and placed so much emphasis in their Answering Brief on their standing to seek relief against the Pandora Entities under 6 *Del. C.* § 805 [sic] as Respondents never challenged Petitioners’ standing to do so in the first place.”).

LLC Agreements in which the members purported to waive these rights. The petitioners concede that the contractual language purports to effect such a waiver, but nonetheless argue that the waiver is invalid as a matter of law.¹⁵ Because neither Delaware’s LLC Act nor its policy precludes such a waiver, and because the waiver of such rights would not leave an LLC member inequitably remediless, this Court concludes that petitioners have indeed waived these rights and grants the Waiver Entities’ motion to dismiss.

1. The LLC Agreements

The seven Waiver Entities have identical LLC Agreements and each one addresses dissolution explicitly. Specifically, their Agreements limit the events that shall cause dissolution to five events:

(i) an Event of Withdrawal of a Member . . .; (ii) the affirmative vote of all Members; (iii) upon the sale of all or substantially all of the Company’s assets; (iv) the conversion of the Company into a corporation or other Person; or (v) upon the entry of a decree of judicial dissolution under Section 18-802 of the Act.

The Agreements, however, further provide that the Members have waived the right to seek dissolution under section 18-802. The seven LLC Agreements contain the following provision:

Waiver of Dissolution Rights. The Members agree that irreparable damage would occur if any member should

¹⁵ *E.g.*, Petition at ¶ 25 (“Although certain of the operating agreements purport to waive the members’ right to seek judicial dissolution and/or the appointment of a liquidator, the provisions are unenforceable.”).

bring an action for judicial dissolution of the Company. Accordingly each member accepts the provisions under this Agreement as such Member's sole entitlement on Dissolution of the Company and waives and renounces such Member's right to seek a court decree of dissolution or to seek the appointment by a court of a liquidator for the Company.

Although not addressed by the parties, the Court notes that there is an apparent tension between these two provisions. Section 10.1 provides that one means by which dissolution of the limited liability company will occur is the "entry of a decree of judicial dissolution under Section 18-802 of the Act." Section 13.1, however, appears to prohibit members from seeking the entry of such a decree. If these provisions actually conflicted, the Waiver Entities' argument would be rendered unpersuasive by virtue of ambiguity in the Agreement. This Court is constrained, however, by rules of interpretation that require it to attempt to "harmoniz[e] seemingly conflicting contract provisions,"¹⁶ and these provisions can in fact be harmonized. A "decree of judicial dissolution" may be entered by the Court under section 18-802 upon an "application by *or for* a member or manager." Although the members and managers of the Waiver Entities have apparently waived *their* rights to make an application under section 18-802, the members and managers cannot waive the rights of others to make such applications

¹⁶ See *United Rentals, Inc. v. RAM Holdings, Inc.*, 937 A.2d 810, 831–32 (Del. Ch. 2007); see also *Counsel of the Dorset Condo Apartments v. Gordon*, 801 A.2d 1, 7 (Del. 2002) ("A court must interpret contractual provisions in a way that gives effect to every term of the instrument, and that, if possible, reconciles all of the provisions of the instrument when read as a whole.")

for them.¹⁷ Consequently, under the interpretive principle requiring harmonization, sections 10.1 and 13.1 do not conflict because it is possible both that a court could enter a “decree of judicial dissolution under Section 18-802 of the Act” and that the members could nonetheless have waived *their* right to seek such a decree.

2. Freedom of Contract and Limited Liability Companies

As this Court has noted, “Limited Liability Companies are creatures of contract, ‘designed to afford the maximum amount of freedom of contract, private ordering and flexibility to the parties involved.’”¹⁸ Delaware’s LLC Act leaves to the members of a limited liability company the task of “arrang[ing] a manager/investor governance relationship;” the Act generally provides defaults that can be modified by contract.¹⁹ Indeed, the Act itself explicitly provides that “[i]t is the policy of this chapter to give the maximum effect to the principle of freedom of contract and to the enforceability of limited liability company

¹⁷ The Court assumes without affirmatively ruling that there is a difference between applications made *by* members and managers and those made *for* them. This assumption is justified by the principle of statutory construction that requires the Court to give meaning to every word. *See Oceanport Indus., Inc. v. Wilmington Stevedores, Inc.*, 636 A.2d 892, 900 (Del. 1994) (“[W]ords in a statute should not be construed as surplusage if there is a reasonable construction which will give them meaning.”).

¹⁸ *TravelCenters of Am., LLC v. Brog*, C.A. No. 3516-CC, 2008 WL 1746987, at *1 (Del. Ch. Apr. 3, 2008) (quoting *In re Grupo Dos Chiles, LLC*, C.A. No. 1447-N, 2006 WL 668443, at *2 (Del. Ch. Mar. 10, 2006)).

¹⁹ *See* Myron T. Steele, *Judicial Scrutiny of Fiduciary Duties in Delaware Limited Partnerships and Limited Liability Companies*, 32 DEL. J. CORP. L. 1, 5 (2007) (concluding that courts should not “superimpose[e] their view *ex post* on how that relationship should be structured and scrutinized”).

agreements.”²⁰ It is this flexibility that gives “unincorporate” entities like limited liability companies their allure;²¹ “a principle attraction of the LLC form of entity is the statutory freedom granted to members to shape, by contract, their own approach to common business ‘relationship’ problems.”²²

The members of the Waiver Entities obviously availed themselves of this flexibility. Their respective LLC Agreements outline—often in great detail—the governance structure the members agreed would best serve the companies. Moreover, as noted above, the LLC Agreements also provide for the dissolution of the entities. In those Agreements, the members agreed that the initiation of a dissolution action would cause “irreparable damage,” and they therefore agreed to waive their rights to seek dissolution or the appointment of a liquidator.²³ To the

²⁰ 6 *Del. C.* § 18-1101(b); *see also* Sandra K. Miller, *What Fiduciary Duties Should Apply to the LLC Manager after More than a Decade of Experimentation?*, 32 *J. CORP. L.* 565, 569–70 (2007) (“The contractarian view of investors in unincorporated entities is that parties should be free to strike their own bargain free from external interference. This position has gained significant popularity, particularly in Delaware. The contractarian philosophy embraces the view that statutory business laws should be kept to a minimum, giving maximum freedom to business participants to contractually determine their legal rights and responsibilities. Based on this philosophy, several LLC statutes, including that of Delaware, expressly defer to the parties’ agreement. The Delaware statute contains few default statutory rules for the operating agreement and fails to provide the statutory remedy of a dissolution or buy-out in the event that the controlling LLC owner engages in fraudulent, illegal, or oppressive conduct.”).

²¹ *See* Larry E. Ribstein, *The Rise of the Incorporation* 3 (Illinois Law and Economics Research Papers Series, Research Paper No. LE07-026, 2007) (“[U]nincorporate firms have flexible control rules and permit contractual modification or even elimination of fiduciary duties.”), *available at* <http://ssrn.com/abstract=1003790>.

²² *Haley v. Talcott*, 864 A.2d 86, 88 (Del. Ch. 2004).

²³ Petitioners argue that the language of the purported waiver—*i.e.*, the use of “liquidator” rather than “receiver”—precludes this Court from determining that petitioners have waived their rights under 6 *Del. C.* § 18-805. Indeed, section 18-805 does not use the term liquidator, but it is unambiguously clear from the language of the LLC Agreement that the term liquidator was

extent this waiver is enforceable under the statute and public policy, petitioners' suit against the Waiver Entities under sections 18-802, 18-803, and 18-805 is barred by contract and must be dismissed.²⁴

3. The LLC Act Does Not Prohibit Waiver of these Rights

Petitioners make two distinct but ultimately unavailing arguments as to why the LLC Act prohibits waiver of a member's right to seek dissolution. First, petitioners point to 6 *Del. C.* § 18-109(d) for the proposition that non-managing members may not waive their rights to maintain legal actions in Delaware courts absent an agreement to arbitrate. Because the petitioners are not managing members and because there is no agreement to arbitrate in place, petitioners argue that the section 13.1 waiver violates this statutory provision and is therefore void.

meant to include a receiver under section 18-805. "Liquidator" is not itself a defined term under the LLC Agreement, but "liquidation" is defined in section 1.1(s) as "the process of winding up the Company after its Dissolution." Thus, a "liquidator" must be a person who conducts the winding up of the company's unfinished business. A "receiver" under 6 *Del. C.* § 18-805 is appointed "to take charge of the limited liability company" and its property with the power "to do all . . . acts which might be done by the limited liability company . . . that may be necessary for the final settlement of the unfinished business of the limited liability company." It is clear from this statutory language and from the LLC Agreement that the term "liquidator" as used in the Agreement is tantamount to a section 18-805 receiver.

²⁴ *Cf. CIT Comm'ns Fin. Corp. v. Level 3 Comm'ns, LLC*, No. 06C-01-236 JRS, 2008 WL 2586694, at *5 (Del. Super. Ct. June 6, 2008) (noting that "party may waive the right to trial by jury in many ways, including by contract."); *Fisk Ventures, LLC v. Segal*, C.A. No. 3017-CC, 2008 WL 1961156, at *11 (Del. Ch. May 7, 2008) (dismissing third-party claims for breach of fiduciary duty because such claims and duties were waived in the operative LLC Agreement); *Matria Healthcare, Inc. v. Coral SR LLC*, C.A. No. 2513-N, 2007 WL 763303, at *9 (Del. Ch. Mar. 1, 2007) (dismissing two counts of a complaint because the relief sought had to be brought in accordance with the parties' arbitration agreement); *Hintmann v. Fred Weber, Inc.*, C.A. No. 12839, 1998 WL 83052, at *10 (Del. Ch. Feb. 17, 1998) (noting that "a purchaser of preferred shares may contract away his or her right to have this Court determine the shares' fair value").

Section 18-109, however, is captioned “Service of process on managers and liquidating trustees,” and is at most a venue provision.

In its entirety, section 18-109(d) reads:

In a written limited liability company agreement or other writing, a manager or member may consent to be subject to the nonexclusive jurisdiction of the courts of, or arbitration in, a specified jurisdiction, or the exclusive jurisdiction of the courts of the State of Delaware, or the exclusivity of arbitration in a specified jurisdiction or the State of Delaware, and to be served with legal process in the manner prescribed in such limited liability company agreement or other writing. Except by agreeing to arbitrate any arbitrable matter in a specified jurisdiction or in the State of Delaware, a member who is not a manager may not waive its right to maintain a legal action or proceeding in the courts of the State of Delaware with respect to matters relating to the organization or internal affairs of a limited liability company.²⁵

Although petitioners emphasize the final sentence, the gist of the provision read in its entirety is about venue and preventing members from forming an LLC in Delaware while barring jurisdiction in the state; it has nothing to do with members’ broader ability to structure the entity and their substantive rights with respect to it. On the whole, section 18-109 ensures that Delaware retains ultimate jurisdiction over its limited liability companies by providing for service of process through a registered agent in the state and for jurisdiction in the state courts or an arbitration forum.

²⁵ 6 *Del. C.* § 18-109(d).

Petitioners’ out-of-context interpretation of the final sentence of section 18-109(d) is untenable. If petitioners were correct, the LLC Act would conflict with itself, and the rules of statutory construction caution this Court against such a conclusion.²⁶ For example, under petitioners’ reading, a non-managing member could not waive his or her right to maintain a claim for a breach of fiduciary obligations in the Delaware courts because fiduciary duties are an essential part of an entity’s “internal affairs.”²⁷ In spite of this, the LLC Act specifically permits the members of limited liability companies to eliminate fiduciary duties.²⁸ Because section 18-109 can (more reasonably) be construed to avoid this conflict, the Court concludes that section 18-109 does not operate outside its plain language and governs only service of process and venue.

²⁶*E.g., Christina Educ. Ass’n v. Del. State Bd. of Educ.*, No. 93A-07-015, 1994 WL 637000, at *3 (Del. Super. Ct. May 25, 1994) (“There is a rule of statutory construction that provides guidance for the interpretation of conflicting statutes. Essentially, it states: ‘If statutes appear to conflict, they must be construed, if possible, to give effect to each.’”).

²⁷ *Cf. In re Topps Co. S’holders Litig.*, 924 A.2d 951, 960 (Del. Ch. 2007) (“Delaware’s system of corporate law, the adjudication of cases involving the fiduciary duties of directors in new business dynamics is one of the most important methods of regulating the internal affairs of corporations, as these cases articulate the equitable boundaries that cabin directors’ exercise of their capacious statutory authority.”).

²⁸ 6 *Del. C.* § 18-1101(c) (“To the extent that, at law or in equity, a member or manager or other person has duties (including fiduciary duties) to a limited liability company or to another member or manager or to another person that is a party to or is otherwise bound by a limited liability company agreement, the member’s or manager’s or other person’s duties may be expanded or restricted or eliminated by provisions in the limited liability company agreement.”); *Fisk Ventures*, 2008 WL 1961156, at *11 (dismissing claims for breach of fiduciary duties where “the LLC Agreement, in accordance with Delaware law, greatly restricts or even eliminates fiduciary duties”); *see also* 3 EDWARD P. WELCH, ANDREW J. TUREZYN, AND ROBERT S. SAUNDERS, *FOLK ON THE DELAWARE GENERAL CORPORATION LAW* § 18-1101.6 (supp. 2007).

Petitioner’s second statutory argument is based on the principle that certain provisions of the LLC Act are mandatory and non-waivable. As the Supreme Court has explained, “[t]he Act can be characterized as a ‘flexible statute’ because it generally permits members to engage in private ordering with substantial freedom of contract to govern their relationship, provided they do not contravene any mandatory provisions of the Act.”²⁹ Generally, the mandatory provisions of the Act are “those intended to protect third parties, not necessarily the contracting members.”³⁰ Finally, “[i]n general, the legislature’s use of ‘may’ connotes the voluntary, not mandatory or exclusive, set of options.”³¹

Petitioners proffer a far broader rule and argue that “[s]tatutory provisions that do not contain the qualification ‘unless otherwise provided in a limited liability company agreement’ (or a variation thereof) are mandatory and may not be waived.”³² Petitioners, however, offer no authority for this assertion and, in fact, authorities they cite directly contradict it. In *Elf Atochem North America, Inc. v. Jaffari*, for example, a case on which petitioners heavily rely, the Supreme Court

²⁹ *Elf Atochem N. Am., Inc. v. Jaffari*, 727 A.2d 286, 290 (Del. 1999).

³⁰ *Id.* at 292; *see also* 1 LARRY E. RIBSTEIN AND ROBERT R. KEATINGE, RIBSTEIN AND KEATINGE ON LIMITED LIABILITY COMPANIES § 4:16, 4-36 to 4-47 (“The operating agreement generally controls except to the extent that it is inconsistent with mandatory statutory provisions. Such provisions include those . . . which are intended to protect third parties.”); *Id.* § 4:16, 4-43 (“If an LLC statute provides that statutory rights may be varied by an operating agreement, the statute should specify that the operating agreement does not vary statutory rights of nonparties. LLC statutes do not allow the operating agreement to vary provisions that affect third-party creditors, or provide in general terms that an operating agreement governs only rights among the members.”).

³¹ *Elf*, 727 A.2d at 296.

³² Petitioner’s Answering Br. at 8.

held that a provision of the LLC Act *not* containing petitioners’ magical phrase was nonetheless permissive and subject to modification.³³ Indeed, in *Elf*, the Supreme Court explicitly noted that the “unless otherwise provided” phrase was merely one example of the means by which a court could ascertain the intent of the General Assembly.³⁴ Indeed, in other provisions, the General Assembly explicitly forbids waiver. For example, the Act overtly bars members from “eliminat[ing] the implied contractual covenant of good faith and fair dealing.”³⁵

Sections 18-802, 18-803, and 18-805 are not mandatory provisions of the LLC Act that cannot be modified by contract. First, the Act does not expressly say that these provisions cannot be supplanted by agreement, and, in fact, section 18-803 does include the “unless otherwise provided” phrase. Second, the provisions employ permissive rather than mandatory language. Section 18-802 states that the “Court of Chancery *may* decree dissolution”³⁶ and section 18-805 states that “the Court of Chancery . . . *may* either appoint” a trustee or receiver.³⁷ Finally, and most importantly, none of the rights conferred by these provisions that are waived in the LLC Agreement is designed to protect third parties. This Court has

³³ 727 A.2d at 292–96 (concluding that 6 *Del. C.* § 18-109(d) is not mandatory).

³⁴ *Id.* at 291.

³⁵ 6 *Del. C.* § 1101(c).

³⁶ 6 *Del. C.* § 18-802 (emphasis added).

³⁷ 6 *Del. C.* § 18-805 (emphasis added).

recognized that third parties have no interest in dissolution under section 18-802,³⁸ and section 18-805 specifically permits creditors to petition the Court for the appointment of a receiver for a canceled limited liability company. The rights of third-party creditors under section 18-805 are not affected by the LLC Agreement. In sum, the LLC Act “expressly encourages ‘made-to-order’ structuring of limited liability companies” and “offers explicit assurance that contractual arrangements will be given effect to the fullest permissible extent.”³⁹ Because the waiver of a member’s right to petition for dissolution or the appointment of a receiver does not violate the LLC Act and does not interfere with the rights of third parties, the waiver is valid and enforceable under the statute.

4. Public Policy Does Not Prohibit Waiver of these Rights

Finally, petitioners argue that the Court should refuse to enforce their knowing, voluntary waiver of their right to seek dissolution or the appointment of a receiver because such waivers violate the public policy of Delaware and offend notions of equity. This argument too must fail. First, as discussed throughout this Opinion and others, in treatises, and in the LLC Act itself, the public policy of Delaware with respect to limited liability companies is freedom of contract. Second, there are legitimate business reasons why a firm would want to set up its

³⁸ *The Follieri Group, LLC v. Follieri/Yucaipa Invs., LLC*, C.A. No. 3015-VCL, 2007 WL 2459226, at *1–2 (Del. Ch. Aug. 23, 2007) (refusing to allow a putative creditor to intervene in a statutory dissolution action).

³⁹ ROBERT L. SYMONDS, JR. AND MATTHEW J. O’TOOLE, SYMONDS & O’TOOLE ON DELAWARE LIMITED LIABILITY COMPANIES § 1.03[A][1] (2007).

governance structure so that its members could not petition the Court for dissolution. Finally, the LLC Act provides protections that cannot be waived; this Court need not exercise its equitable discretion and disregard a negotiated agreement among sophisticated parties to allow this action to proceed.

The hunt for legislative intent with respect to Delaware’s LLC Act is rather simple, because the General Assembly explicitly stated that the “policy” of the Act is “to give the maximum effect to the principle of freedom of contract and to the enforceability of limited liability company agreements.”⁴⁰ The LLC Act provides members with “the broadest possible discretion in drafting their [LLC] agreements” and assures that “once [members] exercise their contractual freedom in their [LLC] agreement, the [members] have a great deal of certainty that their [LLC] agreement will be enforced in accordance with its terms.”⁴¹ One treatise concludes that “[f]lexibility lies at the core of the DLLC Act. Rather than imposing a host of immutable rules, the statute generally allows parties to order their affairs, contractually, as they deem appropriate.”⁴²

Chief Justice Steele has powerfully argued that the freedom of contract principle must be assiduously guarded lest the courts erode the primary attraction of limited liability companies. In his remarks on fiduciary duties and alternative

⁴⁰ 6 *Del. C.* § 18-1101(b).

⁴¹ *Elf Atochem N. Am., Inc. v. Jaffari*, 727 A.2d 286, 291 (Del. 1999) (quoting MARTIN I. LUBAROFF AND PAUL ALTMAN, *DELAWARE LIMITED PARTNERSHIPS* § 1.2 (1999)).

⁴² SYMONDS AND O’TOOLE, *supra* note 39, at § 1.03[A][1][a].

entities, the Chief Justice rhetorically asks, “why should courts seek to incorporate uncertainty, inconsistency, and unpredictability into the world of negotiated agreements?”⁴³ Similarly, Professor Larry Ribstein, whose scholarship on limited liability companies has been frequently cited by both this Court and the Supreme Court, emphasizes that it is the rigor with which Delaware courts apply the contractual language of LLC Agreements that makes limited liability companies successful.⁴⁴ Indeed, “Delaware is a freedom of contract state, with a policy of enforcing the voluntary agreements of sophisticated parties in commerce.”⁴⁵ Here, the LLC Agreement is a contract between sophisticated parties. The business relationships between the individuals behind the petitioners and Lynda Merritt is extensive; clearly these were parties who knew how to make use of the law of alternative entities. The mere fact that the business relationship has now soured cannot justify the petitioners’ attempt to disregard the agreement they made. Therefore, contrary to petitioners’ argument that Delaware’s public policy will not

⁴³ Steele, *supra* note 19, at 30.

⁴⁴ See generally Larry E. Ribstein, *The Uncorporation and Corporate Indeterminacy* (Ill. Law and Econ. Research Paper Series, Research Paper No. LE08-012, 2008), available at http://papers.ssrn.com/pape.tar?abstract_id=1115876; cf. Larry E. Ribstein, *An Analysis of the Revised Uniform Limited Liability Company Act*, 3 VA. L. & BUS. REV. 35. 67 (2008) (“In fact, detailed case analysis reveals that the courts have done a good job of interpreting and applying limited partnership agreements under the Delaware freedom-of-contract regime.”).

⁴⁵ *Personnel Decisions, Inc. v. Bus. Planning Sys., Inc.*, C.A. No. 3213-VCS, 2008 WL 1932404, at *6 (Del. Ch. May 5, 2008).

countenance their unambiguous contractual waiver, the state's policy mandates that this Court respect and enforce the parties' agreement.⁴⁶

In addition to Delaware's general policy promoting the freedom of contract, there are legitimate business reasons why members of a limited liability company may wish to waive their right to seek dissolution or the appointment of a receiver. For example, it is common for lenders to deem in loan agreements with limited liability companies that the filing of a petition for judicial dissolution will constitute a noncurable event of default. In such instances, it is necessary for all members to prospectively agree to waive their rights to judicial dissolution to protect the limited liability company. Otherwise, a disgruntled member could push the limited liability company into default on all of its outstanding loans simply by filing a petition with this Court. In fact, one of the petitioners here, R&R Capital, LLC, has acted as a lender to some of the Waiver Entities and included such a provision in its loan agreement with respondent Unionville Land, LLC.⁴⁷

Finally, petitioners' plea to this Court's sense of equity is misplaced. The LLC Act does not abandon petitioners with no recourse as they "sit idly by while

⁴⁶ See *Seidensticker v. Gasparilla Inn, Inc.*, C.A. No. 2555-CC, 2007 WL 4054473, at *1 (Del. Ch. Nov. 8, 2007) ("Under Delaware law, courts interpret contracts to mean what they objectively say.").

⁴⁷ This information, of course, is not included in the petition and the Court does not rely on it in reaching its decision. See *In re Gen. Motors (Hughes) S'holders Litig.*, 897 A.2d 162, 168 (Del. 2006) ("The complaint generally defines the universe of facts that the trial court may consider in ruling on a Rule 12(b)(6) motion to dismiss"). The Court notes this merely in passing to illustrate the deficiency of the petitioners' policy based argument.

Merritt (the manager) seeks to continue operating seven entities that have had their certificates of formation canceled and two entities whose narrow purposes have been fulfilled.”⁴⁸ Instead, the LLC Act preserves the implied covenant of good faith and fair dealing.⁴⁹ The petition filed is replete with allegations about the unbecoming conduct of Merritt, and petitioners’ brief opposing the motion to dismiss likewise criticizes her. Petitioners, however, have not named Merritt as a party in this action. Although, fairly construed, the petition may allege a breach of the implied covenant, the petitioners unambiguously have failed to state a claim upon which relief can be granted because they have not named the alleged bad-faith actor in their petition. It is the unwaivable protection of the implied covenant that allows the vast majority of the remainder of the LLC Act to be so flexible.⁵⁰ There is no threat to equity in allowing members to waive their right to seek

⁴⁸ Petitioners’ Answering Br. at 11.

⁴⁹ See 6 *Del. C.* § 1101(c).

⁵⁰ See Deborah A. Demott, *Fiduciary Preludes: Likely Issues for LLCs*, 66 U. COLO. L. REV. 1043, 1059–62 (1995) (noting the backstop protection of the implied covenant: “The presupposition of mutual intent to benefit, which in turn produces mutual obligation, is an inevitable offspring of founding contract doctrine in exchange-based consideration. In consequence, an agreement is not enforceable as a contract unless it contemplates mutuality of obligation. Put differently, an LLC or limited partnership agreement that completely abjured fiduciary obligation would, in the absence of a robust implied obligation of good faith, resemble a gift of members’ property to those in control of the enterprise who would be free to use the entity’s property as they saw fit. Anglo-American contract doctrine has not enforced executory promises to make gifts because such promises do not contemplate an exchange. Moreover, persons who invest or participate in business ventures lack donative intent toward those who control the venture; it strains credulity excessively to characterize membership in an LLC or a limited partnership, once formed, as indicative of intention to execute a gift transaction.”).

dissolution, because there is no chance that some members will be trapped in a limited liability company at the mercy of others acting unfairly and in bad faith.

III. CONCLUSION

When parties wish to launch a new enterprise, the form of the limited liability company offers a highly customizable vehicle in which to do so. The flexibility of such an entity springs from its roots in contract; the parties have “the broadest possible discretion” to set the structure of the limited liability company.⁵¹ Indeed, “LLC members’ rights begin with and typically end with the Operating Agreement.”⁵² The allure of the limited liability company, however, would be eviscerated if the parties could simply petition this court to renegotiate their agreements when relationships sour. Here, the sophisticated members of the seven Waiver Entities knowingly, voluntarily, and unambiguously waived their rights to petition this Court for dissolution or the appointment of a receiver under the LLC Act.⁵³ This waiver is permissible and enforceable because it contravenes neither the Act itself nor the public policy of the state. Moreover, with respect to the two other respondent entities—the Pandora Entities—the petitioners lack statutory

⁵¹ *Elf Atochem N. Am., Inc. v. Jaffari*, 727 A.2d 286, 291 (Del. 1999).

⁵² *Walker v. Res. Dev. Co.*, 791 A.2d 799, 813 (Del. Ch. 2000).

⁵³ See 6 *Del. C.* §§ 18-802, 18-803, and 18-805.

standing to seek dissolution or the winding up of the entities. They may, however petition for the appointment of a receiver.⁵⁴

These parties have cases pending in both state and federal courts in Delaware, Pennsylvania, and New York. These parties, however, originally came together and negotiated a series of agreements that led to the nine entities presently before the Court; perhaps the most prudent resolution to their problems is once again negotiation—a negotiated settlement. With Shakespeare this Opinion began, and with Shakespeare it too shall end:

Recall—lest another court these parties try—
“Our remedies oft in ourselves do lie.”⁵⁵

An implementing Order has been entered.

⁵⁴ The parties should confer regarding an appropriate revision to the Status Quo Order as it relates to the Pandora Entities. In the event the parties cannot agree on a revised order, each side should submit a proposed form of status quo order for this Court’s consideration.

⁵⁵ WILLIAM SHAKESPEARE, *ALL’S WELL THAT ENDS WELL* act 1, sc. 1, ln. 231.