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BREACHES OF FIDUCIARY DUTY AND THE DELAWARE UNIFORM CONTRIBUTION ACT

J. Travis Laster and Michelle D. Morris*

"[I]f a breach of fiduciary duty is not a tort action, what is it?"[1]

What is the nature of a claim for breach of fiduciary duty against the directors or officers of a Delaware corporation?[2] Is it a tort? Is it contractual? Is it something else altogether? Recent cases have raised whether the Delaware Uniform Contribution Among Tortfeasors Act ("DUCATA") applies to breach of fiduciary duty claims, but the Delaware courts have not yet decided this difficult issue. We conclude that a breach of a fiduciary duty is in fact a tort, although a unique species historically called an "equitable tort." The history of the Uniform Contribution Among Tortfeasors Act (the "Uniform Act"), on which DUCATA is based, provides unclear and conflicting indications regarding how its drafters intended to treat equitable torts. We conclude that DUCATA should apply to breaches of fiduciary duty, although given the substantial interpretive uncertainty, the most expedient solution would be for the Delaware General Assembly to amend DUCATA to clarify its application.

In Part I, we briefly discuss contribution generally and the origins of the common law rule that there was no contribution among tortfeasors. In Part II, we turn to the development of contribution among tortfeasors in Delaware and the currently ambiguous state of the law regarding contribution among directors for breaches of fiduciary duty. In Part III we introduce DUCATA, the statute enacted to abrogate the common law's no-contribution rule. Because DUCATA is based upon the Uniform Act, and there is no legislative history for DUCATA itself, we turn in Part IV to the 1939 drafting and the 1955 revision of the Uniform Act, searching for clues about the drafters' intent. As it turns out, both sets of drafters considered breaches of fiduciary duty to be "equitable torts" — a concept that has largely disappeared from the collective legal consciousness — but the 1939 drafters sought to include them within the Act's coverage while the 1955 drafters sought to exclude them. Ironically, both sets of drafters intended for contribution to exist, and their conflicting approaches reflected differing beliefs about the availability of contribution at common law for "equitable torts." The 1939 drafters sought to include equitable torts because they believed contribution outside of the Uniform Act was ineffective at best and non-existent at worst. The 1955 drafters sought to exclude equitable torts because they believed a well developed system for contribution for equitable torts already existed and the Uniform Act should not interfere with it. In Part V, we conclude that with respect to contribution among directors for breaches of fiduciary duty, the drafters of the 1939 Act were closer to the truth. There was a limited and uncertain right of contribution among directors at common law, but it was far less developed than the right of contribution among trustees, which is what the drafters of the 1955 Act appear to have had in mind.

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* J. Travis Laster is a Vice Chancellor of the Delaware Court of Chancery. Michelle D. Morris is a member of the District of Columbia bar and law clerk to the Honorable George W. Miller of the United States Court of Federal Claims.

1. Charles Hansen, *The* Technicolor *Case—A Lost Opportunity*, 19 Del. J. Corp. L. 617, 637 n.152 (1994).

2. Directors and officers of Delaware corporations owe "identical" fiduciary duties. Gantler v. Stephens, 965 A.2d 695, 708-09 (Del. 2009). This article generally refers to the duties owed by corporate directors, rather than officers. The analysis for both should be the same or very similar, although the origin of the duties may differ. *See infra* note 83.

In Part VI, we explore the notion of "equitable torts" and find that it historically referred to torts falling within the exclusive jurisdiction of courts of equity. With the general merger of law and equity, the concept of "equitable torts" faded. Debate over the proper characterization of a claim for breach of fiduciary duty shifted to whether it fell within the rubric of tort or contract, an issue driven largely by fights over the proper statute of limitations, with a strong majority of jurisdictions adopting the tort characterization. In Part VII, we turn to Delaware, which has both retained its separate courts of law and equity and has treated breaches of fiduciary duty as something different from a traditional, or "legal," tort. Armed with the concept of the "equitable tort," we are able to explain this feature of Delaware law, which has otherwise been criticized by commentators. Because a claim for breach of fiduciary duty is best viewed as an equitable tort, it falls within the contemplation of the drafters of the 1939 Uniform Act, which is the version Delaware adopted. Moreover, as we saw in Part V, the drafters of the 1939 Uniform Act were largely correct in their belief that the common law had not developed effective doctrines of contribution where corporate directors were concerned. Thus we conclude that Delaware ought to interpret DUCATA as governing claims for breach of fiduciary duty against directors, and in Part VIII we explain why this is consistent with other aspects of Delaware law. But because of the interpretive quagmire, we recommend that the Delaware General Assembly amend DUCATA to clarify its application.

I. THE "NATURAL JUSTICE" OF CONTRIBUTION

> *"The right to contribution, being founded in natural justice, is not restricted to any special relation, but applies to original contractors, or any other relation, where equity between the parties is equality of burden, and one discharges more than his share of the common obligation."*[3]

When more than one person is jointly liable for a loss, but one defendant pays the plaintiff all (or a disproportionate share) of the total, the doctrine of contribution allows the overpaying defendant to pursue anyone else who is jointly liable, so that each liable person pays a fair share of the debt.[4] The rule operates in a straightforward fashion where the loss is contractual, such as the payment of a debt by one of several co-sureties.[5]

Where the underlying loss arises in tort, contribution is more complicated. The common law rule was described in the 1799 case of *Merryweather v. Nixan*,[6] where an English court held that one of two joint tortfeasors could not obtain contribution from the other. Lord Kenyon stated that "he had never before heard of such an action … where the … recovery was for tort."[7] The rationale was that tortfeasors had committed a morally wrong act, and *ex turpi causa non oritur*

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3. Bragg v. Patterson, 4 So. 716, 716 (Ala. 1888).

4. Levy v. HLI Operating Co., Inc., 924 A.2d 210, 220 (Del. Ch. 2007).

5. *See generally* 4 John Norton Pomeroy, Treatise on Equity Jurisprudence § 1418 (5th ed. 1941); 3 Ardemus Stewart, American and English Decisions in Equity 156 (1897).

6. Merryweather v. Nixan, 101 Eng. Rep. 1337 (K.B. 1799).

7. *Id.* at 1337.

action ("from a dishonorable cause an action does not arise").[8] Later English cases distinguished between intentional and negligent acts, denying contribution in the former case, but permitting it in the latter.[9]

By the mid-nineteenth century, however, most American courts had erased any distinction between intentional and negligent torts and barred contribution among all joint tortfeasors.[10] American common law thus distinguished between joint obligations arising from an express or implied contract, which fell under the Latin heading "*ex contractu*," and those arising in tort, which fell under the heading "*ex delicto*." Contribution was allowed *ex contractu* but not *ex delicto*.[11]

II. THE PRESENT STATE OF CONTRIBUTION AMONG DIRECTORS OF A DELAWARE CORPORATION

The development of the doctrine of contribution in Delaware followed the general path of the common law. By 1847, the Court of Chancery recognized as settled law the right of contribution among co-sureties.[12] Contribution

8. 1 Thomas Atkins Street, The Foundations of Legal Liability: A Presentation of the Theory and Development of the Common Law 490 (1906). A famous example is the *Highwayman's Case*, in which two criminals committed a robbery and then sued in equity when they disagreed on the division of the spoils. The English court understandably declined to assist one wrongdoer in suing the other. Everet v. Williams (1725), printed in Notes, 9 L.Q. Rev. 197 (1893).

9. *See* Courtney Stanhope Kenny, A Selection of Cases Illustrative of the English Law of Tort 221-22 (3d ed. 1920) ("The current of subsequent decisions has limited the rule to cases where the person who claims the contribution must have known when he committed the tort, that what he was doing was tortious."). *Merryweather* established this rule for the law courts, and a similar prohibition on contribution between intentional wrongdoers applied in equity. *See* W.L.F., *Right of Contribution Among Co-Trustees*, 22 Va. L. Rev. 804, 806-07 (1936); *see also* M. Kevin Queenan, Comment, *Civil Code Article 2324: A Broken Path to Limited Solidary Liability*, 49 La. L. Rev. 1351, 1361 (1989); George Tucker Bispham, The Principles of Equity: A Treatise 442-43 (5th ed. 1893) ("No right of contribution exists where the demand is ex delicto. In cases of breach of trust, however, not involving actual fraud, contribution may be enforced by trustees as between themselves.").

10. William Prosser, The Law of Torts 306 (4th ed. 1971); Philip M. Nichols, *Symmetry and Consistency and the Plaintiff's Risk: Partial Settlement and the Right of Contribution in Federal Securities Actions*, 19 Del. J. Corp. L. 1, 7-12 (1994) (describing rule); Robert A. Leflar, *Contribution and Indemnity Between Tortfeasors*, 81 U. Pa. L. Rev. 130, 130 (1932) (same); *see also* Northwest Airlines, Inc. v. Transport Workers Union of America, AFL-CIO, 451 U.S. 77, 86-87 n.16 (1981) ("[T]he common law in this country traditionally prohibited contribution among joint tortfeasors in all cases.") (citations and quotations omitted).

11. *See* A. Sieber Hollinger, *Contribution Among Tortfeasors*, 44 Dick. L. Rev. 49, 50 (1940) ("Several reasons are generally given as to why contribution should not be permitted as between two or more persons who intentionally commit a tort, or a crime which, at the same time, amounts to a tort. The first of these may best be explained by the maxims *Ex turpi causa, non oritur actio*, and *In pari delicto, potior est conditio defendentis*. With these, and the doctrine of contributory negligence, and clean hands in equity, courts have frequently reiterated their determination not to aid a wrongdoer in his suit against another wrongdoer."); John Indermaur, An Epitome of Leading Common Law Cases with Some Short Notes Thereon 66 (3d ed. 1875) (the whole decision [*i.e., Merryweather v. Nixan*] may be shortly expressed by saying that as between defendants *ex contractu* the law allows contribution, but not between defendants *ex delicto*."); Street, Foundations of Legal Liability, *supra* note 8, at 490 ("Connected with the rule that a plaintiff can enforce reparations against one or more of the wrongdoers to the exclusion of others, is the further principle that one joint tortfeasor who pays or is compelled to pay all the damages, cannot obtain indemnity or contribution from those who are equally guilty as himself, or even more guilty than he. Such, in broad terms, was the ruling in *Merryweather v. Nixan* (1799). This is a necessary consequence of the principle embodied in the maxim *ex turpi causa non oritur actio*. Modern decision has limited the doctrine to situations where the person who claims contribution must be presumed to have known that he was doing an unlawful act.").

12. Jefferson v. Tunnell, 2 Del. Ch. 135 (Del. Ch. 1847), *rev'd on other grounds*, 5 Harr. 206 (Del. 1849); *see also* De Paris v. Wilmington Trust Co., 104 A. 691, 695 (Del. 1918) ("[Contribution] is an equitable principle based on natural justice, and was

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flowed from the premise that "[e]quality is equity," a proposition that was "universal" and "as simple a principle of natural justice as can be put."[13] For joint tortfeasors, Delaware followed the American courts' (over)expansive interpretation of *Merryweather v. Nixan* in prohibiting contribution among both intentional and negligent tortfeasors.[14]

Delaware courts had no occasion to consider whether contribution existed among directors for breaches of fiduciary duty prior to the current millennium. The issue likely did not arise for a combination of reasons. The risk of personal liability for breaches of fiduciary duty has always been low.[15] The dynamics of fiduciary duty litigation further reduce the potential for contribution disputes, because defendant directors typically "work as a relatively unified force to defeat the shareholder-plaintiffs' claims."[16] Directors historically followed this strategy even at the risk of compromising

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originally enforcible in equity only, but is now enforcible at law, the duty of one guarantor to reimburse his co-guarantor being the basis of an implied promise to do so. This promise is considered as made when the liability is assumed.") (internal citations omitted); Hutchinson v. Roberts, 11 A. 48, 51 (Del. Ch. 1887), *aff'd*, 17 A. 1061 (Del. 1889).

13. Eliason v. Eliason, 3 Del. Ch. 260 (1869) ("Equality is equity. One shall not bear a common burden in ease of the rest. Hence, if as often may be done, a lien, charge or burden of any kind, affecting several, is enforced at law against one only, he should receive from the rest what he has paid or discharged on their behalf. This is the doctrine of equitable contribution, resting upon as simple a principle of natural justice as can be put. Its most common application is to sureties and to owners of several parcels of land, subject to a lien or charge for the payment of money. But … the principle is universal.") (internal citations omitted); *see also* Wilmington Trust Co. v. Copeland, 94 A.2d 703, 708-09 (Del. 1953) (citing *Eliason* as concerning "the doctrine of equitable contribution — itself but an application of the ancient maxim 'equality is equity'" and observing "[t]hat this doctrine is a part of the law of Delaware admits of no doubt.") (internal citation omitted).

14. DiStefano v. Lamborn, 81 A.2d 675 (Del. Super. Ct. 1951), *disapproved on other grounds*, Halifax Chick Express, Inc. v. Young, 137 A.2d 743 (Del. 1958); *accord* Cox v. Delaware Elec. Coop., Inc., 823 F. Supp. 241, 246 (D. Del. 1993) ("The general rule of common law, and that operable in Delaware prior to 1949, is that where two or more individuals jointly or independently negligently cause harm to a plaintiff, one putative defendant is not entitled to contribution from the other."); Clark v. Teeven Holding Co., Inc., 625 A.2d 869, 877 (Del. Ch. 1992) ("Under Delaware law, however, there was no right to contribution among joint tort-feasors until the enactment of the Uniform Contribution Among Tort-Feasors Act on May 7, 1949. Because the substantive right to contribution among joint tort-feasors was not created until the adoption of the Uniform Act in 1949, that right was never a part of equity's traditional jurisdiction in Delaware.") (internal citations omitted); Lankford v. Richter, 1989 WL 12229, at *2 (Del. Super. Ct. Jan. 27, 1989) ("Prior to the enactment of [DUCATA], no common law right of contribution existed between joint tortfeasors."); Clark v. Brooks, 377 A.2d 365, 368 (Del. Super. Ct. 1977) ("The most startling change made by [DUCATA] was to provide a remedy of contribution among tortfeasors."); Lutz v. Boltz, 100 A.2d 647, 647 (Del. Super. Ct. 1953) ("Prior to 1949, no right of contribution existed between joint tort-feasors in this State."). It is somewhat ironic that Delaware did not address the pre-DUCATA rules governing contribution until some two years after DUCATA's adoption on May 7, 1949.

15. *See generally* Bernard Black, et al., *Outside Director Liability*, 58 Stan. L. Rev. 1055 (2006) (concluding based on empirical investigation that instances of outside director liability are rare). Directors under Delaware law are protected against liability by the business judgment rule and, after 1985, by the availability of charter provisions authorized by Section 102(b)(7) of the General Corporation Law. Del. Code Ann. tit. 8, § 102(b)(7). That statutory provision permits corporations to exculpate their directors for personal liability for breaches of fiduciary duty except for those falling into specific categories, upshot of which is to permit corporations to eliminate the threat of damages for breaches of the duty of care, but not for breaches of the duty of loyalty or the subsidiary duty of good faith. *Id. See generally* Karl E. Stauss, *Indemnification in Delaware: Balancing Policy Goals and Liabilities*, 29 Del. J. Corp. Law 143 (2004).

16. *In re* Telecorp PCS Inc., 2003 WL 22901025, at * 2 (Del. Ch. Nov. 19, 2003).

their individual defenses.[17] It is thus "rare for the defendants not to work out some allocation of the costs that avoids the need for litigation within the defendant class itself."[18]

In certain recent disputes, however, only some of the directors have settled, leaving others to face a potential money judgment. This has provided a powerful incentive for the remaining defendants to seek contribution from the settling directors.[19] In other cases, plaintiffs have chosen to sue fewer than all of the potentially liable fiduciaries, again providing an incentive for those who were sued to seek contribution from those who were not.[20]

The first Delaware case to address the potential for director contribution was *Odyssey Partners,* a 1997 decision.[21] Minority stockholders sued four directors and the corporation's controlling stockholder for allegedly breaching their fiduciary duties by allowing the controller to foreclose on the corporation's assets. After several months of discovery, the four director-defendants moved to assert a third-party claim for contribution against a fifth director, Banks, who had been appointed by the minority stockholders. It was undisputed that all of the actions challenged in the litigation had been approved unanimously by all five directors, and Chancellor William T. Allen appeared to accept that the four directors possessed a claim for contribution. He declined to permit Banks to be joined because "[o]bviously if the defendants are not liable, it would be more efficient to save Banks the expense associated with active party status."[22] The application therefore offered "only a very unclear claim of greater efficiency and certainly represents an attempt to use the joinder of party rules to gain tactical advantage."[23] Chancellor Allen did not discuss the scope or source of the potential contribution claim.[24]

17. In *Smith v. Van Gorkom*, for example, one of the outside directors held liable in that case did not attend critical meetings and potentially had a unique defense to liability. Rather than raising this defense, he joined in the arguments made by all of the directors by their jointly retained defense counsel. It was not until a motion for reargument on appeal, *after* the Delaware Supreme Court rendered its decision, that the director retained separate counsel and asserted that he was differently situated. Not surprisingly, the Delaware Supreme Court found that the argument was not timely asserted. *See* Smith v. Van Gorkom, 488 A.2d 858, 898-99 (Del. 1985). The Delaware Supreme Court also rejected the argument on the merits based on the director's participation in a later meeting. *Id.*

18. *Telecorp*, 2003 WL 22901025, at *2. In terms of who would pay in the rare case where the defendants were held liable, many directors, particularly those who serve on the boards of publicly traded corporations, are protected by liability insurance, and they can look to the insurer to satisfy a judgment. Directors also are typically protected by indemnification provisions under which the corporation obligates itself to indemnify the director for fees, expenses, and amounts paid in settlement. *See* Del. Code Ann. tit. 8, §§ 145(a) & (b). A third party such as a corporate acquirer may agree to provide direct, contractual indemnification to directors or officers of a Delaware corporation. *See* La. Mun. Police Empl. Ret. Sys. v. Crawford, 918 A.2d 1172, 1180 (Del. Ch. 2007) (noting existence of direct, contractual promise of indemnification by acquirer). Even in the celebrated case of *Smith v. Van Gorkom*, no director had to pay. The parties reached a settlement involving a total cash payment of $23 million of which approximately $10 million was paid by Trans Union's insurers and the rest by the Pritzker family, whose acquisition of Trans Union gave rise to the case. *See* Stephen M. Bainbridge, The Story of Smith v. Van Gorkom, in Corporate Law Stories 225 (J. Mark Ramseye ed., 2009).

19. *See, e.g.*, Valeant Pharmaceuticals Int'l v. Jerney, 2007 WL 2813789 (Del. Ch. Mar. 1, 2007).

20. *See In re* Am. Int'l Group, Inc., 965 A.2d 763 (Del. Ch. 2009).

21. Odyssey Partners, L.P. v. Fleming Cos., Inc., 1997 WL 38134 (Del. Ch. Jan. 24, 1997).

22. *Id*. at *3.

23. *Id*.

24. For a similar issue and identical result, see Transcript of Oral Argument, Teachers' Retirement System of Louisiana v. Greenberg, C.A. No. 20106-VCS, at 6-7 (Del. Ch. July 10, 2007). Stockholders of American International Group, Inc. asserted

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A passing snippet in *Grace Brothers*[25] evinced an assumption that contribution was available among directors. Defendant-directors moved to dismiss a breach of fiduciary duty action in part because two entities involved in the transaction were unlikely to be subject to jurisdiction in Delaware, and the defendant-directors argued that the entities were indispensible parties. Vice Chancellor Leo E. Strine, Jr. rejected this argument, noting that "if this case gets to that point, the court can fashion an award of monetary damages that holds the defendant-directors accountable for any *and only* the harm that their breaches of fiduciary duty may have caused the plaintiffs."[26] The court continued, "[i]f the defendant-directors believe that [the entities] should shoulder a portion of their liability, the defendant-directors may file a separate action for contribution against [them] in the domiciles of those entities."[27]

Contribution was addressed more directly in *Telecorp*,[28] where stockholders of Telecorp PCS, Inc. sued its directors and its controlling stockholder, AT&T Wireless Services, Inc. Shortly before trial, the plaintiffs settled with AT&T and the directors of Telecorp who were affiliated with AT&T, but the outside directors and their insurers refused to contribute. AT&T funded the settlement, mooting the trial, and then sought to amend its answer to assert cross-claims for contribution against the non-settling defendants. Vice Chancellor Strine permitted the claims to be asserted, accepting the parties' assumption that DUCATA applied to breaches of fiduciary duty, but expressly declining to rule on the issue.[29]

The Court of Chancery again found it unnecessary to confront the issue directly in *Valeant*.[30] Stockholder plaintiffs sued twelve directors of ICN Pharmaceuticals, Inc. for granting large cash bonuses to themselves and other corporate officers as part of a restructuring. After a change of control, the corporation realigned as plaintiff and took over the claims. All of the defendants except for a single insider settled, and the remaining insider asserted that in the event

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derivative claims challenging insurance agency agreements between AIG and C.V. Starr & Co., Inc., a corporation owned by Maurice R. Greenberg and other senior executives at AIG. The plaintiffs originally sued all of the directors of AIG, then settled with various outside and inside directors of AIG after Greenberg left the company. The suit continued against Greenberg and two senior executives who departed with him, and they sought to assert claims for contribution against the directors who settled. Greenberg and his co-defendants argued that their claims for contribution should be heard as part of the underlying action so as to preserve the possibility of disproportionate fault, which the language of DUCATA suggests can be adjudicated against co-defendants only in the underlying proceeding. Without resolving the question of what law applied, the Court of Chancery rejected the application for practical reasons, finding that it would be "an awkward, weird trial to have" in which Greenberg would be arguing for part of the trial that no one had done anything wrong and then for another part of the trial that the other directors had engaged in the wrongful conduct. *Id.* By contrast, if Greenberg prevailed, there would be no need for a contribution action. The court also noted that the outside directors who had settled would have potentially viable motions to dismiss any contribution claims. The court concluded that any contribution action should be brought, if at all, after the resolution of the underlying proceeding, with the possibility of disproportionate liability specifically preserved.

25. Grace Bros. Ltd. v. Uniholding Corp., 2000 WL 982401, at *16 (Del. Ch. July 12, 2000).

26. *Id*.

27. *Id*.

28. *In re* Telecorp PCS, Inc., 2003 WL 22901025 (Del. Ch. Nov. 19, 2003).

29. *Id*. at *1 n.1 ("The parties have assumed the applicability of [DUCATA] to breach of fiduciary duty claims and in the absence of a dispute, I have as well.").

30. Valeant Pharmaceuticals Int'l, Inc. v. Panic, 921 A.2d 732 (Del. Ch. 2007).

he was held liable, he could seek contribution under DUCATA from his fellow directors.[31] The company argued that a breach of fiduciary duty was not a tort and therefore no contribution was available under DUCATA.[32] After noting that the relevance of DUCATA was a question of first impression, Vice Chancellor Stephen P. Lamb held that contribution was not implicated because the plaintiffs sought to recover each director's *pro rata* share of the costs of a special litigation committee process and non-director bonuses: "Pro rata payments do not, of course, give rise to claims for contribution among persons who are jointly and severally liable for the same loss."[33] The plaintiffs also sought to cause an officer to disgorge his unfair profits, "an obligation that is not a joint liability."[34] The availability of contribution was thus not presented by the case.

The consistent theme running through these decisions is that contribution among directors is available, but none of the cases have addressed the origin, nature or extent of the obligation. The United States District Court for the Northern District of Illinois, however, held squarely that DUCATA governs claims for breach of fiduciary duty, reasoning that Delaware's General Assembly "did not adopt the provision of the Uniform Act which prohibits a contribution claim based upon the breach of a fiduciary duty."[35] The court found that "Delaware's failure to adopt that portion of the uniform act is deemed intentional."[36]

Unfortunately for the *Hollinger* court's analysis, the Delaware legislature adopted the original 1939 version of the Uniform Act in 1949. As discussed below, the 1939 version did not contain the provision prohibiting the act from applying to fiduciary obligations.[37] That language did not appear until the 1955 revision of the Uniform Act, well after the Delaware General Assembly had considered and adopted DUCATA. *Hollinger*'s rationale that the provision was intentionally rejected is thus temporally impossible and unpersuasive. Existing precedent leaves open the core issue of whether DUCATA applies to breach of fiduciary duty claims.

III. WHAT IS THE SCOPE OF DUCATA?

As statutes go, DUCATA is short. It consists of eight sections, seven of which are substantive.[38]

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31. Valeant Pharmaceuticals Int'l v. Panic, Def. Jerney's Supp. Post Trial Br., 2006 DE Ch. Ct. Briefs LEXIS 89 (Dec. 1, 2006); Valeant Pharmaceuticals Int'l v. Panic, Plaintiff's Supp. Br. on Contribution and Damages, 2006 DE Ch. Ct. Briefs LEXIS 88 (Dec. 1, 2006).

32. Plaintiff's Supp. Br., 2006 DE Ch. Ct. Briefs LEXIS 88, at *5 (citing Cede & Co. v. Technicolor, Inc., 634 A.2d 345, 370 (Del. 1993); Prod. Res. Group v. NCT Group, Inc., 863 A.2d 772, 801 & n.88 (Del. Ch. 2004); IM2 Merchandising & Mfg. v. Tirex Corp., 2000 WL 1664168, at *6 (Del. Ch. Nov. 2, 2000); Clark v. Teveen Holding Co., Inc., 625 A.2d 869, 877 (Del. Ch. 1992)).

33. 921 A.2d at 753 n.48.

34. *Id.*

35. Hollinger Int'l v. Hollinger, Inc., 2006 WL 1444916 (N.D. Ill. Jan. 25, 2006).

36. *Id*. at *2.

37. *See infra* Part IV.

38. Del. Code Ann. tit. 10, §§ 6301-08. So short is the statute that we reproduce it here in its entirety:

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Section 6302 establishes the fundamental purpose of DUCATA, providing that "[t]he right of contribution exists among joint tort-feasors."[39] Section 6301 in turn defines "joint tort-feasors" as "2 or more persons jointly or severally

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§ 6301. Definition

For the purposes of this chapter, "joint tort-feasors" means 2 or more persons jointly or severally liable in tort for the same injury to person or property, whether or not judgment has been recovered against all or some of them.

§ 6302. Right of contribution; accrual; pro rata share

(a) The right of contribution exists among joint tort-feasors.
(b) A joint tort-feasor is not entitled to a money judgment for contribution until he or she has by payment discharged the common liability or has paid more than his or her pro rata share thereof.
(c) A joint tort-feasor who enters into a settlement with the injured person is not entitled to recover contribution from another joint tort-feasor whose liability to the injured person is not extinguished by the settlement.
(d) When there is such a disproportion of fault among joint tort-feasors as to render inequitable an equal distribution among them of the common liability by contribution, the relative degrees of fault of the joint tort-feasors shall be considered in determining their pro rata shares.

§ 6303. Judgment against one tort-feasor

The recovery of a judgment by the injured person against one joint tort-feasor does not discharge the other joint tort-feasors.

§ 6304. Release of one joint tort-feasor

(a) A release by the injured person of one joint tort-feasor, whether before or after judgment, does not discharge the other tort-feasor unless the release so provides; but reduces the claim against the other tort-feasors in the amount of the consideration paid for the release, or in any amount or proportion by which the release provides that the total claim shall be reduced, if greater than the consideration paid.
(b) A release by the injured person of one joint tort-feasor does not relieve the one joint tort-feasor from liability to make contribution to another joint tort-feasor unless the release is given before the right of the other tort-feasor to secure a money judgment for contribution has accrued, and provides for a reduction, to the extent of the pro rata share of the released tort-feasor, of the injured person's damages recoverable against all the other tort-feasors.

§ 6305. Indemnity

This chapter does not impair any right of indemnity under existing law.

§ 6306. Third-party practice

(a) Third-party practice under this chapter shall be as provided by rule of court except as provided in this section.
(b) A pleader may either (1) state as a cross-claim against a coparty any claim that the coparty is or may be liable to the cross-claimant for all or part of a claim asserted in the action against the cross-claimant; or (2) move for judgment for contribution against any other joint judgment debtor, where in a single action a judgment has been entered against joint tort-feasors one of whom has discharged the judgment by payment or has paid more than his or her pro rata share thereof. If relief can be obtained as provided in this subsection no independent action shall be maintained to enforce the claim for contribution.
(c) The court may render such judgments, one or more in number, as may be suitable under the provisions of this chapter.
(d) As among joint tort-feasors against whom a judgment has been entered in a single action, subsection (d) of § 6302 of this title applies only if the issue of proportionate fault is litigated between them by cross-complaint in that action.

§ 6307. Uniformity of interpretation

This chapter shall be so interpreted and construed as to effectuate its general purpose to make uniform the law of those states that enact it.

§ 6308. Short title

This chapter may be cited as the "Uniform Contribution Among Tort-Feasors Law."

39. Del. Code Ann. tit. 10, § 6302.

liable in tort for the same injury to person or property, whether or not judgment has been recovered against some or all of them."[40]

Through this simple language, DUCATA effected drastic changes in the common law of contribution.[41] Most significantly, Section 6302(a) expressly permitted contribution between tortfeasors, a result which one Delaware court described as a "startling change."[42] As described above, prior to DUCATA, and consistent with the American courts' broad application of *Merryweather v. Nixan*, Delaware declined to recognize any right of contribution among tortfeasors, regardless of the degree of culpability involved.[43]

What DUCATA did not do was specify whether individuals who breached their fiduciary duties were "joint tortfeasors" for purposes of the act. As is typical for a Delaware statute, there is no legislative history to shed light on the scope of the term. Section 6307 of the act states only that "This chapter shall be so interpreted and construed as to effectuate its general purpose to make uniform the law of those states that enact it."[44] Without clear statutory language or Delaware legislative history, we turn to the drafting history of the Uniform Act upon which DUCATA was based to determine its intended scope.

IV. FIDUCIARY DUTIES AND THE UNIFORM ACT

The drafters of the Uniform Act intended to work significant change in the law and discussed many topics during their labors. We, however, are interested only in whether they intended for claims for breach of fiduciary duty to be treated as torts within the meaning of the Uniform Act. Unfortunately, the historical evidence on that point is muted and conflicting.

A. The 1939 Uniform Act Includes Equitable Torts By Refusing To Exclude Them

By the mid-1930s, academic scholarship was highly critical of the American rule against contribution among tortfeasors. Attempting to accelerate the death of the rule, the American Law Institute and the National Conference of Commissioners on Uniform State Laws agreed in the spring of 1935 to cooperate in drafting a uniform act to help guide the law's development.[45] As advisors, the ALI selected Harvard torts professor Warren Abner Seavey, Columbia torts profes-

40. *Id.* at § 6301. Whether another person is a "joint tortfeasor" within the meaning of DUCATA requires a finding by the trier of fact or an admission by the defendant. *See, e.g.*, Med. Ctr. of Del., Inc. v. Mullins, 637 A.2d 6, 9 (Del. 1994); Ferguson v. Davis, 102 A.2d 707, 708 (Del. Super. Ct. 1954).

41. Other major changes arising from DUCATA included (1) allowing contribution among both intentional and negligent tortfeasors, Section 6302(a); allowing defendants who caused more harm to be disproportionately liable, as opposed to the common law's strict pro rata rule, Section 6302(d); and allowing a plaintiff to settle with one tortfeasor without releasing all of the tortfeasors, in contravention of the common law rule, Section 6304(a).

42. Clark v. Brooks, 377 A.2d 365, 368 (Del. Super. Ct. 1977) ("The most startling change made by the Act was to provide a remedy of contribution among tortfeasors.").

43. DiStefano v. Lamborn, 81 A.2d 675, 677-78 (Del. Super. Ct. 1951), *disapproved on other grounds*, Halifax Chick Express, Inc. v. Young, 50 Del. 596 (1958).

44. Del. Code Ann. tit. 10, § 6307.

45. *Contribution Among Tortfeasors Act: Tentative Draft No. 1* (American Law Institute), Mar. 31, 1938, at 3 ("First Tentative Draft").

sor Young B. Smith, and Edward S. Thurston, a contracts scholar at Yale.[46] The National Conference of Commissioners chose the Dean of the University of Illinois College of Law, Albert J. Harno, as its advisor, and both groups "united in the selection" of Professor Charles O. Gregory as reporter.[47] Professor Gregory was an expert on labor and tort law and had authored the definitive text on that subject.[48]

Professor Gregory prepared an initial report which the "joint committee almost demolished."[49] Several preliminary drafts were subsequently created for discussion at a meeting in February 1938, and the result was a "first tentative draft" of a uniform act.[50]

As one might expect, the vast majority of the discussion relating to the first tentative draft addressed the significant changes it made in the common law. Lengthy deliberations concerned topics such as the efficiency of trying claims for contribution along with the main liability action[51] and whether contribution should extend to intentional tortfeasors.[52] The first tentative draft was held for further consideration at the 1938 meeting of the National Conference of Commissioners.[53]

At the 1938 meeting of the American Law Institute, Professor Gregory and Judge Learned Hand had a brief exchange on the topic of what constituted a tort:

> MR. GREGORY: The common law view is that there is no contribution among tortfeasors at all, and it is a decided change in substantive law.
>
> JUDGE LEARNED HAND: Is there any definition whatever of the kind of tort?
>
> MR. GREGORY: None at all. That is left completely open.
>
> JUDGE HAND: Are you sure that is desirable?

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46. *Id.*

47. *Id.*; *Handbook of the National Conference of Commissioners on Uniform State Laws and Proceedings of the Forty-Seventh Annual Conference* 136 (1937) ("1937 Proceedings").

48. Charles Oscar Gregory, Labor and the Law (1961).

49. 1937 Proceedings, *supra* note 47, at 136.

50. First Tentative Draft, *supra* note 45, at 3.

51. *Id.* at 29.

52. *Id.* at 20-21. The joint committee noted that in some jurisdictions, the rule was more complex, with the right of contribution "confined to tortfeasors who were 'passively' negligent or who qualified as 'joint tortfeasors' under some rather narrow local rule defining that phrase, and denied to tortfeasors who were 'actively' negligent or who were 'negligent' because of the inadvertent breach of some safety statute or who were liable for their own negligence and not merely vicariously liable for another's tort." *Id*. at 20. The joint committee regarded a broad rule as "an attempt to be practical" and "a repudiation of the moral note which has always made the common-law rule seem so unreal." *Id*. at 21.

53. *Handbook of the National Conference of Commissioners on Uniform State Laws and Proceedings of the Forty-Eighth Annual Conference* 188, 392 (1938) ("1938 Proceedings"); *Contribution Among Tortfeasors Act: Proposed Final Draft No. 1* (American Law Institute), Apr. 24, 1939, at 3 ("Proposed Final Draft").

> MR. GREGORY: Not at all sure. The matter was debated for a long time in drafting the Act, and we finally concluded, in view of the fact that one could not find any specific way to draw a meaningful line, that the whole thing should be left open.[54]

Mr. Charles V. Imlay, a prominent practitioner from Washington D.C., then expressed his continuing discomfort with contribution for intentional torts, but stated that "we are all agreed that in defining for the first time the principle of contribution we want it to go at least as far as we admit it is equitable it should go."[55] Mr. Imlay next brought up a recent case involving "one of the most striking illustrations of the case where it is fair to have contribution":

> MR. IMLAY: Within the last few weeks a decision has been rendered in this District making a group of eighteen bank directors liable. The liability cannot be said to be a case of a malicious tort. Nobody contends that. The liability arose out of the fact that the corporation organized under the Alabama law, Mr. Sims, continued after its charter had expired and the directors were held liable as liquidating trustees for what assets were in their hands at the time of the expiration of the charter and nobody contends that it was malicious and I am not sure that anybody can contend it was negligent.
>
> MR. PEPPER: Was it a tort at all?
>
> MR. IMLAY: These eighteen directors – and to relieve your minds I will tell you I am not one of them – these eighteen directors were acting as directors usually do through their agents and relying upon statements made by certified public accountants and it would be very difficult to say they were negligent and yet the liability is a tortious liability.[56]

Mr. Imlay suggested that if the ALI or the National Conference chose to limit the definition of a tort, it should adopt the "distinction that is made in the Bankruptcy Act" which discharged all liabilities "except a malicious tort."[57] Another participant suggested "simply excluding anything which is defined as a crime."[58]

If adopted, these positions would have gone a long way toward reinstating the distinction between intentional and negligent torts that the first portion of the act was meant to abolish. Professor Gregory, continuing to battle for the broadest application of the proposed statute, asked:

> How about breach of statutes? A great many cases of inadvertent breaches of statute are crimes but are treated as negligence. I think it would be highly unfortunate to exclude these cases from the operation of the act. There is a division of opinion among the states, where they do have contribution, on that very point.[59]

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54. 15 *American Law Institute Proceedings* 356 (1938) ("1938 ALI Proceedings").

55. *Id.* at 357-58.

56. *Id*. at 358-59. We believe this statement refers to the trial court decision in *Tenison v. Wilson*, 151 S.W.2d 327 (Tex. Civ. App. 1941), although that case involved seven directors and eighteen stockholders. The finding that the directors were liable was overturned on appeal.

57. 1938 ALI Proceedings at 358.

58. *Id.*

59. *Id*. at 359.

In assembling the final draft, the question of whether tort-like claims would fall under the statute arose.[60] At the 1939 meeting of the American Law Institute committee, Philip Halpern (then a torts professor at the University of Buffalo) inquired whether contribution would be available in cases where a second tortfeasor "by reason of his relationship to the person injured would not be liable to the person injured," referring specifically to workers' compensation cases.[61] He envisioned a situation in which an employee was injured in a traffic accident while on the job. The driver of the other car might be liable for the employee's injuries as a tortfeasor, but the employer would not be jointly liable, because workers' compensation would cover the employee and pre-empt a tort claim against the employer. Mr. Halpern suggested that additional language be added to clarify that contribution was available when the tortfeasor was liable for a judgment, rather than simply liable in tort.[62] Professor Gregory rejected this suggestion, replying that such an approach "would be very unfortunate because there is such a thing now known as the equitable tort and we feel courts should be left free to permit contribution in such cases."[63]

The 1939 Act, in final form, sought to aid the "recent trend toward legislative and judicial repeal or modification of the common-law rule" by providing a uniform act states could adopt if they wished that would overturn the "policy of Anglo-American common law … to deny assistance to tortfeasors on the understanding that they are wrongdoers and hence not deserving of the aid of courts in achieving equal or proportionate distribution of the common burden."[64] The 1939 Act ultimately did not define the term "joint tortfeasors," thereby excluding nothing and following Professor Gregory's approach with respect to "equitable torts." Equitable torts fall within the scope of the 1939 Act because they are not excluded.

B. Delaware Adopts The 1939 Uniform Act With Modifications

In 1949, Delaware adopted the Uniform Contribution Among Tortfeasors Act, principally in the form that had been approved by the National Conference of Commissioners in 1939.[65] The General Assembly adopted the first

60. Proposed Final Draft at 3.

61. 16 *American Law Institute Proceedings* 353 (1939) ("ALI 1939 Proceedings").

62. *Id.* at 351-53.

63. *Id*. at 354 ("We have discussed this point and my Advisers and I all agreed that we might well follow equity but for the juridical statements on this very point to the effect that since there is no tort liability at all as between certain persons, therefore, there is no tort as between them and that the Compensation Acts involve a statutory liability rather than a tort liability. I think we might in the interests of clarity on this point cause considerable harm in other directions. I would prefer, unless there is any strong feeling on it, to leave it as it is."). The group agreed to expand the commentary accompanying the uniform law to make clear its position on workers' compensation. *Id.*

64. Unif. Contr. Among Tortfeasors Act, 12 U.L.A. 196 (1976) ("As an original proposition, all might agree that courts should not lend their aid to rascals in adjusting differences among them. But all tortfeasors are not rascals, in spite of the literal translation of the term as wrongdoers. Most joint and several tort liability results from inadvertently caused damage, although it is almost impossible to draw a practical line between torts of inadvertence and others. It is, then, somewhat ironic to note that at common law contribution was denied among all tortfeasors and is allowed as a matter of course to one who has deliberately chosen to violate a contractual obligation undertaken with others. And this situation is aggravated by the common-law view that the injured person is 'lord of his action' and, when injured by the joint and several tort of two or more, may place the loss where and how he sees fit.").

65. 47 Del. Laws 151 (1949); 12 U.L.A. 193 (1976).

six sections and the final three sections of the Uniform Act as proposed by the commissioners.[66] The General Assembly modified the "third party practice" section of the law, providing that "third party practice … shall be as provided by rule of court," with certain exceptions.[67] The Delaware version did *not* provide for the serving of a third-party complaint (although Delaware had already adopted a version of the federal rules, which permitted that practice).[68] The Delaware version also modified the 1939 Act by permitting the defendant to "move for judgment for contribution" only against "any other joint judgment defendant," a view contrary to the recommendation of the National Conference of Commissioners on Uniform State Laws.[69] But there is no evidence that the Delaware legislature considered the application of DUCATA to breaches of fiduciary duty.

C. The 1955 Uniform Act Specifically Excludes Breaches Of Fiduciary Duty, As Equitable Torts, From Its Scope

The 1939 Act was adopted by Arkansas, Delaware, Hawaii, Maryland, New Mexico, Pennsylvania, Rhode Island and South Dakota, although the commissioners lamented that "[m]ost of these states have made important changes in the act which have defeated the whole idea of uniformity, and in anything like its original form it is now in effect only in Arkansas, Hawaii and South Dakota."[70] Due to this frustrating circumstance and "unfavorable reports as to the progress

66. The first six sections provided the substance of liability for contribution, while the final three sections provided for severability in the event some portion was found unconstitutional, applicability of the law of other states enacting the uniform law to interpret its meaning, and a short title.

67. 47 Del. Laws 151 (1949); Del. Code Ann. tit. 10, § 6301 ("(1) A pleader may either (a) state as a cross-claim against a co-party any claim that the co-party is or may be liable to the cross-claimant for all or part of a claim asserted in the action against the cross-claimant; or (b) move for judgment for contribution against any other joint judgment debtor, where in a single action a judgment has been entered against joint tortfeasors, one of whom has discharged the judgment by payment or has paid more than his pro rata share thereof. If relief can be obtained as provided in this subsection no independent action shall be maintained to enforce the claim for contribution. (2) The court may render such judgments, one or more in number, as may be suitable under the provisions of this Act. (3) As among joint tortfeasors against whom a judgment has been entered in a single action, the provisions of Section 2, Subsection (4) of this Act apply only if the issue of proportionate fault is litigated between them by cross-complaint in that action."). Section 2, subsection 4 reads: "When there is such a disproportion of fault among joint tortfeasors as to render inequitable an equal distribution among them of the common liability by contribution, the relative degrees of fault of the joint tortfeasors shall be considered in determining their pro rata shares."

68. Daniel L. Hermann, *New Rules of Procedure in Delaware*, 18 F.R.D. 327 (1956).

69. In promulgating the 1939 draft, the commissioners noted regretfully that the legislatures in six states only allowed contribution among tortfeasors subject to a joint judgment, thereby "leaving to the injured person control of the distribution of loss through contribution" because the plaintiff "cannot be compelled to take judgment against tortfeasors whom he does not wish to sue." 12 U.L.A. 196. The prefatory note to the commissioners' 1955 revision observed that eight states had contribution statutes not based upon the Uniform Act, regrettably "limited in their effect to contribution between joint judgment defendants" (Michigan, Mississippi, Missouri, New York, North Carolina, Texas & West Virginia), and that "[t]o this list should now be added Delaware, which has amended the 1939 act to limit it in this manner." 12 U.L.A. at 195; *National Conference of Commissioners on Uniform State Laws, Proceedings in the Committee of the Whole, Uniform Contribution Among Tortfeasors Act 3* (Aug. 18, 1955) ("1955 Notes of Proceedings") ("That, of course, as was so effectively pointed out in the introductory comment to the 1939 Act, put it entirely within the hands of the plaintiff to determine in what situations there should be contribution because the failure to sue, the failure to get a judgment, of course, made it possible for the principle of contribution to apply except as to those against whom a judgment was rendered.").

70. 12 U.L.A. 195.

and operation of the act, the commissioners withdrew it for further study and revision."[71] This revision committee was chaired by Kansas District Judge Spencer A. Gard, who also chaired the committee on Uniform Rules of Evidence.[72] Delaware never adopted the 1955 revision. Again, we concentrate only on the discussion related to including breaches of fiduciary duty within the scope of the revised act.

The most significant comment on that topic was made by George Gleason Bogert, Professor of Law at the University of Chicago Law School, member of the drafting committee for the *Restatement of Trusts* and author of *Bogert's Trusts and Trustees*. He inquired whether:

> [the Uniform Act] was intended to cover breaches of trust and other fiduciary relations which are sometimes called loosely equitable torts? There is a body of law, as I understand it, established that there is a right to have contribution between persons who commit joint breaches of trust, and I would rather suppose that your intention was to have this Act cover legal causes of action. Is that clear, do you think, in the Act?[73]

Chairman Gard replied that he was "not certain that anybody has considered that particular question," but that "if it falls in the category of a tort, it is covered. We have not defined what a tort is."[74]

Mr. Bogert thought the matter worthy of "rather serious consideration" due to the existing body of law "with regard to breaches of fiduciary relations, and it seems to me the situation isn't the same as it is with regard to legal causes of action like actions for negligence."[75] Mr. Bogert strongly believed that the Uniform Act should make explicit that wrongs by fiduciaries were outside its scope:

> MR. BOGERT: I think this matter that I raised about so-called equitable torts, breaches of trust and other fiduciary relations is of sufficient importance so that it should be settled one way or another and made clear, because otherwise it is going to involve litigation as to whether that is left to the courts of equity or whether it is covered by this Act, and for the purpose of getting the judgment of the meeting, I would like to move that the Act be framed so that it be made clear that the word "tort" does not include breaches of trust or other fiduciary relations.
>
> CHAIRMAN COE: Breaches of trust or breaches of other fiduciary relations?
>
> MR. BOGERT: Yes. Those are called, very loosely, equitable torts, but I don't think they really are, strictly speaking, torts, and it seems to me there is a body of law developed with regard to that subject entirely

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71. *Id*. The principal concerns giving rise to the 1955 amendments were (1) the 1939 act's failure to exempt intentional wrongdoers from the right to contribution; (2) the lack of a statute of limitations on the contribution action; (3) the 1939 act's allowing consideration of comparative fault in setting defendants' liability; (4) a belief that the initial act had the effect of discouraging voluntary settlements; and (5) general discontent with the third-party procedure provisions of the act. 1955 Notes of Proceedings at 4-5.

72. *Id.* The other members of the committee were Otis S. Allen, of Topeka, Kansas, George H. Hafer of Harrisburg, Pennsylvania, Nathaniel M. Haskell of Portland, Maine, Homer B. Harris of Lincoln, Illinois, Blakey Helm of Louisville, Kentucky, Miller Manier of Nashville, Tennessee, and Godfrey L. Munter, of Washington, D.C.

73. 1955 Notes of Proceedings at 8.

74. *Id.*

75. *Id.*

different from the body of law with regard to torts that can be brought into a court of law, and that it would be unfortunate to do away with that existing and satisfactory body of equitable principles.[76]

Later in the meeting, Professor Bogert suggested that the revised act contain a subparagraph (g) to section 1, reading "This act does not apply to breaches of trust or other fiduciary relationships."[77] Mr. Hicks Epton of Oklahoma (most famous as the founder of Law Day) stated that the "language is not essential to the draft. Nevertheless, we feel that it certainly would be helpful in spelling it out, that we do not intend to include that sort of thing."[78] Chairman Gard concurred, along with Karl Llewellyn, whose only suggestion was that the word "of" be included after the word "or."[79] The note accompanying subsection (g) in the final draft of the 1955 Act reads only "The meaning is clear. It is not intended that the act should extend to liabilities arising out of breaches of fiduciary relationships."[80] Thus the 1955 Act did not include any breaches of fiduciary duty within its scope.

D. Breaches Of Fiduciary Duty, As Equitable Torts, Were Included In The 1939 Act And Excluded From The 1955 Act Due To Conflicting Assumptions

The 1939 Act swept broadly and sought to include breaches of fiduciary duty within its coverage on the premise that contribution otherwise was not was available. The 1955 Act proceeded from the opposite premise — namely, that there was an existing common law right to contribution for breaches of fiduciary duty. The 1955 Act therefore included a provision excluding these issues from its coverage to avoid interfering with existing rights. Both acts contemplated that contribution would be available for fiduciary relationships; they differed only over whether the right would arise under the Uniform Act or from common law principles. Thus contribution was intended to exist for breaches of fiduciary duty, either by statute (under the 1939 Act) or under the common law (under the 1955 Act).[81]

V. THERE WAS A LIMITED RIGHT OF CONTRIBUTION AMONG DIRECTORS FOR BREACH OF FIDUCIARY DUTY AT COMMON LAW

It is clear that the common law recognized a right of contribution among directors for some breaches of fiduciary duty.[82] This right, however, was uncertain and limited. Professor Bogert was correct in his understanding of the broader

76. *Id.* at 11.

77. *Id.* at 35.

78. *Id.* Mr. Epton was appointed the "Chairman" of the committee as to Subsection F.

79. *Id.* at 35-36.

80. Unif. Contr. Among Tortfeasors Act § 1, cmt. to subsection (g), 12 U.L.A. 204 (1976).

81. It thus should be clear that the failure of DUCATA to include Section 1(g) of the 1955 Act, which provides that [t]his act does not apply to breaches of trust or of other fiduciary relationships," cannot be interpreted as a conscious decision by the Delaware General Assembly to exclude fiduciary relationships from the scope of the act. The language did not appear in the 1939 Act that the Delaware legislature adopted in 1949, and thus the Hollinger court was wrong to infer anything from its absence.

82. Early cases involving director contribution did not involve breaches of fiduciary duty, but rather instances where directors bound "themselves for [the corporation's] benefit on the same obligation," as when "directors become the makers and endorsers

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availability of contribution for breaches of fiduciary duty by trustees, which was a far more developed and sophisticated system. Although the liability of directors to a corporation was originally grounded in analogies to trust law, it has over time become settled that the obligations of a director are "*sui generis*."[83]

The seminal decision confronting the puzzle of contribution for breaches of fiduciary duty by directors was Lord Hardwicke's 1742 ruling in *Charitable Corporation v. Sutton*.[84] Lord Hardwicke rejected the idea that each director only could be held liable for his own actions, and not those of his fellow directors, because "if this doctrine should prevail, it is indeed *laying the axe to the root of the tree.*"[85] Lord Hardwicke wrote, "I will never determine that frauds of this kind are out of the reach of courts of law or equity, for an intolerable grievance would follow from such a determination." [86]

After grounding directorial liability in trust law, Lord Hardwicke next required directors to "make good" losses paid by fellow directors: that is, he recognized a right to contribution.[87] As interpreted by Henry Osborn Taylor, the author of a leading early twentieth century treatise on corporations, the logic of Lord Hardwicke's rule "must end in allowing contribution or indemnification of directors and other officers of a corporation."[88] Taylor did not believe, however, that the directors who were personally involved in the wrongdoing could seek contribution from their fellow directors.[89]

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of a note to raise money for the corporation." Henry O. Taylor, A Treatise on the Law of Private Corporations Having Capital Stock §§ 805-06 (1884) (distinguishing that situation from common failure to file an annual report, where contribution would not be allowed). Even when there was no express agreement between the directors that they would be jointly liable for the loan amount, courts held that because the money was obtained for the furtherance of the company, all of the directors were "in the nature of sureties for the company" and "there existed between them a mutual responsibility in case of loss" that gave rise to "[t]he principle of contribution." Slaymaker v. Gundacker's Executors, 10 Serg. & Rawle 75, 1823 WL 2206, at *7 (Pa. 1823); *see also* Peoples Nat. Bank of Souderton v. Onorato, 63 Pa. D & C. 2d 485 (Pa. Com. Pl. 1972); Fix v. Isaacs' Adm'rs, 60 S.W. 2d 986 (Ky. 1933); Holston v. Haley, 135 A. 98 (Me. 1926); Aldrich v. Rowell, 166 N.W. 89 (Iowa 1918); Hall v. Gleason, 166 S.W. 608 (Ky. Ct. App. 1914); Weeks v. Parsons, 58 N.E. 157 (Mass. 1900); Middleton v. McCartee, 2 Mackey 420, 1883 WL 20227 (D.C. 1883).

83. The source of directors' fiduciary duties wavered between agency law and trust law, before finally settling on the "*sui generis*" description. *See* Henry Winthrop Ballantine, *Questions of Policy in Drafting a Modern Corporation Law*, 19 Cal. L. Rev. 465, 476 (1931) ("The practice of calling directors 'trustees' and subjecting them to the strict and rigorous rules which apply to dealings between a trustee and his beneficiary requires some modification. Directors must be held to reasonable limitations of fiduciary duty, but there is a distinct policy in favor of upholding contracts made by directors even though they may be interested on their own behalf or on behalf of another corporation if such contracts are just and reasonable."); *see also* Rudolph E. Uhlman, *The Legal Status of Corporate Directors*, 19 B.U. L. Rev. 12 (1939); Sveinbjorn Johnson, *Corporate Directors as Trustees in Illinois*, 23 Ill. L. Rev. 653 (1928). Delaware has a particularly strong tradition of analogizing directors' fiduciary duties to those of trustees. *See infra* note 151. The fiduciary duties of officers arise out of agency law. Lyman P.Q. Johnson & David Millon, *Recalling Why Corporate Officers are Fiduciaries*, 46 Wm. & Mary L. Rev. 1597 (2005).

84. 26 Eng. Rep. 642 (1742).

85. *Id*. at 645 (emphasis in original). Lord Hardwicke concluded that directors could be "guilty of acts of commission or omission, of mal-feasance or non-feasance." *Id*. at 644. Neglect of duty (non-feasance) by allowing others to "intirely" manage the corporation would make the director guilty of the "breaches of trust that are committed by others." *Id*.

86. *Id*.

87. According to Lord Hardwicke, those directors who "engaged in that confederacy are certainly liable to make up the losses which the corporation have sustained in the first place, and the committee-men [directors] who were not partners in this affair are liable in the second place only." *Id*.

88. Taylor, A Treatise on the Law of Private Corporations, *supra* note 82, at § 803.

89. *Id.* According to Taylor,

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Another early twentieth century treatise on corporations authored by Seymour D. Thompson and Joseph W. Thompson also spoke to the issue of contribution. The Thompson treatise likewise stated that "[d]irectors are not responsible for losses resulting from the wrongful acts or omissions of other directors, unless the losses are a consequence of their own neglect of duties."[90] The Thompson treatise further supported the notion that those directors who were not directly involved in the wrongdoing were entitled to contribution from each other so as to share equally in the loss.[91]

Echoing Lord Hardwicke, the Thompson treatise noted a distinction between acts "which involve bad motive or moral turpitude" and "those which consist of mere negligence or non-feasance."[92] As the treatise explained, "[i]t is universally conceded as already stated, that as to the first class there can be no contribution; but in the latter class, there may be."[93] American courts appear to have generally followed this distinction between misfeasance and non-feasance, although one nineteenth century commentator argued that contribution should be available when directors inadvertently violated a statute that imposed personal liability among them.[94]

The right of directors to contribution at common law was thus limited and unclear. Although its exact scope differed from jurisdiction to jurisdiction, it was frequently available only to those directors who did not participate in a decision or course of action, and courts would freely impute knowledge to directors to bar contribution claims. Directors who participated in (or knew about) the events giving rise to liability could not obtain contribution.

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A rule for such cases might perhaps be stated thus: If Directors A, B, C and D are held liable for the wrongful act of Director E, with which there was no way concerned, either actively or by connivance, they will have the right as against E to complete indemnification; and if one of their number, as for instance A, has been forced to pay all or more than his proportion then his proportion of the loss arising from the wrongful act, he will be, as against B, C and D, entitled to contribution.

Id. at 792.

90. 2 Seymour D. Thompson and Joseph W. Thompson, Commentaries on the Law of Corporations 939 (3d ed. 1927).

91. *Id*. at 936-37 ("There may be cases which hold that an absent director will not be liable for affirmative acts done by the remaining members of the board in his absence; but for losses occasioned by the negligent conduct of directors and found to properly supervise, examine, and inquire into the affairs of the corporation, it is obvious that no single director could escape liability.").

92. *Id*. at 1055.

93. *Id*.

94. Frederic C. Woodward, *When Contribution Between Joint Wrong-Doers May Be Enforced*, 1 N.Y. L. Rev. 115, 121 (1895) ("Even though such persons, as a result of negligence or a misapprehension of rights, have committed a tort, they cannot with any pretence of justice, or upon any possible ground of public policy, be denied their appeal to the courts to adjust their liability fairly as between each other …. If the directors of a corporation, by mere inadvertent omission, from forgetfulness or otherwise, with no intention of violating the law, fail to make and file the required annual report, they may in the eye of the law be joint tort-feasors. But they are not guilty of conscious or willful wrong-doing and are therefore clearly entitled to contribution."). Another author argued that if all the potential defendants had "certain continuing duties, and the injury results from an omission to act on the part of all" then "contribution may be had." Comment, *Indemnity and Contribution Between Joint Tort Feasors*, 34 Yale L.J. 427, 431 (1925). In an 1885 decision, Widrig & Co. v. Newport St. Ry. Co., 1885 WL 5744 (Ky. Ct. App. Jan. 8, 1885), the Court of Appeals of Kentucky suggested that contribution could be available even for directors who had engaged in misfeasance. This case appears to be an exception, and the general rule appears to have been that "No contribution can be enforced among directors guilty of a breach of trust for which a part are held liable." 3 William W. Cook, A Treatise on the Law of Corporations Having a Capital Stock § 749 (8th ed. 1923).

The abbreviated right to contribution among directors contrasts with the ability of a trustee to obtain contribution — and the latter is likely what Professor Bogert was referencing during the debates on the 1955 Act. Under the law of trusts, when two trustees are liable to the beneficiary for a breach of trust, each is generally entitled to contribution from the other.[95] If one trustee is "substantially more at fault than the other," then he is not entitled to contribution and instead must indemnify the other trustee.[96] Professor Bogert wrote in 1946 that "The trustee who is obliged to pay more than his proportionate share of the damage may have a cause of action for contribution against his cotrustees who are equally or more guilty than he."[97] If the trustee held liable "was guilty of less fault than the other trustee, or committed only a technical breach of trust, he may claim from the active violator of the trust … indemnity."[98]

The common law rules of contribution as applied to trustees thus did not principally rely on concepts of malfeasance or nonfeasance, but instead on relative fault.[99] The right of contribution generally existed for breaches of the duty of care. It even existed for some conflict transactions and breaches of the duty of loyalty not involving bad faith.[100] It thus made sense for Professor Bogert and the drafters of the 1955 revision of the Uniform Act to defer to the common law system of contribution that had developed for trustees. The same cannot be said for the common law of contribution among directors. Although a right of contribution existed, it was not the type of well-developed body of law that Professor Bogert sought to leave intact. It rather resembled more closely the largely ineffective and potentially unfair set of principles that Professor Gregory and the drafters of the 1939 Act sought to replace.

VI. RECALLING THE CONCEPT OF THE EQUITABLE TORT

The concept of the "equitable tort" provides a unifying theme for the limited discussions of breaches of fiduciary duty that preceded both the 1939 Act and the 1955 revision. The 1939 and 1955 drafters had different assumptions about the extent to which the common law provided a right of contribution for "equitable torts," but they both used the term. We believe this relatively antiquated notion has particular explanatory power for understanding the different approaches taken by the drafters of Uniform Act and for comprehending the interplay between DUCATA and Delaware's treatment of claims for breach of fiduciary duty.

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95. Restatement (Second) of Trusts § 258.

96. *Id.*

97. George Gleason Bogert, Bogert's Trusts and Trustees § 701 (1946).

98. *Id*.

99. Under comment d of the *Restatement*, the following factors are to be used in evaluating disproportionate fault:

> (1) whether [the trustee] fraudulently induced the other to join in the breach of trust; (2) whether he intentionally committed a breach of trust as the other was at most guilty of negligence; (3) whether because of his greater experience he controlled the conduct of the other … ; (4) whether he alone committed the breach of trust and the other is liable only because of an improper delegation, or failure to exercise reasonable care to prevent him from committing a breach of trust, or neglect to take proper steps to compel him to redress the breach of trust.

Restatement (Second) of Trusts § 258 cmt. d.

100. *See id*. cmt. f and illus. 5.

The notion of "equitable torts" appears to have fallen out of the collective memory. We find only seven uses of the term "equitable tort" in the Westlaw "allcases" database after 1945, and the phrase is almost uniformly used with quotation marks around it.[101] But prior to the merger of law and equity,[102] the proper characterization of a claim as "legal" or "equitable" was a question of some moment, because it determined whether the action was properly brought at law or in chancery. In a court of law, the claim generally would be tried to a jury with the remedy limited to money damages. In chancery, the claim would be tried before a judge — the chancellor — who could also grant equitable relief, including decrees ordering specific performance, rescission, reformation, or injunctions.

Within this system, a purely "equitable tort" was one that derived from a special relationship between one person and another, a definition that includes fiduciary relationships, and particularly the relationship between trustee and beneficiary.[103] Christopher Columbus Langdell, scholar and dean of the Harvard Law School distinguished legal rights from equitable rights as follows:

> [T]rue equitable rights, and true equitable wrongs, the latter being violations of equitable rights. A true equitable right is always derivative and dependent, i.e., it is derived from, and dependent upon, a legal right. A true equitable right exists when a legal right is held by its owner for the benefit of another person, either in whole or in part.[104]

That is, "[t]he liability is a peculiar one dependent entirely on the fiduciary relation … and is additional to the liability for torts which are independent of that relationship."[105] An early twentieth century treatise on corporate law cautioned that liability for an equitable tort such as breach of fiduciary duty "should not be confused with the ordinary rules of the

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101. *See, e.g.*, Hart Enters., Inc. v. Cheshire Sanitation, Inc., 1999 WL 33117189 (D. Me. Feb. 22, 1999) ("The defendants offer no authority to support their argument that a party cannot be liable for aiding and abetting the 'equitable tort' of breach of fiduciary duty, as opposed to other torts."). Several of these cases decline to decide whether an "equitable tort" is a tort within the meaning of the Federal Tort Claims Act. Gould v. United States, 2007 WL 2325177 (W.D. Va. 2007) ("To the extent that Plaintiff seeks to avoid the strictures of the Federal Tort Claims Act, he fails, because if equitable tort claims are truly distinct from common-law tort claims (which I do not decide), they would require their own waiver of sovereign immunity apart from the FTCA."); San Carlos Apache Tribe v. United States, 272 F. Supp. 2d 860, 883 n.13 (D. Ariz. 2003) (concluding the court need not address whether Federal Tort Claims Act provided the exclusive remedy for the equitable tort of nuisance); Land v. United States, 35 Fed. Cl. 345 (1996) (utilizing Federal Tort Claims Act case law to decide congressional reference case involving equitable torts).

102. This term refers to the period during which jurisdictions combined their separate courts of law and equity, or unified the separate dockets (or "sides") in jurisdictions where matters at law or in equity were heard by the same court. In the United States, the movement towards consolidation began in 1848 in New York with the adoption of a new code of civil procedure, championed by David Dudley Field, which sought to "revise, reform, simplify, and abridge" the practice and pleadings of the state's courts. Charles E. Clark, Law of Code Pleading § 7 (2d ed. 1947) (quoting N.Y. Const. art. 6, § 2 (1846)); *see also* Mildred V. Coe & Lewis W. Morse, *Chronology of the Development of the David Dudley Field Code*, 27 Cornell L.Q. 238 (1942). At the federal level, merger was accomplished in 1938 when the Federal Rules of Civil Procedure went into effect. *See generally* 4 Charles Alan Wright & Arthur R. Miller, Federal Practice & Procedure § 1042 (1995).

103. 1 Joseph Story, Commentaries on Equity Jurisprudence § 29 (1839) (observing that equity courts provide remedies for rights which "Courts of Common Law do not recognize at all, or if they do recognize them, they leave them wholly to the conscience and good will of the parties" such as trusts, which are "equitable estates").

104. C.C. Langdell, A Brief Survey of Equity Jurisdiction 5 (2d ed. 1908).

105. 1 Arthur W. Machen, A Treatise on the Modern Law of Corporations § 400 (1908) (describing the liability of promoters as fiduciaries).

common law as to liability for torts."[106] Courts historically characterized breaches of fiduciary duty by directors as falling within the narrow band of "equitable torts."[107]

The second category consisted of torts that could be sued upon either in equity or at law.[108] These "legal" torts, over which concurrent jurisdiction existed, were distinct from true "equitable" torts.[109] A plaintiff could assert a legal right in equity to obtain an adequate or more complete remedy, but the claim was still upon a legal right. It was not a "true equitable right" that when violated creates a "true equitable wrong."[110]

The first *Restatement of Agency*, the first *Restatement of Restitution*, and the first *Restatement of Torts*, all of which were being drafted at around the same time as the first Uniform Act, treated breaches of fiduciary duty as capable of being remedied either at law or in equity (and thus "legal" torts). The *Restatement (First) of Agency*, finalized in 1933, observed explicitly that for breaches of the duty of loyalty, the principal could maintain either a "bill to enforce a constructive trust" in equity or an action at law for the value of the things taken.[111] The *Restatement (First) of Restitution*, finalized in 1936, likewise viewed breaches of fiduciary duty as remediable at law or in equity.[112]

Section 874 of the first *Restatement of Torts*, completed in 1939, stated that "A person standing in a fiduciary relation with another is subject to liability to the other for harm resulting from a breach of duty imposed by such relation."[113] Comment b to § 874 confirmed that "[a] fiduciary who commits a breach of his duty as a fiduciary is guilty of

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106. *Id.*; *see also* George P. Costigan, Jr., *Trusts Based on Oral Promises To Hold In Trust, To Covey, Or To Devise, Made By Voluntary Grantees*, 12 MICH. L. REV. 423, 431 (1914) (suggesting that for a breach of trust, equity "may recognize an equitable tort, i.e., a tort remediable only in equity, regardless of the fact that there is no corresponding legal tort").

107. Wood v. Perkins, 57 F. 258, 260 (D. Mass. 1893) (suit for breach of duty in joint venture was cognizable in equity because co-venturer who breached agreement was "an equitable tort feasor"); Moseley v. Briggs Realty Co., 69 N.E.2d 7, 10 (Mass. 1946) (describing suit for wrongful payment of dividends as falling within "the class of equitable 'actions of tort'"); Old Dominion Copper Mining & Smelting Co. v. Bigelow, 74 N.E. 653, 659 (Mass. 1905) (claim for breach of fiduciary duty against promoter of corporation was an "equitable tort").

108. *See* H. GERALD CHAPIN, HANDBOOK OF THE LAW OF TORTS § 13 (1917) (stating that any wrong remediable by damages is a tort, even though courts of equity or admiralty have concurrent jurisdiction).

109. *See* Zechariah Chafee, Does Equity Follow the Law of Torts? *in* SOME PROBLEMS OF EQUITY 103, 115 (1950) (distinguishing a "new equitable wrong like breaches of trust" from a court of equity's providing equitable relief for a legal tort such as waste); *see also id*. at 128 (observing that some new torts were concurrently developed by law and equity).

110. LANGDELL, SURVEY OF EQUITY JURISDICTION at 5; *see id*. at 258-59 ("Perhaps, however, it is not very material whether they be regarded as breaches of obligation or as equitable torts; for, whether they be one or the other, it seems that the relief which equity will give will be the same. For equity never gives damages for an infringement of an equitable right, but makes the wrong-doer a debtor to the person wronged instead, and proceeds upon the theory of compelling the former to restore to the latter what he has lost, or to place him in the situation in which he would have been if the wrong had not been committed.").

111. RESTATEMENT (FIRST) OF AGENCY § 403 & cmt. f. The authors of the *Restatement of Agency* observed that "[i]t is not within the scope of the Restatement of this Subject to state generally the conditions under which the principal has a particular remedy."

112. RESTATEMENT (FIRST) OF RESTITUTION § 138 cmt. a ("A fiduciary who commits a breach of his duty as fiduciary is guilty of tortious conduct and the beneficiary can obtain redress either at law or in equity for the harm done."). A number of courts have relied on Section 138 when addressing claims against corporate fiduciaries. *See, e.g.*, Shanno v. Magee Indus. Enters., 856 F.2d 562, 565 (3d Cir. 1988); Brown v. New York Life Ins. Co., 58 F. Supp. 252, 257 (D. Or. 1944), *aff'd*, 152 F.2d 246 (9th Cir. 1945); Gray v. Sutherland, 268 P.2d 754, 761 (Cal. Ct. App. 1954); Weisbecker v. Hosiery Patents, 51 A.2d 811, 813 (Pa. 1947).

113. RESTATEMENT (FIRST) OF TORTS § 874.

tortious conduct."[114] The comment then continued by stating that "[t]he local rules of procedure, the type of relation between the parties and the intricacy of the transaction involved, determine whether the beneficiary is entitled to redress at law or in equity."[115]

The first *Restatement of Trusts*, on the other hand, took the definite position that the breach of fiduciary duty by a trustee was an "equitable" tort. It arose out of a purely equitable right and therefore only could be remedied in equity. The only time a beneficiary could maintain an action at law was if the trustee had an unconditional duty to pay money or transfer property immediately.[116] In all other cases, the remedies of the beneficiary were "exclusively equitable."[117] This type of breach of fiduciary duty was therefore a true "equitable tort."

The distinct nature of the world of trusts, in which a breach of fiduciary duty was a purely "equitable tort" and operated within a well-developed system of contribution, could perhaps explain the different positions of the 1939 and 1955 Uniform Acts. Professor Bogert, who asked about the scope of the Uniform Act during the 1955 revision, was an expert on trust law, and he appears to have viewed a fiduciary obligation as a purely equitable tort that carried with it a framework for contribution that should not be disturbed. Professor Gregory, the reporter for the 1939 Act, was an export in labor and tort law, and he probably started from the premise articulated in the *Restatement of Torts* that "[a] fiduciary who commits a breach of his duty as a fiduciary is guilty of tortious conduct." Outside of the world of trusts, a breach of fiduciary duty was generally a "legal" tort upon which suit could be brought either at law or in equity, and which lacked a well-developed system of contribution.

We will see in the next section that in addition to providing insight into the intentions of the drafters of the Uniform Act, the nuances of equitable torts also potentially explain the seemingly unique approach to breaches of fiduciary duty taken by the Delaware courts, one of the few jurisdictions that retained the division between law and equity. Otherwise, with the merger of law and equity largely complete by 1938, the characterization of a breach of fiduciary duty as a "legal" versus "equitable" tort ceased to have much meaning.

Instead, to the extent the proper classification of a breach of fiduciary duty claim arose, the debate was framed in terms of tort versus contract. Parties joined issue frequently in disputes over the applicable statute of limitations, where a longer period typically applies to contract claims.[118] Disputes also arose when the administrator or executor of an estate argued that the claim sounded in contract and therefore survived the death of the fiduciary.[119]

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114. *Id.* at cmt. b.

115. *Id.* The *Restatement (Second) of Torts*, published in 1979, continued this approach. Section 874 retained the general statement of regarding liability and the comment that "[a] fiduciary who commits a breach of his duty as a fiduciary is guilty of tortious conduct." It also retained the statement that "[t]he local rules of procedure, the type of relation between the parties and the intricacy of the transaction involved, determine whether the beneficiary is entitled to redress at law or in equity." The Reporters' Note added the caution that "[s]ome fiduciary relations, such as those of … director and corporation are the subject of a considerable group of substantive rules of law; and a breach of fiduciary duty has usually been regarded as controlled by the substantive law rules governing the relationship." The note then stated, "But the action may properly be regarded as in tort for damages, being an equitable tort even when the action is in the traditional scope of equitable jurisdiction." Thus while concluding that a breach of fiduciary duty was a tort, the *Restatement (Second) of Torts* continued to leave other matters up to "[t]he local rules of procedure, the type of relation between the parties and the intricacy of the transaction involved."

116. Restatement (First) of Trusts § 198.

117. *Id.* §§ 197, 199.

118. Delaware has had no need to address this question because the same three-year limitations period applies to both contract claims and to any "action to recover damages caused by an injury unaccompanied with force or resulting directly from the act of the defendant," which has been interpreted to govern fiduciary duty claims. Del. Code Ann. tit. 10, § 8106; *see* Kahn v. Seaboard Corp., 625 A.2d 269, 270-71 (Del. Ch. 1993) (applying Section 8106).

119. Delaware has not needed to address this issue because by statute, "all causes of action, except actions for defamation, malicious prosecution, or upon penal statutes shall survive." Del. Code Ann. tit. 10, § 3701.

Litigants who argued that a breach of fiduciary claim sounded in contract consistently pointed to the typically contractual underpinnings of the fiduciary relationship in question, which for suits against directors meant the certificate of incorporation and bylaws that governed the relationship among the directors, the corporation, and its stockholders. Litigants also asserted an implied contractual undertaking based on an individual's agreement to serve as a director or, when an oath of office is required, the oath itself.[120] Although the decisions were mixed, in the late nineteenth and early twentieth centuries, the contract-based arguments were often successful, both in obtaining the longer contractual statute of limitations[121] and for purposes of the survival of actions.[122]

The savings and loan crisis of the 1980s brought the proper characterization of breach of fiduciary duty claims back to the forefront. After a brief flirtation with the earlier theories that breaches of fiduciary duty arose in contract,[123]

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120. Many of the decisions involved federally chartered banks and asserted violations of specific provisions of the National Bank Act in addition to general breaches of fiduciary duty. In *Cockrill v. Cooper*, the United States Court of Appeals for the Eighth Circuit held that a section of the National Bank Act that provided for personal liability for directors for violations of the act was "nothing more than a recognition of a liability which the directors of such institutions would incur at common law and in the absence of the statute." 86 F. 7, 12 (8th Cir. 1898); *accord* Orth v. Mehlhouse, 36 F.2d 367, 368 (D. Minn. 1929) (quoting *Cockrill*). The *Cockrill* court interpreted the specific provisions of the statute as establishing "a standard of liability … without creating a new cause of action, or altering the foundation upon which the personal liability of directors for wrongful or negligent acts ultimately rests or depends." *Cockrill*, 86 F. at 11. The court noted that as a result of their fiduciary duties, directors must "act within the scope of the bank's charter and by-laws" and "exercise at all times a reasonable degree of care and diligence in the discharge of duties which they have been appointed to perform." *Id*. at 13. "If they are guilty of a culpable violation of this obligation, and the corporation thereby sustains damage, the directors are personally liable therefor…." *Id.*

121. *See, e.g.*, Hughes v. Reed, 46 F.2d 435, 441 (10th Cir. 1931) (applying longer statute of limitations for breach of contract: "While the measure of the obligation is that of ordinary care and prudence, the obligation arises from the implied agreement, and not alone by failure to exercise such care."); Wallace v. Lincoln Savings Bank, 15 S.W. 448, 453 (Tenn. 1891) (applying longer statute of limitations applicable to breach of contract actions to claims for breach of duty against bank directors). *But see* McNair v. Burt, 68 F.2d 814, 816 (5th Cir. 1934) (holding that the claim for breach of fiduciary duty "must rest … upon the statutory and common-law right to recover for negligence and dereliction of duty in the management of the bank's affairs"); Squire v. Guardian Trust Co., 72 N.E.2d 137, 145 (Ohio. Ct. App. 1947) ("Where facts alleged fall short of establishing an express trust and the defendants have failed to exercise skill and prudence in caring for and investing the bank's funds, *a fortiori*, such defendants are liable in tort for such dereliction.").

122. *See, e.g.*, Boyd v. Schneider, 131 F. 223, 229 (7th Cir. 1904) (holding that directors owed duties to bank depositors and that a suit by depositors of an insolvent bank in equity for breach of duty "survives against the representatives of deceased directors, because it is a suit on contract, and not in tort"); Curtis v. Phelps, 208 F. 577, 577 (N.D.N.Y. 1913) ("There is an implied contract and undertaking on the part of the directors of a national bank to properly and faithfully perform their duties as directors, and if by misconduct or negligence they fail to perform such duty and damage results to the creditors of the bank, or the stockholders, a cause of action arises which may be enforced by the receiver in behalf of the creditors and stockholders. Such a cause of action is contractual, and arises out of the contractual relation of the parties, and is not in tort."); Allen v. Luke, 163 F. 1018 (D. Mass. 1908) ("As to one defendant who died before the bill was filed; that the action did not survive. The weight of authority is otherwise."); Cunningham v. Commissioner of Banks, 144 N.E. 447, 459 (Mass. Super. Ct. 1924) ("Action by or in behalf of a corporation against one of its directors for negligent performance of his managerial duties sounds in contract. In substance and effect it is a breach of the contract which springs in to existence by acceptance of the office of director and the assumption of its duties."). *But see* Orth v. Mehlhouse, 36 F.2d 367, 369 (D. Minn. 1929) (declining to treat claim against director as contractual).

123. *See* Fed. Deposit Ins. Corp. v. Former Officers and Directors of Metro. Bank, 884 F.2d 1304, 1307 (9th Cir. 1989) (applying longer contractual statute of limitations to breach of fiduciary duty claims); Federal Sav. & Loan Ins. Corp. v. Burdette, 696 F. Supp. 1196, 1201 (E.D. Tenn. 1988) (same); Bibo v. Jeffrey's Restaurant, 770 P.2d 290 (Alaska 1989) (applying contract statute of limitations as the longer of two periods that reasonably could apply).

a strong majority view emerged that characterized breaches of fiduciary duty as tort claims.[124] For example, in the part of the country that was ground zero for the savings and loan crisis, courts consistently held that claims for breach of fiduciary duty against corporate fiduciaries were tort claims, such that corporate fiduciaries received the protection of a shorter statute of limitations.[125]

As a result of these authorities, there is now a large body of case law outside of Delaware that treats a claim for breach of fiduciary duty against corporate directors as a tort. These decisions do not make fine distinctions between "legal" or "equitable" torts, nor do they delve into the nuances of the equitable underpinnings of the fiduciary relationship. They simply hold that a breach of fiduciary duty is a tort.[126] The natural consequence of such an approach is that contribution under the Uniform Act would exist, unless a state has adopted the provision from the 1955 revision excluding breaches of fiduciary duty from its coverage. Delaware's approach to fiduciary duties, however, is not so simple.

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124. *See, e.g.*, Freeland v. Enodis Corp., 540 F.3d 721, 740-41 (7th Cir. 2008); Federal Deposit Ins. Corp. v. Abel, 1995 WL 716729, at *9 (S.D.N.Y. Dec. 6, 1995); Resolution Trust Corp. v. Gravee, 1995 WL 75373, at *3 (N.D. Ill. Feb. 22, 1995); Resolution Trust Corp. v. Fortunato, 1994 WL 478616, at *4 (N.D. Ill. Sept. 1, 1994); Resolution Trust Corp. v. Zimmerman, 853 F. Supp. 1016, 1020 (N.D. Ohio 1994); Resolution Trust Corp. v. O'Bear, Overholser, Smith & Huffer, 840 F. Supp. 1270, 1278 (N.D. Ind. 1993); Federal Deposit Ins. Corp. v. Gonzalez-Gorrondona, 833 F. Supp. 1545, 1560 (S.D. Fla. 1993); Washington Bancorporation v. Said, 812 F. Supp. 1256, 1272 (D.D.C. 1993); Federal Deposit Insurance Corporation v. Dannen, 747 F. Supp. 1357, 1361 (W.D. Mo. 1990); C-T of Virginia, Inc. v. Barrett, 124 B.R. 689, 693 (W.D. Va. 1990); Beloit Liquidating Trust v. Grade, 677 N.W.2d 298, 311 (Wis. 2004); Brooks v. Hill, 717 So.2d 759, 764 (Ala. 1998). *But see* United States Small Business Administration v. Wasson, 865 F. Supp. 753, 754 (W.D. Okla. 1994) (finding "plaintiff's claims for breach of fiduciary duty, failure to keep adequate books and records and absence of internal controls are based in contract").

125. *See* Askanase v. Fatjo, 130 F.3d 657, 665-66 (5th Cir. 1997); Federal Deposit Ins. Corp. v. Dawson, 4 F.3d 1303, 1307 (5th Cir. 1993); Federal Deposit Ins. Corp. v. Fay, 1993 WL 740984, at *4-5 (S.D. Tex. Dec. 17, 1993).

126. Maryland and Illinois have taken different paths. In the leading Maryland case, the appellant sought to overturn a judgment in favor of a trustee because the case had not been tried to a jury. Kann v. Kann, 690 A.2d 509 (Md. 1997). The Court of Appeals of Maryland rejected the idea that all claims for breaches of fiduciary duty were torts for which a right to jury trial existed. *Id*. at 521. The court held that the presented claim against the trustee was properly tried in equity, and that "there is no universal or omnibus tort for the redress of breach of fiduciary duty by any and all fiduciaries." *Id*. Thus, in future cases, "identifying a breach of fiduciary duty will be the beginning of the analysis, and not its conclusion." *Id*. The court will "identify the particular fiduciary relationship involved, identify how it was it was breached, consider the remedies available, and select those remedies appropriate to the . . . problem." *Id*.

In the leading Illinois case, a taxpayer sued Chicago's mayor and several public officials for breach of fiduciary duty for misappropriating funds. Kinzer v. City of Chicago, 539 N.E.2d 1216 (Ill. 1989). The Illinois Supreme Court refused to hold that the claim sounded in tort such that the officials were immune from suit under the Illinois Tort Immunity Act. The court declined to accept "the Restatement (Second) of Torts view" and instead "regarded breach of fiduciary duty as controlled by the substantive laws of agency, contract and equity." *Id*. at 1220. Subsequent Illinois courts have held flatly, citing *Kinzer*, that contribution under the Illinois version of the Uniform Act is not available for breach of fiduciary duty claims because the claims do not impose liability in tort. People v. Cmty. Hosp. of Evanston, 545 N.E.2d 226, 230 (Ill. Ct. App. 1989); *accord* Weiboldt Stores v. Schottenstein, 111 B.R. 162, 169 (N.D. Ill. 1990); *In re* HA-LO Indus., Inc., 2004 WL 45499, at *2 (Bankr. N.D. Ill. Jan. 5, 2004). Parties in turn have sought to reallocate losses under various alternative theories, all of which have been rejected as applied to breach of fiduciary duty claims. Because the Illinois version of the Uniform Act does not apply, the Illinois courts have defaulted to harsh common law doctrines that the Uniform Act was intended to prevent, such as the rule that releasing one defendant automatically constitutes a release of all. *See* Cherney v. Soldinger, 702 N.E.2d 231, 236 (Ill. Ct. App. 1998) (common law "release of one, release of all" rule applied where breach of fiduciary duty was not a tort and therefore not covered by Illinois version of Uniform Act).

VII. UNDER DELAWARE LAW, A CLAIM FOR BREACH OF FIDUCIARY DUTY AGAINST A CORPORATE DIRECTOR IS LIKELY AN EQUITABLE TORT

The analysis of the proper characterization of a breach of fiduciary duty claim under Delaware law is dominated by *Cede & Co. v. Technicolor*.[127] In this opinion from 1993, the Delaware Supreme Court decisively rejected the application of traditional common law tort elements and burdens to a claim for breach of fiduciary duty. These rulings were roundly criticized,[128] prompting one commentator to ask, "[I]f a breach of fiduciary duty is not a tort action, what is it? A contract action?"[129] With the history of the Uniform Act having reminded us of a largely forgotten concept, the answer would appear to be "an equitable tort."

The *Technicolor* saga[130] began as an appraisal proceeding brought by Cinerama, Inc. following the acquisition of Technicolor, Inc. by MacAndrews & Forbes Group, Inc., an investment vehicle of Ronald Perelman. During discovery in the appraisal action, Cinerama developed evidence that it believed supported claims for breaches of Technicolor directors' duties of loyalty and care. Cinerama filed a plenary action asserting these claims, which eventually was consolidated with the appraisal proceeding.[131] After a 47-day trial, Chancellor William T. Allen ruled on the appraisal,[132] then issued a second opinion addressing the breach of fiduciary duty action.[133] Chancellor Allen rejected the breach of loyalty claims and, relying on then-District Judge Learned Hand's decision in *Barnes v. Andrews*, held that even if he assumed that the directors failed to exercise due care, the plaintiffs had the burden to establish causation and damages.[134] Having already

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127. 634 A.2d 345 (Del. 1993).

128. *See, e.g.*, Bernard S. Sharfman, *Being Informed Does Matter: Fine Tuning Gross Negligence Twenty Plus Years After* Van Gorkom, 62 Bus. Law. 135, 152 (2006) ("[*Technicolor*] was received by the legal community with possibly even less enthusiasm than the opinion in *Van Gorkom*."); William A. Gregory, *The Fiduciary Duty of Care: A Perversion of Words*, 38 Akron L. Rev. 181, 188 (2005) (criticizing *Technicolor* as "silly" and noting that "[a] duty of care claim is always a tort action and is always based on negligence"); Franklin A. Gevurtz, Corporation Law 302 (2000) ("The *Cede* court's rejection of tort law causation principles, in favor of a sort of reverse application of the business judgment rule, seems bizarre. Indeed, it appears to illustrate the power of the so-called business judgment rule to confuse courts."); Michael P. Dooley, Fundamentals of Corporation Law 269 (1995) ("*Technicolor*'s conflation of care and loyalty doesn't clarify matters any … ."); Lyman P. Johnson, *Rethinking Judicial Review of Director Care*, 24 Del. J. Corp. L. 787, 801 (1994) ("[N]o clear and reasoned prior authority exists for the [*Cede*] holdings … ."); Lawrence A. Cunningham and Charles M. Yablon, *Delaware Fiduciary Duty Law After* QVC *and* Technicolor*: A Unified Standard (and the End of Revlon* Duties?), 49 Bus. Law. 1593, 1600-01 (1994) (discussing revolutionary approach in *Cede*)

129. Charles Hansen, *The* Technicolor *Case—A Lost Opportunity*, 19 Del. J. Corp. L. 617, 637 n.152 (1994).

130. The "extraordinarily protracted and voluminous" Technicolor case began in 1983 when Cinerama sought appraisal of its Technicolor shares. Cede & Co. v. Technicolor, Inc., 1999 WL 65042, at *1 (Del. Ch. Jan. 29, 1999). After two decades of litigation, in 2001 Chancellor William B. Chandler, III observed that "the conflict between them not only appears to sustain both combatants, but has in part come to define them." Cede & Co. v. Technicolor, Inc., 2001 WL 515106, at *1 (Del. Ch. May 7, 2001). The final judgment issued after the case was remanded by the Supreme Court for a sixth time in 2005. *See* Cede & Co. v. Technicolor, Inc., 884 A.2d 26, 30 (Del. 2005) ("[T]he history of this 'sempiternal appraisal action' is thoroughly recorded in the annals of Delaware corporate law … .").

131. *See* Cede & Co. v. Technicolor, Inc., 542 A.2d 1182 (Del. 1988).

132. *See* Cede & Co. v. Technicolor, Inc., 1990 WL 161084 (Del. Ch. Oct. 19, 1990).

133. *See* Cinerama, Inc. v. Technicolor, Inc., 1991 WL 111134 (Del. Ch. June 24, 1991).

134. *Id*. at *3 (citing Barnes v. Andrews, 298 F. 614 (S.D.N.Y. 1924)).

found that in his appraisal ruling the deal price exceeded the fair value of the dissenter's shares, Chancellor Allen held that Cinerama could not meet its burden.

By citing *Barnes* and requiring the plaintiff to establish damages, Chancellor Allen relied on basic common law tort concepts that he believed were equally applicable to a claim for breach of the duty of care.[135] Chancellor Allen required the plaintiff to show a duty, a breach, causation and damages — all of the traditional elements of a tort claim.[136]

Cinerama appealed, squarely presenting the Delaware Supreme Court with the propriety of applying common law tort principles to a claim for breach of the duty of care. The Supreme Court rejected the Court of Chancery's approach, noting that the defendants conceded "the lack of any Delaware corporate law precedent for applying tort principles of liability to a fiduciary duty of care analysis."[137] According to the Delaware Supreme Court, "While *Barnes* may still be 'good law,' *Barnes*, a tort action, does not control a claim for breach of fiduciary duty."[138] The Delaware Supreme Court held explicitly that "[t]he tort principles of *Barnes* have no place in a business judgment rule standard of review analysis."[139]

Eschewing the traditional common law tort framework in which the burden of proof of each element of the claim rested on the plaintiff, the Delaware Supreme Court held that in an equitable proceeding for breach of fiduciary duty, the plaintiff only has to establish a breach of either the duty of loyalty or the duty of care. In the event of either showing, the burden of proof shifts to the defendant fiduciaries to prove that the challenged transaction was entirely fair.[140] "[B]reach of the duty of care, without any requirement of proof of injury, is sufficient to rebut the business judgment rule."[141] It therefore was "fundamental error" for the Court of Chancery to "inject[] into the duty of care element a burden of proof of resultant injury or loss."[142]

Although *Technicolor* dealt with a breach of the duty of care rather than a breach of the duty of loyalty, the Delaware Supreme Court's rejection of common law tort concepts echoed similar language in its 1944 decision in *Bovay v. H.M. Byllesby & Co.*[143] The *Bovay* court refused to treat self-interested conduct by a fiduciary as a "mere tort" to which

135. In *Barnes*, the receiver of an insolvent corporation sued a corporate director who had been negligent. Although the case involved what now would be viewed as a *Caremark* claim, Judge Hand framed the question in terms of the tort of negligence. In a passage quoted by Chancellor Allen, Judge Hand observed,

This cause of action rests upon a tort, as much though it be a tort of omission as though it had rested upon a positive act. The plaintiff must accept the burden of showing that the performance of the defendant's duties would have avoided loss, and what loss it would have avoided.

Id. at *17 (quoting *Barnes*, 298 F. at 616-18).

136. *Id.* at *18. He held that "a shareholder-plaintiff must prove by a preponderance of evidence that director negligence did cause some injury and must introduce sufficient evidence from which a responsible estimation of resulting damage can be made." *Id.*

137. *Cede*, 634 A.2d at 360.

138. *Id*. at 370.

139. *Id*.

140. *Id*. at 371.

141. *Id*.

142. *Id.*; *see also* Young v. Colgate-Palmolive Co., 790 F.2d 567, 570 (7th Cir. 1986) ("[A] claim for breach of fiduciary duty is sufficient if it alleges the fiduciary relationship and its breach, as these two elements alone would establish liability" (citing Restatement (Second) of Torts § 874 cmt. b)).

143. 38 A.2d 808 (Del. 1944).

the statute of limitations would apply.[144] Similarly in *Harman v. Masoneilan International, Inc.*,[145] the Delaware Supreme Court declined to view a claim for breach of fiduciary duty against a controlling stockholder as a legal tort over which the Court of Chancery exercised concurrent jurisdiction, such that an action seeking only damages had to be brought at law in the Delaware Superior Court.[146] In reversing the Court of Chancery's dismissal of the claim, the Delaware Supreme Court held that when "[a] majority shareholder in alleged breach of its fiduciary duty has exercised control over corporate machinery to impose its will upon the minority to accomplish a force out merger," the resulting claim "falls within equity's inherent or exclusive jurisdiction."[147] In other words, it was an inherently "equitable" tort.

Since *Technicolor*, there has not been any significant discussion in Delaware decisions about the proper characterization of breach of fiduciary duty claims. The cases nevertheless appear to treat breach of fiduciary duty claims as distinct from common law tort or contract claims. In a 2007 opinion, for example, the Delaware Supreme Court differentiated between a claim "arising out of contract or tort," which a creditor of an insolvent corporation could bring directly in its own name, and "a purported breach of fiduciary duty," which creditors only could assert derivatively.[148] In a 2008 ruling, the Delaware Court of Chancery remarked that a defendant "could be viewed as having committed actions in the nature of a tort — a breach of fiduciary duty, an equitable obligation — in Delaware" for purposes of subjecting himself to jurisdiction under Delaware's Long Arm Statute.[149] With other bases for jurisdiction rendering the discussion *dictum*, the court nevertheless was careful to describe the breach of fiduciary duty claim as "in the nature of a tort" and as "an equitable obligation."

Without the concept of an "equitable tort," these decisions — and particularly *Technicolor* — could be read to suggest that a breach of fiduciary duty claim in Delaware is *sui generis*. At a minimum, *Technicolor* would cast doubt on characterizing a breach of fiduciary duty under Delaware law as a tort. These conclusions in turn would call into question whether DUCATA could apply to a breach of fiduciary duty.

The concept of an "equitable tort" brings coherence to these issues. Because an equitable tort differs from a common law tort, it should come as no surprise that an equitable tort could involve different burdens of proof and elements.

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144. *Id*. at 820. Delaware continues to judge the timeliness of claims for breach of fiduciary duty using the doctrine of laches, rather the statute of limitations. *In re* Trados Inc. S'holders Litig., 2009 WL 2225958, at *5 (Del. Ch. July 24, 2009) ("This Court, however, is not bound by the analogous statute, and 'as the equities require, may apply a period either shorter or longer than that fixed by statute.'" (quoting Elster v. Am. Airlines, Inc., 128 A.2d 801, 805 (Del. Ch. 1957)).

145. 442 A.2d 487 (Del. 1982).

146. In *Harman*, the defendants sought to have the case dismissed from the Court of Chancery for lack of subject matter jurisdiction. Divorced of context, the defendants' position today seems counter-intuitive, because corporate and director defendants generally prefer the Court of Chancery for the experience of its judges in corporate disputes, lack of a jury, and inability to award punitive damages. But at the time, the Superior Court did not have a class action mechanism. *Id*. at 500. The plaintiff stockholder thus only would have been able to sue individually. Forcing the action to be brought at law in the Superior Court could prevent the case from being economically viable. This anomaly has since been changed, and the Superior Court now has a class action procedure.

147. *Id.* at 499.

148. *See* North Am. Catholic Educ. Programming Found., Inc. v. Gheewalla, 930 A.2d 92, 103 n.43 (Del. 2007); *see also* IM2 Merch. and Mfg., Inc. v. Tirex Corp. 2000 WL 1664168, at *6 (Del. Ch. Nov. 2, 2000) ("[P]laintiffs' claim is really one based on contract or tort law, rather than the law of fiduciary duty.").

149. Sloan v. Segal, 2008 WL 81513, at *9 (Del. Ch. Jan. 3, 2008). Subsection (3) of the Delaware Long Arm Statute permits the exercise of jurisdiction over anyone who "[c]auses tortious injury in the State by an act or omission in this State." Del. Code Ann. tit. 10, § 3104(c)(3).

The differences between common law fraud and equitable fraud, in which a showing of *scienter* is not required, illustrate this possibility.[150] Characterizing a breach of fiduciary duty as an equitable tort is also consistent with Delaware authorities that derive the fiduciary duties of directors from analogies to the law of trusts.[151] As we have seen, claims for breaches of fiduciary duty against trustees present the purest case of an equitable tort.[152] Most significantly for present purposes, characterizing a claim for breach of fiduciary duty claim as an equitable tort logically brings the claim within the scope of DUCATA, because "equitable torts" were meant to be included in the 1939 draft that Delaware adopted.

VIII. POLICY SUPPORTS THE APPLICATION OF DUCATA

It thus appears legally correct to apply DUCATA to breaches of fiduciary duty by directors of a Delaware corporation. Furthermore, there are important public policy considerations that weigh in favor of applying DUCATA. First and perhaps most significant is the underlying purpose of the Uniform Act, which was to ameliorate the consequences of harsh common law rules governing contribution. If DUCATA does not apply to claims for breach of fiduciary duty, harsh common law rules could continue to control.[153] The Delaware Supreme Court and the Delaware Court of Chancery could ameliorate the common law rules by developing new doctrines and principles, such as those set forth in the *Restatement (Second) of Trusts*, but favorable development of the law would require changes in the common law's traditional approach. Changing the common law rules was precisely what the Uniform Act and DUCATA sought to achieve, and it would be oddly redundant for Delaware courts to decline to apply DUCATA only to embark upon their own ameliorative effort.

Second, there is some evidence of a general expectation that DUCATA applies to breach of fiduciary duty claims. As demonstrated by the arguments made in *Telecorp*, *Valeant*, *Greenberg*, and *Hollinger*, practitioners have looked to DUCATA to govern contribution issues. A majority of jurisdictions outside of Delaware treat a breach of fiduciary duty as a tort to which the Uniform Act logically would apply, such that applying DUCATA to breaches of fiduciary duty would be consistent with the expectations of other jurisdictions. As demonstrated by the reactions to the *Technicolor* decision, a number of commentators already believe a breach of fiduciary duty is a tort, and they were surprised when the Delaware

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150. *See generally* 3 John Norton Pomeroy, A Treatise on Equity Jurisprudence § 873 at 420-422 (5th ed. 1941); 1 Joseph Story, Commentaries on Equity Jurisprudence § 184 at 159-60 (1839); Donald J. Wolfe, Jr. and Michael A. Pittinger, Corporate and Commercial Practice in the Delaware Court of Chancery § 2.03[b][1] at 2-32 (2009).

151. In 2008, the Delaware Supreme Court wrote that the fiduciary duties of directors "stem in part from the quasi-trustee and agency relationship directors have to the corporation and stockholders that they serve." Schoon v. Smith, 953 A.2d 196, 206 (Del. 2008). This continued a long tradition of analogizing directors to trustees. *See, e.g.*, Guth v. Loft, Inc., 5 A.2d 503, 510 (Del. 1939) ("While technically not trustees, [directors] stand in a fiduciary relation to the corporation and its stockholders."); Bodell v. General Gas & Elec. Corp., 132 A. 442, 446 (Del. Ch. 1926) ("There is no rule better settled in the law of corporations than that directors in their conduct of the corporation stand in the situation of fiduciaries. While they are not trustees in the strict sense of the term, yet for convenience they have often been described as such."); Lofland v. Cahall, 118 A. 1, 3 (Del. Ch. 1922) ("Directors of a corporation are trustees for the stockholders, and their acts are governed by the rules applicable to such a relation."); Bowen v. Imperial Theatres, 115 A. 918, 921-22 (Del. Ch. 1922) ("Directors of a corporation are frequently spoken of as its trustees. Their acts are scanned in the light of those principles which define the relationship existing between trustee and cestui que trust."); State v. Jessup & Moore Paper Co., 72 A. 1057, 1057 (Del. 1909) ("[I]t is the duty of the directors of corporations to afford to their stockholders every reasonable opportunity to get accurate information as to the conduct and management of the business of which they merely act as trustees").

152. *See* Part V, *supra*.

153. This has been the result in Illinois. *See supra* note 126.

Supreme Court suggested otherwise. Under a "duck" approach to the law,[154] there is benefit to treating breaches of fiduciary as torts, albeit as equitable torts, and applying DUCATA.

Third, there is virtue in the certainty of DUCATA, which addresses a number of nuts-and-bolts issues where predictability is desirable. DUCATA covers, for example, matters such as when a claim for contribution can be filed, the effects of a judgment against one joint tortfeasor on others, the effects of a release on other joint tortfeasors, and availability of third party practice. If DUCATA did not apply, then the Delaware courts would need to create rules to govern these areas. Until rules were established, litigants would act in a vacuum and potentially at their peril. Applying DUCATA is consistent with Delaware's goal of providing clear guideposts for parties to follow, particularly in the corporate context.

Fourth, the substantive concepts underlying DUCATA are consistent with Delaware fiduciary duty law. The premise that joint tortfeasors could be liable to different degrees is akin to the director-by-director analysis that Delaware law already requires before damages can be awarded against an individual director.[155] In a situation where some directors have breached their duty of loyalty while others have breached their duty of care, the possibility of disproportionate responsibility should be readily apparent. Indeed, if the corporation has a Section 102(b)(7) provision, it is unlikely that the directors who merely breached their duty of care could be subject to contribution claims, given the absence of any underlying basis for a monetary judgment against those directors. Even where multiple directors have breached their duty of loyalty, however, the possibility for differently situated defendants exists. A court might readily impose liability on a director who was self-interested in a transaction, while at the same time hold another director liable for failing to carry his burden of proof that he acted independently and not because of his loyalty to the self-interested fiduciary.[156] Depending on the equities of the case, a court in a contribution action could allocate liability equally among the directors, or could place a more significant portion of the liability on the self-interested director, particularly if the self-interested director actually received a quantifiable benefit from the challenged transaction that the other directors did not receive.

Importantly, the potential for contribution in a situation in which the director seeking contribution had a conflict or was held to have breached the duty of loyalty is consistent with the principles governing indemnification under Section 145(a) and (b) of the General Corporation Law. Both provisions permit directors to be indemnified "if the person acted in good faith and in a manner the person reasonably believed to be in or not opposed to the best interests of the corporation, and, with respect to a criminal action or proceeding, had no reasonable cause to believe the person's conduct was

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154. That is, if it looks like a duck, swims like a duck, and quacks like a duck, it is probably a duck. *See* McMillan v. Intercargo Corp., 768 A.2d 492, 506 n.62 (Del. Ch. 2000) (applying a "duck" approach in determining which provisions with defensive impacts would be reviewed as defensive measures); Hillsboro Energy LLC v. Secure Energy, Inc., 2008 WL 4561227, at *1 (Del. Ch. Oct. 3, 2008) (applying a "duck" analogy in concluding that the contract claim sought legal, rather than equitable, relief).

155. *See In re* Emerging Commc'ns, Inc., S'holders Litig., 2004 WL 1305745, at *38 (Del. Ch. 2004) (engaging in a director-by-director analysis before imposing liability on any individual director); *see also* William T. Allen et al., *Function Over Form: A Reassessment of Standards of Review in Delaware Corporation Law*, 56 Bus. Law. 1287, 1318 (2001) ("In cases where the transaction cannot be undone, the court must conduct a director-by-director inquiry into which specific directors actually engaged in a breach of fiduciary duty sufficient to justify monetary liability. The fact that a transaction is found to be 'unfair' does not necessarily mean that all the directors have the same exposure to liability. Where the corporation has a charter provision that exculpates directors from monetary liability for breaching their duty of care, the plaintiff must establish that a director who had no conflicting self-interest in the transaction nonetheless acted in bad faith. If a director did not benefit from the unfair transaction, the plaintiff who seeks to subject that director to money damages liability should have the burden to prove that the director consciously breached his duties to the corporation.").

156. *See Emerging Commc'ns*, 2004 WL 1305745, at *40.

unlawful."[157] Delaware law thus already recognizes the possibility that a director who has breached his or her duty of loyalty could obtain indemnification, although it would be in the rare case where the statutory standard was met. DUCATA similarly would permit directors, even after an adjudicated breach of the duty of loyalty, to seek a discretionary ruling by the court permitting some form of contribution.

Finally, regardless of whether DUCATA applies, the Court of Chancery will retain its ability to apply equitable doctrines to reach equitable results. Most notably, in a case involving bad faith conduct by multiple defendants, the court could readily apply the doctrine of *in pari delicto* to decline to adjudicate the issue of contribution among the bad faith tortfeasors.[158] The right of contribution and the potential for a disproportionate allocation of responsibility that exist under DUCATA provide an opportunity for Delaware courts to reallocate responsibility if the case requires it. The converse is not true, and the Court of Chancery would not be required to permit contribution in every case, simply because DUCATA theoretically applied.

But despite the sound policy reasons for applying DUCATA to contribution among corporate directors, it is possible that Delaware courts could conclude DUCATA does not apply to a breach of fiduciary duty claim. This would not eliminate a right to contribution among directors, of course, but would leave the development of that right to the common law. Failure to apply DUCATA would leave Delaware corporations and litigants adrift for an unknown length of time while courts worked out the ground rules in a case-by-case fashion.

Given the interpretive uncertainty, the best solution would be for the Delaware General Assembly to pass legislation clarifying that DUCATA includes breaches of fiduciary duty, although these "equitable torts" should continue to be litigated in courts of equity. The application of DUCATA to contribution among corporate directors for breach of fiduciary duty provides clear, identifiable and specific benefits. Failing to apply the statute, though retaining flexibility, does not confer any similarly identifiable advantages. Applying DUCATA should not undermine settled expectations or suddenly change the ground rules for litigation — in fact, many commentators and practitioners appear to have assumed that DUCATA applies. It is time to conform the law to these long-held beliefs.

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157. Del. Code Ann. tit. 8, §§ 145(a) & (b).

158. *See In re* Am. Int'l Group, Inc. Consol. Deriv. Litig., 976 A.2d 872 (Del. Ch. 2009) (applying doctrine of *in pari delicto*).

THE ROLE OF HISTORICAL CONTEXT IN *NEW JERSEY v. DELAWARE III* (2008)

Matthew F. Boyer*

"The past is a foreign country: they do things differently there."
—L. P. Hartley, from "*The Go Between*"

The 2008 decision of the United States Supreme Court in *New Jersey v. Delaware*[1] ("*NJ v. DE III*") was hailed as a victory for Delaware, and so it was. The Court upheld Delaware's authority to block the construction of a liquefied natural gas ("LNG") unloading terminal that would have extended from New Jersey's side of the Delaware River well into Delaware territory. But while the case involved modern concerns over the environment, clean energy, and even the threat of terrorist attack, the States' underlying dispute was, like the River itself, of ancient origin, with a folklore of its own, and powerful, sometimes twisting currents. This was New Jersey's third Supreme Court original jurisdiction action against Delaware since the Civil War, all challenging Delaware's claim to sovereignty within a twelve-mile circle from the town of New Castle, which reaches across the River to within a few feet of the New Jersey side. In *NJ v. DE III*, the Court was called on to (i) construe a 1905 interstate compact (the "Compact" or "1905 Compact")[2] by which the States settled the first suit in 1907 ("*NJ v. DE I*")[3]; (ii) apply the Compact in light of the Court's 1934 decision resolving the States' boundary dispute in the second suit ("*NJ v. DE II*")[4]; and then (iii) determine the effect of the Compact and the boundary decision on Delaware's authority to enforce its 1971 Coastal Zone Protection Act.[5] This would prove no simple task.

At the heart of the dispute lay Article VII of the 1905 Compact, which allowed that each State "may, on its own side of the river, continue to exercise riparian jurisdiction" and make grants "of riparian lands and rights" under its own laws.[6] These few words spawned five different readings in *NJ v. DE III*: one by the Special Master in his 2007 report to the Court,[7] one by a five-member majority of the Court, one by Justice Stevens concurring in the judgment, one by Justice Scalia in dissent, and another proposed extemporaneously by Justice Ginsburg at oral argument. At one end of

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* Partner, Connolly Bove Lodge & Hutz LLP. The author was part of a team led by Collins J. Seitz, Jr. that represented the State of Delaware in *New Jersey v. Delaware III*.

1. *NJ v. DE III*, 552 U.S. 597 (2008).

2. The Compact was adopted by the States in 1905 (*see* 23 Del. Laws 12 (1905) and 1905 N.J. Laws 67), and ratified by Congress on January 24, 1907, Act of Jan. 24, 1907, ch. 394, 34 Stat. 858 (the "Compact"). The text of the Compact is included in the Appendices to Report of the Special Master, *NJ v. DE III,* 2007 WL 4266844, at *3A (Apr. 16, 2007) (Appendix B).

3. *See NJ v. DE I*, 205 U.S. 550 (1907) (granting dismissal without prejudice).

4. *See NJ v. DE II*, 291 U.S. 361 (1934) (decision resolving boundary dispute).

5. Del. Code Ann. tit. 7, § 7001 *et seq.*

6. Compact, Appendix B to Report of Special Master, 2007 WL 4266844, at *7A.

7. *NJ v. DE III,* Report of the Special Master, dated April 12, 2007 (quoting letter from Delaware Gov. James Ponder to New Jersey Gov. Joel Parker (May 14, 1872)) (the "Report"). The Report and all filings in the proceedings before the Special Master are available at http://www.pierceatwood.com/custompagedisplay.asp?Show=2.

this interpretive spectrum, Article VII ceded to New Jersey complete riparian jurisdiction over projects extending from its side of the River, including the proposed LNG terminal; at the other, Article VII conceded no jurisdictional rights at all, but merely permitted unobjectionable prior activities to continue.

In an early decision confirming its original jurisdiction over boundary disputes, the Court found it appropriate to "look to the history of the times, and examine the state of things existing when [the Constitution] was framed and adopted, to ascertain the old law, the mischief and the remedy."[8] So too, in *NJ v. DE III*, the Court did well to examine the 1905 Compact in its historical context. To the extent that an interpretation overlooked or misread that context, or was driven by events occurring several decades thereafter, it invariably veered off course. Conversely, to the extent that a reading harmonized the words of the Compact with "the state of things existing" when it was framed and adopted, that reading drew closer to the drafters' intent. In the end, the reading that best fit the historical context may well have been that of Justice Ginsburg, not in her opinion for the Court, but in her suggestion at oral argument that Article VII permitted the States to continue unobjectionable exercises of riparian jurisdiction in the shadow of their unresolved boundary dispute, without "do[ing] anything dispositive."[9]

I. THE HISTORICAL BACKGROUND

On the western side of the River near New Castle in 1682, by the ancient ritual of livery of seisin, William Penn received "turf and twig and water and Soyle of the River of Delaware," supposedly leaving him "in quiet and peaceable possession thereof."[10] But Penn's grant first led to a decades-long dispute with Lord Baltimore and then to an even longer feud between Delaware and New Jersey, marked by arrests at gunpoint, threats of military action, and three Supreme Court cases. The attorneys who represented Delaware before the Supreme Court included figures of historical significance, such as Thomas F. Bayard (1828-1898), George Gray (1840-1925), and Clarence A. Southerland (1889-1973). And while Delawareans would point with pride to Southerland's triumphant advocacy in the 1930's boundary case, which confirmed Delaware's sovereignty throughout the twelve-mile circle, New Jersey would insist, seven decades later, that Southerland had made key concessions that all but guaranteed victory for New Jersey in *NJ v. DE III*. The story bears some telling.

A. The River, Penn's Deed, and Early Jurisdictional Disputes

Prior to the arrival of the European settlers, the Lenni Lenape lived on both sides of the Delaware River, paddling their dugout canoes to harvest its fish with woven nets, spears, and sometimes even their bare hands.[11] While fur

8. Rhode Island v. Massachusetts, 37 U.S. 657, 723 (1838); see also U.S. Const. art. III, § 2 (extending the judicial power of the Supreme Court to "Controversies between two or more States").

9. *See* Transcript of November 27, 2007 Oral Argument at 4, *NJ v. DE III*, 552 U.S. 597 (2008) (No. 134), *available at* http://www.supremecourtus.gov/oral_arguments/argument_transcripts.html.

10. *NJ v. DE II*, 291 U.S. at 364-65 (internal quotations omitted). For an explanation of the ritual, see Thomas F. Bergin & Paul G. Haskell, Preface to Estates in Land and Future Interests 10-11 (2d ed. 1984) ("Without a modern system of land records, it would be desirable that the transfer be effected with sufficient ceremony not only to mark itself indelibly in the memories of the participants, but also to give notice to interested persons such as the mesne lord about the transferor…. The transferor and transferee would go to the land to be transferred, and the transferor would then hand to the transferee a lump of soil or a twig from a tree -- all the while intoning the appropriate words of grant ….").

11. This paragraph, including the quotations from early settlers, draws heavily from a beautifully written expert report authored by historian Carol E. Hoffecker, Ph.D., with the assistance of Barbara E. Benson, Ph.D., which Delaware submitted to the

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trading and whaling brought the first Europeans to the River in the 17th century, explorers could not help but notice its uncommon abundance of fish. Thomas Yong, sailing for England in 1634, compared the climate to that of Italy, and of the fish he noted, "heere is plenty, but especially sturgeon all the sommer time …."[12] Peter Lindeström, who came over in about 1650 as part of the New Sweden Colony, described shad for his masters in Stockholm as "a kind of large fish like the salmon, runs against the stream like a salmon … a very fine flavored and excellent tasting fish …."[13] And within a year of his arrival on the Delaware, William Penn wrote to friends back in England that "the sorts of fish in these parts are excellent and numerous. Sturgeon leap day and night that we can hear them … in our beds."[14]

By 1664, the Duke of York (later, King James II) had seized New Castle and the surrounding land from the Dutch. The Duke wanted to protect the town, so in 1680 his secretary proposed a circle boundary from its courthouse as a territorial buffer. In 1682, the Duke conveyed the territory, including the twelve-mile circle, to Penn, by livery of seisin.[15] Over time, Penn's Three Lower Counties on the Delaware were recognized as a separate colony, and in 1776, when the United States declared independence from Great Britain, Delaware inherited the twelve-mile circle as its northeastern border.

By the end of the Revolutionary War, the cause of the first dispute over territory within the circle had arisen, literally, from the waters within it. In about 1783, there appeared at low tide in the River, about five miles below New Castle, a small muddy exposure of soil "about the size of a man's hat."[16] The exposure grew until it formed an island of about 87 acres. Based on a tradition that a vessel laden with peas had once sunk on the spot where the island arose, it was named "Pea Patch." In 1784, New Jersey officials granted the island to private parties, and during the War of 1812, Delaware conveyed it to the federal government for the construction of a fort. By the 1840's, these inconsistent conveyances led to a dispute between James Humphrey, who claimed title from New Jersey, and the United States, which claimed from Delaware.[17]

Pursuant to an act of Congress, in 1847 President Polk appointed the Honorable John Sergeant, an attorney and congressman from Pennsylvania, to arbitrate the dispute. After a lengthy evidentiary hearing, Sergeant found in the *Case of Pea Patch Island*[18] that Delaware had good title to convey throughout the twelve-mile circle. According to one legal journal, "Mr. Sergeant's opinion … having been formed after full and grave publick argument before him for many days … , is far more authoritative than any opinion merely professional, and has all the intrinsick weight of the highest judicial opinion."[19]

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Court in *NJ v. DE III* (hereinafter, the "Hoffecker Report"). *See* Barbara E. Benson and Carol Hoffecker, *The Compact of 1905 and its Role in the United States Supreme Court Cases: New Jersey v. Delaware I, II, and III,* Del. History, Spring-Summer 2008 (vol. XXXII, no. 2), at 61 (publishing the Hoffecker Report with an introduction addressing the Court's opinion). Citations to the Hoffecker Report herein refer to the page numbers in the published version rather than the version submitted to the Court.

12. Hoffecker Report at 64-65.

13. *Id.*

14. *Id.* at 66-67.

15. *Id*. at 67.

16. *See* Case of Pea Patch Island, 30 F. Cas. 1123, 1123 (1848) (No. 18, 311).

17. *Id.* at 1123-24.

18. *Id.* at 1123.

19. *Id*. at 1124 (quoting North American and United States Gazette, Jan. 17, 1848).

The journal went on to predict that Sergeant's opinion "can scarcely be reversed in any case which may again involve the question of this boundary."[20] But as Justice Cardozo noted in his 1934 opinion in *NJ v DE II*, although Sergeant's opinion was "a careful and able statement of the conflicting claims of right," still "the controversy would not down."[21]

B. *New Jersey v. Delaware I* (1877 – 1907) and the 1905 Compact

On the morning of May 2, 1872, a tugboat named the *Falcon* steamed out from the Port of Wilmington with officers on board to intercept New Jersey fishermen on the eastern half of the River. The *Falcon's* mission was to enforce Delaware's 1871 "Act to Protect Fishermen," which sought to save an industry already plagued by overfishing and pollution by requiring non-Delawareans to purchase a $20 annual license to fish in the River.[22] The *Falcon* stopped twenty-two New Jersey fishermen without licenses, arrested them, and impounded their boats. When one resisted, a Delaware officer "drew a pistol and pointed it at the person so refusing, and said if he … did not come on board of the 'Falcon,' he would make him …."[23]

The arrests sparked outrage in New Jersey and ignited oratorical salvos from both sides of the River. New Jersey Governor Joel Parker put "all persons" (read: Delaware) on notice of New Jersey's jurisdiction "easterly of the middle line of said river." His Delaware counterpart, James Ponder, responded that Delaware did not regard the matter "as an open question," it being clear that Delaware's jurisdiction is "exclusive over the waters of said river to low water mark, on the eastern side of said river, within the twelve mile circle from New Castle."[24] Eventually, the States appointed commissioners to negotiate an interstate compact, but their efforts failed. In 1876, Delaware gave notice that it intended to resume enforcement of its 1871 fishing law.

On March 13, 1877, the Court granted New Jersey leave to file a Complaint challenging Delaware's territorial claim over the twelve-mile circle, launching *NJ v. DE I*.[25] The Complaint set forth a two-pronged attack. First, Delaware's chain of title from Penn was flawed, so that New Jersey had title to the middle of the River under the Treaty of Paris in 1783. Second, even if Delaware's claim was originally valid, New Jersey nevertheless had gained title to the middle of the River under the doctrine of "prescription and acquiescence" (akin to adverse possession) by virtue of its "long, peaceable and undisputed possession, use and enjoyment" of the River.[26] In support of its prescription claim, New Jersey alleged that it had taken numerous actions within the twelve-mile circle without objection by Delaware, including regulating fishing, exercising criminal jurisdiction over "wrongs committed," and authorizing residents to build piers.[27] This last allegation sowed the seeds of the jurisdictional conflict that would ultimately result in *NJ v. DE III*.

20. *Id.*

21. *NJ v. DE II*, 291 U.S. at 377 (Delawareans were charged only $5).

22. An Act for the Protection of Fisherman (Mar. 28, 1871); *see* Report, *supra* note 7, at 3. The full text of the Act is set forth in Delaware's Appendix on Cross-Motions for Summary Judgment before the Special Master, filed December 22, 2006, volume 2, at pp. 913-916 ("Del. App.").

23. *NJ v. DE I*, Affidavit of George Stanton, dated February 13, 1877 (1 Del. App. at 59).

24. Report, *supra* note 7, at 4.

25. *NJ v. DE I*, Order dated March 13, 1877 (1 Del. App. at 19).

26. *NJ v. DE I,* Complaint (1 Del. App. at 20-54).

27. *Id.* at 36-37.

Along with its Complaint, New Jersey filed a motion for a preliminary injunction to stop Delaware from enforcing its 1871 fishing law. In support of its motion, New Jersey submitted affidavits from fishermen who recalled the *Falcon* incident and warned that "if such arrests are attempted again they will be resisted and … violence, bloodshed, and loss of life will be the … almost certain result."[28] Within less than two weeks, on March 26, 1877, the Court issued an order granting New Jersey's motion, noting the threat of violence on the River.[29] But thereafter, the case went into a slumber of Van Winklean proportions, for over twenty years, as neither side was sufficiently bothered by the status quo to embark upon the tedious process of litigating the underlying chain of title and prescription claims.

Finally, in 1901, the clerk of the Court prodded counsel to resolve the matter. On or about February 14, 1901, Delaware Governor John Hunn, a respected Quaker businessman and son of a noted abolitionist,[30] issued a message to the General Assembly calling upon it to fund the defense of the State's birthright. In words that convey a depth of conviction that may sound quaint to modern ears, Hunn stated:

> The unanimity with which the people of this State, through various General Assemblies and Executives, have always defended the integrity of the jurisdiction, territory, and sovereignty of this State in this controversy, constitutes a just guide for present action. I cannot bring myself to believe that the present generation of Delawareans will, when properly advised on the subject, find themselves less sensitive and earnest in maintaining the rights of the State than the generations which have preceded us….
>
> I therefore recommend that the General Assembly renew its dedication of purpose, not to abandon the vindication of its sovereign right and title to the territory which immemorially has been conceded to be a part of its domain, and that it shall make such provision for the further defense thereof against what must be considered the unfounded pretensions of the State of New Jersey, as will comport with the honor, dignity and best interests of the State.[31]

Needless to say, such provision was made.

In October 1901, Delaware filed a 67-page, type-set, single spaced Answer setting forth in meticulous detail its chain of title from William Penn and rebutting New Jersey's prescription claim.[32] As to the latter, Delaware stated that it did not know whether or not New Jersey residents had built wharves or other improvements on the easterly side of the River within the twelve-mile circle. But even if they had, the building of such structures could not "affect in any way" Delaware's title to any part of the soil or bed of the River within the twelve-mile circle not "actually and physically occupied" by the structures. And even then:

> [New Jersey] cannot, whether by such actual or physical occupation, if any such occupation there be, of any part of the original territory … of [Delaware] … acquire any part or portion of such territory,

28. *See NJ v. DE I*, Affidavit of George Stanton, dated February 13, 1877, and Affidavit of Joe Barber, dated February 13, 1877 (1 Del. App. at 59-61).

29. *NJ v. DE I,* Order for Preliminary Injunction, dated March 26, 1877 (1 Del. App. at 66-68).

30. Henry Clay Conrad, History of the State of Delaware 852-53 (1908).

31. 2 Del. App. at 1056-61 (Message of the Governor to the General Assembly, accompanied by an Opinion by Attorney General Ward on the status of the case).

32. Defendant's Answer, *NJ v. DE I*, 205 U.S. 550 (1907) (No. 1) (1 Del. App. at 95-162).

> jurisdictions, rights, privileges, franchises, powers or estates, or any of them, of any and every nature and description … of [Delaware], unless and until [Congress and Delaware and New Jersey] have expressly and formally consented thereto.[33]

In other words, while a resident of New Jersey (or Delaware) might gain ownership of the subaqueous soil underneath a particular wharf by adverse possession, New Jersey could not, by such occupation, acquire any jurisdiction from Delaware, let alone full sovereignty to the middle of the River. In *NJ v. DE II*, a unanimous Court would agree: "From acquiescence in these improvements of the river front, there can be no legitimate inference that Delaware made over to New Jersey the title to the stream up to the middle of the channel or even the soil under the piers."[34] But Delaware's 1901 Answer also signaled a willingness to grant New Jersey some authority to regulate wharves entering the circle — within the broad spectrum of powers identified in its Answer — in a mutually-agreeable interstate compact.

On January 31, 1903, Delaware's Attorney General, Herbert H. Ward, reported to Governor Hunn that, in light of a mutual concern over the "very considerable expense" of trying the case, counsel on both sides had agreed to attempt to "adjust all differences" out of court.[35] Ward advised that the "very laborious and critical examination of ancient documents" which preceded the preparation of Delaware's Answer had "greatly strengthened the belief and reliance of counsel for this state upon the justice of her claim."[36] Nevertheless:

> Notwithstanding this well grounded hope that the State of Delaware would be ultimately successful in the suit now depending [sic] in the Supreme Court of the United States, … if the entire controversy between the two states can be settled out of court in a manner creditable and satisfactory to both states, it would seem the part of good reason to attempt to make such a settlement.[37]

Governor Hunn agreed, and after legislative approval, commissioners from both States met in Philadelphia on March 12-14, 1903, to draft what would become the 1905 Compact.[38]

Delaware's commissioners, Hunn, Ward, and outside counsel George H. Bates, brought to the negotiating table a remarkable breadth of experience. Bates's mentor had been Thomas F. Bayard, Delaware's first counsel in *NJ v. DE I*. Bayard had served in the United States Senate from 1869 until 1885, as Secretary of State under President Grover Cleveland from 1885 to 1889 and, after a brief return to private practice, as ambassador to Great Britain from 1893-1897. Bates had gained diplomatic experience, first under Bayard, and then under Bayard's successor as Secretary of State, James G. Blaine. In particular, Bates had represented the United States in negotiating agreements with Germany and Great Britain to preserve the United States' interests in the Samoan Islands.[39] Similarly, Ward, before becoming Attorney General, was

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33. *Id.* (1 Del. App. at 118-19).

34. *NJ v. DE II*, 291 U.S. at 375-76.

35. 2 Del. App. at 1075-76.

36. *Id.*

37. *Id.*

38. *See* 2 Del. App. at 1104-05 (communication from Delaware's commissioners to the General Assembly, dated Mar. 16, 1903).

39. *See* Dennis J. Siebold, *Delaware and the Key to the Pacific: Thomas F. Bayard, George H. Bates, and the Acquisition of American Samoa*, 1886-1899, Del. History, Spring-Summer 2008 (vol. XXXII, no. 2), at 105, 148.

a partner of George Gray. In addition to representing Delaware in *NJ v. DE I* in the 1890s, Gray served in the United States Senate from 1885 to 1899, on an 1898 United States commission that negotiated with Canada over fishing rights in the Great Lakes, on the commission that arranged terms to end the Spanish-American War, and as a judge on the newly-constituted international court at the Hague.[40] As such, Delaware's commissioners were not only determined to defend the "integrity of the jurisdiction" of Delaware against New Jersey's "unfounded pretentions," but also familiar with diplomatic approaches to disputes between sovereigns, such as *modus vivendi* agreements that found "a way of living together" despite conflicting claims.[41]

For their part, New Jersey's commissioners (Attorney General Thomas N. McCarter, Governor Franklin Murphy, and future Governor Edward C. Stokes) brought their State's history of interstate compacts with Pennsylvania and New York over the rivers between them. Particularly relevant was the 1834 New Jersey-New York Compact ("1834 Compact"),[42] which drew an interstate boundary at the middle of the Hudson River, gave New York jurisdiction over the waters of the River to the low water-mark on the westerly or New Jersey side, and provided that New Jersey "shall have the exclusive jurisdiction of and over the wharves, docks, and improvements, made and to be made on the shore of the said state …."[43]

By March 14, 1903, the commissioners had produced a Compact. As Bates would later describe it to the Court, the Compact was "not a settlement of the disputed boundary, but a truce or a *modus vivendi*," the "main purpose" of which was to "provide for enacting and enforcing a joint code of fishing laws regulating the business of fishing in the Delaware River and Bay.[44] Of immediate effect, the Compact permitted each State to serve criminal and civil process on the River concurrently (Articles I and II) and declared that the citizens of each State "shall have and enjoy a common right of fishery" (Article III).[45] To further define this shared authority, the Compact called for the creation of an interstate commission to draft uniform fishing laws within two years (Article IV). Upon the adoption of these uniform fishing laws, the Compact declared that each State "shall have and exercise exclusive jurisdiction" to arrest its own citizens (Article IV).[46] Until then, all laws not contrary to the common right of fishery would remain in force (Article V).[47]

The final two substantive provisions of the Compact, Articles VI and VII, addressed the shellfish industry and regulation of riparian rights. In Article VI, the drafters clarified that "nothing herein shall affect the planting, catching, or taking of oysters, clams, or other shell fish, or interfere with the oyster industry as now or hereafter carried on under the

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40. *See* William T. Quillen, Potter Anderson & Corroon, An American Law Practice: The First 175 Years 27-46 (2001) (describing the careers of Gray and Ward in the firm of Gray, Ward and Gray).

41. *See* Black's Law Dictionary 1021 (7th ed. 1999) (defining *modus vivendi* as an "instrument of toleration" that sets forth "the basis of a method of living together with a problem … pending a permanent settlement").

42. Compact between the State of New Jersey and the State of New York, 4 Stat. 708 (1834) (2 Del. App. at 885).

43. *NJ v. DE III*, 552 U.S. at 616.

44. *See id.* at 605 n.5. Bates delivered his "Statement of reasons submitted orally for the joint application of Counsel on both sides for suspension of proceedings until the further order of the Court" in February of 1906, in support of the counsels' request for an indefinite stay of *NJ v. DE I* while the Compact was pending in Congress and commissioners from both States were drafting joint fishing laws pursuant to Article IV thereof. 1 Del. App. at 190-91.

45. Compact, Appendix B to Report of Special Master, 2007 WL 4266844, at *5A.

46. *Id.* at *6A-7A.

47. *Id.* at *7A.

laws of either State."[48] And in Article VII, the drafters agreed that "[e]ach State may, on its own side of the river, continue to exercise riparian jurisdiction of every kind and nature, and to make grants, leases, and conveyances of riparian lands and rights under the laws of the respective States."[49]

Article VII addressed a legal rather than a practical dispute. As noted above, New Jersey had claimed sovereignty to the middle of the River based on its regulation of those wharves, and Delaware had denied that New Jersey's actions had given it any jurisdictional rights whatsoever. But the piers on the New Jersey side of the River that entered the disputed twelve-mile circle were few and non-controversial. They included docks for ferries that provided transportation between the States, and a pier serving an industrial facility owned by the Wilmington-based Du Pont company.[50] In the absence of a practical dispute, the States agreed only that New Jersey "may … continue" regulating riparian rights as it had been.

Article VIII of the Compact, a reservation of rights provision, stated: "Nothing herein contained shall affect the territorial limits, rights, or jurisdiction of either State of, in, or over the Delaware River, or the ownership of the subaqueous soil thereof, except as herein expressly set forth."[51] Finally, Article IX stated that, after approval by the legislatures of the States and ratification by Congress, the Compact would be "binding in perpetuity upon both of said States" and the suit would be "discontinued without costs to either party and without prejudice."[52]

On March 16, 1903, with the ink on the Compact barely dry, the commissioners submitted it to their respective legislatures for approval. New Jersey's commissioners explained that:

> … while it was not found practicable to settle the exact geographical boundary line between the two States, nevertheless every interest of the State of New Jersey has been protected, all its riparian, fishery and other rights and jurisdiction thoroughly safeguarded, and every question of practical difficulty between the two States settled for all time. At the same time, the interests of our sister State of Delaware have been amply protected in a manner acceptable to the Commissioners from that State.[53]

New Jersey's legislature approved the Compact. However, Delaware's House of Representatives objected that the submission of the Compact only a few days prior to the close of the legislative session required it to be "rushed through … with undue haste."[54] The House did not act on the Compact before the legislative session expired.

At its next session, in 1905, Delaware's General Assembly approved the Compact, but only after stiff debate. As the evidence started to come in, and Delaware's case looked strong, Bates, for one, had second thoughts about a settlement. He argued that "no agreement should be made until the Supreme Court has judicially decided the underlying and basic question of territorial jurisdiction."[55] Former State Senator Alexander B. Cooper agreed, prophesying that "Jerseymen

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48. *Id.*

49. *Id.*

50. *See* Hoffecker Report at 83-85.

51. Compact, Appendix B to Report of Special Master, 2007 WL 4266844, at *7A.

52. *Id.* at *7A-8A.

53. 2 Del. App. at 1110.

54. 4 Del. App. at 4749-50.

55. Hoffecker Report at 91 (quoting Bates).

are fighters, and if the matter is not settled by the court, they will continue their contentions whenever the opportunity arises."[56] But Ward and Delaware's new Attorney General, Robert H. Richards, who took office in January of 1905 along with the new Governor, Preston Lea, persuaded the General Assembly to approve the Compact in order to avoid further expense. In their view, the Compact would not "yield[ ] one foot of property or title," but if it were rejected, they warned, the General Assembly would be asked to provide another $10,000 to fund the suit.[57]

After Delaware and New Jersey approved the Compact, the States appointed commissioners under Article IV to a joint commission charged with developing uniform fishing laws. When their work was nearing completion, the States sought congressional approval of the Compact as required by the Constitution.[58] Congress ratified the Compact on January 24, 1907, and on April 15, 1907, the Court dismissed *NJ v. DE I* without prejudice.[59]

Ironically, the Compact achieved neither of its goals of establishing uniform fishing laws or of avoiding costly litigation. While the joint commission proposed uniform laws, Delaware's General Assembly made "certain modifications" so that the Delaware version did not match the bill as passed by New Jersey.[60] From time to time efforts were made to conform the bills, without success. Then, in the mid 1920's another dispute forced the States back into the expensive boundary litigation that they had hoped to avoid. By application of Murphy's Law, the Compact's only enduring contribution would be to spark yet a third Supreme Court litigation a century later, in 2005, this time over the meaning of the Compact itself.

C. *New Jersey v. Delaware II* (1929 – 1938)

In 1925 the controversy resurfaced when New Jersey officials arrested Delaware oystermen working in water claimed by both States in the Delaware Bay south of the River.[61] Again, the States appointed commissioners to seek a compromise, and again their efforts failed. In 1929, New Jersey filed *NJ v. DE II*, seeking a ruling on the boundary between the States both within the twelve-mile circle and south of the River into the Delaware Bay. In its Complaint, New Jersey revived the same two claims that it had dismissed without prejudice in *NJ v. DE I*: (i) that Delaware's chain of title from Penn was flawed and therefore of no effect, and (ii) that New Jersey had gained jurisdiction to the middle of the River by prescription.

This time the laborious task of producing evidence was completed, involving over two years of discovery and numerous days of live testimony.[62] But after discovery had ended, New Jersey injected a new issue into the case, based

56. Alexander Cooper, Editorial, *The Boundary Question*, Every Evening (Wilmington, Del.), Mar. 9, 1905, at 2-3 (produced in *NJ v. DE III* as NJ00692-93) (on file with author).

57. Hoffecker Report at 96.

58. U.S. Const. art. I, § 10, cl. 3 ("No State shall, without the Consent of Congress, … enter into any Agreement or Compact with another State ….").

59. *NJ v. DE II*, 205 U.S. 550 (1907).

60. See Biennial Message of Delaware Governor Preston Lea to the General Assembly (Jan. 5, 1909) (identifying lack of conformity). This document is set forth in the Appendix of the State of New Jersey on Motion for Summary Judgment, vol. 3, filed Dec. 22, 2005 ("NJ App.") at 356a-358a.

61. Hoffecker Report at 102.

62. *NJ v. DE II,* 55 S. Ct. 934, 934 (1933) (Report of the Special Master).

on Article VII of the Compact. Like Pea Patch Island, the argument appeared inconspicuously at first, on page 126 of New Jersey's mammoth 749-page opening "brief" before the Special Master, filed on August 15, 1932. There, New Jersey argued that Article VII "clearly acknowledges and confirms the jurisdiction which [New Jersey] had previously, and has since, exercised in the ownership and disposition of lands under water in the disputed area" to the middle of the River in the twelve-mile circle. New Jersey contended that the Compact "alone, is sufficient to sustain the title of [New Jersey] and its grantees in the bed of the river east of the ship channel, independent of all other considerations."[63]

The task of responding to New Jersey's brief was assigned to Delaware's outside counsel, the formidable Clarence A. Southerland, who had been Delaware's Attorney General (1925-1929) and would go on to serve a twelve-year term as the first Chief Justice of Delaware's separately-constituted Supreme Court (1951-1963).[64] In Delaware's reply brief, submitted on September 12, 1932, Southerland pointed out that the Compact had never been at issue in the case. While New Jersey's Complaint set forth with "great particularity the sources of [its] claim to title" on the eastern half of the River [*i.e.,* Delaware's allegedly flawed chain of title and New Jersey's exercises of jurisdiction], the Complaint "nowhere mentions the Compact as the source of that claim."[65] The construction previously placed on the Compact "has been the reverse to that now contended for" by New Jersey.[66] Indeed, Southerland pointed out, this was "the first time the idea has ever been advanced that the Compact of 1905 settled the boundary dispute within the twelve-mile circle."[67]

Because no discovery had been taken on the meaning of the Compact, and the Delaware commissioners involved in drafting it, Bates, Hunn, and Ward, had passed away,[68] Southerland was left to make what arguments he could based on the text. He was sure that Article VII did not acknowledge any jurisdiction to the middle of the River, but less sure exactly what it did do. In Delaware's reply brief, he argued that Article VII was "merely a recognition of the rights of the riparian owners of New Jersey and *a cession to the State of New Jersey by the State of Delaware of jurisdiction to regulate those rights*."[69] At oral argument, also on September 12, 1932, Southerland told the Special Master that "*in my view* the Compact of 1905 *ceded* to the State of New Jersey all the right to control the erection of those wharves and to say who shall erect them, and it was a very sensible thing to do." [70] Therefore, New Jersey had no case "for the application of any doctrine of prescription."[71]

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63. Plaintiff's August 15, 1932 Brief Before the Special Master at 126, *NJ v. DE II,* 55 S. Ct. 934 (1933) (No. 13) (on file with Delaware State Archives).

64. *See* Delaware Bar in the Twentieth Century 375-379 (H. Winslow, A. Bookout, & P. Hannigan eds. 1994).

65. Reply Brief of Defendant Before Special Master at 9-10, *NJ v. DE II,* 55 S. Ct. 934 (1933) (No. 13) (1 NJ App. at 123a-124a).

66. *Id.*

67. *Id.*

68. Bates died in 1916, Hunn in 1926, and Ward in 1927.

69. Reply Brief of Defendant Before Special Master at 9-10, *NJ v. DE II,* 55 S. Ct. 934 (1933) (No. 13) (emphasis added) (1 NJ App. at 123a-124a).

70. Transcript of September 12, 1932 Oral Argument, *NJ v. DE II*, 55 S. Ct. 934 (1933) (No. 13) (emphasis added) (1 NJ App. at 126a-1 to 127a).

71. ***Id.*** A year later, in Delaware's brief to the Court on New Jersey's exceptions to the Special Master's recommendations, Southerland restated the point more tentatively: "*Even if* the Compact of 1905 be construed as ceding to the State of New Jersey the

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On October 9, 1933, the Special Master issued a report recommending that Delaware's claim to sovereignty throughout the twelve-mile circle be upheld as its chain of title was good and such title was not lost due to prescription or the Compact.[72] South of the circle and into the Delaware Bay, the Special Master agreed with New Jersey that the States' boundary should follow the thalweg (the mid-point of the shipping channel), rather than the geographic middle of the River as Delaware had argued.[73] In a unanimous opinion authored by Justice Cardozo, issued on February 5, 1934, the Court affirmed the report in all respects.[74] Along the way the Court quickly dispatched New Jersey's Compact argument, stating:

> We are told that by this compact the controversy was set at rest and the claim of Delaware abandoned. It is an argument wholly without force. The compact of 1905 provides for the enjoyment of riparian rights, for concurrent jurisdiction in respect of civil and criminal process, and for concurrent rights of fishery. Beyond that it does not go.[75]

In rejecting New Jersey's boundary claim, the Court was not required to parse Article VII or other provisions of the Compact. But the Court left ample room for dispute by stating that "[w]ithin the twelve-mile circle, the river and the subaqueous soil thereof up to low water mark on the easterly or New Jersey side will be adjudged to belong to the state of Delaware, *subject to the Compact of 1905*."[76]

In a report to Delaware Attorney General Percy Warren Green dated July 3, 1935, shortly after the Court had issued its final decree, Southerland admitted that, "[t]he meaning of [Article VII] of the compact is far from clear."[77] But he was certain of one thing: "there will obviously be a difference of opinion between the States on the proper construction of this compact."[78] As late as 1938, New Jersey filed motions petitioning the Court to reconsider its ruling on the twelve-mile circle.[79] Although the Court denied them, the motions were, like Southerland's report, intimations that the controversy still "would not down."

D. *New Jersey v. Delaware III* (2005 - 2008)

In the decades after the Court resolved the boundary dispute, the Compact gathered dust as the fishing industry on the River died out and the States adopted a cooperative approach to boundary-straddling riparian projects. Delaware did

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right to determine to whom riparian rights … shall be granted, it would still not affect the boundary between the States." Reply Brief of Defendant (on exceptions to the report of the Special Master) at 28-29, *NJ v. DE II*, 55 S. Ct. 934 (1933) (No. 13) (emphasis added) (1 NJ App. 141a-142a).

72. *NJ v. DE II,* 55 S. Ct. at 965-66.

73. *Id.* at 966.

74. *NJ v. DE II,* 291 U.S. 361 (1934) (opinion of the Court); *see also NJ v. DE II*, 295 U.S. 694 (1935) (decree).

75. *NJ v. DE II*, 291 U.S. at 377-78.

76. *Id*. at 385.

77. Report from Clarence A. Southerland to Warren Green (July 3, 1935) (2 NJ App. at 199a).

78. *Id.*

79. *See* Report, *supra* note 7, at 17.

not begin regulating riparian rights until the 1960's, when it first passed laws regulating the use of its subaqueous lands.[80] In 1971, Delaware adopted the Delaware Coastal Zone Act ("DCZA") to preserve its fragile coastal zone for tourism and recreation.[81] New Jersey's public officials did not object when, in 1972, Delaware denied an application by El Paso Eastern under the DCZA to construct an LNG terminal from the New Jersey side of the River into the twelve-mile circle just north of Wilmington.[82] In 1980, New Jersey stated in a document filed under the Federal Coastal Management Act[83] that "any New Jersey project extending beyond mean low water must obtain coastal permits from both states."[84] Apart from the El Paso Eastern proposal, from 1969 through 2004, only three riparian structures were built from the New Jersey side of the River into the circle, and Delaware regulated all three.[85]

The era of cooperation ended in 2005, soon after British Petroleum ("BP") sought permission from Delaware to construct an LNG terminal on the River on almost the same spot as the proposed El Paso Eastern terminal in 1972. BP's project called for a 2,000 foot long, 50 foot wide pier extending from the New Jersey bank of the River into Delaware territory. To build the pier and accommodate the supertankers that would berth there, the project would require dredging 1.24 million cubic yards of riverbed, affecting approximately 29 acres of Delaware soil. The supertankers would transport 200,000 cubic meters of LNG up the River and under the Delaware Memorial Bridge, past densely-populated areas to an offloading point just north of Wilmington.[86]

On February 2, 2005, Delaware's Department of Natural Resources and Environmental Control determined that the proposed LNG terminal would constitute a prohibited bulk product transfer facility under the DCZA. After BP lost an administrative appeal, it looked to New Jersey for help. BP's outside counsel had represented Virginia successfully in another original jurisdiction case, *Virginia v. Maryland* (2003), involving a dispute over riparian rights in the Potomac River.[87] With some coaching from BP, New Jersey advised Delaware that, under Article VII of the Compact and *Virginia v. Maryland*, Delaware had no authority to interfere with BP's project. Delaware disagreed, and the ensuing rhetoric recalled the days of the tugboat *Falcon*. New Jersey legislators introduced a bill threatening to withdraw State

80. *See id*. at 70-71. In 1986 Delaware adopted its current Subaqueous Lands Act, 65 Del. Laws ch. 508, Del. Code Ann. tit. 7, ch. 72.

81. The DCZA declares that "the coastal areas of Delaware are the most critical areas for the future of the State in terms of the quality of life in the State." Del. Code Ann. tit. 7, § 7001. The public policy of Delaware is to control the location, extent and type of industrial development in Delaware s coastal areas. *Id.* "[O]ffshore bulk transfer facilities represent a significant danger of pollution to the coastal zone and generate pressure for the construction of industrial plants in the coastal zone, which construction is declared to be against public policy." *Id.* Therefore, a "prohibition against bulk transfer facilities in the coastal zone is deemed imperative." *Id.*; *see also* Del. Code Ann. tit. 7, § 7003 (offshore gas, liquid or solid bulk product transfer facilities which are not in operation on June 28, 1971, are prohibited).

82. *See NJ v. DE III,* 552 U.S. at 619-20.

83. 16 U.S.C. § 1451 *et seq*.

84. Report, *supra* note 7, at 72-73.

85. *Id*. at 73-76.

86. *NJ v. DE III*, 552 U.S. at 606-07.

87. Virginia v. Maryland, 540 U.S. 56 (2003). In that case, the Court held that Maryland, the owner of the Potomac to the Virginia shore, could not interfere with Virginia's plans to construct a water intake pipe from the Virginia side of the Potomac into Maryland territory on the river, based on the terms of a 1785 compact between the states and an 1877 arbitration award.

pension funds from Delaware banks if Delaware did not relent. Two Delaware legislators responded by introducing a bill to authorize the National Guard to protect Delaware's borders from encroachment. Not to be outdone, a New Jersey legislator explored the seaworthiness of the decommissioned battleship *New Jersey* in the event the State was forced to repel an "armed invasion" by Delaware.[88]

On July 28, 2005, New Jersey filed in the Supreme Court a motion to reopen *NJ v. DE II* seeking a declaration that Delaware could not interfere with New Jersey's regulation of riparian projects appurtenant to its shore. The Court instead authorized New Jersey to commence a third original jurisdiction action and on January 23, 2006, appointed Ralph I. Lancaster, Jr., the Special Master in *Virginia v. Maryland,* to serve in the same capacity in *NJ v. DE III*.[89] The States then undertook extensive discovery into the history surrounding the Compact, followed by briefing and oral argument in Philadelphia, just blocks from where the Compact was drafted.

Both before the Court and the Special Master, New Jersey highlighted Southerland's statements in *NJ v. DE II* that Article VII was a "cession" of jurisdiction.[90] As the case progressed through discovery, Delaware brought to light documents relating to the Compact that Southerland had not been given an opportunity to consider, such as the 1834 New Jersey – New York Compact and Bates's explanation of the Compact to the Court in 1906 as a "truce or *modus vivendi*."[91] Delaware also pointed out that New Jersey officials had made their own inconvenient statements contrary to New Jersey's claim of exclusive jurisdiction over boundary-straddling riparian projects.[92]

On April 2, 2007, the Special Master issued a 100-page report recommending that the Court conclude that Article VII created overlapping jurisdiction over the River. New Jersey could exercise riparian jurisdiction over wharves extending from its shore into the twelve-mile circle. However, New Jersey could not grant lands in Delaware territory. And Delaware was entitled to exercise police power jurisdiction over improvements extending onto its territory, including by enforcing its environmental laws to block the proposed BP project.[93]

In addressing New Jersey's exceptions to the Special Master's Report, the eight Justices who participated in the case[94] proposed four additional readings of Article VII. In Justice Ginsburg's opinion for a majority of five, the Court held that "New Jersey and Delaware have overlapping authority to regulate riparian structures and operations of extraordinary character extending outshore of New Jersey's domain into territory over which Delaware is sovereign."[95] Because BP's LNG terminal was of extraordinary character, Delaware had authority to block it. Justice Stevens concurred with the Court's conclusion that Delaware retained authority to block the terminal, but read Article VII to permit New Jersey to

88. *See* Report, *supra* note 7, at 21.

89. *See NJ v. DE III*, 546 U.S. 1147 (2006) (appointing Special Master).

90. New Jersey's July 28, 2005 Motion to Reopen and for a Supplemental Decree at 7.

91. *NJ v. DE III*, 552 U.S. at 605 n.5.

92. *Id*. at 620 (quoting N.J. Coastal Management Program and Final Impact Statement 20 (Aug. 1980) (emphasis added).

93. Report, *supra* note 7, at 99-100.

94. Justice Breyer, who reportedly held BP stock, took no part in the consideration or decision of the case. *See NJ v. DE III*, 552 U.S. at 620.

95. *Id*. at 603, 623-24.

make grants and authorize the building of wharves within Delaware territory only "to the extent that such activities are not inconsistent with Delaware's exercise of its police power."[96] Justice Scalia, joined by Justice Alito, dissented, stating that Article VII conceded to New Jersey full and exclusive control over riparian projects on the New Jersey side, including the proposed terminal.[97] And at oral argument, Justice Ginsburg proposed that Article VII might have permitted certain conduct to continue without conceding jurisdiction.

II. THE READINGS OF THE COMPACT AND THE "HISTORY OF THE TIMES …."

As the Court acknowledged in *NJ v. DE III*, interstate compacts are presumed to be "drawn by persons competent to express their meaning, and to choose apt words in which to embody the purposes of the high contracting parties."[98] Thus, the Compact drafters presumably expressed their intent clearly and precisely in Article VII by stating:

> Each State may, on its own side of the river, continue to exercise riparian jurisdiction, of every kind and nature, and to make grants, leases, and conveyances of riparian lands and rights under the laws of the respective States.[99]

Unfortunately, a century later, these words yielded five different understandings over a 180-degree spectrum, only one of which (at most) could be correct. In light of "the history of the times,"[100] the reading that was most likely correct was not that of the Court, or of Justice Scalia in dissent, but of Justice Ginsburg at oral argument, proposing that Article VII simply allowed New Jersey to continue unobjectionable conduct in the shadow of an unresolved boundary dispute, without doing anything dispositive.

A. The Court's "Overlapping Authority" Reading

Based on the text of the Compact and its historical context, the Court properly rejected New Jersey's claim that Article VII conceded to it exclusive jurisdiction over all riparian projects extending from New Jersey into the twelve-mile circle.[101] But as to what Article VII did mean, the Court stumbled in relying on two post-Compact considerations: Southerland's statements in the 1930's and the statements of public officials from New Jersey in the 1970's and 1980's. The Court held that Article VII ceded to New Jersey some, but not all, jurisdiction, such that the Court's boundary decision resulted in a regime of overlapping jurisdiction. As to how such a regime would operate, the Court fashioned a test unmoored from

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96. *Id.* at 625 (Stevens, J., concurring).

97. *Id.* at 628 (Scalia, J., dissenting).

98. *Id.* at 615-16 (quoting Rocca v. Thompson, 223 U.S. 317, 332 (1912)).

99. Compact, Appendix B to Report of Special Master, 2007 WL 4266844, at *7A.

100. Rhode Island v. Massachusetts, *supra* note 8, 37 U.S. at 723.

101. *NJ v. DE III*, 552 U.S. at 609.

the text of the Compact, whereby Delaware would retain jurisdiction over projects of "extraordinary character," while New Jersey would have jurisdiction over the exercise of "ordinary and usual riparian rights."[102]

Beginning with the text of Article VII, the Court focused on the term "riparian jurisdiction," in which "riparian" stood as a "limiting modifier."[103] New Jersey was permitted to exercise, not "exclusive jurisdiction" or "jurisdiction unmodified," but only "*riparian* jurisdiction."[104] Thus, New Jersey was not entitled to exercise complete jurisdiction over all issues relating to wharves, but only jurisdiction over riparian rights, which were subject to the general police power of the sovereign under the background law of the time.[105] Particularly in light of Article VIII's requirement that any cession of territorial jurisdiction over the River be "express," the Court "resist[ed]" reading "riparian jurisdiction" as "tantamount to an express cession by Delaware of its entire territorial … jurisdiction … over the Delaware River."[106]

Two historical considerations confirmed the Court's reading of the text.[107] First, the drafters had incorporated into the 1905 Compact, with minor variations, three provisions from the 1834 New Jersey-New York Compact.[108] But in Article VII the drafters had not adopted the provision in the 1834 Compact declaring that New Jersey "shall have the exclusive jurisdiction of and over the wharves, docks, and improvements, made and to be made on the shore of the said state …."[109] Noting this conspicuous disparity, the Court observed that "New Jersey could hardly claim ignorance that Article VII could have been drafted to grant New Jersey 'exclusive jurisdiction' (not merely 'riparian jurisdiction')."[110]

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102. *See id*. at 603 ("New Jersey and Delaware have overlapping authority to regulate riparian structures and operations of extraordinary character extending outshore of New Jersey's domain into territory over which Delaware is sovereign"); *id.* at 623-24 (Decree) ("1.(a) The State of New Jersey may … exercise governing authority over ordinary and usual riparian rights… ; (b) The State of Delaware may … exercise governing authority over the construction, maintenance, and use of … wharves and other improvements appurtenant to the eastern shore of the Delaware River within the twelve-mile circle … to the extent that they exceed ordinary and usual riparian uses").

103. *Id*. at 609.

104. *Id*.

105. As the Court noted, the term "riparian jurisdiction" was "novel," without precedent in fact. *Id*. at 610-11. However, that general term was understandable in light of the States' different approaches to the regulation of riparian rights. Delaware and most other states recognized riparian rights at common law and enforced them in judicial proceedings. New Jersey, however, had developed a statutory regime beginning in 1864 to govern its citizens' riparian rights -- perhaps due to the importance of riparian rights at or near the ports of Trenton, New York, and Philadelphia. Hoffecker Report at 83-85.

106. *NJ v. DE III*, 552 U.S at 611-12.

107. Resort to extrinsic evidence of compact negotiations is "entirely appropriate" to resolve ambiguities in interstate compacts. Oklahoma v. New Mexico*,* 501 U.S. 221, 236 n.5 (1991) (citing cases) (noting that "a congressionally approved compact is both a contract and a statute," that the Court repeatedly has looked to legislative history to construe ambiguous statutes, and that it had "on occasion looked to evidence regarding the negotiating history of other interstate compacts").

108. *See* Compact between the State of New Jersey and the State of New York, 4 Stat. 708 (1834) (2 Del. App. at 885) and Appendix J to Report of Special Master, *NJ v. DE III,* 2007 WL 4266844, at *153A (Table Comparing Similar Provisions in the New-Jersey-New York Compact of 1834 and the New Jersey-Delaware Compact of 1905).

109. *Id*.

110. *NJ v. DE III*, 552 U.S. at 616-17 (quoting Report at 67).

Second, the Court referenced contemporaneous evidence suggesting that "Delaware would not have willingly ceded all jurisdiction over matters taking place on land that [Delaware adamantly] contended it owned exclusively and outright."[111] In particular, the Court noted Ward's statement to Governor Hunn in 1903 that the process of preparing Delaware's Answer had "greatly strengthened the belief and reliance of counsel … upon the justice of her claim,"[112] and Bates's 1906 description of the Compact as "a truce or *modus vivendi*."[113] In light of such evidence, the Court agreed with the Special Master that New Jersey's claim that Delaware had surrendered complete jurisdiction over projects entering the twelve-mile circle, through Article VII, was "implausible."[114] As the Court noted, such a broad concession would have rendered the Court's 1934 settlement of the boundary "an academic exercise with slim practical significance."[115]

Based on those historical considerations, the Court might have questioned whether Article VII conceded to New Jersey any jurisdiction. After all, Article VII stated only that New Jersey "may … continue to exercise" jurisdiction. But Southerland had read Article VII as a "cession" of jurisdiction to New Jersey, and his statements exerted a powerful influence on both the Special Master and the Court seven decades later. With no discussion, and based only on a reference to Southerland's statements, the Court in *NJ v. DE III* held that New Jersey "did indeed preserve the right to exercise its own jurisdiction over riparian improvements appurtenant to its shore."[116] And while the Court would say only that New Jersey had "preserved" jurisdiction, rather than that Delaware had ceded it, the Court's holding was the same.

In fact, the historical evidence weighs heavily against such a concession. As the drafters sat down to negotiate the Compact on March 12-14, 1903, the States had staked out contrary positions on the effect of New Jersey's regulation of wharves entering the twelve-mile circle. New Jersey had alleged in its Complaint that its acts had established full jurisdiction to the middle of the River. Delaware had responded, in its Answer, that New Jersey's actions could not manufacture any jurisdiction. In other words, as far as Delaware was concerned, New Jersey had no jurisdiction to preserve. If, from that locked-horns position, Delaware's commissioners had emerged from the negotiations in March of 1903 with a document that "preserves for New Jersey" riparian jurisdiction, as the Court stated,[117] then Delaware would have abandoned its position without receiving anything in return, as New Jersey retained its larger claim to complete jurisdiction to the middle of the River. Such a concession would have been especially odd because it would have enabled New Jersey effectively to annex portions of Delaware, pier by pier, by conveying them away, at the same time that Delaware was insisting that it had preserved in full its sovereignty over the subaqueous lands within the twelve-mile circle.

Moreover, Southerland had been blind-sided by New Jersey's introduction of the Compact into the case via its post-discovery brief on August 15, 1932. He was required to construe Article VII, along with 748 pages of other arguments in New Jersey's brief, in time to file his reply brief and participate in oral argument before the Special Master on September 12, 1932. The voluminous record that the parties had compiled over the previous three years dealt with the

111. *Id.* at 613-14.

112. *Id.* at 614 n.15.

113. *Id.* at 605 n.5; *id.* at 614 n.15.

114. *Id*. at 613.

115. *Id*. at 622.

116. *Id.* at 614-15 (quoting Report at 89).

117. *Id*. at 622.

chain of title and prescription issues, and did not include evidence relating to the drafting of the Compact.[118] Indeed, neither the 1834 New Jersey - New York Compact nor the contemporaneous statements of Ward and Bates that the *NJ v. DE III* Court found so informative were part of that record. Given that Southerland was forced to construe a nearly 30-year-old document in short order and in a virtual evidentiary vacuum, his reading should not have been treated as effectively binding on Delaware.[119]

In concluding that Article VII ceded some but not all riparian jurisdiction to New Jersey, the Court also relied on tenuous "course of conduct" evidence from the 1970s and 1980's.[120] In particular, the Court pointed to New Jersey's 1980 submission in connection with the federal Coastal Zone Management Act, in which New Jersey stated that "any New Jersey project extending beyond mean low water mark must obtain coastal permits from both states."[121] This document, written over seventy years after the framing of the Compact, with no proof that the authors were even aware that it existed, casts no real light on the original meaning of the Compact.[122] Instead, the gaping absence of any relevant course of conduct over the decades between 1905 and the 1970s demonstrates how deeply the Compact had fallen into desuetude.

In any event, the Court's conclusion that Article VII conceded some, but not all, riparian jurisdiction led it into an analytical thicket. In a regime of dual jurisdiction over riparian projects, whose jurisdiction controls? Article VII did not say, so the Court was required to fashion a solution out of whole cloth. The Court declared that Delaware could not "impede ordinary and usual exercises of the right of riparian owners to wharf out from New Jersey's shore" but could exert governing authority over wharves of "extraordinary character."[123] Tellingly, the Court's Decree setting forth this result did not even refer to Article VII.

Thus, while the Court began well by using historical context to reject New Jersey's claim that Article VII gave it exclusive jurisdiction over riparian projects, unfortunately, the Court relied too heavily on ahistorical considerations in

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118. *See* Stipulated Record, Descriptive List of Exhibits, Volume II, and Plaintiff's Aug. 15, 1932 Brief Before Special Master at 126, *NJ v. DE II*, 55 S. Ct. 934 (1933) (No. 13) (citing only Exhibit 53, copy of the Compact) (both documents are on file at the Delaware State Archives).

119. New Jersey argued before the Special Master that Delaware was judicially estopped from opposing New Jersey's cession claim based on Southerland's reading of Article VII. The Special Master rejected this contention, at least in part, in concluding that "Delaware is not judicially estopped from challenging New Jersey's contention that New Jersey alone has jurisdiction to regulate any riparian improvements occurring on New Jersey's side." Report, *supra* note 7, at 91. In its exceptions to the Report, New Jersey did not renew its judicial estoppel claim, *see NJ v. DE III*, 552 U.S. at 608 n.12, but relied heavily on the statements as evidence of the meaning of Article VII, to great effect. In fact, application of the doctrine of judicial estoppel would have been unwarranted at least because (i) nothing in the Court's opinion in *NJ v. DE II* indicated that Delaware had "succeeded in persuading" the Court "to accept" Southerland's particular reading of Article VII; and (ii) "considerations of equity" -- in particular, New Jersey's assertion of the Compact claim only after discovery was closed in *NJ v. DE II* -- weighed heavily against binding Delaware to Southerland's reading of the text in *NJ v. DE III*. New Hampshire v. Maine, 532 U.S. 742, 750, 755 (2001).

120. Course of conduct evidence is considered in interpreting ambiguous contracts because the parties to an agreement "know best what they meant, and their action under it is often the strongest evidence of their meaning." Restatement (Second) of Contracts § 202 cmt. g.

121. *NJ v. DE III*, 552 U.S. at 621 (quoting N.J. Coastal Management Program and Final Impact Statement 20 (Aug. 1980)) (emphasis added).

122. While acknowledging the lack of evidence demonstrating that the government officials in question knew of the Compact, the Court relied on the general principle that "[a]ll citizens … are presumptively charged with knowledge of the law." *Id*. at 621 n.20.

123. *Id*. at 622-23; *see also id*. at 603 (Delaware has jurisdiction over riparian uses of "extraordinary character").

concluding that Article VII, together with the boundary decision, created a dual jurisdiction regime. While the Court's "extraordinary character" test solved the trumping problem inherent in such a regime, the jerry-built character of that test invited criticism, which Justice Scalia would not hesitate to provide.

B. Justice Scalia's "Full and Exclusive Control" Reading

In the opening paragraph of his dissent, Justice Scalia immediately put his finger on two key weaknesses in the Court's analysis. First, the Court's concession that Article VII had "preserved" riparian jurisdiction for New Jersey — or, as he would say more directly, "that jurisdiction and power over [riparian rights] *were given to New Jersey*"[124] — supported New Jersey's contention that it had jurisdiction over a riparian project such as BP's LNG offloading terminal. Second, the Court's "extraordinary character" test, which it devised to sustain Delaware's authority to block the terminal, was unsatisfying on many levels: it was unclear, it had "absolutely no basis in prior law," and it was "so unheard-of … that its first appearance in this case is in the Court's opinion."[125] But Justice Scalia's reading suffered from its own weaknesses, including its failure to offer any persuasive rebuttal to the textual and historical evidence suggesting that Delaware did not concede jurisdiction over riparian projects, and its misplaced reliance on Southerland's reading of Article VII.

For Justice Scalia, Article VII was nothing less than a full surrender of the "authority of a sovereign power to govern or legislate" by which Delaware "convey[ed]" to New Jersey "riparian jurisdiction of every kind and nature."[126] At common law, riparian rights included the right "to erect wharves for the loading and unloading of goods."[127] While riparian jurisdiction did not allow New Jersey to put a casino on the end of a pier, such jurisdiction covered the "core riparian right of building a wharf to be used for the … unloading of cargo," including BP's proposed LNG terminal.[128]

Justice Scalia's reading of the Compact was unpersuasive because it failed to account for the nuances in the text that reflected the historical context in which it was written. For Justice Scalia, there could be no "presumption against concession of sovereignty" because, in his view, "[t]here is no way the Compact can be interpreted other than as a yielding by both States of what they claimed to be their sovereign powers."[129] But in fact, the drafters had hard-wired into the Compact, in Article VIII, a *textual* presumption against jurisdictional cession: "nothing herein contained" could affect "the territorial limits, rights, or jurisdiction of either State of, in, or over the Delaware River, or the ownership of the subaqueous soil thereof, except as herein *expressly* set forth."[130] Both sides had agreed to disagree about their larger jurisdictional dispute, and neither wanted to face, down the road, clever arguments as to alleged concessions made in ambiguous terms.

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124. *Id*. at 628 (emphasis added).

125. *Id*.

126. *Id*.

127. *Id*. at 633; *see also id*. at 631 (At common law, it was considered "a necessary incident of the right [to construct wharves and piers] that they shall project to a distance from the shore necessary to reach water which shall float vessels, the largest as well as the smallest, that are engaged in commerce upon the water into which they project").

128. *Id*. at 633-34.

129. *Id*. at 629-30.

130. Compact, Appendix B to Report of Special Master, 2007 WL 4266844, at *7A.

Nor did the drafters limit themselves to a collection of binary win-lose propositions, as Justice Scalia suggested. For example, they agreed to leave certain issues unresolved (the boundary, oystering) and put in place a process for resolving others by sharing jurisdiction over service of process and fashioning uniform fishing laws. Also, the legal background suggested that Article VII accomplished something more nuanced than a jurisdictional white flag. While *NJ v. DE I* was pending, the Court had addressed an analogous situation in *Coffee v. Groover*,[131] involving a dispute between persons claiming land under competing grants from Georgia (which, like New Jersey, had first exercised *de facto* jurisdiction) and Florida (which, like Delaware, turned out to be the true sovereign). In reversing a judgment for the party claiming from Georgia, the Court had held that "when the true boundary is ascertained … grants made by [a] sovereign beyond the limits of his rightful territory, whether he had possession or not, (unless confirmed by proper stipulations) fail for want of title in the grantor."[132] Thus, New Jersey needed at least a stipulation authorizing its grants and other actions in order to avoid forfeiture of its riparian interests and those of its riparian owners. Delaware, for its part, also needed at least to authorize such activities to continue to prevent New Jersey from adding evidence to its prescription claim. Neither State's needs required that Delaware surrender jurisdiction over the very lands within the twelve-mile circle that it adamantly claimed were its own, and that were the subject of the larger boundary dispute that they had agreed they could not resolve.

Justice Scalia's argument as to the historical plausibility of a complete surrender of riparian jurisdiction by Delaware was also unpersuasive.[133] For example, he suggested that Delaware might have given up such jurisdiction because the case "appeared to be going badly" for it, based solely on the Court's "rather ominous sounding" order granting a preliminary injunction barring Delaware from enforcing its 1871 fishing law.[134] But that order was entered in 1877, over twenty-five years before the drafters sat down to negotiate the Compact. While the Court had stopped Delaware from attempting to enforce a facially discriminatory (and probably unconstitutional) law in the face of threats of violence, the 1877 injunction hardly signaled how the Court would resolve the complex boundary dispute on a full record.[135] At least, New Jersey did not seem particularly emboldened by the injunction, as it waited until 1901 to prosecute the case, and then only after the Court prodded it to do so. Any speculation about the impact of the 1877 order on the view of Delaware's 1903 commissioners as to how their case "was going" seems strained as compared with the contemporaneous statements of those commissioners — such as Ward's 1903 statement to Governor Hunn that Delaware's recently gathered evidence had only strengthened its "belief and reliance" upon "the justice of her claim"[136] — which Justice Scalia did not address.

Finally, while Justice Scalia concluded that post-Compact conduct was irrelevant because he found no ambiguity in the text, his reading was at least confirmed (and possibly influenced) by Southerland's statements in *NJ v. DE*

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131. 123 U.S. 1 (1887).

132. *Id*. at 10.

133. *NJ v. DE III*, 552 U.S. at 629-30.

134. *Id.*

135. March 26, 1877 Order for Preliminary Injunction, *NJ v. DE I,* 205 U.S. 550 (1907) (No. 1) (1 Del. App. at 66-68). New Jersey had filed several affidavits from its fishermen in connection with its Complaint and motion, and some of these warned of violence if Delaware continued to arrest Jerseymen attempting to earn their living on the River.

136. *NJ v. DE III*, 552 U.S. at 614 n.15. Justice Scalia also stated that Delaware "received plenty" in the Compact as a whole, including access to fisheries on the eastern half of the River and release from the suit. *Id.* In fact, the Compact avoided windfalls to either side. Both States wanted to avoid the cost of further litigation. And both agreed to a common right of fishery and reciprocal rights to make arrests on the water until the uniform laws were adopted, after which time each State would arrest its own.

II. Justice Scalia found Southerland's "concessions" to be a "powerful indication that Delaware's understanding of the Compact was the same as the one I assert."[137] But as discussed above, Southerland's reading of the Compact in *NJ v DE II* — without any opportunity to explore its historical context — did not warrant the weight that Justice Scalia and the other Justices gave it.

In sum, while Justice Scalia's dissent threw a powerful light upon the lack of a textual foundation for the Court's "extraordinary character" test, his own reading was at odds with the nuanced language of Article VII and its historical context.

C. Justice Ginsburg's Status Quo Reading

Neither the Court nor the dissent in *NJ v. DE III* offered a reading of Article VII that fit the historical context in an entirely satisfying way. But Justice Ginsburg's suggested reading at oral argument — like the youngest child — is still left to consider. In the first exchange between the Court and New Jersey's counsel, Justice Ginsburg stated:

> … one of the striking things about this Compact is that to the extent that it is definite, there is a lot in here in detail about … arrests on the river and about fishing, but then you get to these two articles at the end … they certainly don't have that same definite detailed quality. As I read the Article VII … , it says – let's see – "may continue to exercise." So it seems to me that "may continue to" was just whatever was the status quo, that will continue; not to do anything dispositive, just whatever was will continue.[138]

Both as a matter of textual analysis and historical context, this simple "status quo" reading is remarkably compelling.

Only this reading gives weight to the verbal nuance in the central predicate clause in Article VII, "may … continue to exercise." Just as "riparian jurisdiction" did not mean "exclusive jurisdiction," so also "may continue to exercise" did not mean "shall have and exercise," or even, "may continue forever to exercise." "Continue" means "to remain in a given place or condition."[139] When the attorneys who drafted the Compact intended to declare a right in a dispositive way, they did so in the express terms required by Article VII, through traditional *habendum* clauses denoting the formal conveyance of both the right (to "have") and the use (to "enjoy" or "exercise").[140] In Article III, they declared that the citizens of both States "shall have and enjoy" a common right of fishery. In Article IV, they agreed that, once uniform

137. *Id*. at 637-38.

138. Transcript of November 27, 2007 Oral Argument at 4, *NJ v. DE III,* 552 U.S. 597 (2008) (No. 134), *available at* http://www.supremecourtus.gov/oral_arguments/argument_transcripts/06-134orig.pdf.

139. Webster's International Dictionary 314 (1898) (6 Del. App. at 4195).

140. A *habendum* clause refers to the part of a deed that defines the interest being granted, typically introduced with the words "to have and to hold" or some variation thereof. Black's Law Dictionary 716 (7th ed. 1999). In Roman law, the term *habere* signified "to have (the right to) something," which was sometimes distinguished from "*tenere* (to hold)," with *habere* referring to the right, [and] *tenere* to the fact." *Id.* The Court in *NJ v. DE I* had previously alluded to the distinction between a claim of right and the actual exercise of jurisdiction. In its March 26, 1877 order in *NJ v. DE I*, the Court held that it "appear[ed]" that New Jersey "has *claimed and exercised* jurisdiction over the easterly portion of the river." 1 Del. App. at 67 (emphasis added). In *NJ v. DE II,* the Special Master made the same distinction in the finding that "Delaware at all times since 1783 has *claimed, asserted and exercised* exclusive dominion and jurisdiction over the lands and waters within the boundaries fixed by the said title deeds, as modified by the Compact of 1905 between the states of Delaware and New Jersey." *NJ v. DE II*, 55 S. Ct. at 964-65 (emphasis added).

laws were adopted, each State "shall have and exercise exclusive jurisdiction" to arrest its own inhabitants for violation of those laws. The drafters did not employ such a clause in Article VII — even though they could have borrowed one from the 1834 New Jersey – New York Compact, from which they took other provisions. Basic rules of construction require that their choice be given weight.

The status quo reading is in harmony with the legal context in which the drafters were working, as defined by the pleadings in *NJ v. DE I* and the background legal principles that they presumably knew. With Article VII, New Jersey had for the first time authorization from Delaware to continue to exercise riparian jurisdiction, such that its grants would not be null and void under *Coffee v. Groover*[141] in the event the Court later determined that New Jersey had conveyed disputed land outside its territory. And for its part, Delaware, by granting New Jersey permission to continue to regulate riparian jurisdiction, prevented any accumulation of evidence of prescription. By granting such permission, both sides safeguarded their interests.

The status quo reading is consistent with the contemporaneous statements by the drafters from both sides. Bates's description of the Compact as a "truce or *modus vivendi*" well characterizes a provision in which sovereigns agree to disagree as to legal rights so that a practical peace can be achieved. And New Jersey's commissioners advised their legislature that while the "questions of practical difficulty between the two States" — service of civil and criminal process and rights of fishery — had been "settled for all time," each State's riparian interests had only been "safeguarded."[142] By gaining permission from Delaware to "continue" acting as it had, New Jersey had indeed obtained a "safeguard" against forfeiture but had not "settled" the underlying jurisdictional issue.

Finally, the status quo reading has an attractive simplicity about it, as something the drafters might actually have agreed upon on March 12-14, 1903, after addressing the practical issues of fishing rights and arrests on the water. The States had not been at loggerheads over New Jersey's few exercises of riparian jurisdiction within the twelve-mile circle.[143] And New Jersey certainly had every right to regulate riparian uses above the low water mark on its side of the River. Why not allow New Jersey to "continue" doing what it had been doing without objection, so long as each State's rights were protected? One can well imagine Delaware agreeing to act in a spirit of interstate comity, saying in effect to its neighbor, "I think your tomato patch is crossing into my yard, but you may continue to garden there."

Neither the text of the Compact nor its historical context undermines the status quo reading. In arguing that Article VII should not be read as a temporary provision, the Special Master pointed out that, under Article IX, the Compact was "binding in perpetuity."[144] If that phrase were read into every individual provision of the Compact, then Article VII could be read as if the drafters had stated, "Each State may, on its own side of the River, continue to exercise riparian jurisdiction *in perpetuity*." But such intent could have been expressed far more directly by simply conveying the right at issue, as the drafters did with respect to fishing and arrests in Articles III and IV. Also, other Compact provisions were not designed to remain in effect in perpetuity (*e.g.*, the arrest provisions of Articles I and II were to be superseded, at least in

141. 123 U.S. 1 (1887).

142. 2 Del. App. at 1110.

143. *NJ v. DE II,* 291 U.S. at 377.

144. Report at 38. Delaware had argued that the reference to New Jersey's "own side of the River" in Article VII meant that New Jersey's "side" ended at the low water mark as of the 1934 boundary decision. In rejecting this contention, the Special Master relied on Southerland's "representations to the Court" in *NJ v. DE II*. *Id*. at 39. The Court agreed with the Special Master's analysis, dismissing the argument as "altogether fallacious." *NJ v. DE III*, 552 U.S. at 615. But neither the Special Master nor the Court discussed the separate "may … continue" language of Article VII.

part, by the arrest provision in Article IV that was to go into effect after adoption of uniform fishing laws). The general statement that the Compact was "binding in perpetuity" more likely meant that the Compact, as a whole, was a permanent agreement, while more specific provisions stood on their own and were either permanent, temporary, or open-ended, as necessary to achieve the drafters' purpose.[145]

The Special Master also stated that Bates referred to the Compact as a *modus vivendi* "only in connection with the still unresolved boundary dispute … rather than as a representation that the entire Compact was intended merely as a temporary measure."[146] But reading Article VII as merely permitting unobjectionable conduct to continue would not render the entire Compact temporary, as the agreements in Articles III and IV over fishing rights and arrests on the water were meant to be permanent. And even if the Compact was a *modus vivendi* only with regard to the boundary dispute, the status quo arrangement in Article VII would have fit well within that concept. After all, boundary determines ownership. Because Article VII involved the right to convey riparian lands, the language in Article VII that permitted the exercise of such jurisdiction to continue, while stopping short of a formal cession of jurisdiction, was consistent with the drafters' decision to leave unresolved the larger issue of boundary, which would determine ownership of the lands within the twelve-mile circle.

While Justice Ginsburg's status quo reading of Article VII never found its way into her opinion for the Court, it may help explain why the Court properly resisted as "implausible" New Jersey's claim that Delaware had surrendered complete jurisdiction over riparian projects within the twelve-mile circle. The status quo reading best fits the historical context — that is, the "state of things existing" when the Compact was framed and the "old law, the mischief, and the remedy."[147] The "state of things" in 1903-1905 was that there was no practical dispute over the construction of wharves on the New Jersey side of the River. The "old law" was, for Delaware, its historical claim of sovereignty over the lands and water within the twelve-mile circle, and for New Jersey, the statutes under which it had regulated the riparian rights of its citizens. The "mischief" was, for New Jersey, the prospect of forfeiture of grants made if Delaware was right about the boundary; and for Delaware, the risk of fueling New Jersey's prescription claim by ignoring its actions. The "remedy" was to permit New Jersey to continue its unobjectionable conduct while safeguarding both States' claims to sovereignty. Article VII was part of a larger *modus vivendi* that resolved the States' practical problems, safeguarded their respective jurisdictional claims, and enabled them to end their expensive litigation without prejudice.

III. CONCLUSION

In attempting to discover the meaning of Article VII of the Compact, the Court was forced to operate without much applicable precedent or evidence of a contemporaneous course of conduct. The term "riparian jurisdiction," was

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145. Even if Delaware had given New Jersey a perpetual license to exercise riparian jurisdiction, New Jersey's authority would always be subject to the paramount police power of the sovereign within its own territory. Justice Stevens essentially adopted this reading of Article VII in concurring with the result reached by the Court. *See NJ v. DE III*, 552 U.S. at 626 ("I would hold, therefore, that New Jersey may only grant, and thereafter exercise governing authority over, the rights of construction, maintenance, and use of wharves and other riparian improvements beyond the low-water mark to the extent that the grant and exercise of those rights is not inconsistent with the police power of the State of Delaware").

146. Report, *supra* note 7, at 39.

147. *Rhode Island v. Massachusetts*, *supra* note 8, 37 U.S. at 723.

not defined by legal precedent, and the "may continue" language never garnered much attention. As the River's fishing industry died out, the Compact also became a dead letter — until exhumed by BP and New Jersey in 2005.[148]

Under these circumstances, historical context is more than just one consideration among many. Rather, it is the reliable narrator, the trustworthy guide to understanding the thought expressed by the words chosen by persons who were living in that context. A reading that reflects the drafters' agreement can be reached only through a sympathetic understanding of the circumstances of those who drafted the words in dispute, recognizing that the drafters may have known what they were about in a way that we might not easily appreciate from a century away, and that our assumptions may not have been theirs. Ahistorical considerations, such as Clarence Southerland's reading of Compact text thirty years later, should not be given special weight. And ordinary assumptions, such as that a compact provision resolves rather than preserves an issue, may well not hold where, as here, the Compact was also a settlement agreement that reserved for another day the parties' dispute over ownership of subaqueous lands.

Fortunately, in *NJ v. DE III*, the Special Master and the Court entered into the world of the Compact drafters sufficiently to prevent New Jersey from gaining, through desuetude, a surrender of sovereignty over rights and lands that it did not obtain in Philadelphia in March of 1903. But time took its toll, and Delaware's sovereignty over its historic territory was compromised. Cooper and Bates were right in having second thoughts about the wisdom of entering into the Compact in order to avoid the expense of resolving the boundary dispute. An expedient compromise did cause mischief; Delaware would have been better served by pressing its boundary claim to conclusion first; and Delaware's gesture of inter-state comity would not go unpunished. Time and chance conspired to cloud the drafters' intent, and only by a jerry-built ruling did the Court preserve Delaware's historic sovereignty within the twelve-mile circle, at least enough to enable Delaware to block the construction of a massive LNG unloading terminal within its territory and contrary to its laws.

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148. *See* Hoffecker Report at 67-70, 102-04. In 1907, the joint commission charged with drafting uniform fishing laws reported the "gradual disappearance of the shad … and the almost total disappearance of the valuable sturgeon industries" due to industrial pollution and the destruction of small food fish by menhaden fishermen. *Id.* at 100. By the 1930's, "few if any fishermen cast their nets within the twelve-mile circle because there were few fish to be caught there." *Id.* at 104.

CRIMINAL LAW: 2008 DELAWARE SUPREME COURT DECISIONS

Michael F. McTaggart*

This article reviews and summarizes some of the fifty-five criminal law opinions issued by the Delaware Supreme Court in 2008, a substantial increase over the thirty-seven criminal law opinions in 2007. The article addresses the court's search and seizure decisions, trial evidentiary decisions, and decisions of significance or issues of first impression.

I. SEARCH AND SEIZURE DECISIONS

A. Community Caretaking Doctrine—*Williams v. State*

In *Williams v. State*,[1] the court held that a police officer's initial encounter with a person walking on a highway in the early morning hours of a cold day was not a seizure, and the stop of the individual was reasonable under the community caretaker doctrine.[2]

The defendant Williams was walking along the median of Route 113, Georgetown at 3:50 a.m. when he was observed by Corporal Brittingham of the Georgetown Police Department. The weather was cold and windy and the officer pulled up around ten feet behind Williams before activating his strobe light. Corporal Brittingham asked Williams if he wanted a ride and the defendant, declining the ride, stated that his car broke down and he was walking to a nearby gas station to be picked up by his mother. The officer did ask Williams for his name and date of birth as a matter of routine. After obtaining that information, the officer checked the information and learned that Williams had outstanding arrest warrants for unpaid traffic fines. The officer approached Williams a second time and asked if he knew the reason for the contact. Williams admitted that he had outstanding warrants, and upon further inquiry, further admitted to possession of a concealed handgun. The defendant was charged and convicted on the crime of Carrying a Concealed Deadly Weapon.[3]

In his appeal, Williams challenged the decision of the Superior Court which denied his motion to suppress the fruit of the claimed unlawful stop.[4] The court reviewed the question under the protections against illegal searches and seizures under the Delaware Constitution[5] and considered whether "a reasonable person would have believed he or she was not free to ignore the police presence."[6] Even under this standard which is more stringent than federal precedent,

* Mr. McTaggart is a Deputy Attorney General in the Delaware Department of Justice.

1. 962 A.2d 210 (Del. 2008).

2. *Id.* at 216-22.

3. *Id.* at 213.

4. *Id.*

5. Del. Const. Art. I, § 6.

6. *Williams,* 962 A.2d at 215 (citing Michigan v. Chesternut, 486 U.S. 567, 573 (1988); Jones v. State, 745 A.2d 856, 862 (Del. 1999)). The court noted that as a matter of Delaware constitutional law, the applicable standard for reviewing the legality of a seizure is the *Michigan v. Chesternut* decision. The Delaware law follows *Chesternut*, and not the subsequent decision modifying

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the court noted that police may initiate contact with citizens to ask questions and this type of encounter if consensual is not a seizure for Fourth Amendment purposes.[7] In Wright's case, the court ruled that the defendant was not seized as a result of the initial contact with the police officer.[8] The court found the encounter to be brief and noted that Williams voluntarily answered the officer's questions.[9] In the court's view, the brief encounter lacked the physical force or submission to authority to constitute a seizure.[10]

The court next ruled that, even if the defendant was seized, the initial encounter was reasonable and valid under the "community caretaker" or "public safety" doctrine.[11] Tracing the community caretaker role of police to *Terry v. Ohio,*[12] the court found that the majority of jurisdictions that have considered the issue have adopted the community caretaker doctrine.[13] The court relied on these surrounding jurisdictions and adopted the community caretaker function of police in Delaware.[14] The court stated that the "role of police in Delaware is not limited to merely the detection and prevention of criminal activity, but also encompasses a non-investigatory, non-criminal role to ensure the safety and welfare of our citizens."[15]

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federal law in *California v. Hodari D.*, 499 U.S. 621 (1991) (U.S. Supreme Court read *Chesternut* more closely to require some "physical force or submission to the assertion of authority").

7. *Williams,* 962 A.2d at 215 (citing Muehler v. Mena, 544 U.S. 93, 101 (2005); Royer v. State, 460 U.S. 491, 497-98 (1983); Lopez-Vazquez v. State, 956 A.2d 1280, 1286 n.5 (Del. 2008); Ross v. State, 925 A.2d 489, 494 (Del. 2007)).

8. *Williams*, 962 A.2d at 216.

9. *Id.*

10. *Id.* The court did not review the propriety of the encounter under Del. Code Ann. tit. 11, § 1902 which was not implicated because the police did not "demand" the defendant's name. The court noted that § 1902 codifies the reasonable suspicion standard for investigatory stops. *Id.* at 216 n.19 (citing Harris v. State, 806 A.2d 119, 126 n.20 (Del. 2002)).

11. *Williams,* 962 A.2d at 221.

12. 392 U.S. 1 (1968).

13. *Williams*, 962 A.2d at 217 (citing Terry, 392 U.S. at 13 ("[s]treet encounters between citizens and police officers are incredibly rich in diversity…. Encounters are initiated by the police for a wide variety of purposes, some of which are wholly unrelated to a desire to prosecute for crime."); Cady v. Dombrowski, 413 U.S. 433, 441 (1973) ("[l]ocal police officers … frequently … engage in what, for want of a better term, may be described as community caretaking functions, totally divorced from the detection, investigation, or acquisition of evidence relating to the violation of a criminal statute")).

14. *Williams*, 962 A.2d at 217-18 (citing Duck v. Alabama, 518 So. 2d 857, 859-60 (Ala. Crim. App. 1987); Crauthers v. Alaska, 727 P.2d 9, 10-11 (Alaska Ct. App. 1986); State v. Enos, 2003 WL 549212, at *4 (Del. Super. Feb. 26, 2003); Illinois v. Luedemann, 857 N.E.2d 187, 197 (Ill. 2006); Massachusetts v. Evans, 764 N.E.2d 841, 843 (Mass. 2002); Maine v. Pinkham, 565 A.2d 318, 319 (Me. 1989); Kozak v. Comm'r Pub. Safety, 359 N.W.2d 625, 628 (Minn. Ct. App. 1984); Montana v. Lovegren, 51 P.3d 471 (Mont. 2002); New Jersey v. Martinez, 615 A.2d 279, 281 (N.J. App. Div. 1992); Vermont v. Marcello, 599 A.2d 357, 358 (Vt. 1991); Barrett v. Virginia, 447 S.E.2d 243, 246 (Va. Ct. App. 1994), rev'd, 462 S.E.2d 109 (Va. 1995); Washington v. Acrey, 64 P.3d 594, 599 (Wash. 2003); Bies v. Wisconsin, 251 N.W.2d 461, 471 (Wis. 1977); Wilson v. Wyoming, 874 P.2d 215 (Wyo. 1994)).

15. *Williams,* 962 A.2d at 218. The court further stated that evidence found incident to the officer's discharge of the community caretaking function can be seized and need not be ignored. *Id.* at 218 n.31 (citing *Cady, supra*, 413 U.S. at 447-48; 3 Wayne R. LeFave, Search And Seizure § 5.4(c) (4th ed. 2004)).

In defining the community caretaking doctrine, the court noted the need to balance the doctrine against the constitutional protections against illegal searches and seizures. In doing so, the court adopted Montana's three-part test to set forth the scope of the newly recognized doctrine:

> First, as long as there are objective, specific and articulable facts from which an experienced officer would suspect that a citizen is in need of help or is in peril, then that officer has the right to stop and investigate. Second, if the citizen is in need of aid, then the officer may take appropriate action to render assistance or mitigate the peril. Third, once, however, the officer is assured that the citizen is not in peril or is no longer in need of assistance or that the peril has been mitigated, then any actions beyond that constitute a seizure implicating … the protections provided by the Fourth Amendment, but more importantly, those greater guarantees afforded under [state law].[16]

The court declared that a police officer's limited request for information is reasonable under the community caretaking doctrine because it allows the officer to maintain a record of his contact with the individual.[17] The officer who contacted Wright was aware of the early morning hour and weather conditions which both were objective, specific facts suggesting that the defendant was in need of assistance. The officer did take appropriate steps to assist Wright by stopping his car a short distance from him and asking if help was needed. There was a brief exchange during which Williams declined assistance and volunteered his name and date of birth.[18] The officer acted reasonably in requesting this background information so he could make an administrative record of the encounter.[19] The officer also concluded the contact by advising Wright that he could contact the officer if he did need further assistance.[20] In conclusion, the court ruled that the officer acted pursuant to the community caretaking doctrine and the initial encounter was not a Fourth Amendment seizure.[21] The defendant's conviction was affirmed.[22]

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16. *Williams,* 962 A.2d at 219 (quoting Lovegren, supra, 51 P.3d at 75-76).

17. *Williams*, 962 A.2d at 221 (citing Evans, 764 N.E.2d at 843; New Hampshire v. Brunelle, 766 A.2d 272, 274 (N.H. 2000)). The court did not find that the officer's questions to Wright violated Del. Code Ann. tit. 11, § 1902. The court noted that § 1902 is based on the Uniform Arrest Act ("UAA"). Several jurisdictions have recognized the community caretaker doctrine and the provisions of the UAA. The court found that no other jurisdiction has interpreted the UAA to limit the ability of police under the community caretaker doctrine to identify a person who has been offered a*id.* Williams, 962 A.2d at 220 & n.38 (citing and comparing Ark. Crim. Proc. R. 2.2 & Allen v. Arkansas, 1997 WL 86362 (Ark. Ct. App. Feb. 26, 1997); Kan. Crim. Proc. Code Ann. § 22-2402 & Kansas v. Gonzales, 141 P.3d 501 (Kan. Ct. App. 2006); Mass. Gen. Laws Ann. Ch. 41 § 98 & Massachusetts v. Evans, 764 N.E.2d 841 (Mass. 2002); Mont. Code Ann. § 46-50-401 & Montana v. Lovegren, 51 P.3d 471 (Mont. 2002); N.H. Rev. State. Ann. § 594:2 & New Hampshire v. Brunelle, 766 A.2d 272 (N.H. 2000); R.I. Gen. Laws § 12-7-1 & Rhode Island v. Lombardi, 727 A.2d 670 (R.I. 1999)).

18. *Williams*, 962 A.2d at 221.

19. *Id.*

20. *Id.* at 221-22.

21. *Id.* at 222.

22. *Id.*

B. Emergency Doctrine Exception—*Blake v. State*

In *Blake v. State,*[23] the court ruled that exigent circumstances, including the blood curdling screaming of a baby after a loud boom sound from the dwelling, justified the police officers' warrantless entry into the defendant's apartment.[24]

In *Blake*, the defendant had appealed the trial court's denial of his motion to suppress evidence seized from the warrantless entry into his apartment. The defendant had been identified by New York Police Department ("NYPD") detectives as the suspect in a Manhattan shooting in which three people were shot. NYPD and Wilmington Police ("WPD") had located the defendant's residence as a second floor apartment in a Wilmington apartment building. NYPD detectives and a uniformed WPD officer went to the location to apprehend the defendant. While several officers knocked on the front door, other officers covered the outside of the building. The officers at the front door heard movement inside along with the muffled cry of a baby. After knocking for twenty to thirty minutes, detectives from WPD and NYPD left to obtain a search warrant. A NYPD officer at the scene observed an individual, later identified as Blake, open a window in the apartment and point a handgun at the officers while challenging them to shoot him. The outside NYPD officer then saw Blake crash through the apartment window in an escape attempt. The officers at the front door heard the crash of the window breaking followed by a "boom," and then the baby's crying turning into "blood curdling" screaming. The officers, concerned for the safety of the infant, forcibly entered the apartment and saw the infant on the floor. A safety sweep of the premises led to identification of a small amount of crack cocaine and drug paraphernalia. The trial judge ruled that the emergency entry was authorized under *Guererri v. State*[25] and denied the motion to suppress.[26]

On appeal, Blake argued that the trial court misapplied the three part test established in *Guererri*. Under *Guererri*, the court noted that the State's burden was to prove:

> (1) The police must have reasonable grounds to believe that there is an emergency at hand and an immediate need for their assistance for the protection of life or property[;] (2) The search must not be primarily motivated by intent to arrest and seize evidence [;and] (3) There must be some reasonable basis approximating probable cause, to associate the emergency with the area or place to be searched.[27]

On the first prong, the trial court found that the police had announced their presence and tried knocking on the door of the apartment for a considerable time. The police had also heard the muffled cry of an infant along with footsteps that approached and then retreated from the front door. The trial judge's finding that the police had reasonable grounds to check on the baby was found not to be clearly erroneous.[28]

The court also upheld the trial judge's determination under the second prong that the police detectives entered in response to the "blood-curdling screams from a baby" and not in an attempt to arrest or seize evidence. The court noted

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23. 954 A.2d 315 (Del. 2008).

24. *Id.* at 318-19.

25. 922 A.2d 403 (Del. 2007).

26. *Blake,* 954 A.2d at 316-17.

27. *Id.* (citing *Guererri*, 922 A.2d at 406).

28. *Id.* at 318.

the duty of the police to conduct the search for the primary purpose of a community caretaking function.[29] In Blake's case, the officer's actions were directed at protecting the infant in the house whose screams had gone from ordinary to "blood-curdling."[30]

On the third factor, the trial judge had ruled that emergency required the police entry to check on the screaming infant and also ruled that the police could conduct a protective sweep of the premises to ensure there was no further danger. The court found this was exactly what the police did upon entry into the apartment and there was no error in the analysis by the trial court.[31]

The court concluded that the trial judge had properly applied the emergency doctrine as set forth in *Guererri* and the motion to suppress was properly denied.[32]

C. Absence of Probable Cause for Stop Based on Four Corners of Arrest Warrant—*McDonald v. State*

In *McDonald v. State,*[33] the court held that the "four corners" of an arrest warrant did not set forth probable cause for a traffic stop by an officer of a vehicle leaving private property that failed to use a turn signal.[34]

Defendant McDonald was a passenger in a vehicle stopped by a Delaware State Police Corporal who pulled over the vehicle after it had exited from the parking lot of a Shore Stop. The corporal had observed the vehicle at approximately 12:15 a.m. in the parking lot with a driver and passenger in the car. The officer ran the tag on the car but inadvertently transposed some of the digits which incorrectly caused the vehicle to be reported as unregistered. The officer observed that the driver failed to activate his turn signal as he made a right turn to enter the public road. The corporal activated his emergency equipment to stop the car for failing to use the turn signal. Based on events subsequent to the stop, both occupants of the vehicle were transported back to the police station. The officer later filed an arrest warrant with the Justice of the Peace Court which contained in part a description of the reason for the original stop. In the arrest warrant, the corporal stated that he stopped the vehicle due to the perceived failure to turn violation.[35]

The Supreme Court reviewed the decision of the trial court that denied the motion to suppress evidence obtained subsequent to the stop of the vehicle.[36] The court focused on the four corners of the arrest warrant to determine whether

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29. *Id.* & n.4 (citing *Guererri*, 922 A.2d at 407; Cady v. Dombrowski, 413 U.S. 433, 441 (1973) ("[l]ocal police officers, unlike federal officers, frequently investigate vehicle accidents in which there is no claim of criminal liability and engage in what, for want of a better term, may be described as community caretaking functions…."); Virginia v. Waters, 456 527, 530 (Va. Ct. App. 1995)).

30. *Blake*, 954 A.2d at 318.

31. *Id.* at 318-19.

32. *Id.* at 319.

33. 947 A.2d 1073 (Del. 2008).

34. *Id.* at 1079-80.

35. *Id.* at 1075-76.

36. *Id.* at 1076-77.

probable cause existed for the vehicle stop.[37] The court viewed the arrest warrant as contemporaneous evidence that was probative on the issue for the corporal's reason for the stop.[38] In the affidavit, the officer only cited the driver's failure to signal a right hand turn when leaving the private lot as the basis for the vehicle stop.[39] The court found that the officer could not have probable cause to believe the driver violated DEL. CODE ANN. tit. 21, § 4155.[40] The provisions of DEL. CODE ANN. tit. 21, Ch. 41 were applicable only to public highways, not to vehicles exiting from private parking lots.[41] The court also noted that the parking lot was only 200 feet in total, which made it impossible for the driver to comply with the requirement of § 4155 to signal not less than 300 feet prior to the intended turning point.[42] In the court's view, there was no factual basis to establish that the officer properly stopped the vehicle for a § 4155 turn signal violation.[43] The court concluded that the police officer's subsequent search of the occupants and seizure of drug evidence from the vehicle were inadmissible as the original stop was unreasonable, and reversed the judgment of the trial court.[44]

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37. *Id.* at 1078. The arrest warrant was issued for nine criminal offenses that were the result of drugs seized from the vehicle during a search. *Id.*

38. *Id.*

39. *Id.* at 1078-79.

40. *Id.* at 1079 (citing DEL. CODE ANN. tit. 21, § 4155). Section 4155 provides:

> § 4155 Turning movements and required signals.
>
> (a) No person shall turn a vehicle at an intersection unless the vehicle is in proper position upon the roadway as required in § 4152 of this title, or turn a vehicle to enter a private road or driveway, or otherwise turn a vehicle from a direct course or move right or left upon a roadway or turn so as to proceed in an opposite direction unless and until such movement can be made with safety without interfering with other traffic. No person shall so turn any vehicle without giving an appropriate signal in the manner hereinafter provided.
>
> (b) A signal of intention to turn or move right or left when required shall be given continuously during not less than the last 300 feet or more than one-half mile traveled by the vehicle before turning.

DEL. CODE ANN. tit. 21, § 4155.

41. *McDonald*, 947 A.2d at 1079.

42. *Id.*

43. *Id.*

44. *Id.* at 1079-1080. In a dissenting opinion, Justice Berger noted that it was unclear from the record that the officer only stopped the vehicle because of the perceived turn signal violation. In his testimony at the suppression hearing, the officer had also referred to the perceived registration violation and that he had removed the tag from the car as evidence. *Id.* In another dissenting opinion, Vice Chancellor Noble, joined by Justice Berger, declared that the vehicle stop was reasonable under the Fourth Amendment and the evidence subsequently seized should not be suppressed. *Id.* at 1081-86. The dissent noted the officer had probable cause to believe the vehicle was not properly registered and his good faith mistake of fact was not a basis for a Fourth Amendment violation. *Id.* at 1081-82.

II. TRIAL EVIDENCE DECISIONS

A. Circumstantial Evidence to Prove *Corpus Delicti* of Drug Offenses—*Wright v. State*

In *Wright v. State,*[45] the court held that the defendant could be convicted of delivery of cocaine based on his own confession and the testimony of his uncharged co-conspirator who independently proved that Wright sold cocaine.[46]

The New Castle County police arrested defendant Wright on two counts of delivery. As part of an investigation, the police had previously arrested Raheem Cannon on charges of possession with intent to deliver cocaine and other drug offenses in June, 2006. On July 13, 2006, Cannon came to the police station and admitted to selling cocaine to the defendant on two different occasions on the evening of July 8, 2006. Cannon admitted to selling cocaine on a daily basis for two years and stated that Wright was a regular customer every other week for over a year. On the date in issue, Cannon advised police that his business was slow and he called Wright for a potential sale. Wright called back after some time and requested 1.6 grams of cocaine. Cannon bagged the cocaine and delivered it to Wright in the parking lot of a local bar. Cannon described the substance as cocaine based on his experience with the texture and smell of the drugs. Cannon left after receiving payment of $100 and returned to a social gathering. Wright then called Cannon and requested another $80 to $100 worth of cocaine. Cannon subsequently delivered the drugs to Wright in the presence of another unknown person. The police never recovered any of the cocaine but did question the defendant on the transactions. Wright admitted that he had purchased cocaine from Cannon two times on the night of July 8, 2006 and confessed to delivering the drugs to others. Wright denied that the drugs were for personal use.[47]

At trial, Cannon received immunity and testified at trial to the cocaine sales to Wright. The trial court denied the defense motion for acquittal claiming that the State had failed to establish the *corpus delicti* for the two delivery offenses. Wright was convicted of both offenses and appealed.[48]

As an initial matter, the court noted that the defendant's case would be reviewed under the "trustworthiness" approach to the *corpus delicti* rule established in *DeJesus v. State*.[49] The provisions of DEL. CODE ANN. tit. 11, § 301(c), which revised the Delaware common law rule of *corpus delicti*, only applied to compound crimes which were not present in Wright's case.[50] Under the rule in *DeJesus,* the court ruled that the State must present "some evidence of the existence of a crime, independent of the *defendant's* confession, to support a conviction."[51] While noting that the quantum of inde-

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45. 953 A.2d 188 (Del. 2008).

46. *Id.* at 190.

47. *Id.* at 190-91.

48. *Id.* at 191.

49. *Id.* at 192 (citing *DeJesus*, 655 A.2d 1180, 1199-1202 (Del. 1995)). The court noted that the progeny of the *DeJesus* "trustworthiness" analysis consisted of three decisions which ruled that "the Delaware *corpus delicti* rule requires the prosecution to show some evidence of the crime apart from the defendant's confession." *Id.* at 192 n.11 (citing Bailey v. State, No. 7, 2006, 2007 WL 1041748, at *2-3 (Del. Apr. 9, 2007); Rogers v. State, No. 247, 2004, 2004 WL 2830898, at *1 (Del. Nov. 30, 2004); Barlow v. State, No. 565, 2003, 2004 WL 1874699, at *3 (Del. Aug. 17, 2004); citing Superior Court authority in State v. Wells, 2004 WL 15551515 (Del. Super. June 16, 2004); State v. Bright, 1998 WL 283391 (Del. Super. Feb. 4, 1998)).

50. *Wright*, 953 A.2d at 191-92 (citing Del. Code Ann. tit. 11, § 301(c); 70 Del. Laws 463, S.B. 256 (1995)).

51. *Wright*, 953 A.2d at 192 (quoting Bright v. State, 490 A.2d 564, 569 (Del. 1985) (emphasis added); citing *DeJesus*, 655 A.2d at 1202; Jenkins v. State, 401 A.2d 83, 86 (Del. 1979)).

pendent evidence was not precisely defined, the court stated that the standard of review was the same as for a challenge to the sufficiency of the evidence.[52]

On the elements of the delivery charges, the court noted that the State was required to prove that the defendant delivered or possessed cocaine with the intent to deliver.[53] The court found that Cannon's testimony about the details of the two cocaine deliveries established the *corpus delicti* of the "delivery" element.[54] The second element concerned proof that the substance, which was never recovered, was cocaine. At trial, the State had relied on Cannon's lay witness testimony about the appearance and texture of the substances to prove he delivered cocaine to Wright.[55] The court noted that a number of state and federal courts have allowed the use of lay opinion testimony from someone experienced with drugs to establish the identification of drugs.[56] The court adopted the approach taken by these other jurisdictions and held that "[a] lay witness with familiarity and experience with the drug in question may testify and establish a drug's identity by factors other than the witness's personal use."[57] Under this rule, the testimony of Cannon was sufficient independent evidence to establish that the substance was cocaine and met the *corpus delicti* rule.[58] The court concluded that, viewing the evidence in the light most favorable to the State, there was sufficient evidence to support the defendant's convictions.[59]

B. Mapquest Printouts of Distance and Driving Time Were Not Admissible Under Rule 803(17) as Published Compilations—*Jianniney v. State*

In *Jianniney v. State*,[60] the court held that the State's use of Mapquest printouts to prove distances and driving times was not admissible under the hearsay exception in Rule 803(17) for "published compilations, generally used and relied upon by the public or by persons in particular occupations."[61]

The defendant Jianniney was charged with sexual solicitation of a child. The State alleged that on February 28, 2006, around 11:30 a.m., a man later identified as the defendant approached a thirteen year old boy who was working

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52. *Wright*, 953 A.2d at 192-93.

53. *Id.* at 193.

54. *Id.* at 193-94.

55. *Id.* at 194.

56. *Id.* at 194-95 (citing United States v. Dominguez, 992 F.2d 678, 681 (7th Cir. 1993); United States v. Westbrook, 896 F.2d 330, 336 (8th Cir. 1990); United States v. Palva, 892 F.2d 148, 157 (1st Cir. 1989); Gooch v. Georgia, 549 S.E.2d 724 (Ga. Ct. App. 2001); Smalley v. Indiana, 732 N.E.2d 1231, 1235 (Ind. Ct. App. 2000); Clifton v. Indiana, 499 N.E.2d 256, 258 (Ind. 1986); Reynolds/Herr v. Indiana, 582 N.E.2d 833, 840 (Ind. Ct. App. 1991)).

57. *Wright*, 953 A.2d at 195.

58. *Id.*

59. *Id.* The court declined to consider the defense argument that Wright should have been barred from testifying in the form of an opinion since he was never offered as an expert. The issue had not been raised before the trial court and the court would not consider the issue pursuant to Supreme Court Rule 8. *Id.*

60. 962 A.2d 229 (Del. 2008).

61. *Id.* at 231.

outside his house in Glasgow Pines, Delaware. The suspect began to talk to the boy who did not respond and went into his house. Around 6:00 p.m. on the same day, the boy was taking out the trash to the front curb when the same man again contacted the victim and offered him $40 if he would show his penis. The boy immediately ran into the house and called his mother who returned home to attempt to locate the suspect.[62]

At trial, Jianniney claimed that he was working on the day in issue for Wilson Fuel Services in Elkton, Maryland and was making deliveries all day. The work records showed that the defendant started his shift at 7:59 a.m. and made eight deliveries before lunch. He later went out on afternoon deliveries and returned to his house for dinner by 5:15 p.m. Two witnesses at trial testified that they saw the defendant on the street where the victim lived at 6:00 p.m. The defendant's employer Wilson also testified about Jianniney's work schedule and provided estimates of the driving time from the locations on the assigned stops. The employer stated that Jianniney would not have had enough time to be home by 11:30 a.m. On cross-examination, Wilson admitted that he was familiar with Mapquest and had previously used the website to calculate driving distances. The trial court permitted the State to admit a number of Mapquest printouts of driving directions and driving times which, for some of the routes, calculated driving times that were ½ of the time estimated by Wilson. The defendant was convicted as charged at trial.[63]

On appeal, the court reviewed the sole issue of the admission of the Mapquest printouts at trial. The court noted the hearsay exception in Rule 803(17) for market reports and commercial publications.[64] The court stated that the trial court could likely have taken judicial notice of the Mapquest printouts for the limited issue of identified streets, driving routes, and driving distances.[65] Courts in Delaware and other jurisdictions have taken judicial notice of such information.[66] The issue with the Mapquest printouts used at trial was that the information was admitted for the truth of the calculated driving time estimates.[67] There was no admitted evidence that these driving time estimates are relied upon by the public or professional drivers.[68] The court also noted the Mapquest website has a specific disclaimer regarding the accuracy of its information that provides:

> THIS WEBSITE AND THE MATERIALS ARE PROVIDED WITH ALL FAULTS ON AN "AS IS" AND "AS AVAILABLE" BASIS. MAPQUEST, ITS LICENSORS AND OTHER SUPPLIERS

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62. *Id.* at 230.

63. *Id.*

64. *Id.* at 232 (citing D.R.E. 803(17) (Market reports; commercial publications. Market quotations, tabulations, lists, directories or other published compilations, generally used by the public or persons in particular occupations)).

65. *Id.* (citing D.R.E. 201(b) (judicial notice may be taken of facts "not subject to reasonable dispute [because they are] either (1) generally known … or (2) capable of accurate and ready determination by resort to sources whose accuracy cannot reasonably be questioned.")).

66. *Id.* & n.6 (citing United States v. Kelly, 535 F.3d 1229, 1237 (10th Cir. 2008); Saco v. Tug Tucana Corp., 483 F. Supp. 2d 88, 93 (D. Mass. 2007); Gordon v. Lewistown Hospital, 272 F. Supp. 2d 393, 429 (M.D. Pa. 2003); Coppola v. Ferreligas, Inc., 250 F.R.D. 195, 199 (E.D. Pa. 2008); Caithness Resources, Inc. v. Ozdemir, 2000 WL 1741941, at *3 (Del. Ch. Nov. 22, 2000); S.H. v. G.W., 2007 WL 3202484 (Del. Fam. Ct. 2007)).

67. *Jianniney*, 962 A.2d at 232.

68. *Id.*

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On this record, the court concluded that the Mapquest driving distance estimates were not admissible under Rule 803(17).[70] The court next ruled that the admission of the evidence was harmless error.[71] The court indicated that the driving estimates were not particularly persuasive, and only addressed the issue of whether the defendant could have been in the victim's neighborhood by 11:30 a.m. In addition, an impartial witness placed the defendant on the victim's street at the time of the charged offense. The court found the evidence to be only minimally prejudicial and affirmed the conviction.[72]

C. Use of Videotaped Statements by Jury in Deliberations—*Waterman v. State*

In *Waterman v. State,*[73] the court held that the trial court committed harmless error in departing from the *Flonnory v. State*[74] default rule by allowing the videotaped statement of child victim to go to the jury during deliberations.[75]

The defendant Waterman was tried and convicted on multiple counts of rape and related offenses. The victim and her siblings regularly visited a farm where the defendant lived with his step-grandmother. When the victim was eight, she was sexually abused by the defendant whom she knew as "Uncle Brian." She reported the assaults to her mother over a year later and then began to keep a journal at her mother's suggestion. The Children's Advocacy Center worker taped an interview with the victim and retained four pages of the journal which was later turned over to police. During a police interview, the defendant denied any improper contact with the victim despite the detective's representations that the victim was telling the truth and her account could not have been made up by an eight-year old. At trial, the jury saw the victim's videotaped statement but the court indicated that the tape would not be sent to the jury room for deliberations. The defendant's statement was played as well for the jury. The trial judge at the close of the case permitted the jury to access the victim's videotape during deliberations.[76]

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69. *Id.*

70. *Id.*

71. *Id.* at 232-33.

72. *Id.* at 233.

73. 956 A.2d 1261 (Del. 2008).

74. 893 A.2d 507 (Del. 2008).

75. *Waterman*, 956 A.2d at 1262.

76. *Id.* at 1262-63.

On appeal, the defendant first claimed that the jury should not have been allowed to view the four pages from the victim's journal because the other pages were not made available. The evidence at trial was that the victim either misplaced or destroyed the remainder of the journal. The court noted that there was no basis to find that the lost portion of the journal contradicted any of the four pages introduced at trial. In addition, the court stated that the defendant was able to question the victim and two child care supervisors who had knowledge of the entire contents of the journal.[77]

On a second issue, the court reviewed the trial court's decision to allow the victim's videotaped statement to be sent to the jury room.[78] The court noted the *Flonnory* default rule that "written or tape or video recorded § 3507 statements should *not* be admitted into evidence as separate trial exhibits that go with the jury into the jury deliberations."[79] In this trial, the judge had initially ruled that the victim's videotaped statement would not be sent to the jury room during deliberations. The trial court then reversed itself due to concerns over parts of the defendant's taped statement which contained inadmissible comments by the police detective during the interrogation. The trial court gave a cautionary instruction to the jury regarding the inadmissible comments by the officer on the defendant's taped statement, but the tape was never redacted. The trial judge ultimately decided to allow the victim's taped statement to go to the jury as a separate exhibit based on concerns about the inadmissible statements on the defendant's tape.[80]

The court ruled that the concerns of the trial court did not justify departure from the "default" rule.[81] Under *Flonnory*, the tape could only be sent to the jury if it was either requested by the jury or if both parties consented.[82] The trial court's concerns about the defendant's statement could have been addressed by redaction of the tape prior to it being played to the jury. Since the defendant did object to the use of the victim's taped statement during jury deliberations, the court ruled that the trial court abused its discretion in departing from the default rule. [83]

The court then proceeded to find the trial court's ruling to be harmless error.[84] The victim gave credible testimony that was detailed and unequivocal. The case was not close and even if the jury had reviewed the tape during deliberations, it was likely that the evidence from the short trial would still have been fresh. The court ruled there was no violation of the defendant's fair trial right.[85]

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77. *Id.* at 1263.

78. *Id.*

79. *Id.* at 1263-64 (quoting *Flonnory*, 893 A.2d at 526-27).

80. *Waterman*, 956 A.2d at 1264.

81. *Id.* at 1265.

82. *Id.*

83. *Id.*

84. *Id.* (citing Hawkins v. State, No. 257, 2005, 2006 WL 1932668, at *3 (Del. July 11, 2006)).

85. *Waterman*, 956 A.2d at 1265.

III. OTHER SIGNIFICANT DECISIONS

A. Special Accommodations for Child Witness—*Czech v. State*

In *Czech v. State,*[86] the court held that a special accommodation by the trial court to allow the mother to sit behind a testifying child complainant was harmless error as child's testimony had little probative value.[87]

The defendant Czech was convicted of three charges of rape committed against the five year old granddaughter of his girlfriend. The five-year old "Mary" and her three-year old sister stayed with their grandmother about one weekend every two months from January, 2004 through February, 2006. The defendant lived in the house with the children's grandmother. On March 12, 2006, the victim's mother observed her daughter who was sitting on the sofa moving her hands up and down in her pants. Mary stated that she hurt and that was why she was rubbing inside her pants. The mother asked if Mary had been touched inappropriately and after an initial denial, Mary stated that the defendant had touched her improperly every day. During a recorded interview with the Child Advocacy Center, Mary told a child abuse investigator that the defendant had also assaulted her eleven year old cousin "Ruth." The victim later gave a second recorded statement to the Child Advocacy Center about the alleged abuse by the defendant of her cousin Ruth.[88]

At trial, cousin Ruth testified and denied that the defendant had abused her or anyone else in the family. The victim was called to the stand but did not respond to questions. The prosecution then played the two prior recorded interviews for the jury. The defendant testified at trial and denied all improper contact with Mary.[89]

On appeal, Czech challenged the decision by the trial judge to allow the complaining witness' mother to sit behind her when she testified. After the mother had testified, the State requested that she remain in the courtroom while her daughter testified. The trial judge suggested that the mother remain on the witness stand and sit behind her daughter. The trial court then instructed the jury on the special accommodation provided to the child witness.[90]

The Supreme Court reviewed this issue of first impression in Delaware, namely whether an adult support person may sit in close proximity to a testifying child.[91] The court noted that other jurisdictions have addressed the issue and approved such special accommodations as long as procedural safeguards are used.[92] The range of procedural rules have included "a showing of substantial need",[93] proof of a "compelling need",[94] a cautionary instruction,[95] or permitting the

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86. 945 A.2d 1088 (Del. 2008).

87. *Id.* at 1095.

88. *Id.* at 1091-92.

89. *Id.* at 1092.

90. *Id.* at 1093-94. The trial judge instructed the jury that "[t]he testimony of Ms. Smith is complete and she is excused as a witness. However, the State has made a request that she be permitted to sit up here because her daughter is going to be called as a witness and I have granted the State's request." *Id.* at 1094.

91. *Id.* at 1093.

92. *Id.* (citing Connecticut v. Menzies, 603 A.2d 419 (Conn. Ct. App. 1992); New Jersey v. T.E., 775 A.2d 686, 697 (N.J. App. Div. 2001); North Carolina v. Reeves, 448 S.E.2d 802 (N.C. 1994)).

93. *T.E.*, 775 A.2d at 697.

94. *Menzies*, 603 A.2d at 429.

95. Mosby v. Texas, 703 S.W.2d 714 (Tex. App. 1985).

defense to suggest alternative procedures.[96] The court found that the trial judge committed error by *sua sponte* suggesting the special accommodation without performing a balancing analysis and applying procedural safeguards.[97] Absent extraordinary circumstances, the trial court should not implement special accommodations for child witnesses.[98] According to the court, a trial judge should only grant a special accommodation for a witness after a motion that demonstrates "substantial need" for the implementation.[99]

The court also found that the trial judge committed error in denying the defense request for a cautionary instruction.[100] In the court's view, a contemporaneous instruction explaining the purpose of the support person would have mitigated any impact of the accommodation on the jury.[101] The court did rule that any error by the trial judge in permitting the special accommodation was harmless in light of the lack of probative value in the child's testimony.[102] The complaining witness was ill when she testified and provided mostly one word answers that did not implicate the defendant. The State presented the substance of the child's testimony through her two videotaped statements. The court concluded that the child's testimony did little to help the State's case and any error regarding the special accommodation was harmless.[103]

In reviewing this issue, the court recognized the sensitive issues involved with the testimony of a child witness and noted the requirement under Delaware law that child witnesses be treated with "additional consideration."[104] While not questioning the propriety of a support person for a child witness, the court addressed the legal framework for a trial court to employ when addressing a motion for a special accommodation.[105] In so ruling, the court relied on New Jersey precedent which balanced the competing interests of the State, defense, and child witness.[106] The court adopted the following six factors to be considered in future cases by a trial judge presented with a motion for a special accommodation:

> (1) A preliminary showing must be made to establish a substantial need for the procedure. It must be demonstrated that without accompaniment, the child is likely to be substantially non-responsive,

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96. *T.E.*, 775 A.2d at 697.

97. *Czech*, 945 A.2d at 1094.

98. *Id.*

99. *Id.*

100. *Id.* at 1095.

101. *Id.*

102. *Id.*

103. *Id.* (citing Van Arsdall v. State, 524 A.2d 3, 11 (Del. 1987)).

104. *Id.* at 1096 (citing Del. Code Ann. tit. 11, § 5131).

105. *Czech*, 945 A.2d 1096.

106. *Id.* (citing T.E., 775 A.2d at 697-98).

and that with accompaniment, the child is likely to provide meaningful, probative testimony. The court may consider the age of the witness, the nature of the testimony, evidence of fear, embarrassment or inability to testify, and the degree of trauma experienced by the witness in the underlying event and by the courtroom experience.

(2) A defendant should be given the opportunity to suggest alternatives. [Examples deleted.]

(3) Choice of the support person should minimize potential prejudice. A parent or other close relative will more likely be viewed as family support than vouching for the witness' credibility, as might result with a counselor, therapist or other professional. The advisability of identifying the status of a non-family support person should be considered. Whether the support person is also a witness in the trial should be considered; for example this might impact a sequestration order, and, depending upon the scope and extent of the support person's testimony, it might tend to unduly bolster the child's testimony. A representative of the prosecutor's office should not be used.

(4) The logistics should only be as intrusive as necessary to accomplish the purpose of the procedure. Placing the support person in the front row of the gallery or at counsel table, for example, would be minimally intrusive. Permitting the support person to stand behind or sit alongside the witness is moderately intrusive. Contact, such as holding the child's hand or permitting the child to sit on the support person's lap is highly intrusive and should be considered only as a last resort. The view of the child by the defendant and the jury should not be obstructed.

(5) A cautionary instruction should be given to the support person not to speak, prompt, communicate by signals or expression, and to give no indication of approval or disapproval of the answers.

(6) An appropriate instruction should advise the jurors that the purpose of the support person is to attempt to place the child at ease while testifying and that the presence of the support person should not affect their assessment of the credibility of the child's testimony. The standard "passion, prejudice or sympathy" charge should also be given.[107]

The court found no error in the defendant's remaining claims of error and affirmed the convictions.[108]

B. Defendant's Right to Speedy Sentencing—*Harris v. State*

In *Harris v. State,*[109] the court held that a delay of six and one-half years between the defendant's plea and his eventual sentence violated a defendant's right to speedy sentencing which the court continued to assume existed under the Sixth Amendment.[110]

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107. *Id.* (quoting *T.E.*, 775 A.2d at 697-98).

108. *Id.* at 1098-99. The defendant claimed that the trial court committed error by admitting the portion of Mary's videotaped statements that alleged the defendant also abused her cousin Ruth. The defendant failed to object to this evidence at trial and used this evidence to attack the victim's credibility. The court found the defendant had therefore waived any argument about the admissibility of the evidence. *Id.* at 1097-98. The court also rejected the defense argument that the prosecutor committed error by improperly vouching for the victim's credibility in closing arguments. The court found the statements were tied to the evidence and suggested a logical and proper inference from the evidence. *Id.* at 1098-99.

109. 956 A.2d 1273 (Del. 2008).

110. *Id.* at 1274.

The defendant Harris pled guilty on January 3, 2001 to the charge of Unlawful Sexual Intercourse in the First Degree. The court ordered a presentence investigation and sentencing was scheduled for March 16, 2001. This sentence date was continued after the defendant sought to withdraw his guilty plea. Harris' counsel at the time of the plea suggested that he contact other counsel if he was going to move to withdraw the plea. There was no sentencing date set until October 22, 2007, when a summons was issued to the defendant for sentencing on November 2, 2007. Harris and his original counsel appeared and moved to dismiss the indictment based on the delay in sentencing. The trial court denied the motion and sentenced the defendant to two years at Level V, suspended for eighteen months at Level I probation.[111]

On appeal, Harris claimed that the almost seven year delay violated his due process and speedy trial rights. The court noted that there was no decision of the United States Supreme Court deciding whether the Sixth Amendment contains the right to a speedy sentencing.[112] The court, relying on its previous decision in *Johnson v. State,*[113] assumed that the Sixth Amendment did require speedy sentencing and analyzed the right under the speedy trial factors.[114]

On the first factor, the court noted that the length of the delay was extraordinary and weighed in favor of the defendant.[115] Regarding the second factor, the reason for the delay, the court found this factor also weighed in the defendant's favor as there was no reason for the delay in the record.[116] The case, according to the Superior Court, "simply fell through the cracks."[117] The court ruled the delay was the responsibility of the trial court and not the fault of the defendant.[118]

As to the third factor, there was no assertion of his right to a speedy sentencing by the defendant and this factor weighed against him.[119] The court next noted that the fourth factor, prejudice to the defendant was neutral on the facts.[120] The defendant essentially served a six and one-half year sentence prior to his actual sentencing.[121] The defendant's pretrial compliance also created mitigating sentencing evidence in his behalf.[122]

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111. *Id.* The Superior Court denied the motion to dismiss after considering the four part test for speedy trial claims under Barker v. Wingo, 407 U.S. 514, 530 (1972). Harris, 956 A.2d at 1274 & n.3.

112. *Id.* at 1275.

113. 305 A.2d 622 (Del. 1973).

114. 956 A.2d at 1275 (citing Key v. State, 463 A.2d 633, 636 (Del. 1983); Boyer v. State, No. 418, 2002, 2003 WL 21810824, at *2 (Del. Aug. 4, 2003); Bodnari v. State, No. 97, 2003, 2003 WL 22880372, at *3 (Del. Dec. 3, 2003)). The court also noted that the Supreme Court of Arkansas, at least seventeen other jurisdictions, and almost every Court of Appeals have analyzed the right to speedy trial issue under the same approach under *Barker*. *Harris*, 956 A.2d at 1275 n.8.

115. *Id.* at 1276.

116. *Id.*

117. *Id.*

118. *Id.* The defendant had requested a postponement of his original sentencing date but the court found the delay after the initial continuance was unreasonable and attributable to the trial court. *Id.* at 1277.

119. *Id.* (citing *Key*, 463 A.2d at 637 (defendant has some responsibility "to call attention to a speedy [sentencing] violation")).

120. *Harris*, 956 A.2d at 1277.

121. *Id.* at 1278.

122. *Id.*

Considering all of the *Barker* factors, the court concluded that the extraordinary delay and the lack of any justifiable reason for the delay weighed most heavily in favor of the defendant.[123] The court ruled that Harris' right to a speedy sentencing under the Sixth Amendment was violated and reversed the ruling of the Superior Court.[124]

C. Denial of Severance for Sexual Abuse Charges of Same Nature Involving Two Victims—*Wood v. State*

In *Wood v. State,*[125] the court held that multiple counts of Rape and Continuous Sexual Abuse of a Child were properly tried together where charges involved two victims of similar ages who were deceived into performing sex acts and the offenses were sufficiently similar in nature.[126]

Defendant Wood was charged with sexual abuse charges involving two different children. The first victim, CG, was a child who lived in the Linden Green apartments on the third floor from January 1994 to July 2001. The defendant lived on the second floor of the same building and began sexually abusing CG in 1996 when she was six years old. The abuse occurred when CG and her siblings came to the defendant's apartment to play games with his son. The defendant would play hide and seek with the children and then place CG in his locked bedroom and sexually abuse her. Some of the incidents involved the defendant feeding the girl ice cream while blindfolded. The defendant also would show pornographic material to the victim. The victim testified this abuse occurred over fifty times over a three year period. In 2005, the victim told her mother about the abuse and the police were contacted.[127]

The second victim was the defendant's stepdaughter, SP. The defendant first met SP's mother in 1997 and moved in four months later. The defendant began abusing this victim on a daily basis when she was ten years old. On the first occasion, the defendant claimed to be in pain and gave a "doctor's note" to SP which described various sex acts to be performed. The victim testified that the defendant would sometimes videotape and blindfold her, and she was told to keep the sexual abuse secret from her mother. This sexual abuse over the five year period from 2000 to 2005 occurred between 500 to 2,000 times. In 2004, SP told her boyfriend about the acts of her stepfather and advised a counselor in 2005.[128]

The State indicted the defendant on eighteen counts of Rape First Degree and two counts of Continuous Sexual Abuse of a Child for criminal acts committed against both children. The trial court denied the defense motion to sever. At trial, Wood was convicted on all charges except two counts of Rape First Degree on which the jury could not agree on a verdict.[129]

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123. *Id.* at 1279. The court noted that other states have also found speedy sentencing violations for comparable delays. *Id.* & n.39 (citing Jolly v. Arkansas, 189 S.W.3d 40, 48-49 (Ark. 2004); Trotter v. Mississippi, 554 So. 2d 313, 318 (Miss. 1989); Massachusetts v. Ly, 875 N.E.2d 840, 845-46 (Mass. 2007); New York v. Drake, 462 N.E.2d 376, 380 (N.Y. 1984); Washington v. Ellis, 884 P.2d 1360, 1362 (Wash. App. Ct. 1994)).

124. *Harris*, 956 A.2d at 1279.

125. 956 A.2d 1228 (Del. 2008).

126. *Id.* at 1232.

127. *Id.* at 1229.

128. *Id.* at 1229-30.

129. *Id.* at 1230.

The sole issue on appeal concerned the trial court's denial of the motion for severance. In the court's view, the offenses were properly joined in the indictment as the charged derived from the sufficiently similar incidents.[130] The offenses were similar and suggested a common scheme or plan.[131] All of the charges involved victims of similar ages and both victims were deceived by the defendant to commit sex acts. Both children were also shown pornography and were threatened to not tell anyone of the abuse.[132] The court found that the multiple offenses implied a common scheme or plan, or at least were sufficiently of a similar nature to allow joinder under Superior Court Criminal Rule 8(a).[133]

The court did not find that the defendant had met his high burden of demonstrating a reasonable probability of prejudice to warrant severance under Rule 14.[134] The record did not support the defendant's claim that joinder led the jury to accumulate evidence and infer that he had a criminal propensity.[135] The jury did send out a number of notes during its deliberations and was unable to agree on a verdict on two counts. In addition, the trial court did instruct the jury on the burden of proof on each count and the jury was presumed to follow that instruction. The court also rejected the defense argument that joinder prevented him from testifying.[136] The defendant did argue at trial that the two victims knew each other, had tried to coordinate their stories, and both delayed in reporting any criminal acts.[137] The court concluded that the joinder was proper and the trial court did not abuse its discretion in denying the motion to sever.[138]

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130. *Id.* at 1231-32 (citing Super.Ct. Crim. R. 8(a); Massey v. State, 953 A.2d 210, 216 (Del. 2008); Caldwell v. State, 780 A.2d 1037, 1054-55 (Del. 2001); Skinner v. State, 575 A.2d 1109, 1117 (Del. 1990)).

131. *Harris*, 956 A.2d at 1232 (citing State v. Hermes, 2002 WL 484647 (Del. Super. Mar. 28, 2002)).

132. *Id.*

133. *Id.*

134. *Id.* The court noted that prejudice which may make severance appropriate exists where:

> (1) [T]he jury may cumulate the evidence of various crimes charged and find guilt when, if considered separately, it would not so find; (2) [T]he jury may use the evidence of one of the crimes to infer a general criminal disposition of the defendant in order to find guilt of the other crime or crimes; and (3) [T]he evidence may be subject to embarrassment or confusion in presenting different and separate defenses to different charges.

Id. at 1231 (quoting *Caldwell*, 780 A.2d at 1055 (quoting Wiest v. State, 542 A.2d 1193, 1195 (Del. 1988)).

135. *Harris*, 956 A.2d at 1232.

136. *Id.*

137. *Id.*

138. *Id.*

APPENDIX
DELAWARE SUPREME COURT
CRIMINAL LAW OPINIONS—2008

Allen v. State, 953 A.2d 699, 701 (Del. 2008) (trial court did not err in rejecting defendant's instruction that jury must not accumulate the evidence).

Benge v. State, 945 A.2d 1099, 1101-02 (Del. 2008) (defendant's challenge to guilty plea was procedurally defaulted and he was not prejudiced by error in plea colloquy; defendant waived a double jeopardy claim at his sentencing hearing; Delaware sentencing scheme with nonbinding Truth in Sentencing guidelines did not entitle defendant to relief under an Apprendi claim of illegal sentence).

Blake v. State, 954 A.2d 315, 318-19 (Del. 2008) (exigent circumstances including blood curdling screaming of baby after loud boom justified the police officers' warrantless entry into defendant's apartment).

Brown v. State, 958 A.2d 833, 834 (Del. 2008) (trial court erred in failing to give alibi instructions after both defendants had requested such instructions and credible evidence was presented at trial to support their alibi defenses).

Burrell v. State, 953 A.2d 957, 962-63 (Del. 2008) (historic factual record supporting trial court's finding that defendant committed murder "in furtherance of" an armed robbery that he planned with accomplice; jury instruction on felony murder was legally adequate).

Carrigan v. State, 945 A.2d 1073, 1078 (Del. 2008) (conversation between judge and probation officer about defendant's noncompliance with probation terms did not violate defendant's due process right to an impartial judge at violation of probation hearing).

Chavous v. State, 953 A.2d 282, 286-87 (Del. 2008) (defendant's motion to withdraw guilty plea was properly denied where alleged breach by State was harmless as defendant received benefit of the plea agreement).

Claudio v. State, 958 A.2d 846, 851-52 (Del. 2008) (Superior Court properly denied defendants' postconviction motions as jury instructions on felony murder at the trial substantially complied with Court's decision in Williams and did not track language used in Chao).

Coles v. State, 959 A.2d 18, 24-25 (Del. 2008) (trial court did not err in refusing to issue a material witness warrant for a defense witness whose potential testimony was neither "material" or "favorable" to the defense; prior statement of witness that referred to a different shooting was not admissible under D.R.E. 807; rational basis existed for trial court's instructions on lesser included offenses of Murder in the Second Degree and Manslaughter).

Cseh v. State, 947 A.2d 1112, 1115-16 (Del. 2008) (defendant who brandished sledgehammer during attempted robbery of store clerk failed to present any evidence supporting lesser included instruction for Attempted Robbery Second Degree, Aggravating Menacing, or Attempted Felony Theft).

Culver v. State, 956 A.2d 5, 14-15 (Del. 2008) (majority held that probation officers unlawfully searched home of defendant probationer based on tip from anonymous caller to police to probation since search violated Del. Code Ann. tit. 11, § 4321 and Parole and Probation Procedure 7.19).

Czech v. State, 945 A.2d 1088, 1095, 1097-98 (Del. 2008) (special accommodation to allow mother to sit behind child who was testifying was harmless error as child's testimony had little probative value; defendant waived issue regarding admission of statements made by complainant's mother since defense had refrained from objecting at trial for tactical reasons; prosecutor's closing argument that asked jurors to draw on collective life experience when evaluating credibility of young child witness did not constitute improper vouching).

Dabney v. State, 953 A.2d 159, 169 (Del. 2008) (delays in the scheduling of the defendant's trial on charge of Rape Second Degree violated constitutional right to speedy trial).

Dailey v. State, 956 A.2d 1191, 1194-95 (Del. 2008) (State could admit videotaped statement of complaining witness under § 3507 after her trial testimony touched on the events and the prior statement; defendant's decision not to testify mooted any claim that trial judge may have erred in indicating that his prior conviction would be admissible; prosecutor's comments in closing merely commented on the evidence and were not improper).

Fisher v. State, 953 A.2d 258, 260 (Del. 2008) (defendant's conviction for possession of cocaine was not a lesser-included offense of maintaining a dwelling).

Flamer v. State, 953 A.2d 130, 134-36 (Del. 2008) (failure of appellate counsel to cite any authority in support of legal argument constituted waiver of issue; trial court did not err in permitting State to play only portion of witness' taped conversation with defendant who raised no objection at trial).

Foster v. State, 961 A.2d 526, 528-30 (Del. 2008) (State's reference in opening statement to CSI was not plain error; complaining witness' statements immediately after the robbery were admissible under exited utterance hearsay exception and § 3507).

Gattis v. State, 955 A.2d 1276, 1285, 1287, 1289, 1291, 1293 (Del. 2008) (current trial judge did not abuse discretion in denying motion to disqualify; defendant's attempt to relitigate ineffective assistance of counsel claim was procedurally barred; trial court was not required under Apprendi to find beyond a reasonable doubt that the aggravating circumstances outweighed the mitigating circumstances; defendant failed to demonstrate that contact by trial judge with discharged jurors was prejudicial; record did not support claim that trial judge gave undue weight to jury's penalty hearing recommendation).

Greene v. State, 967 A.2d 144, 145 (Del. 2008) (State's motion to affirm denied where arguable issue existed concerning lack of Miranda warnings given to defendant before police questioning).

Hardy v. State, 962 A.2d 244, 247-48 (Del. 2008) (State in closing argument improperly vouched for State's case and conduct constituted plain error).

Harris v. State, 956 A.2d 1273, 1278-79 (Del. 2008) (six and one-half year delay between the defendant's plea and sentence violated his Sixth Amendment right to a speedy sentencing).

Hignutt v. State, 958 A.2d 863, 867-68, 870 (Del. 2008) (State witness' brief testimony about his lifetime goals was admissible on issue of "good character" of witness; no basis existed for instruction on lesser-included offense of theft misdemeanor as there was no dispute that value of parts appropriated exceeded $1,000).

Hudson v. State, 956 A.2d 1233, 1237-39 (Del. 2008) (trial court did not err in permitting State's chief investigating officer, who had sufficient specialized narcotics training, to testify as both a fact witness and as an expert).

Jianniney v. State, 962 A.2d 229, 230 (Del. 2008) (admission of Mapquest driving time estimates not proven to be reliable or generally accepted were inadmissible under D.R.E. 803(17) but error was harmless beyond a reasonable doubt).

Johnson v. State, 962 A.2d 233, 234 (Del. 2008) (defendant's direct appeal that challenged her guilty plea and sentence was barred by Superior Court Rule 32(d) as proper relief should be sought under Rule 61).

Justice v. State, 947 A.2d 1097, 1099 (Del. 2008) (prosecutor's question and witness' answer regarding DELJIS search for defendant's date of birth was harmless based on trial court's curative instruction).

LeGrande v. State, 947 A.2d 1103, 1105 (Del. 2008) (police search warrant for defendant's apartment lacked probable cause as a matter of law where police relied on anonymous tip but failed to corroborate any information to establish the reliability of the tip asserting that the defendant possessed drugs in his premises).

Lopez-Vazquez v. State, 956 A.2d 1280, 1291-92 (Del. 2008) (police lacked reasonable suspicion to stop suspect who was observed conversing with target of drug investigation, and who later entered and exited a multi-unit apartment building, and his subsequent consent to search his vehicle was tainted).

Mason v. State, 963 A.2d 124, 127 (Del. 2008) (trial court erred in admitting portion of taped statement that contained questions about suspect's pending violation of probation where suspect was arrested for murder, but error was harmless beyond reasonable doubt).

Massey v. State, 953 A.2d 210, 215-18 (Del. 2008) (photographs of victim's knife wounds were not inflammatory and did not require limiting instruction; deficiency in jury instruction on PDWDCF was harmless; denial of severance on PDWPP charge was not prejudicial error; trial court's decision use of limiting instruction on issue of defendant's prior crimes which differed from defense proposal was not error).

McDonald v. State, 947 A.2d 1073, 1079-80 (Del. 2008) (four corners of arrest warrant failed to set forth probable cause for officer's traffic stop of vehicle leaving private property that failed to use turn signal).

McKinley v. State, 945 A.2d 1158, 1164-65 (Del. 2008) (State presented sufficient evidence to prove Murder Second Degree charge where defendant was traveling around 93 to 100 miles per hour at the time of impact with victim's car after leading police on a high speed chase in which he ignored several red lights and drove on the wrong side of the road).

Morgan v. State, 962 A.2d 248, 252-54 (Del. 2008) (search warrant to search defendant's home, based on corroborated tip from past proven reliable informant, was supported by probable cause; trial court was not required to give sua sponte curative instruction after detective testified about forfeiture form completed by defendant after arrest).

Newman v. State, 942 A.2d 588, 590-91 (Del. 2008) (defendant's conviction for resisting arrest affirmed as suspect's knowledge of identity of law enforcement officer is not an element of the offense).

Nyala v. State, 955 A.2d 1275 (Del. 2008) (defendant's original sentence in 2001 which contained a probationary term that did not exceed the maximum term of confinement was not an illegal sentence under Del. Code Ann. tit. 11, § 4333).

Revel v. State, 956 A.2d 23, 27-30 (Del. 2008) (witness' isolated comment about defendant declining to make a statement and requesting a lawyer was improper comment on defendant's Fifth Amendment rights but did not warrant granting of a mistrial).

Scarborough v. State, 945 A.2d 1103, 1105-06 (Del. 2008) (court ruled that State and defendant entered an oral agreement in addition to the written plea agreement and that the State excused the defendant from the term of that agreement, so that the terms of the original sentence that were contrary to the oral agreement were vacated).

Sierra v. State, 958 A.2d 825, 832-33 (Del. 2008) (warrantless administrative search by probation officers was not supported by reasonable suspicion where officers relied on a tip from an informant who was not past proven reliable, and the officers violated the internal Probation Regulations).

Smith v. State, 963 A.2d 719, 722-23 (Del. 2008) (witness' statement that referenced defendant's possible sentence as habitual offender and plea offer of ten years was sufficiently cured by trial court's instruction and did not warrant mistrial).

Staats v. State, 961 A.2d 514, 517-20 (Del. 2008) (defendant's Rule 61 motion filed within one year of Supreme Court mandate on direct appeal was timely, but claims of ineffective assistance of counsel were without merit).

State v. Meades, 947 A.2d 1093, 1095-97 (Del. 2008) (police lacked reasonable suspicion to detain suspect and court would not consider new theory advanced on appeal by the State that the suspect voluntarily responded to police questioning).

State v. Sturgis, 947 A.2d 1087, 1089 (Del. 2008) (Superior Court's reduction of sentence of Attempted Murder in the First Degree from fifteen years to eleven years and six months of time served was not permissible under Rule 35(b) or under Del. Code Ann. tit. 11, § 4217(f)).

Swanson v. State, 956 A.2d 1242, 1243 (Del. 2008) (defense witness' invocation of Fifth Amendment on cross-examination did not constitute manifest necessity for grant of a mistrial).

Sykes v. State, 953 A.2d 261, 267, 269, 271-73 (Del. 2008) (sentence of death by lethal injection did not constitute cruel and unusual punishment; trial judge's comment to jury during guilt phase that defendant would have opportunity to allocute did not warrant mistrial based on curative instruction; complete Batson analysis did not show State used its peremptory challenges to exclude jurors based on race; defendant failed to establish actual prejudice from denial of change of venue motion; contact by defense witness with jurors at baseball game did not require new trial; trial court's imposition of the death penalty was not arbitrary or capricious and death sentence was not disproportionate to penalty imposed in similar cases).

Taylor v. State, 982 A.2d 279, 281-83 (Del. 2008) (victim's late disclosure of a second journal on first day of trial did not constitute a Rule 16 discovery violation by the State nor was there a clear record to support his claim of prejudice from a denied continuance request).

Turner v. State, 957 A.2d 565, 571-73 (Del. 2008) (trial court did not err in admitting defendant's statement seeking to speak to police if his girlfriend would not be incarcerated on conspiracy charge; trial judge did not err in sentencing defendant as habitual offender under DEL. CODE ANN. tit. 11, § 4214(a) to sentence of two life terms plus 87 years when court was required by statute to impose sentence greater than the statutory maximum).

Wallace v. State, 956 A.2d 630, 631-32 (Del. 2008) (trial court's finding defendant of guilty but mentally ill on charges of Murder First Degree and PDWCF for killing his nine year old cousin when the defendant was age 15 3/4 years, did not violate U.S. CONST. AMEND. 8 or DEL. CONST. ART. I, § 11).

Waterman v. State, 956 A.2d 1261, 1265 (Del. 2008) (trial court committed harmless error in departing from the Flonnory default rule by allowing videotaped statement of child victim to go to the jury during deliberations).

Wilkerson v. State, 953 A.2d 152, 157 (Del. 2008) (trial court did not abuse discretion in limiting defense cross-examination of prior act of abuse that was collateral).

Williams v. State, 962 A.2d 210, 216, 219-21 (Del. 2008) (police officer's initial encounter with person walking on a highway at 3:50 a.m. in cold, windy weather was not a seizure, and actions were further reasonable under the community caretaker doctrine).

Wilson v. State, 950 A.2d 634, 639-40 (Del. 2008) (trial court erred in permitting redaction of portion of plea agreement of testifying co-conspirator).

Winer v. State, 950 A.2d 642, 647-49 (Del. 2008) (trial court properly found sufficient circumstantial evidence supported defendant's arson conviction; defendant was properly tried on the arson charge and on a charge of criminal mischief at the police station after his arrest since both offenses were offenses involving property and were of the same of similar character).

Wood v. State, 956 A.2d 1228, 1232 (Del. 2008) (multiple counts of Rape and Continuous Sexual Abuse of a Child were properly tried together where charges involved two victims of similar ages who were deceived into performing sex acts and the offenses were sufficiently similar in nature).

Clifford Wright v. State, 953 A.2d 188, 190 (Del. 2008) (defendant could be convicted of delivery of cocaine based on his own confession and the testimony of his uncharged co-conspirator who independently proved that Wright sold cocaine).

Jerrin A. Wright v. State, 953 A.2d 144, 150-51 (Del. 2008) (defendant could not seek accident instruction at trial where he committed act with criminal negligence from firing handgun multiple times into populated parking lot).

RECENT CASE LAW DEVELOPMENTS RELATING TO DELAWARE'S ALTERNATIVE ENTITIES

Bernard J. Kelley and Amelia R. Hahn

The Delaware courts have addressed a number of significant issues over the past year relating to alternative entities formed under the Delaware Revised Uniform Limited Partnership Act (the "LP Act")[1] and the Delaware Limited Liability Company Act (the "LLC Act"). Some of the areas addressed by the courts include fiduciary duties, the inspection of books and records, the applicability of the statute of frauds, indemnification, judicial dissolution, and various procedural issues. This article discusses these cases and their practical effects on the use of Delaware alternative entities.

I. FIDUCIARY DUTIES

A. Contractually Assumed Fiduciary Duties

In *In re Cencom Cable Income Partners, L.P. Litigation,*[2] the Delaware Court of Chancery analyzed a plaintiff's right to enforce a voluntarily assumed duty. This case added to a series of decisions stemming from ongoing litigation by class representatives of limited partners against a limited partnership, its general partner, and the general partner's executive officers. In this case, the general partner, pursuant to authority conferred by the LP agreement, agreed to sell certain partnership assets to various affiliates. The general partner invoked the appraisal process set forth in the LP agreement and, although not required pursuant to the LP agreement, retained a law firm to act as special outside counsel on behalf of the limited partners in connection with such sale. In disclosure material, the general partner noted that the role of the law firm was to "assure that the Appraisal Process and the Sale Transaction would be fair to the Limited Partners and to protect the rights of the Limited Partners in connection therewith."[3] The law firm was to deliver an opinion that the appraisal process, the general partner's solicitation of consent, and the sale transaction were each in compliance with the LP agreement.[4]

In prior litigation, the court had held that the general partner had voluntarily assumed a duty that the law firm would fulfill its obligations. In this part of the litigation, the defendants, including the general partner, were seeking summary judgment based upon an argument that the plaintiffs had no right to enforce the voluntarily created duty, regardless of its scope, because the plaintiff had not actually bargained for the created duty and had not given the general partner any consideration to support its assumption of such duty. As a result, in the defendants' view, the only theory of recovery

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* Mr. Kelley is a director and Ms. Hahn is an associate with Richards, Layton & Finger, P.A. in Wilmington, Delaware. Richards, Layton & Finger, P.A. was involved in some of the cases discussed herein, but the opinions expressed in this article are those of the authors and not necessarily those of Richards, Layton & Finger, P.A. or its clients.

1. *See*, respectively, Del. Code Ann. tit. 6, §§ 17-101, *et seq*., and §§ 18-101, *et seq*.

2. C.A. No. 14634, 2008 WL 5050624 (Del. Ch. Nov. 26, 2008).

3. *Id.* at *2.

4. *Id.*

available to the plaintiffs was promissory estoppel. Since the limited partners had not read the disclosure statement and had not relied upon the disclosure, the elements of promissory estoppel could not be met. The court disagreed with the defendants' use of the contractual-based promissory estoppel theory and reasoned that the duty at issue '"arose not out of contract, but out of the common law"' and therefore the promissory estoppel argument was unavailing.[5] As the general partner had voluntarily undertaken to deliver the opinion and had "imported common law fiduciary duties into the relationship," the court denied the defendants' motion for summary judgment on this issue.[6]

B. Modification of Fiduciary Duties

As a general matter, the default rule under the LP Act and the LLC Act is that traditional corporate fiduciary duties apply in the limited liability company and limited partnership context. As both limited liability companies and limited partnerships are creatures of contract, the LP Act and the LLC Act allow modification within the applicable LP agreement or LLC agreement, including the waiver or elimination of duties (including fiduciary duties), except for the implied contractual covenant of good faith and fair dealing.[7] The risk associated with any contract is the presence of unclear or ambiguous language left for a court to interpret upon a dispute among the parties involved. In *Kahn v. Portnoy,*[8] Chancellor Chandler analyzed an LLC agreement that attempted to modify traditional fiduciary duties but did so in an ambiguous manner.

The *Kahn* case involved a derivative complaint brought by a shareholder (i.e., member) of an LLC against various directors and beneficial owners of the LLC. The plaintiff alleged that the defendant directors had breached their fiduciary duties when they approved a lease transaction between the LLC and an affiliated company of the LLC, which transaction the plaintiff contended was designed to benefit the defendant directors at the expense of the LLC. In response to this claim, the defendant directors filed a motion to dismiss for failure to state a claim.

The LLC agreement at issue provided that the fiduciary duties of the board of directors would be identical to those of a board of directors of a Delaware corporation under the Delaware General Corporation Law (the "DGCL"), unless otherwise specifically provided within the LLC agreement. Section 7.5(a) of the LLC agreement first modified fiduciary duties by specifically permitting or approving the board of directors' actions in respect of certain types of conflicts of interest if specified conditions were met. Section 7.5(a) also set forth a presumption that the board of directors acted properly even in interested transactions, with such presumption only capable of being overcome by clear and convincing evidence. The defendant directors argued that this section of the LLC agreement altered the pleading standard and created a presumption that they acted within their duties, notwithstanding the fact that their approval of the lease transaction had been interested. The court disagreed with the defendants and found that the application of section 7.5(a) of the LLC agreement to the current situation was susceptible to more than one reasonable interpretation, and, as a result, the court would not choose between the interpretations during the motion to dismiss stage of the case proceedings. Further, the court noted that the evidentiary standard set forth in section 7.5(a) of the LLC agreement was not in any event applicable in the motion to dismiss stage of the proceedings.

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5. *Id.* at *4.

6. *Id.*

7. LP Act § 17-1101; LLC Act § 18-1101.

8. C.A. No. 3515-CC, 2008 WL 5197164 (Del. Ch. Dec. 11, 2008).

In addressing plaintiff's fiduciary duty claims, the defendants also argued that the challenged transaction had been disclosed and therefore accepted by the shareholders when the LLC had been formed. In rejecting that assertion, the court recognized that the LLC agreement specifically addressed fiduciary duties "and thus negate[d] any other implied approval of conflicted board decisions."[9] As a result, the court was of the view that, in this context, "other disclosures [did] not impliedly override the express provisions of [the LLC's] primary governing document."[10]

The court then examined whether the defendants could be held personally liable for violating their duties under the exculpation section of the LLC agreement. After attempting to reconcile two arguably conflicting provisions exculpating the directors, the court determined that neither provision protected directors from liability if they acted in bad faith. As part of its analysis of the motion to dismiss, the court included an interesting discussion of good faith. Noting that good faith is not "an independent fiduciary duty" but rather a part of the duty of loyalty, the court made clear that a breach of the duty of loyalty need not involve a conflict of interest between a director and the company. "A director does not act in good faith, even if there is not a direct conflict of interest as to that director, unless the director 'acts in the good faith belief that her actions are in the corporation's best interest.'"[11] The court described the failure to so act as "'classic, quintessential bad faith.'"[12]

The court explained that bad faith also "includes conduct that can be defined as 'a conscious disregard for one's responsibilities' or 'intentionally fail[ing] to act in the face of a known duty to act,'"[13] and the court denied the defendants' motion to dismiss, finding that the plaintiff had sufficiently alleged a quintessential element of bad faith to survive such a motion. In so doing, the court focused on allegations regarding one director's divided loyalties to the LLC and regarding the other directors' being beholden to such director to the detriment of the LLC.

In *Bay Center Apartments Owner, LLC v. Emery Bay PKI, LLC,*[14] the Delaware Court of Chancery further examined the concept of the modification of fiduciary duties in an LLC agreement. The plaintiff and defendant were each LLCs that together formed another LLC ("Emery Bay") to own a condominium project and in which the defendant LLC acted as the managing member. An individual defendant ("Nevis") was the manager of the defendant LLC. The defendant LLC was given considerable power and authority under the LLC agreement of Emery Bay, although most of its management responsibilities were set forth in a separate agreement signed by one of its affiliates and to which it was only a counterparty.

The project encountered many problems. Emery Bay defaulted under a third-party loan that Nevis had personally guaranteed. The plaintiff claimed that upon the default, the defendants held secret negotiations that resulted in the creation of a separate note to divert cash flow from Emery Bay and that were designed to avoid triggering both the personal guarantee by Nevis under the third-party loan and capital calls on the defendant LLC to make contributions to Emery Bay.

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9. *Id.* at *5. n.22.

10. *Id.*

11. *Id.* at *7.

12. *Id.*

13. *Id.*

14. C.A. No. 3658-VCS, 2009 WL 1124451 (Del. Ch. Apr. 20, 2009).

Once the project had completely failed, the plaintiff brought action against the defendant LLC, Nevis, and others for monetary damages under several theories of liability, including breach of fiduciary duties. The defendants filed a motion to dismiss on all claims other than the plaintiff's contract claims. The court denied the motion to dismiss in its entirety.

The court addressed whether the LLC agreement had modified the traditional fiduciary duties of loyalty and care owed to the members of Emery Bay. The defendants argued that the LLC agreement had completely eliminated all fiduciary duties, while the plaintiff argued that the LLC agreement had specifically preserved the traditional fiduciary duties. In its review of the LLC agreement, the court referenced two sections of the LLC agreement, one that seemed to provide that the members owed each other default fiduciary duties and the other that seemed to provide that the members owed each other no duty of any kind not imposed under the LLC agreement. The court favored the plaintiff's interpretation based in part on the view that modifications of fiduciary duties must be clearly stated: "And, the interpretive scales also tip in favor of preserving fiduciary duties under the rule that the drafters of chartering documents must make their intent to eliminate fiduciary duties plain and unambiguous."[15]

With respect to the defendant LLC, who had been accused of various breaches of fiduciary duties, the court did not dismiss such claims because it had already concluded that the LLC agreement had not modified the defendant LLC's fiduciary duties. More interestingly, the court then examined the fiduciary duty claims against Nevis, who was not a direct member, manager, or officer of Emery Bay. In this analysis, the court relied upon *In re USACafes, L.P. Litigation,*[16] which provides that "'those affiliates of a general partner who exercise control over the partnership's property may find themselves owing fiduciary duties to both the partnership and its limited partners.'"[17] The court noted that the duty is limited to circumstances where the affiliate exerts control over the assets of the entity. The court found that the plaintiff had sufficiently pled facts that Nevis had exerted direct control over Emery Bay's property. The duty of an affiliate is also limited to circumstances where the affiliate has used its control to benefit itself at the expense of the entity. Here, the court also found that the plaintiff had sufficiently pled facts to show that Nevis had benefitted himself at the expense of Emery Bay by renegotiating a loan to avoid triggering his personal guarantee. Thus, the court denied the motion to dismiss the claims relating to the fiduciary duties owed by Nevis.

In *Brinckherhoff v. Texas Eastern Products Pipeline Company, LLC,*[18] the Delaware Court of Chancery had been asked to approve a settlement of two actions. The first action included a count alleging breaches of fiduciary duties in connection with a master limited partnership's engaging in a joint venture transaction and an asset sale. There was significant ownership and control overlap between the master limited partnership and the joint venture partner and buyer. The second action arose out of a challenge by the plaintiffs to a merger of two entities controlled by the defendant, which the plaintiffs claimed was effectuated by the defendant solely to extinguish the plaintiffs' standing to maintain the first action. As *Brinckherhoff* was a decision to approve a settlement agreement, the court did not render any final decisions regarding the plaintiffs' fiduciary duty claims, but rather discussed the strength of potential arguments made by each side in determining the appropriateness of the settlement agreement.

In evaluating the settlement, the court noted the strength of the plaintiffs' underlying claims of breaches of fiduciary duties. As part of their case, the plaintiffs relied on a provision of the applicable LP agreement that specifically provided

15. *Id.* at *9.

16. 600 A.2d 43 (Del. Ch. 1991).

17. *Bay Center*, 2009 WL 1124451, at *9 (quoting Bigelow/Diversified Secondary P'ship Fund 1990 v. Damson/Birtcher Partners, C.A. No. 16630-NC, 2001 WL 1641239, at *8 (Del. Ch. Dec. 4, 2001)).

18. 986 A.2d 370 (Del. Ch. 2010).

that transactions between affiliates under the LP agreement be "fair and reasonable" and on terms "no less favorable to [the partnership] than those generally being provided to or available from unrelated third parties."[19] The defendants argued that provisions of the LP agreement providing the general partner with general managerial authority and defining "sole discretion" protected the defendants' actions. The court was not persuaded by the defendants' interpretation, finding that the provision specifically addressing affiliated transactions controlled the issue because, from a contractual interpretation standpoint, the more specific provision controls over a general provision. The court noted that the restriction on transactions with affiliates did not involve discretionary action by the general partner but instead set forth a standard ("fair and reasonable") that the transaction must satisfy. In applying the more specific provision to the facts, the court stated:

> Whether the terms of the Pioneer Sale and the Jonah Joint Venture met the contractual standard established by Section 6.6(e) is a hotly disputed issue. At this stage of the case, I believe the plaintiffs have made a strong showing that the terms of the transactions dramatically undervalued Teppco's assets, were structured by conflicted fiduciaries who had powerful economic and personal reasons to favor Enterprise, were less favorable to Teppco than a third party transaction, and were unlikely to meet the "fair and reasonable" test. I thus believe that there is a strong case to be made that Section 6.6(e) was breached.[20]

While the court felt that the plaintiff had strong arguments as to why the affiliated transaction provision had been breached, it did not feel that claims styled as common law breach of fiduciary duty claims would succeed. The court acknowledged that the LP Act permits parties to limit or eliminate fiduciary duties. As a result, the court believed that the affiliate transaction provision replaced common law fiduciary duties. In evaluating the second action, however, the court recognized that under the LP Act, parties may not eliminate the implied covenant of good faith and fair dealing.

C. Application of Entire Fairness Standard

In evaluating a breach of fiduciary duty claim in certain self-interested transactions, courts may apply the more stringent entire fairness standard of review rather than the deferential business judgment rule. The Delaware Court of Chancery applied the entire fairness standard of review in the limited partnership context in *Venhill Limited Partnership v. Hillman*.[21] In *Venhill*, various family trusts formed and funded a limited partnership (the "Partnership"), of which the defendant was the sole general partner. The Partnership owned a significant stake in Auto-Trol Technology Corporation ("Auto-Trol"), and the defendant was the chairman, chief executive officer, and president of Auto-Trol. Auto-Trol had initially been successful, but, through the years, its revenues rapidly declined until it was insolvent. Through the use of his sole discretion to control the funds of the Partnership, the defendant, as general partner, repeatedly caused the Partnership to lend funds to Auto-Trol, draining cash from the Partnership. The terms of the loans were set completely by the defendant and were much more favorable to Auto-Trol than what would have been received by Auto-Trol in an arm's-length transaction. Over the years, despite calls from his family member trustees to stop the loans, the defendant caused the Partnership to loan millions of dollars to Auto-Trol. After years of seeing no returns from money the Partnership had invested in Auto-Trol, the limited partners opted to remove the defendant as the general partner of the Partnership. Sensing his imminent removal as general partner, the defendant transferred, for no consideration, the majority equity interest of

19. *Id.* at 387.

20. *Id.* at 388.

21. C.A. No. 1866-VCS, 2008 WL 2270488 (Del. Ch. June 3, 2008).

Auto-Trol from the Partnership to a new entity owned by the Partnership that he personally managed. He also funneled another $2 million from the Partnership into Auto-Trol. The Partnership and two family trust limited partners, as the plaintiffs in *Venhill*, brought action against the defendant for alleged breaches of his fiduciary duties of care and loyalty.

The plaintiffs and the defendant in *Venhill* agreed that the entire fairness standard applied to the investment decisions made by the defendant, as he was both the general partner of the Partnership and the chairman, chief executive officer, and president of Auto-Trol. Initially, the defendant argued that the plaintiffs were barred from contending that the loans breached any fiduciary duties because they had stood by and not used their voting powers earlier to remove him as the general partner of the Partnership and had therefore ratified or acquiesced to his actions. The court, however, disagreed and found that it would not be a "productive innovation" to adopt a rule that would "impose on stockholders a duty to remove a fiduciary who was bent on pursuing what the stockholders believed to be an imprudent strategy because if they do not do that, the fiduciary's actions will be immunized from the ordinary scrutiny of equity."[22] The court stated that any such policy would create a "crudely overbroad immunity from liability" for a fiduciary.[23] Further, based on the facts in this case, and particularly that the defendant had engaged in several transactions without any notice to the trustees, the traditional corporate doctrines of acquiescence or ratification were not applicable.[24]

The court "concluded that [the defendant] breached his duty of loyalty by undertaking action on behalf of [the Partnership] for the bad faith reason that it advanced his personal interests and knowing that the action was unfair to [the Partnership]."[25] The defendant nonetheless argued that he was exonerated by the exculpation section of the Partnership's LP agreement, which stated that the general partner would not be liable to the Partnership or the limited partners for any acts or omissions, "so long as the General Partner *acts in good faith and is not found to be guilty of gross negligence or willful or wanton misconduct with respect thereto.*"[26] The court noted that this section of the LP agreement appeared to provide that the defendant would not be liable for dealings that, while unfair to the Partnership, were "well-motivated and undertaken without gross negligence."[27] The court also found that the defendant could still be liable to the plaintiffs for acts in bad faith and with gross negligence and acts shown to be willful misconduct.

In assessing the defendant's liability under the exculpation standard, the court noted that it would be helpful to use the entire fairness standard to evaluate the conduct of the defendant in the loan transactions. In applying the entire fairness standard, the court first considered the process used to implement the transactions in order to determine the fairness of the transaction. The court found an absence of fair process in that (1) the defendant never attempted any type of market check by either considering other alternative investments or by considering what loan terms similarly situated lenders would have provided to Auto-Trol; (2) the defendant failed to seek the advice of any professional who could provide objective advice on the future for Auto-Trol or on the prudence of the Partnership investment in Auto-Trol; and (3) the defendant lacked any kind of analytical process for the investments in Auto-Trol made by the Partnership. Further,

22. *Id.* at *20.

23. *Id.* at *21.

24. The doctrines of acquiescence or ratification typically apply in scenarios where a "stockholder is informed of all the material facts regarding a transaction and then, by act or deed, either acquiesces in the transaction or gives it affirmative approval." *Id.* (quoting *In re* Wheelabrator Techs., Inc., S'holders Litig., 663 A.2d 1194, 1201 n.4 (Del. Ch. 1995)).

25. *Id.* at *33.

26. *Id.* at *22.

27. *Id.* at *24.

the court found that the transactions, based in part on the grossly unfair loan terms and lack of investment rationale for the loans made, lacked substantial fairness to the Partnership. Relying upon this analysis, the court concluded that the exoneration clause in the LP agreement did not insulate the defendant from liability because he did not act in the good faith pursuit of the Partnership's best interests. Instead, the defendant acted in bad faith and with willful misconduct, as he knew he was making investments in an "imprudent and irrational manner."[28] He was also found to have acted in a grossly negligent manner, as his decisions "did not involve any rational consideration of relevant factors."[29] As a result, the court held that the defendant would be liable for monetary damages.

D. Breach of Contract, Implied Covenant of Good Faith and Fair Dealing, and Fiduciary Duties

In *Fisk Ventures, LLC v. Segal,*[30] the Delaware Court of Chancery considered a dispute involving a counterclaim for a breach of contract, a breach of the implied covenant of good faith and fair dealing, and breach of fiduciary duties. An LLC had been set up with two classes of members who had the power to place representatives on a board of managers. A supermajority vote of the board was required for all essential decisions relating to the LLC. The LLC had persistent problems raising enough money to continue its operations. The class A and class B members could not agree on a course of action for financing the LLC's operations, and the board was deadlocked. After various proposals had been rejected, one of the class B members, Fisk Ventures, LLC, brought an action for judicial dissolution of the LLC under sections 18-801 and 18-802 of the LLC Act. In response, one of the class A members, Dr. Andrew Segal, brought counterclaims against Fisk Ventures, LLC and other class B members alleging a breach of contract, a breach of the implied covenant of good faith and fair dealing, and a breach of fiduciary duties.

For the contract claim, Segal argued that section 9.1 of the LLC agreement created a standard of conduct for its members that had been breached by the class B members' rejection of Segal's plans for research, financing, and other issues. Section 9.1 read as follows:

> No [m]ember shall have any duty to any [m]ember of the [LLC] except as expressly set forth herein or in other written agreements. No [m]ember, [r]epresentative, or [o]fficer of the [LLC] shall be liable to the [LLC] or to any [m]ember for any loss or damage sustained by the [LLC] or to any [m]ember, unless the loss or damage shall have been the result of gross negligence, fraud or intentional misconduct by the [m]ember, [r]epresentative, or [o]fficer in question ….[31]

The court found that this language in the LLC agreement did not create a code of conduct and therefore refused to "turn an expressly exculpatory provision into an all encompassing and seemingly boundless standard of conduct."[32] Further, even if section 9.1 did create a code of conduct, no facts were alleged that were sufficient to show that the class B members had

28. *Id.* at *30.

29. *Id.*

30. C.A. No. 3017-CC, 2008 WL 1961156 (Del. Ch. May 7, 2008).

31. *Id.* at *9.

32. *Id.*

acted with "gross negligence, willful misconduct, in bad faith, or by knowingly violating the law."[33] The court granted the motion to dismiss the contract claim.

Segal also had argued that the class B members had breached the implied covenant of good faith and fair dealing by blocking various financing opportunities proposed by Segal for the LLC. "Every contract contains an implied covenant of good faith and fair dealing that 'requires a "party in a contractual relationship to refrain from arbitrary or unreasonable conduct which has the effect of preventing the other party to the contract from receiving the fruits" of the bargain.'"[34] The court rejected this argument and noted that as the implied covenant is in fact implied, it is in place to "protect[] the *spirit* of the agreement" and "it cannot be invoked where the contract itself expressly covers the subject at issue."[35] Segal argued that the implied covenant had been breached by the class B members impeding the financing alternatives that Segal wanted. The court noted that Segal did not have the contractual right to decide how to finance the LLC and instead found that the LLC agreement expressly dealt with the subject of financing by requiring board approval with respect to financing. Segal could not bring a claim to grant him a substantive right for which he had not negotiated.

The court also rejected Segal's arguments relating to his breach of fiduciary duty claims against the class B members. The court found that, in accordance with section 18-1101(c) of the LLC Act, the LLC agreement had eliminated fiduciary duties to the maximum extent permitted by law by expressly stating that "members have no duties other than those expressly articulated in the [LLC agreement]."[36] Thus, in the court's view, since the LLC agreement did not expressly articulate any fiduciary obligations, the LLC agreement had in fact eliminated them. Further, even if there were fiduciary duties set forth in the LLC agreement to not act in bad faith or with gross negligence, the court held that Segal had failed to allege any facts sufficient to show a breach of any such duty.

II. PROCEDURAL ISSUES

A. Demand Futility

In order to bring a derivative action on behalf of an LLC, a member or assignee, as applicable, must either make a demand on the managers or members with authority to do so to bring the suit and such managers or members must have refused to do so, or demonstrate demand futility in that "an effort to cause those managers or members to bring the action is not likely to succeed."[37] In the previously discussed *Kahn* case,[38] the court evaluated a derivative action claim based

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33. *Id.* at *10.

34. *Id.* (quoting Dunlap v. State Farm Fire & Cas. Co., 878 A.2d 434, 442 (Del. 2005), quoting Wilgus v. Salt Pond Inv. Co., 498 A.2d 151, 159 (Del. Ch. 1985)).

35. *Id.*

36. *Id.* at *11.

37. LLC Act § 18-1001; *see also* LP Act § 17-1001 (providing comparable standards for limited partners or assignees to bring derivative actions).

38. *Kahn*, 2008 WL 5197164, at *9-13 (as the plaintiff did not make a demand on the board of directors, the plaintiff had to properly allege demand futility).

on demand futility. In assessing the futility of the demand, the court applied the corporate law *Aronson* test.[39] The court found that the plaintiff had adequately pled facts in the complaint to create reasonable doubt as to the disinterestedness or independence of a majority of the LLC's board of directors and therefore demand on the board of directors was futile.

In this case, the court focused on the first prong of the *Aronson* test; namely, whether there were particularized factual allegations that a majority of the directors were either interested or not independent. "A director is interested in a transaction when the director receives a personal benefit (or detriment) from a transaction that is not shared by the other shareholders of the corporation and the benefit is of subjective material significance to the director" and "where the director stands on both sides of the transaction."[40] In contrast, independence focuses on whether a "director's decision was impartial and based on the merits of the subject to be decided."[41] It does not require an allegation of a benefit or detriment from the transaction. Applying these standards, the court found that the allegations were sufficient to demonstrate that two of the directors were "interested" in the transaction due to conflicts that existed among various entities. The other three directors were deemed to be not "independent" under Aronson due to various relationships that they had with various interested parties.

The court also analyzed whether the LLC agreement altered the pleading requirements of section 18-1001 of the LLC Act. Interestingly, in analyzing the facts of the case, the court noted that the LLC agreement "certainly *could* have altered the demand futility and *Aronson* requirements."[42] Nonetheless, the court concluded that no such alteration had occurred.

The Supreme Court of Delaware also applied the *Aronson* test to a limited liability company derivative action case in *Wood v. Baum,*[43] where the Delaware Court of Chancery had previously dismissed a complaint for failure of the plaintiff to show that demand on the board would have been futile. The plaintiff had originally filed a derivative action alleging various breaches of fiduciary duties by the board of the LLC. Having failed to make a pre-suit demand upon the board of directors of the LLC, the plaintiff was required to establish that demand on the board would have been futile.

Before analyzing the facts of the case, the court first noted that there are two tests that should be construed in determining demand futility. First, in cases where there are claims that involve a "contested transaction," the previously discussed *Aronson* test applies.[44] Second, in cases where there are allegations regarding a board of directors' oversight duties, the *Rales* test applies, which requires the plaintiff to "allege particularized facts establishing a reason to doubt that 'the board of directors could have properly exercised its independent and disinterested business judgment in responding to a demand.'"[45]

The plaintiff, having conceded that the first prong of the *Aronson* test was not applicable as the majority of the LLC's board was generally independent and disinterested, attempted to create a reasonable doubt that the board would have

39. *Id.* at *9 (noting that the *Aronson* test requires a plaintiff to create reasonable doubt that either "(1) the directors are disinterested and independent [or] (2) the challenged transaction was otherwise the product of a valid exercise of business judgment") (quoting Aronson v. Lewis, 473 A.2d 805, 814 (Del. 1984)).

40. *Id.*

41. *Id.* at *10.

42. *Id.* at *11.

43. 953 A.2d 136 (Del. 2008).

44. *See supra* note 39.

45. *Baum*, 953 A.2d at 140 (quoting Rales v. Blasband, 634 A.2d 927, 934 (Del. 1993)).

properly exercised its business judgment as the board was disabled due to a "substantial risk of liability."[46] For this reason, the court examined the exculpation provision in the LLC agreement, which provided that the directors were exempted from all liability except in cases of '"fraudulent or illegal conduct.'"[47] The court further noted that under section 18-1101(e) of the LLC Act, except for an act or omission that "constitutes a bad faith violation of the implied contractual covenant of good faith and fair dealing," an LLC agreement may limit or eliminate any liability for a breach of duties (including fiduciary duties) of a person who is a party to or is otherwise bound by the LLC agreement.[48] Under the LLC agreement and the LLC Act, the directors had limited exposure to any liability. For this reason, in the court's view, the complaint must have alleged particularized facts that would prove that a majority of the board "knowingly engaged in 'fraudulent' or 'illegal' conduct or breached 'in bad faith' the covenant of good faith and fair dealing."[49]

The court found that the plaintiff had failed to plead the specific facts required to show fraud, had failed to allege facts that showed the defendants "knowingly" engaged in illegal conduct, and, finally, had not alleged a bad faith violation of the covenant of good faith and fair dealing. As part of its opinion, the court stated that "board approval of a transaction, even one that later proves to be improper, without more, is an insufficient basis to infer culpable knowledge or bad faith on the part of individual directors" and that membership on an audit committee is not sufficient to infer scienter.[50] Overall, based on the standard set by the LLC agreement's exculpation provision, the plaintiff had failed to establish that pre-suit demand was futile, and the decision of the Court of Chancery was affirmed.

The court also provided constructive advice to the plaintiff. Because particularized allegations are needed in demand futility cases, it would have been wise for the plaintiff to have instituted a books and records request. In cases where allegations need to be pled with specificity, "the failure to allege particularized facts is frequently compounded by a failure to make a statutory 'books and records' request concerning the matters alleged and the Board's consideration of such matters. Here, plaintiff could have, but chose not to, make a books and records request pursuant to [the LLC Act]."[51]

B. Personal Jurisdiction

The Delaware Court of Chancery considered personal jurisdiction issues in connection with the previously discussed *Fisk Ventures* case.[52] In *Fisk Ventures,* one of the third-party respondents, H. Fisk Johnson, who was a class B member of the LLC and a former member of the board of managers, moved to dismiss Segal's claims of breach of fiduciary duties on the theory that the court had no personal jurisdiction over him. In response, Segal argued that service of process was proper under Del. Code Ann. tit.10, § 3104 or section 18-109 of the LLC Act. Segal reasoned that because Johnson had sat on the board of the LLC and now controlled and directed the actions of his appointed representatives on

46. *Id.* at 141.

47. *Id.*

48. *Id.* (quoting LLC Act § 18-1101(e)).

49. *Id.*

50. *Id.* at 142.

51. *Id.* at 143-44.

52. *Fisk Ventures*, 2008 WL 1961156, at *6-8.

the board, and because Johnson had caused the LLC to move its domicile to Delaware when he initially invested in the LLC, he should therefore be subject to jurisdiction in Delaware.

"[S]ection 3104 provides for personal jurisdiction over a nonresident where (1) the nonresident transacted some sort of business in the state, and (2) the claim being asserted arose out of that specific transaction."[53] The court concluded that service of process on Johnson under Del. Code Ann. tit. 10, § 3104 was improper because although Johnson had limited contacts with Delaware, such contacts did not have any nexus with the actual claims in the case.

Section 18-109 of the LLC Act provides that service of process is proper as to managers of limited liability companies or those who "participate[] materially in the management of the limited liability company."[54] Segal conceded that Johnson was not a manager, and the court noted that "the mere power to appoint a manager does not force a member of an LLC to impliedly consent to service of process under section 18-109."[55]

Thus, instead of focusing on Johnson as a manager, Segal argued that Johnson had participated materially in the management of the LLC by controlling the actions of his appointed representatives on the board or, in the alternative, that he should be viewed as a *de facto* manager due to the broad rights that the LLC agreement provided him. The court disagreed with both of these arguments. First, the fact that members of the board "occasionally conferred" with Johnson was not enough to support the notion that Johnson had "consented to personal jurisdiction in Delaware."[56] Further, as the LLC agreement specifically provided that *"all management power… shall be exclusively vested in the board,"* the court found that as Johnson was not sitting on the board at the time of the events in question, and even though his representatives were on the board, he could not be viewed as a *de facto* manager.[57] As a result, service of process under section 18-109 was improper since Johnson had not consented to the court's in personam jurisdiction. As service of process was not valid under either section 3104 or section 18-109, the court granted Johnson's motion to dismiss for lack of personal jurisdiction.

In *Total Holdings USA, Inc. v. Curran Composites, Inc.,*[58] Vice Chancellor Strine addressed the issue of personal jurisdiction as it related to a nonresident general partner of a Delaware general partnership. The defendant was a Missouri corporation with no Delaware-related activities that held an interest in a Delaware general partnership (the "General Partnership") that it had formed with the plaintiff. While the General Partnership also did not do business in Delaware, the joint venture agreement establishing the General Partnership contained a provision stating that the General Partnership was being formed by the partners "in accordance with the laws of the State of Delaware," and the joint venture agreement contained a Delaware choice of law provision. There was no forum selection provision in the joint venture agreement. The court concluded that the General Partnership was governed by the Delaware Revised Uniform Partnership Act ("DRUPA").[59]

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53. *Id.* at *7.

54. LLC Act § 18-109(a).

55. *Fisk Ventures*, 2008 WL 1961156, at *7.

56. *Id.*

57. *Id.* at *8.

58. C.A. No. 4494-VCS, 2009 WL 3238186 (Del. Ch. Oct. 9, 2009).

59. Del. Code Ann. tit. 6, §§ 15-101, *et seq.* The court found that despite the fact that the General Partnership had been formed when the Delaware Uniform Partnership Act was in effect, when the Delaware General Assembly enacted DRUPA, it specifically provided that it shall govern "*all*" partnerships after a two-year grace period had expired and therefore DRUPA governed the General Partnership.

The plaintiff and defendant later amended the joint venture agreement; such amendment contained identical Delaware law provisions and also added a new "put" provision. Upon the exercise of the "put" provision, disputes arose over the value of the defendant's interest in the General Partnership, and litigation ensued. The defendant then brought a motion to dismiss claiming a lack of personal jurisdiction in the State of Delaware.

The defendant attempted to argue that the General Partnership should not be governed by Delaware law. The court found this to be unpersuasive, finding that based on the explicit language of, and choice of law provision in, the joint venture agreement, the General Partnership was a Delaware entity governed by DRUPA.

Having determined that the General Partnership was governed by DRUPA, the court next addressed whether the defendant was subject to personal jurisdiction in Delaware. The court turned to the consent provision found in section 15-114 of DRUPA, which provides, in relevant part:

> A partner … of a partnership which is formed under the laws of the State of Delaware or doing business in the State of Delaware may be served with process in the manner prescribed in this section in all civil actions or proceedings brought in the State of Delaware involving or relating to the business of the partnership or a violation by a partner … of a duty to the partnership or any partner of the partnership.[60]

The defendant argued that section 15-114 was not satisfied because the current dispute did not relate to the core business of the General Partnership (i.e., selling composites). The court disagreed with the defendant's argument and held that a dispute where the defendant allegedly owed money to another partner by being overpaid under the put provision in the joint venture agreement was clearly a dispute relating to a "violation by a partner of a duty to any partner of the partnership" as provided in section 15-114. Further, a dispute over the meaning of the joint venture agreement was clearly "involving or relating to the business of the partnership" as provided in DRUPA. "Therefore, the key principle emerging from the cases interpreting § 3114 and similar statutes is that consent to jurisdiction provisions may be used to subject a fiduciary to the jurisdiction of the Delaware courts for disputes over the meaning of and compliance with a Delaware entity's governing documents."[61] Exercising jurisdiction over the defendant under section 15-114 did not offend any of the defendant's due process rights because the dispute concerned the internal affairs of a Delaware partnership in which the defendant had become a partner. Finding that the defendant was subject to personal jurisdiction in the State of Delaware, the court denied its motion to dismiss.

C. Status Quo Order Under Section 18-110

In *Pharmalytica Services, LLC v. Agno Pharmaceuticals, LLC,*[62] the Delaware Court of Chancery imposed a status quo order to prevent irreparable harm to an LLC. The governing board of the LLC had removed the defendant as the president and chief executive officer of the LLC because it had discovered that the defendant had created a separate entity that was competing against the LLC. The LLC later learned that, after such removal, the defendant had been acting on behalf of the LLC by seeking to appoint designees to the board of a company located in and established under the laws of the People's Republic of China. The plaintiff LLC initiated this action seeking a preliminary injunction to prevent the defendant from taking action on behalf of the LLC or representing himself as a representative of the LLC.

60. *Total Holdings*, 2009 WL 3238186, at *10 (quoting Del. Code Ann. tit. 6, §15-114(a)).

61. *Id.* at *10.

62. C.A. No. 3343-VCN, 2008 WL 2721742 (Del. Ch. July 9, 2008).

Although the plaintiff brought an action seeking preliminary injunction against the defendant to prevent him from taking action on behalf of the LLC or holding himself out as representative of the LLC, the court noted that the relief sought by the plaintiff was in the nature of the relief granted under section 18-110 of the LLC Act, which allows for "continued operation of the venture, with a goal of minimal disruption, while the identity of those properly holding corporate power can be established."[63] Since section 18-110 is similar to section 225 of the DGCL, the court followed precedent from actions brought under section 225. The court issued the status quo order in favor of the LLC. In preserving the status quo and providing certainty in the management of the LLC, the court precluded the defendant from representing the interests of the LLC.

III. INTERPRETATION OF GOVERNING AGREEMENTS

A. Distributions Upon Withdrawal

The Delaware Court of Chancery in *Schuss v. Penfield Partners*[64] considered the rights of withdrawing limited partners of a hedge fund to certain distributions under an LP agreement. In Schuss, limited partners of a hedge fund brought suit against the hedge fund itself, the general partner, and the general partner of the general partner for breach of contract, breach of fiduciary duty, and an accounting. The plaintiffs had withdrawn from the hedge fund and had expected to receive an in kind and ratable distribution amounting to their liquidating share as of the time they withdrew. The distributions were made to the plaintiffs in kind but were not ratable, and, as a result of a decrease in the value of the designated securities at the time of the distributions, the distributions had values that were materially less than the plaintiffs' capital accounts at the time of their withdrawal. The defendants filed a motion to dismiss for failure to state a claim, which ultimately was granted in part and denied in part.

On the breach of contract claim, the defendants first argued that the hedge fund itself was an improper party to the suit, as it was not a party to the LP agreement and therefore could not have breached the LP agreement. The court disagreed with this argument, finding that section 17-606(a) of the LP Act specifically provides that once a partner withdraws from a partnership, he or she has the status of a creditor, as the partnership owes a distribution to the partner. Aside from this initial issue, there were two key issues in the case:

> (1) [W]as the general partner required to make any in kind distribution on a pro rata basis; and (2) were the withdrawing partners entitled to the securities the general partner specified at the time of retirement, even if they had declined in value at the time of distribution, or to assets whose aggregated value equaled the withdrawing partners' share of the fund as of the date of their retirement?[65]

On the issue of the defendants' authorization to provide in kind and nonratable distributions, the plaintiffs argued that section 17-605 of the LP Act applied and that they could not be compelled to take any more than their pro rata share of any security as an in kind distribution.[66] In contrast, the defendants argued that the LP agreement had in fact

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63. *Id.* at *3.

64. C.A. No. 3132-VCP, 2008 WL 2433842 (Del. Ch. June 13, 2008).

65. *Id.* at *1.

66. Section 17-605 of the LP Act provides:

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overridden the LP Act. The court agreed with the defendants and found that the LP agreement overrode the default rule of section 17-605 by specifically providing that the general partner in its "sole discretion" could "make a distribution in cash, securities, or a combination, as determined and selected by the [g]eneral [p]artner."[67] The court further held that, as a matter of law, the LP agreement did not require that the distribution be ratable, and therefore the plaintiffs' claim that the general partner was required to make in kind and ratable distributions was dismissed.

On the second issue, there were disagreements between the parties over the application of a section of the LP agreement that provided that payment should be made to fully withdrawing limited partners '"[w]ithin 30 days after the date of retirement of a Partner'" in cash, securities, or a combination of the two '"equal in value to not less than 90% of the estimated amount of the Liquidating Share.'"[68] The arguments stemmed from when the amount due was to be determined, either at the time of withdrawal or the time of distribution. The plaintiffs believed that the amount owed to them was calculated at the time of withdrawal and securities distributed in kind to them at a later point needed to be based upon that value. The defendants, on the other hand, believed that the assets could be segregated based upon the value for distribution within 30 days in accordance with the LP agreement. Thus, in the defendants' view, if the value of such securities should fall within that interim period, the risk was on the plaintiffs. This was important because the value of the assets at the time of distribution had materially decreased. The court denied the defendants' motion to dismiss because it found that there was a possibility that the plaintiffs' interpretation of the LP agreement section was correct.

B. Ability to Retain Counsel

The Delaware Court of Chancery analyzed the ability of a member of an LLC to retain counsel for an LLC in *Maitland v. International Registries, LLC.*[69] The case, which involved an LLC that was held and managed by two equal members, started with an action filed for the inspection of the books and records of the LLC. In connection with the books and records action, one of the members, as the plaintiff, filed a motion seeking an order striking the answer of the LLC, as the defendant, and disqualifying the LLC's counsel. The plaintiff argued that since the LLC had two members who each held 50 percent interests, the answer filed by the LLC and retained counsel was in violation of the LLC agreement, which required action by a majority of the members. The other member argued that the LLC agreement actually gave each member management rights.

The court started its analysis with a review of the management section of the LLC agreement, which provided:

> Management of the [LLC] shall vest solely in the Members, and the decision of the Members holding a majority of all LLC Interests as to all such matters shall be controlling. The Initial Members are hereby granted all rights, powers, authorities, and authorizations necessary, appropriate, and advisable and/or convenient to manage the [LLC] and to determine and carry out its affairs.[70]

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> Except as provided in the partnership agreement, a partner may not be compelled to accept a distribution of any asset in kind from a limited partnership to the extent that the percentage of the asset distributed exceeds a percentage of that asset which is equal to the percentage in which the partner shares in distributions from the limited partnership.

67. *Id.* at *6.

68. *Id.* at *8.

69. C.A. No. 3669-CC, 2008 WL 2440521 (Del. Ch. June 6, 2008).

70. *Id.* at *1.

Based on this language, the court acknowledged that each member may be empowered to manage the LLC when the co-owner was silent; however, the court noted that the LLC agreement did "not contemplate and cannot allow one owner's management wishes to trump the other's where they differ."[71] Therefore, so long as the LLC had two members, neither member was vested with the power to control unilaterally the LLC; where there was a disagreement among the members, the LLC would be deadlocked. The court further noted that a deadlocked LLC could not validly retain counsel or file an answer, so the plaintiff's motion to strike the LLC's answer and disqualify its counsel was granted. The court did, however, analogize the facts of the case to a corporate case, *Engstrum v. Paul Engstrum Associates,*[72] where two shareholders each held a 50 percent interest in a corporation and the court concluded that one stockholder should be permitted to intervene as a party defendant with the authority to defend on behalf of the corporation against the other stockholder as the plaintiff. The court held that the *Engstrum* ruling should be applicable to the *Maitland* facts; therefore, the other member was permitted to intervene as a party defendant with the authority to defend on behalf of the LLC against the plaintiff.

C. Withdrawal Provisions

On a motion to dismiss, the Delaware Court of Chancery analyzed a withdrawal right pursuant to a provision in a supplementary agreement between a limited partner and a general partner in *BASF Corporation v. POSM II Properties Partnership, L.P.*[73] The partnership had been formed with the purpose of owning, and then leasing to an affiliate, a chemical plant in Texas. As a result, the partnership "was indirectly controlled by the operator of the [p]lant."[74]

The contributions toward the plant's construction made by the limited partners of the partnership were set forth in supplementary agreements entered into by each limited partner with the general partner. The supplementary agreement with one initial limited partner contained a provision providing that should the general partner become aware that its general partner or its affiliates were no longer operating the plant, it was required to notify the limited partner. Upon the receipt of such notification, the limited partner was then provided with 90 days to notify the partnership that it wished to withdraw as a limited partner of the partnership and have its interest purchased.

The general partner of the general partner ("Lyondell"), which had been a publicly held company and was the operator of the plant, was eventually acquired by a privately held company. Thus, while Lyondell, as the operator of the plant, remained the same entity, Lyondell's ownership structure had changed. The plaintiff viewed this purchase of stock in Lyondell as a triggering event under the withdrawal provision of its supplementary agreement.

The general partner disagreed about the triggering of the withdrawal right, and consequently, the plaintiff brought an action against the general partner and the partnership seeking a declaration of the occurrence of a change in operation as described in the plaintiff's supplementary agreement. The plaintiff put forth the arguments that (1) there had been a change of Lyondell as the operator as contemplated by the supplementary agreement due to the change in control of the operator of the plant, and (2) the plant was now operated by the new parent entity and not Lyondell. The defendants filed a motion to dismiss and argued that (1) a change of control of Lyondell did not give the plaintiff any rights pursuant to the supplementary agreement because Lyondell was still the operator, and (2) the plaintiff had failed to allege any actual facts to support its argument that Lyondell, as a separate legal entity, no longer operated the Texas plant.

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71. *Id.*

72. 124 A.2d 722 (Del. Ch. 1956).

73. C.A. No. 3608-VCS, 2009 WL 522721 (Del. Ch. Mar. 3, 2009).

74. *Id.* at *2.

The court started its analysis of whether the withdrawal provision of the supplementary agreement was triggered by a change of control of Lyondell by noting that this was a straightforward contract interpretation question and a question of law.[75] Noting that Lyondell was still the operator of the plant regardless of Lyondell's change in ownership structure, the court found that the withdrawal provision was not a change of control provision and was not ambiguous. "Delaware law does not invest judicial officers with the power to creatively rewrite unambiguous contracts in this manner."[76] Furthermore, the court commented that the parties could have included a change of control provision in their agreement and specified the parameters of its application to various factual possibilities. The court stated that the plant was still currently being operated by Lyondell despite the change in control of its equity and therefore the withdrawal provision in the supplementary agreement was not triggered.

Finally, the court discussed the plaintiff's alternative argument that the withdrawal provision was triggered because Lyondell's new parent was actually operating the plant instead of Lyondell. The court agreed with the defendants and concluded that the plaintiff had failed to plead any facts about how there had been a change in the plant's operation. In making its argument, the plaintiff cited the parent's management reports and consolidated financial statements, which contained statements about its operation of the plant. The court was uninfluenced by these reports of consolidated operations and instead viewed them as merely evidence that the parent entity was actually a corporate holding company, which would naturally have operating subsidiaries (such as Lyondell) hold and operate its assets. "A holding corporation like LyondellBasell must present reports of their affairs on a consolidated basis."[77] The court concluded that Lyondell was still operating the plant and therefore the withdrawal provision in the supplementary agreement was not triggered. The court dismissed the plaintiff's complaint.

D. Covenant v. Condition

In *Travelcenters of America LLC v. Brog,*[78] the Delaware Court of Chancery examined the difference between noncompliance with a condition as opposed to a covenant in a contract. In the case, the plaintiff was an LLC and the defendants were shareholders (i.e., members) of the LLC. The defendants had previously submitted notice to the LLC purporting to nominate two directors to the board of directors of the LLC. The LLC brought an action in the Court of Chancery and obtained a declaration that the notice by the defendants had not complied with the LLC agreement. The LLC then commenced an action seeking indemnification of its costs and fees associated with obtaining the declaration.

The LLC sought indemnification based on a section of its LLC agreement that provided that the shareholder defendants would "indemnify [the LLC] from and against all costs and expenses, including reasonable attorneys' and other professional fees, arising from such shareholder's breach of any provision of the LLC [a]greement."[79] The LLC argued that the defendants had breached the LLC agreement because their notice did not comply with the LLC agreement requirements. The issue before the court was whether the failure to comply with the notice requirements constituted a breach of the LLC agreement by the defendants.

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75. *Id.* at *4

76. *Id.* at *6.

77. *Id.* at *8.

78. C.A. No. 3751-CC, 2008 WL 5272861 (Del. Ch. Dec. 5, 2008).

79. *Id.* at *2.

The court first explained that there is a distinction between promises and conditions, as "[p]romises give rise to a duty to perform, and conditions are events that must occur before a party is obligated to perform."[80] Furthermore, the court stated that "[w]hile the non-performance of a promise or covenant can result in a breach of a contract, the non-occurrence of a condition is not considered a breach unless the party promised that the condition would occur."[81] In considering the notice requirements under the LLC agreement, the court concluded that such requirements were merely conditions to the LLC's performance and not promises by the shareholders. The notice provisions simply establish the conditions for a shareholder to nominate a person for election to the board of directors. As the defendants' conduct constituted only a nonoccurrence of a condition and not a breach of contract, the LLC was not entitled to indemnification and the court granted the defendants' motion for judgment on the pleadings.

E. Oral Modification of LLC Agreement

In *Tunney v. Hilliard,*[82] the Delaware Court of Chancery addressed whether a provision of an LLC agreement could be orally modified. The plaintiff and defendant in Tunney had entered into a business venture where they owned and operated a restaurant and marina. Pursuant to this venture, they formed a corporation to serve as the operating entity and an LLC to be a real estate holding entity. The business venture was successful, and eventually the parties sold the business for a sizable profit. The governing documents of the LLC provided for a 50-50 division of profits. The plaintiff claimed, however, that due to the defendant's decision to reduce his time spent on the venture, the parties had orally agreed to a modification of the profit allocation whereby the plaintiff would be entitled to a 20 percent commission on the sales proceeds and the remainder would then be divided equally among the parties. The defendant denied any such oral modification.

Based on the evidence presented, the court determined that the plaintiff had failed to prove adequately an oral modification of the LLC agreement. The court stated that although oral modifications of written contracts are allowed under Delaware law, they are not favored; therefore, a heightened evidentiary burden is placed on the party seeking to prove an oral modification. This heightened burden requires proof of an "intended change to the written agreement with sufficient 'specificity and directness as to leave no doubt of the intention of the parties to change what they previously solemnized by formal document.'"[83] With a lack of any contemporaneous written evidence or any credible witness testimony, the plaintiff had failed to prove adequately an oral modification of the agreed-upon allocations, and therefore the court held that the written allocations would remain unaltered.

F. Actual v. Apparent Authority

In *Jack J. Morris Associates v. Mispillion Street Partners, LLC,*[84] the Superior Court of Delaware denied a motion for summary judgment in a suit relating to an alleged breach of contract. In Morris, an individual who had originally

80. *Id.* at *3.

81. *Id.*

82. C.A. No. 1317-VCN, 2008 WL 3975620 (Del. Ch. Aug. 20, 2008).

83. *Id.* at *5 (quoting Reeder v. Sanford Sch., Inc., 397 A.2d 139, 141 (Del. Super. 1979)).

84. C.A. No. 07C-04-023-RFS, 2008 WL 3906755 (Del. Super. 2008).

been removed as a general manager of the defendant LLC entered into a letter agreement with the plaintiff for the plaintiff to provide promotional, marketing, and advertising services to the LLC. The plaintiff provided services to the LLC and received assurance of payment from the former general manager, but the LLC did not pay for services provided by the plaintiff. This suit ensued.

The LLC argued that the former general manager was not authorized to sign the letter agreement. The various members of the LLC and the former general manager provided inconsistent statements concerning the former general manager's authority to act for the LLC and the LLC's knowledge of the existence of the letter agreement. The court set forth the relevant law on agency as follows:

> In the ordinary course of business dealings, an agent may be cloaked with three types of authority: express, implied and apparent authority. Express authority may be conveyed to an agent, either orally or in writing. Implied authority may be evidenced by conduct of the principal. Apparent authority may be evidenced by the conduct of the agent who holds himself out as possessing authority with the apparent consent or knowledge of the principal. In these circumstances, the principal cannot deny the agent's authority.[85]

Since whether an agency relationship exists is typically a question of fact and since there was a dispute on that basis, the court denied the plaintiff's motion for summary judgment, leaving it for a finder of fact to decide.

The Delaware Court of Chancery also explored the concepts of actual and apparent authority in *B.A.S.S. Group, LLC, v. Coastal Supply Co., Inc.*[86] An employee of a corporation embezzled funds from the corporation. The employee then formed an LLC with a friend and used the embezzled funds to purchase property on behalf of the LLC. When the corporation discovered the embezzlement, the employee was fired and a restitution agreement was reached whereby the employee transferred the property from the LLC to the corporation. The friend of the employee, as the other member of the LLC, commenced this individual and derivative action to void the transfer of the property from the LLC. The corporation counterclaimed for unjust enrichment and conversion. Both sides filed motions for partial summary judgment.

The plaintiff's first contention was that the employee had no authority, actual or apparent, to transfer the property from the LLC. "Actual authority" exists when "a principal expressly or implicitly grants [such authority] to an agent."[87] The plaintiff argued that the employee had no actual authority because the LLC agreement required the consent of both members to transfer the property. The plaintiff's argument was based upon a section of the LLC agreement that required the consent of a majority of the members to take certain actions, which he argued included the transfer of the property. As he had not consented, the plaintiff asserted that the employee did not have actual authority to transfer the property.

The LLC agreement also contained a power of attorney provision whereby the employee was designated as an authorized person who arguably had authority to transfer the property. The plaintiff argued that the power of attorney section was not applicable because the employee had not acted in good faith, which was a requirement of the power of attorney provision. The court determined that there were disputed issues of fact and it could not make a determination of whether the employee had acted in good faith; therefore, summary judgment on the issue of actual authority was not appropriate.

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85. *Id.* at *3.

86. C.A. No. 3743-VCP, 2009 WL 1743730 (Del. Ch. June 19, 2009).

87. *Id.* at *5 (quoting Albert v. Alex. Brown Mgmt. Servs., Inc., C.A. Nos. 762-N, 763-N, 2005 WL 2130607, at *10 (Del. Ch. Aug. 26, 2005)).

In analyzing whether the employee had "apparent authority" in transferring the LLC property to the corporation, the court stated that "'[a]pparent authority is that authority which, though not actually granted, the principal knowingly or negligently permits an agent to exercise, or which he holds him out as possessing.'"[88] A party asserting apparent authority must demonstrate reasonable reliance on the indicia of authority that was originated by the principal. If the third party, based on the surrounding circumstances, relies in good faith upon the agent's apparent authority, then the principal will be bound "'to the same extent as if actual authority had existed.'"[89] The court found that factual disputes existed that precluded a determination of whether apparent authority existed and refused to grant summary judgment.

The corporation raised a counterclaim of unjust enrichment and sought as a remedy the imposition of a constructive trust or damages. Unjust enrichment requires a showing of: "(1) an enrichment; (2) an impoverishment; (3) a relation between the enrichment and the impoverishment; (4) the absence of justification; and (5) the absence of a remedy provided by law."[90] The court found that when the employee used the embezzled funds to purchase the property, all of the elements for unjust enrichment clearly existed. The plaintiff argued that he and the LLC were innocent parties and should not be penalized for the acts of the employee/co-member. The court disagreed and specifically found that the knowledge of the employee, as an officer, director, or manager of the LLC, could be imputed to the LLC. The court also stated that "'[r]estitution is permitted even when the [party] retaining the benefit is not the wrongdoer.'"[91] As a remedy for the unjust enrichment (and also for the corporation's conversion counterclaim), the court ordered the imposition of a constructive trust over the funds and property involved.

G. Breach of Contract and Implied Covenant

On a motion to dismiss, the Delaware Court of Chancery examined claims for, *inter alia,* breach of contract of an LLC agreement and breach of the implied covenant of good faith and fair dealing. In *Kuroda v. SPJS Holdings, L.L.C.,*[92] the plaintiff was a non-managing member of an LLC that was a general partner of a limited partnership that made investments in Japanese corporations. The plaintiff also was an owner of an investment advisor to the partnership.

Over time, tensions developed between the defendant managing members of the LLC and the non-managing member plaintiff concerning the approach being taken with respect to the partnership's activities in Japan. The plaintiff wanted to cease his work as an investment advisor and stated his desire to withdraw as a non-managing member of the LLC. The parties were not, however, able to reach an agreement on the terms of his separation. The plaintiff initiated suit against the managing members making various claims, including that they had breached the terms of the LLC agreement by failing to pay him incentive allocations and other payments that were contractually owed to him, and had breached the implied covenant of good faith and fair dealing by reason of the defendants' improper conduct. The defendant managing members responded with a motion to dismiss.

One of the plaintiff's breach of contract claims alleged that the defendants had breached the LLC agreement by refusing to pay the plaintiff incentive allocations and the balance in his investment capital account, and by issuing to him

88. *Id.* (quoting *Alex. Brown*, 2005 WL 2130607, at *10).

89. *Id.* (quoting Old Guard Ins. Co. v. Kimmy's Grille, Inc., 860 A.2d 811, 2004 WL 2154286, at *3 (Del. Sept. 21, 2004) (ORDER)).

90. *Id.* at *6.

91. *Id.* at *7 (quoting Nash v. Schock, 732 A.2d 217, 232 (Del. 1999)).

92. 971 A.2d 872 (Del. Ch. 2009).

an incorrect Schedule K-1. The defendants argued that such obligations, if owed, were obligations of the LLC for which they, as members, were not liable. The plaintiff was not, however, arguing that the defendant members were liable because they were members, but rather because they were responsible for managing the LLC and "they took affirmative steps in contravention of their own obligations under a contract to which they are signatories-the LLC [a]greement."[93] While the court acknowledged that members, as members, are not generally liable for the obligations of an LLC, it also noted that members may be liable to other members for breach of contract. In this case, the court referred to the LLC agreement's exculpation provision in specifying a member's liability exposure. Because it was ambiguous whether the particular provisions of the LLC agreement imposed a contractual duty upon the defendant members, the court did not dismiss these breach of contract claims. Resolution of that issue would have to wait until trial.

The court also continued Delaware's policy to construe narrowly the implied covenant of good faith and fair dealing. The plaintiff alleged that the defendants had breached the implied covenant of good faith and fair dealing by engaging in

> arbitrary, unreasonable, and/or deceitful conduct, including (1) failing to pay [the plaintiff] monies that they know he is due, (2) using threats of litigation to coerce [the plaintiff] and to retaliate against him, (3) sabotaging negotiations in an effort to reduce the amounts due to [the plaintiff], and (4) disparaging [the plaintiff] in connection with his work with defendants.[94]

The court stated that the implied covenant has a "narrow purpose" and the plaintiff was required to "allege a specific implied contractual obligation and allege how the violation of that obligation denied the plaintiff the fruits of the contract."[95] The implied covenant "cannot be invoked to override express provisions of a contract."[96] Importantly, the court noted that the LLC agreement itself controlled on a claim that the defendants failed to pay money due to the plaintiff under the LLC agreement. Further, the plaintiff had failed to draw a sufficient connection between the alleged violations by the defendants of the implied covenant and specific implied obligations under the LLC agreement. Since the plaintiff's allegations of injury were governed by the expressed contractual terms of the LLC agreement, the court dismissed his claim against the defendants for a breach of the implied covenant of good faith and fair dealing.

The Delaware Court of Chancery also examined a claim for a breach of the implied covenant of good faith and fair dealing in the previously discussed *Bay Center Apartments Owner, LLC v. Emery Bay PKI, LLC*.[97] Based on the previously discussed facts, the plaintiff LLC brought a claim for a breach of the implied covenant against the defendant LLC responsible for managing Emery Bay. The plaintiff's claim was premised on the argument that under Emery Bay's LLC agreement, the defendant LLC had a duty to manage Emery Bay and, in that context, had the power and authority to cause the performance of supporting agreements relating to the management of the project, and failed to do so. The defendant LLC disagreed and argued that the LLC agreement merely provided it with the power to act if it so decided. The court

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93. *Id.* at 881.

94. *Id.* at 887.

95. *Id.* at 888.

96. *Id.*

97. C.A. No. 3658-VCS, 2009 WL 1124451 (Del. Ch. Apr. 20, 2009).

framed the question presented to it as whether an obligation to cause the performance of the supporting agreements by the defendant LLC could be implied in the LLC agreement.

Initially, the court recognized that the implied covenant of good faith and fair dealing should be used infrequently. "Delaware courts rightly employ the implied covenant sparingly when parties have crafted detailed, complex agreements, lest parties be struck by judicial error with duties they never voluntarily accepted. Nevertheless, Delaware courts have 'recognized the occasional necessity of implying contract terms to ensure the parties' reasonable expectations are fulfilled.'"[98] The court found that the defendant LLC had an obligation to manage Emery Bay and to cause the supporting agreements to be carried out in good faith, and it could not prevent the plaintiff from "'receiving the fruits of the bargain.'"[99] The court further found that the plaintiff had alleged sufficient facts to infer reasonably that the defendant LLC's failure to cause the performance of the supporting agreements was not in good faith. The court denied the defendants' motion to dismiss the plaintiff's claim of breach of the implied covenant of good faith and fair dealing.

H. Amendments to Operating Agreements

On a motion for summary judgment, the Delaware Court of Chancery examined the meaning of an amendment provision of an LLC agreement in a petition for judicial dissolution in *In re Nextmedia Investors, LLC*.[100] The claim stemmed from an amendment made to an LLC agreement to extend the term of the LLC, where the consent to amend was not obtained from the petitioners who were members of the LLC. The LLC agreement provided that specific sections of the LLC agreement could not be amended "[w]ithout the consent of each Member to be adversely affected."[101]

When the petitioners had initially invested in the LLC and were admitted as members of the LLC, the LLC agreement provided a clear, eight-year investment horizon for the LLC and the LLC was to dissolve after this period. When the dissolution date was approaching, the LLC attempted to market its assets but, due to an economic downturn, the market conditions at the time were not favorable. The board of managers desired to extend the duration of the LLC with hopes that the economy would improve. To effectuate this extension, the board proposed an amendment to the LLC agreement to extend the term. This amendment was to a section of the LLC agreement that required the consent of each member that would be adversely affected by such amendment, and the petitioners had not consented to the amendment. Attempting to persuade the petitioners to consent, the chief financial officer of the LLC sent the petitioners a letter asserting that dissolution of the LLC would not be in the petitioners' best interests because of the current economic conditions. The letter also suggested that the LLC would assert that the consent of the petitioners was unnecessary since they would not be adversely affected by the amendment.

The LLC informed the petitioners that it viewed the amendment as properly adopted and that the LLC had not been dissolved. In response, the petitioners filed a motion seeking an order for judicial dissolution of the LLC. The petitioners argued that based on the amendment provision in the LLC agreement, the amendment was not properly adopted without their consent. In examining the petitioners' claim, the court noted that the ability to withdraw from an investment is important: "It is not uncommon for organizational documents to require a unanimous vote to avoid dissolution,

98. *Id.* at *7 (quoting Dunlap v. State Farm Fire & Cas. Co., 878 A.2d 434, 443 (Del. 2005)).

99. *Id.* (quoting *Dunlap*, 878 A.2d at 442).

100. C.A. No. 4067-VCS, 2009 WL 1228665 (Del. Ch. May 6, 2009).

101. *Id.* at *2.

in recognition of the importance investors place on the ability to withdraw."[102] In this case, there was a specific date for dissolution provided in the LLC agreement, and the court concluded that a reasonable investor would regard this date as a guaranteed investment end point that would require such investor's consent to change. Such provision was a material economic term of the LLC agreement. In addition, the fact that the LLC had originally sought the consent of the petitioners for the amendment reflected the LLC's view that such consent was necessary for the amendment, despite the arguments made in response to the petitioners' motion. The court concluded that the petitioners had adequately shown a reasonable interpretation of the LLC agreement and that the unanimous consent of the LLC's members was required to adopt the amendment extending the term of the LLC.

The LLC also attempted to argue that dissolution of the LLC was not appropriate because the petitioners should be required to demonstrate that they were actually adversely affected by the amendment to the LLC agreement. The court disagreed with this argument, stating that the only thing the petitioners were required to show was that their consent was required for the amendment and it was not obtained. "Whether they were to be adversely affected … is necessarily a before-the-fact question—a company cannot determine who is entitled to vote on an action by first carrying out the action and then seeing who is adversely affected."[103] The determination of whether an amendment triggers an approval requirement is based on whether the proposed contractual amendment would "alter an economically meaningful term."[104] The court concluded that the amendment to extend the term was clearly an amendment that required the consent of the petitioners and therefore granted the petitioners' motion for summary judgment to judicially dissolve the LLC.

I. Removal of Manager

In *R & R Capital, LLC v. Merritt,*[105] the Delaware Court of Chancery analyzed manager removal provisions in various LLC agreements to determine whether a manager had been validly removed as manager and member of nine LLCs. The defendant had been a manager of various LLCs and a member of some of those LLCs. As to two of the LLCs involved, the plaintiffs attempted to remove the defendant as the manager of the LLCs based on claims that the defendant had: (1) failed to pay taxes relating to the LLCs; (2) conducted activities that led to outstanding judgments and/or liens against the entities; (3) caused many of the LLCs to have their certificates of formation cancelled for failure to pay taxes and failure to maintain a registered agent; (4) failed to make distributions from the sale of property owned by the LLCs; (5) transferred property owned by one of the LLCs to satisfy personal obligations and later sold additional properties of that LLC for below market value; (6) used resources from one group of the LLCs for her personal use without prior authorization; (7) caused government action against one LLC for causing its property to fall into serious disrepair; and (8) failed to dissolve an LLC as required by its operating agreement when she sold all of its property. In response, the defendant argued that her ability to manage the entities was hindered by the fact that the owner of one of the plaintiffs had a felony conviction, which prevented her from obtaining certain licenses, and that the plaintiffs had interfered with her operation of the entities.

Due to their dissatisfaction with the defendant's management, the plaintiffs sent her a notice of removal for "cause" under a section of each of the entities' operating agreements, which provided that a manager could be removed for

102. *Id.* at *4.

103. *Id.* at *7.

104. *Id.*

105. C.A. No. 3989-CC, 2009 WL 2937101 (Del. Ch. Sept. 3, 2009).

"cause" upon written demand setting forth specific facts giving rise to such "cause," including that the manager had: "(a) engaged in fraud or embezzlement, (b) committed an act of dishonesty, gross negligence, willful misconduct, or malfeasance that has a material adverse effect on the Company or any other Member, or (c) been convicted of a felony."[106] The removal notice sent by the plaintiffs was based on an action brought between the parties in Pennsylvania, where the judge had found in favor of the plaintiffs and stated that the defendant had engaged in fraud in connection with a transaction between the plaintiffs and the defendant for the purchase of "pinhooking" horses. The plaintiffs then initiated suit to obtain a declaration that the defendant had been validly removed as a manager.

The defendant argued that since the issue had already been litigated and decided, the plaintiffs were estopped from bringing their removal claim based on the doctrine of res judicata. A res judicata claim must demonstrate that:

> (1) the court making the prior adjudication had jurisdiction; (2) the parties to the present action are either the same parties or in privity with the parties from the prior adjudication; (3) the prior adjudication was final; (4) the causes of action were the same in both cases or the issues decided in the prior action were the same as those raised in the present case; and (5) the issues in the prior action were decided adversely to the party's contention in the instant case.[107]

The court found that the third element needed for a *res judicata* argument was missing from the defendant's claim. While the pinhooking horse transaction had been raised by the plaintiffs in a complaint in New York, the judge hearing that claim had not made a final adjudication on the transaction as it related to the defendant's removal as a manager. Therefore, the court concluded that the plaintiffs were not barred from bringing their action based on the doctrine of *res judicata*. For the same reason that there had not been a final adjudication on the issue involved, the court also rejected the defendant's defenses of collateral estoppel and judicial estoppel.

The defendant also argued that the plaintiffs misinterpreted the removal section of the operating agreements of the LLCs, arguing that even if she had perpetrated a fraud against the plaintiffs, she could not be removed as a manager unless the LLCs had suffered a "material adverse effect" caused by her fraudulent behavior. The court disagreed with the defendant's interpretation of the removal provision and found that the qualification of suffering a "material adverse effect" applied to other provisions in the LLC agreements and there was no such qualification for removal when the manager had committed fraud. The court found the provision to be susceptible to only one meaning and was therefore unambiguous. Further, the court noted that even if there was a contractual requirement to demonstrate a "material adverse effect," the defendant's actions had had such an adverse effect on the members so that she still could be removed for cause. Having found that the removal notice was both proper and effective, the court declared that the defendant had been validly removed as a manager of the LLCs.

J. Arbitrability of Claims

In *Julian v. Julian,*[108] the Delaware Court of Chancery analyzed an arbitration provision in an LLC agreement and addressed the issue of who should decide whether parties to an LLC agreement must submit their particular dispute to arbitration. *Julian* arose from disputes among three brothers who had formed various family-owned LLCs. Due to disputes

106. *Id.* at *2.

107. *Id.* at *3 (quoting Julian v. E. States Constr. Serv., Inc., 2009 WL 1211642, at *5 (Del. Ch. May 5, 2009)).

108. C.A. No. 4137-VCP, 2009 WL 2937121 (Del. Ch. Sept. 9, 2009).

among the members, the plaintiff brother had resigned from some of the LLCs and sought a judicial determination of the fair value of the LLCs from which he had resigned. The defendant brothers responded by arguing that the plaintiff's claims should be dismissed because there was an adequate remedy at law in the form of arbitration, which was set forth in the operating agreements of some of the applicable LLCs.

The court found that the issue presented was one of substantive arbitrability, which the court defined as "whether the parties decided in the contract to submit a particular dispute to arbitration."[109] The court noted that Delaware courts generally favor arbitration when parties bargained for arbitration in their contract. "Delaware's public policy strongly favors arbitration, but arbitration is consensual, so the parties must have agreed to it."[110] Before determining substantive arbitrability, the court stated that an initial issue was who should decide if the parties to the contract chose to submit the dispute to arbitration or to a court. "'[T]he question of whether the parties agreed to arbitrate is generally one for the courts to decide and not for arbitrators.' Consequently, courts should presume the parties did not agree to arbitrate arbitrability, unless there is 'clear and unmistakable evidence that they did so.'"[111]

To make this determination, the court used a two-prong method articulated by the Delaware Supreme Court in *Willie Gary* to determine "whether an arbitration clause constituted 'clear and convincing evidence' of the parties' intent to arbitrate arbitrability."[112] That standard would be met if the arbitration clause "(1) generally refers all disputes to arbitration and (2) references a set of arbitral rules that empowers arbitrators to decide arbitrability."[113] It was undisputed in this case that the arbitration provision at issue generally referred all disputes to arbitration; therefore, the first prong of the standard was met. The arbitration provision also referred matters to the American Arbitration Association rules, which the court found to empower arbitrators to decide arbitrability. The second prong of the standard was also met.

Despite the fact that both prongs of the *Willie Gary* test had been met, the plaintiff still contended that his claims did not arise out of or relate to the LLC agreements, since his claims related to a valuation of his interest upon resignation under section 18-604 of the LLC Act. As a result, he asserted that "a court, and not the arbitrator, should determine that they fall outside the broad scope of the applicable arbitral provision."[114] Further, he had also made fiduciary duty claims, which he argued did not relate to or arise out of the LLC agreements.

The court found the plaintiff's arguments unpersuasive. LLCs are creatures of contract and are required under the LLC Act to have a limited liability company agreement; consequently, the plaintiff's request for the fair value of his interest in an LLC relates to some extent to the terms of the applicable LLC agreement. Having found that the *Willie Gary* test had been met and there was a basis for finding that the disputes related to the relevant LLC agreements, the court determined that an arbitrator should be left to decide whether the disputes should be before an arbitrator.

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109. *Id.* at *4 (quoting James & Jackson, LLC v. Willie Gary, LLC, 906 A.2d 76, 79 (Del. 2006)).

110. *Id.* at *3.

111. *Id.* at *5 (quoting DMS Properties-First, Inc. v. P.W. Scott Assoc., Inc., 748 A.2d 389, 391-92 (Del. 2000); *Willie Gary*, 906 A.2d at 79 (quoting First Options of Chicago, Inc. v. Kaplan, 514 U.S. 938, 944 (1995))).

112. *Id.*

113. *Id.*

114. *Id.* at *6.

IV. INSPECTION OF BOOKS AND RECORDS

A. Scope of the Right to Compel Access to Books and Records

In *Madison Real Estate Immobilien-Anlagegesellschaft Beschrankt Haftende KG v. KanAm USA XIX Limited Partnership,*[115] the Delaware Court of Chancery examined the scope of a limited partner's right to gain access to the books and records of a limited partnership under an LP agreement and the LP Act. The plaintiff in *Madison* was a German entity that was formed as an "acquisition vehicle" to make initial small investments in partnerships. If it determined that the partnership involved was an attractive investment, it then would make a tender offer for the purchase of additional interests.

The limited partnership targeted by the plaintiff in *Madison* was a fund that owned joint venture interests in shopping centers. The plaintiff viewed the fund as a potential tender offer candidate due to some financial problems the fund was having, thereby indicating that the limited partners in the fund might be willing to sell their interests at a discount. To initiate its tender offer plan, the plaintiff purchased a small amount of limited partner interests in the fund and then completely analyzed the partnership and produced various models that priced a potential tender offer. With the purpose of developing its tender offer, the plaintiff made several written books and records inspection demands to the fund's general partner, which included demands for detailed financial and operations information about the fund. Eventually the general partner responded and rejected the demand by citing that the information requested was "proprietary, confidential, and in the nature of trade secrets."[116] After a revised demand was also rejected by the general partner, the plaintiff commenced action to gain access to the information. The plaintiff alleged that the failure of the general partner and the fund to provide such information was a breach of the LP agreement and the LP Act, and such failure had resulted in monetary damages to the plaintiff.

The court first analyzed the plaintiff's claim under section 17-305 of the LP Act. Section 17-305 provides that "a limited partner may obtain access to books and records of a limited partnership upon a reasonable demand for any purpose reasonably related to the limited partner's interest as a limited partner."[117] The plaintiff argued that it had two proper purposes for requesting access to the books and records: (1) valuing the fund as a whole for the purpose of commencing a tender offer, and (2) valuing its existing interests in the fund. In its analysis, the court noted that the "*primary* purpose must be proper," that "any *secondary* purpose, whether proper or not, is irrelevant," and that the plaintiff has the burden of demonstrating a proper purpose.[118]

In analyzing the plaintiff's purpose, the court examined the standards set by case precedent in two cases, *Madison Avenue Investment Partners, LLC v. American First Real Estate Investment Partners, L.P.*[119] ("*Madison I*") and *BBC Acquisition Corp. v. Durr-Fillauer Medical, Inc.*[120] The plaintiff analogized the current facts to *Madison I*, where access to books and records was allowed for the proper purpose of valuing one's investment when there was an objective of acquiring additional

115. C.A. No. 2863-VCP, 2008 WL 1913237 (Del. Ch. May 1, 2008).

116. *Id.* at *3.

117. *Id.* at *2.

118. *Id.* at *5 (quoting BBC Acquisition Corp. v. Durr-Fillauer Med., Inc., 623 A.2d 85, 88 (Del. Ch. 1992)).

119. 806 A.2d 165 (Del. Ch. 2002).

120. 623 A.2d 85 (Del. Ch. 1992).

units. The court rejected the plaintiff's assertion and instead distinguished the *Madison I* facts from the current facts because in *Madison I,* no decision had been made to launch a tender offer. The court here agreed with the general partner that the current facts were more analogous to the corporate law *BBC Acquisition* case, where the court determined that a primary purpose of valuing an interest to consider whether to increase an offering price in a tender offer situation was not reasonably related to an interest as a stockholder and therefore was not a proper purpose within the meaning of DEL. CODE ANN. tit. 8, § 220. Under the current Madison facts, including the concession by the plaintiff, the court found that the primary purpose of the plaintiff in seeking the books and records of the fund was to make a tender offer. The court concluded that the plaintiff's primary purpose was not reasonably related to its interest in the fund and therefore was not a "proper purpose" within the meaning of section 17-305 of the LP Act.

The court also addressed two alternative and independent grounds under section 17-305(b) of the LP Act that would have allowed the general partner and the fund to deny the plaintiff access to the books and records. First, the court found that the general partner had demonstrated that it could keep the requested information confidential pursuant to section 17-305(b) because it reasonably believed that the requested information was in the nature of trade secrets. Further, the court found that the general partner had adequately shown that the fund was required to keep the requested information confidential pursuant to various written and oral third-party agreements.

The court then analyzed the plaintiff's claim that it was entitled, pursuant to the LP agreement of the fund, to inspect the books and records. The LP agreement referred to a right to inspect the "books of account" of the fund, as opposed to the more commonly used term "books and records." The plaintiff argued that the term used in the LP agreement was ambiguous and therefore, based on the doctrine of *contra proferentem*, which resolves ambiguities against the drafter, should be construed in its favor to include the requested information. The general partner disagreed with the plaintiff and felt that the language in the LP agreement was unambiguous and did not encompass the information requested by the plaintiff. Relying on a definition provided by the general partner from *Black's Law Dictionary*, as well as the second sentence of the relevant section of the LP agreement, which stated that the "books of account shall be closed at the end of each year," the court determined that the term "books of account" was limited to documents that the fund had created, controlled, or closed out at the end of each year. Based on this conclusion, the court found that the LP agreement was not ambiguous and, further, the information requested by the plaintiff fell outside the scope of the "books of account" referred to in the LP agreement. The court denied the plaintiff's request to inspect the books and records of the fund.

B. Use of Commission to Request Documents

In *Maitland v. International Registries, LLC, et al.,*[121] the Delaware Court of Chancery ruled on a motion by the plaintiff for a commission requesting documents and deposition testimony where the ultimate case involved an action for the inspection of the books and records of two LLCs under section 18-305 of the LLC Act. The court in *Maitland* first noted that "[b]ecause the issues in a books and records case are narrow, discovery is necessarily narrow as well."[122] The court found that the request for discovery by the plaintiff was not narrow and would effectively grant the plaintiff his final relief of access to the books and records. The court stated that the plaintiff could not "use the discovery process in a books and records case to gain access to the books and records ultimately at issue,"[123] as this would allow the plaintiff to have a way around the LLC agreement and the LLC Act. The court denied the plaintiff's motion for commission.

121. C.A. No. 3669-CC, 2008 WL 2440521 (Del. Ch. June 6, 2008).

122. *Id.* at *2.

123. *Id.*

C. Entitlement to Review Books and Records

The Delaware Court of Chancery examined the entitlement of an individual to review the books and records of an LLC, based upon such individual's relationship to the LLC, in *Mickman v. American International Processing.*[124] In *Mickman*, the defendant LLC moved for summary judgment in a case brought by the plaintiff, Elaine Mickman, for the inspection of the books and records of the LLC. The LLC argued that the plaintiff was not a member or manager of the LLC and consequently was not entitled to inspection rights under section 18-305 of the LLC Act.

The court first quoted section 18-305 of the LLC Act, which explicitly provides certain books and records inspection rights to members and managers of an LLC. The LLC argued that the plaintiff was not listed on the list of members in the LLC agreement, and therefore she was not a member entitled to rights under section 18-305. The plaintiff argued that although she was not listed in the LLC agreement as a member, she was listed by the other two members on various tax forms as a member and should be entitled to the rights of a member. In its analysis, the court noted that LLCs by their nature are "flexible and less formal" than corporations and, accordingly, "it is reasonable to consider evidence [of membership] beyond the four corners of the operating agreement."[125] In this case, the court was willing to examine the evidence that the plaintiff had presented suggesting that, notwithstanding the LLC agreement, the parties to that agreement had intended to admit and thought they had admitted the plaintiff as a member of the LLC. As the court was willing to examine evidence showing that the plaintiff was a member of the LLC and thus entitled to inspection rights under section 18-305 of the LLC Act, the court denied the defendant LLC's summary judgment motion.

Subsequent to that decision, the Delaware Court of Chancery examined in the same case whether the plaintiff was entitled to photocopy the general ledgers of two LLC defendants.[126] The plaintiff first argued that she was entitled to photocopy the general ledgers because the LLCs had waived any objection to her obtaining that information when they granted her counsel the opportunity to review the ledgers. A waiver is the "'intentional relinquishment of a known right, either expressly or by conduct, which clearly indicates an intention to renounce a known privilege or power.'"[127] The court found that, based on their conduct, the LLCs had not waived their objections to the plaintiff's photocopying the ledgers as they had taken affirmative steps to deny the plaintiff that right, which indicated their intent to preserve their objections to the plaintiff's making photocopies.

The plaintiff's second argument was that she was entitled to photocopy the general ledgers under both operating agreements of the LLCs and section 18-305 of the LLC Act. Each of the LLC agreements expressly granted members inspection rights, and the court noted that "LLC agreements can grant members inspection rights that exceed the rights provided in the statute."[128] Each LLC agreement specifically provided that members shall have "access to all books and records" of the applicable LLC, but it did not define exactly what "access" entailed. The parties disagreed as to the interpretation, so the court referred to corporate precedent in interpreting the provision. The court found the language in the LLC agreements to be broad and to include the general ledgers that had been requested. Relying on corporate precedent,

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124. C.A. No. 3869-VCP, 2009 WL 891807 (Del. Ch. Apr. 1, 2009).

125. *Id.* at *2.

126. Mickman v. Am. Int'l Processing, L.L.C., C.A. No. 3869-VCP, 2009 WL 2244608 (Del. Ch. July 28, 2009).

127. *Id.* at *1 (quoting Moore v. Travelers Indem. Ins. Co., 408 A.2d 298, 302 (Del. Super. 1979)).

128. *Id.*

the court interpreted "access" to include making photocopies of the books and records. Since the court found that the plaintiff was contractually entitled to photocopy the general ledgers under the LLC agreements, it did not address the plaintiff's statutory right of access under section 18-305 of the LLC Act.

D. Proper Purpose

In *JAKKS PACIFIC, Inc. v. THQ/JAKKS PACIFIC, LLC,*[129] the Delaware Court of Chancery examined section 18-305 of the LLC Act's proper purpose test in connection with a books and records request. The plaintiff was a non-operating member of an LLC, and the defendant was a second member who was responsible for the day-to-day operations of the LLC and for the books and records of the LLC. The LLC was formed to market and sell videogames pursuant to a license held by the LLC. The company that issued the LLC its license was currently litigating a contract dispute with the LLC, making the future extension of the license extremely speculative. The plaintiff had no capital invested in the LLC and did not have any residual equity interest in the LLC. It was only entitled to a preferred return from the sales revenue of the LLC. The plaintiff's "economic interest in the joint venture, though it is technically a member of the LLC, is less that of an equity owner and more akin to a licensor with rights to royalties based on sales."[130]

The plaintiff sent the defendant a letter demanding a "broad spectrum of financial documents" relating to the LLC. The defendant responded by supplying over 110,000 pages of material to the plaintiff. The plaintiff made multiple follow-up requests for additional LLC information. Subsequently, the plaintiff made an additional books and records demand on the defendant, which demand included an extensive list of items. The plaintiff also provided a list of reasons for this request. The defendant responded that the request was overbroad and failed to state a proper purpose. The plaintiff then initiated a lawsuit to enforce its rights under section 18-305.

The plaintiff cited the following purposes in its demand for documents: "(1) to aid it in negotiating the Preferred Return for the next distribution period, (2) to value its interest in the LLC, and (3) to investigate alleged mismanagement and wrongdoing by [the defendant] in managing the affairs of the joint venture."[131] The court stated that the plaintiff had to establish by a preponderance of the evidence that there was proper purpose for inspection of the books and records.

Since the extension by the LLC of its license agreement was so speculative, the court found the first purpose for the demand by the plaintiff (i.e., to negotiate the preferred return) to be not reasonably related to the plaintiff's interest in the LLC. Further, although the court noted that in most circumstances, a demand to value an interest in an LLC (i.e., the plaintiff's second purpose) is generally a valid purpose for a demand, the plaintiff had no residual equity interest in the LLC and was only entitled to a preferred return and that return was currently being determined through an arbitration. Finally, to support an allegation of mismanagement in a books and records demand (i.e., the plaintiff's third purpose), the plaintiff "must offer a credible basis to suspect mismanagement or wrongdoing."[132] The plaintiff did not offer any credible basis. As the court found that the plaintiff had failed to meet its burden of proof that it had a proper purpose under section 18-305, judgment was entered for the defendant.

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129. C.A. No. 4295-VCL, 2009 WL 1228706 (Del. Ch. May 6, 2009).

130. *Id.* at *2.

131. *Id.* at *4.

132. *Id.* at *5.

V. STATUTE OF FRAUDS

In *Olson v. Halvorsen*,[133] the Delaware Court of Chancery, as a matter of first impression, addressed whether the Delaware statute of frauds applies to LLC agreements. The Delaware statute of frauds states that "an agreement 'that is not to be performed within the space of one year from the making thereof' must be reduced to writing and signed by the party against which the agreement is to be enforced."[134] Prior to the *Olson* case, there had been disagreement among commentators on the statute of fraud's application, as it is not specifically addressed in the LLC Act and there was no case law directly on point.

In *Olson*, a hedge fund had been founded by a number of individuals. One of the individuals was subsequently removed and argued that he was entitled to certain payout terms specified in an unsigned operating agreement. The defendants who as founders had removed the individual plaintiff answered the plaintiff's complaint by asserting that the statute of frauds was applicable to the unsigned operating agreement and the earnout provisions were therefore unenforceable since they could not be performed within one year.

In determining the primary issue of whether the statute of frauds is applicable to LLC agreements, the court first noted that the LLC Act expressly allows oral operating agreements; however, the LLC Act does not specifically address whether the statute of frauds would be applicable to such oral agreements.[135] The court recognized that some commentators believe that without express statutory language overriding the statute of frauds, the principle is still applicable, as compared to other commentators who feel that the authorization of oral agreements along with the general principle under the LLC Act of giving maximum effect to the enforceability of LLC agreements creates an inference that the legislature intended to override the statute of frauds. The court found that the statute of frauds applies to LLC agreements that have terms that cannot be performed within a year. In so finding, the court held that "if an LLC agreement contains a provision or multiple provisions which cannot possibly be performed within one year, such provision or provisions are unenforceable."[136] In following the Delaware legislature's intent, the court also held that "provisions of an oral LLC operating agreement that could possibly be performed within one year will not fall within the statute of frauds and will remain enforceable."[137]

In determining the applicability of the statute of frauds to the *Olson* facts, the court noted that in addition to the payment of money to the plaintiff, the defendants also had certain other obligations that required them to take certain actions and prevented them from taking other actions, all for a period of time that extended beyond a year. Also, the payments that the plaintiff was requesting could not be calculated until more than one year after the date of the purported operating agreement. Based on these facts, the court determined that the statute of frauds was applicable.

The plaintiff asserted that even if the statute of frauds applied, certain exceptions were applicable. First, he argued that the multiple writings exception applied, which allows multiple writings to satisfy the statute of frauds where one of the writings is signed by the parties against whom the documents are to be enforced and the writings "'(a) reasonably identify

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133. C.A. No. 1884-VCL, 2008 WL 4661831 (Del. Ch. Oct. 22, 2008). The Court of Chancery's decision after trial may be found at *Olson v. Halvorsen*, C.A. No. 1884-VCL, 2009 WL 1317148 (Del. Ch. May 13, 2009).

134. *Id.* at *3 (quoting Del. Code Ann. tit. 6, § 2714(a)).

135. *See* LLC Act § 18-101(7) (providing that "a limited liability company agreement means any agreement … written, *oral*, or implied") (emphasis added).

136. *Olson*, 2008 WL 4661831, at *3.

137. *Id.*

the subject matter of the contract, (b) indicate that a contract has been made between the parties or an offer extended by the signing party and (c) state with reasonable certainty the essential terms of the unperformed promises in the contract.'"[138] The court rejected the plaintiff's arguments because the signed documents did not clearly identify the unsigned operating agreement and, in particular, the earnout provision contained therein that the plaintiff wanted the court to enforce. The court also noted that the signed documents failed to set forth any of the essential terms of the unsigned operating agreement, that are required to satisfy the multiple writings exception to the statute of frauds.

The plaintiff also argued that the part performance exception to the statute of frauds should apply. The court disagreed. Following the rule that multiple other jurisdictions have applied, it held that the part performance exception to the statute of frauds is only applicable to contracts for the sale of land, which would not apply to the facts in this case. As no exception was available to the plaintiff, the statute of frauds applied and the court granted summary judgment in favor of the defendants.

On December 15, 2009, the Delaware Supreme Court affirmed the Delaware Chancery Court's conclusion that the statute of frauds applies to LLC agreements.[139] The court applied principles of statutory construction and ruled that the LLC Act did not repeal the application of the statute of frauds to LLC agreements. The court explained that "[t]he LLC Act's explicit recognition of oral and implied LLC agreements does not preclude the statute of frauds."[140]

VI. INDEMNIFICATION

In *Donohue v. Corning*,[141] Vice Chancellor Strine addressed whether a removed managing member of an LLC was entitled to advancement of attorneys' fees. The plaintiff in *Donohue* had been a managing member of the LLC and was purportedly removed by special board approval of the LLC for "cause" in accordance with the LLC agreement. Prior to his removal, the defendant nonmanaging members had offered the plaintiff a reduced role in the LLC as opposed to removal; however, the plaintiff rejected this option and instead threatened to institute adversarial proceedings if he were removed. The defendants never responded with threats of initiating any type of action or suit against the plaintiff. Upon his removal, the plaintiff brought suit disputing the validity of the removal under the LLC agreement, and this decision addressed the plaintiff's motion for partial summary judgment to have his litigation costs advanced.

The plaintiff sought advancement pursuant to the section of the LLC agreement that provided:

> To the fullest extent permitted by law, the [LLC] shall indemnify and hold harmless … the Covered Persons from and against all liabilities and expenses (including, without limitation, judgments, fines, penalties, amounts paid in settlement, attorneys' fees, and costs of investigation) incurred in connection with the *defense* or *disposition* of any claim, action, suit, or proceeding, whether civil, criminal, administrative, or investigative, in which the Covered Person is involved, as a party or otherwise, or with which the Covered Person may be *threatened*, either during the Covered Person's incumbency or thereafter, by reason of having been, or by reason of any action taken by, the Covered Person. The

138. *Id.* at *5 (quoting ROI, Inc., v. E.I. du Pont de Nemours & Co., Inc., 1989 WL 135717, at *5 (Del. Oct. 19, 1989) (citing Restatement (Second) Of Contracts § 131)).

139. 986 A.2d 1150 (Del. 2009).

140. *Id.* at 1161.

141. 949 A.2d 574 (Del. Ch. 2008).

> [LLC] shall advance such expenses to the Covered Person upon receipt of an undertaking from such Covered Person to repay the advanced amount if it is ultimately determined that such Covered Person was not entitled to indemnification.[142]

Based on the indemnification and advancement provision, the plaintiff stated that: (1) he was a "Covered Person" under the definition provided in the LLC agreement,[143] (2) the defendants had threatened to remove him for cause for breaching his duties to the LLC and for acting with malfeasance, and (3) in bringing the suit, he was "disposing" of the threatened action by the defendants. The defendants instead asserted that no action had been threatened against the plaintiff and therefore the plaintiff's action did not fit within the advancement provision of the LLC agreement. Further, the defendants argued that regardless of whether the plaintiff's request for advancement was covered by the LLC agreement, he should not be entitled to advancement because the action was brought by him in furtherance of his own monetary interest and not as a fiduciary to the LLC.

The court acknowledged that although the plaintiff "may have both corporate and personal motivations for bringing [the] action," his decision to bring the action was "consistent with the policy behind allowing companies to advance funds to and indemnify their directors and officers."[144] The court explained that the policy of the Delaware legislature regarding indemnification is to encourage corporate officials to resist what they consider to be frivolous claims against them, secure in their knowledge that if they are vindicated, their reasonable expenses will be paid. Further, the principle purpose of indemnification is to "encourage capable men to serve as corporate directors, secure in the knowledge that expenses incurred by them in upholding their honesty and integrity … will be borne by the corporation they serve."[145]

Despite the favorable public policy of allowing indemnification, the court found that the LLC had contractual discretion in determining whether to grant advancement and the plaintiff was required to prove his entitlement to advancement under the LLC agreement. In trying to make his case, the plaintiff seemed to accept that the LLC agreement's advancement provision required conduct that was responsive or defensive in nature to give rise to an advancement right. The court found that the plaintiff could not identify the threatened suit that he was defending or disposing of by bringing suit. In particular, the court noted that the plaintiff had never been threatened by the defendants, who, to the contrary, had repeatedly told him they were not threatening him with any type of action. The court found that a for-cause removal was not a proceeding contemplated by the advancement provision of the LLC agreement, and the court denied the plaintiff's motion for partial summary judgment and dismissed the count in the plaintiff's complaint seeking entitlement to advancement.

In *Stockman v. Heartland Industrial Partners, L.P.,*[146] the Delaware Court of Chancery examined rights to advancement and indemnification under the terms of an LP agreement. Two officers of a portfolio company owned by a Delaware limited partnership were subject to various criminal proceedings brought against them in connection with their roles at the company. These criminal proceedings were eventually dismissed without prejudice. The former officers then

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142. *Id.* at 576 (emphasis added).

143. The LLC agreement defined "Covered Persons" to include managing members.

144. *Id.* at 577.

145. *Id.*

146. C.A. Nos. 4227-VCS, 4427-VCS, 2009 WL 2096213 (Del. Ch. July 14, 2009).

sought indemnification and advancement of legal fees from the company's parent (i.e., the defendant limited partnership). The partnership refused the requests and the officers responded by initiating legal action seeking advancement and indemnification under the LP agreement.

It was undisputed that the officers were "Indemnitees" under the LP agreement. The officers' claims were based upon their views that the advancement section of the LP agreement was mandatory, as it provided that expenses incurred "*shall* be advanced by the Partnership."[147] The partnership disagreed and argued that advancement under the LP agreement was not mandatory and instead required the written approval of the general partner of the Partnership, as the LP agreement also provided that "[n]o advances shall be made by the Partnership … without the prior written approval of the General Partner."[148]

In interpreting the LP agreement, the court referred to the general principle of contra proferentum, which construes ambiguous terms in an agreement against the drafter under certain circumstances:

> When an agreement like the [LP agreement] makes promises to parties who did not participate in negotiating the agreement, Delaware courts apply the general principle of *contra proferentum*, which holds that ambiguous terms should be construed against the drafter. The *contra proferentum* approach protects the reasonable expectations of people who join a partnership or other entity after it was formed and must rely on the fact of the operating agreement to understand their rights and obligations when making the decision to join … That is, in the case of an entity with ongoing operations, key constituents, including directors, officers and employees, look to the governing instrument's words, and not some obscure archive of parol evidence. As a result, any ambiguities in the [LP agreement] should be resolved in favor of the reasonable expectations of [the partnership's] Indemnitees regarding their indemnification and advancement rights.[149]

In this case, the court construed the ambiguities of the LP agreement in favor of the indemnitees, which included the officers.

In interpreting the advancement provision of the LP agreement, the court found that the officers' interpretation was the only reasonable one and the partnership's interpretation strained the plain meaning of the advancement provision when read in context. Further, the LP Agreement expressly set forth the meaning of "discretion," "sole discretion," and "sole and absolute discretion" in a manner that materially limited the general partner's liability exposure. The court found it to be meaningful that such terms were not used to modify the general partner's consent right in the advancement provision. "It would be very poor drafting indeed for [the partnership] to leave out a contractually important, liability-limiting term like 'sole and absolute discretion,' or at least 'discretion,' where [the partnership] intended to immunize the General Partner from a claim regarding advancement."[150] According to the court, it would have been easy for the drafter to provide specifically that the decision for advancement was at the discretion of the general partner. Since the court felt the general partner's approval role was merely to police the preconditions for advancement rather than to exercise discretion regarding advancement, and in light of the doctrine of *contra proferentum*, the court granted summary judgment to the officers on their claim for advancement of their legal expenses.

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147. *Id.* at *6.

148. *Id.* at *5.

149. *Id.*

150. *Id.* at *6.

On the issue of whether the officers were entitled to indemnification under the LP agreement, the court initially recognized that the LP Act gives parties greater contractual flexibility in drafting indemnification provisions than does the DGCL. Nonetheless, the indemnification provision in the LP agreement contained language similar, although not identical, to that provided under section 145 of the DGCL, which addresses indemnification in the corporate context. The LP agreement's indemnification provision selectively used language from section 145, which created confusion in interpreting it:

> In a nutshell, the Indemnification Provision adopts § 145's standard for good faith and lawful conduct, but is silent about the effect of a disposition of the underlying proceeding in favor of the Indemnitee, which is a key consideration when determining whether a corporate official is entitled to indemnification under § 145.[151]

The issue therefore was whether the plaintiffs had to plead and prove that they acted in accordance with the specific requirements of the indemnification provision so that they could be indemnified with respect to a prior criminal proceeding against them that had already been dismissed in their favor.

To aid its interpretation, the court examined precedent based on section 145. The court noted that section 145 purports to limit indemnifiable conduct to ensure that corporate officials "do not evade the consequences of their own misconduct in such a way that they are rewarded for or encouraged to violate applicable laws and to breach their fiduciary duties to the corporation."[152] When there is no conviction, fine, settlement payment, or other punishment to avoid, the corporation is not allowed under section 145 to inquire into the good faith or lawfulness of its indemnitees; instead, such indemnitees are entitled to indemnification where they were successful on the merits in the underlying proceeding. Applying section 145 to the facts of the case, the court concluded that since the officers' criminal proceedings were dismissed, they would have been entitled to indemnification under section 145.

After the court concluded its section 145 analysis, it proceeded to interpret the indemnification provision in the LP agreement. While the indemnification provision was very similar to section 145, it did not address the indemnification rights of those that had been successful in proceedings initiated against them. The partnership argued that the officers were not entitled to indemnification because the LP agreement required them to prove that their conduct giving rise to the dismissed criminal action "(A) was in or was not opposed to the best interests of the Partnership, (B) in the case of a criminal action or proceeding, the [officers] had no reasonable cause to believe that [their] conduct was unlawful, or (C) did not constitute fraud, bad faith, willful conduct, gross negligence…."[153] The officers argued that they were entitled to mandatory indemnification and the burden was on the partnership to demonstrate that they had acted in a manner that should cause them to be denied indemnification.

The court found the officers' argument to be persuasive, particularly as their criminal proceeding had been dismissed without any adverse finding. In addition, the court rejected the argument by the partnership that an indemnitee must litigate the issue of his conduct to determine if he is entitled to indemnification, as this would be inefficient, costly, and counterproductive to Delaware's public policy of encouraging indemnification. "[I]n a situation where the outcome of the underlying proceeding is favorable to the Indemnitee and provides no rational basis to infer that a breach of duty

151. *Id.* at *8.

152. *Id.* at *10.

153. *Id.* at *1.

occurred, the Indemnitee is not required to litigate over the substance of her conduct and her state of mind."[154] Finally, the court concluded that, based on the doctrine of *contra proferentum*, any ambiguity in the LP agreement surrounding whether the officers were entitled to indemnification should be resolved in favor of the officers.

VII. DISSOLUTION

A. Waiver of Judicial Dissolution

Prior to *R&R Capital, LLC v. Buck & Doe Run Valley Farms, LLC,*[155] the Delaware courts had never analyzed the effect of a waiver of judicial dissolution contained in an LLC agreement. In *R&R Capital*, the petitioners had financed nine Delaware LLCs. The sole and exclusive control of these LLCs was in one appointed manager, and the relationship between the petitioners and the manager had deteriorated over the years. The petitioners initiated suit against the Delaware LLCs seeking the dissolution of the nine LLCs or, in the alternative, the appointment of a receiver. The petitioners argued that (1) many of the LLCs had their certificates of formation cancelled due to statutory issues, and the manager's attempts to revive them were ineffective; (2) the manager had failed to provide an accounting of the cancelled LLCs; and (3) the manager and her boyfriend had defrauded the LLCs and engaged in self dealing.

The court immediately dismissed the claims of the petitioners against two of the LLCs for lack of standing. For those two LLCs, the petitioners were not themselves members of the LLCs, but instead were members of the members. Section 18-802 of the LLC Act provides that only a member or manager may petition the court for judicial dissolution, and this does not include a member of a member. The court did, however, allow the claims against the two LLCs to proceed for the appointment of a receiver under section 18-805 of the LLC Act, as such section allows an application to be brought by any "'person who shows good cause.'"[156]

The petitioners were members of the remaining seven LLCs, so they had statutory standing to seek judicial dissolution of those entities. The seven respondent LLCs argued that the petitioners could not seek judicial dissolution or seek the appointment of a liquidator because the petitioners had waived those rights under a common section of all of the various LLC agreements. The LLC agreements provided that one cause for dissolution would be a decree of judicial dissolution under section 18-802 of the LLC Act. The LLC agreements also contained a provision pursuant to which the members explicitly waived and renounced their right to seek a court decree of dissolution or appointment of a liquidator. In addressing the tension between the two sections of the LLC agreements, the court concluded that a decree of judicial dissolution may be entered by the court upon an application *by or for* a member or manager, so the members were only waiving the right to seek dissolution by them, not the rights of others to petition for them.

In analyzing whether such waivers to seek judicial dissolution were enforceable, the court first emphasized the general view that LLCs are creatures of contract that are designed to afford the maximum amount of freedom of contract, including the enforceability of LLC agreements. The court rejected the statutory arguments the petitioners had raised regarding the waiver and instead found nothing to indicate that waiving judicial dissolution violated the LLC Act.[157] The

154. *Id.* at *17.

155. C.A. No. 3803-CC, 2008 WL 3846318 (Del. Ch. Aug. 19, 2008).

156. *Id.* at *2 (quoting LLC Act § 18-805).

157. The petitioners had first pointed to section 18-109(d) of the LLC Act for the argument that nonmanaging members may not waive their rights to legal action absent an agreement to arbitrate. The court rejected this argument and found that section

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court also concluded that such waiver did not violate public policy, as there is a strong public policy in favor of freedom of contract. "Generally, the mandatory provisions of the [LLC] Act are 'those intended to protect third parties, not necessarily the contracting members.'"[158]

In the court's view, the petitioners were not left unprotected, as the LLC Act preserves the implied covenant of good faith and fair dealing, which protects members against others acting unfairly and in bad faith. As the petitioners were found to have "knowingly, voluntarily, and unambiguously waived their rights to petition [the] Court for dissolution or the appointment of a receiver under the LLC Act"[159] and such waiver is permissible and enforceable, the court granted the respondents' motion to dismiss.

B. Standard for Judicial Dissolution

Section 18-802 of the LLC Act provides that the Delaware 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."[160] The Court of Chancery provided further insight into this standard in *Fisk Ventures, LLC v. Segal*[161]. In *Fisk Ventures,* the plaintiff and defendant were each investors and members in an LLC. The LLC was managed by a five-person board with members appointed by the plaintiff and defendant. The LLC agreement provided that the board could only act upon the approval of 75 percent of its members. Neither party had enough votes individually to meet the 75 percent standard, which allocated for deadlocks. In fact, the parties had an ongoing five-year track record of perpetual deadlock, even having deadlocked over issues such as whether to hold board meetings. The LLC agreement required a 75 percent vote of the members to dissolve the LLC.

The plaintiff wanted the LLC to be dissolved and the defendant disagreed. Since the LLC agreement required a 75 percent vote of the members to dissolve the LLC, there was a deadlock on the issue of dissolution. The plaintiff filed a petition seeking judicial dissolution of the LLC under section 18-802 of the LLC Act.

In addressing the standard set forth in section 18-802, the court looked by analogy to section 17-802 of the LP Act and found the standard to be whether it is "reasonably practicable" to carry on business as opposed to whether it is impossible. The court found that case law had established various factual circumstances for the evaluation of the "reasonably practicable" standard, including: "(1) the members' vote is deadlocked at the Board level; (2) the operating agreement gives no means of navigating around the deadlock; and (3) due to the financial condition of the company, there is effectively no business to operate."[162] No one factor is dispositive, and not all factors must exist for a court to find that it is no longer reasonably practicable to carry on a business.

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18-109(d) of the LLC Act is not applicable and only governs service of process and venue. The petitioners then argued that certain provisions of the LLC Act, including judicial dissolution, were mandatory and nonwaivable. The court also disagreed with this proposition, pointing to discretionary language in the statute such as "may," and further stated that a lack of a phrase such as "unless otherwise provided" does not mean that a provision is nonwaivable. *Id.* at *4-5.

158. *Id.* at *5 (quoting Elf Atochem N. Am., Inc. v. Jaffari, 727 A.2d 286, 292 (Del. 1999)).

159. *Id.* at *8.

160. LLC Act § 18-802.

161. C.A. No. 3017-CC, 2009 WL 73957 (Del. Ch. Jan. 13, 2009).

162. *Id.* at *4.

The court found sufficient evidence to dissolve the LLC based on "the futility of [the LLC's] deadlocked board, the LLC [a]greement's failure to prescribe a solution to a potentially deadlocked board, and [the LLC's] dire financial straits."[163] Notwithstanding these factors supporting judicial dissolution, the defendant argued that the LLC agreement provided a method of resolving the deadlock because the plaintiff had a right to put its interests to the LLC for a specified price, which allowed the plaintiff to have an exit strategy from the LLC. The court, however, disagreed that the put right should be viewed as an alternative to judicial dissolution, as "it would be inequitable for [the] Court to force a party to exercise its option when that party deems it in its best interests not to do so."[164] The court granted the plaintiff's motion for judicial dissolution.

In *Estate of Eric Burke v. Eric S. Burke Home Improvement,*[165] another LLC case involving a deadlock, the Court of Chancery denied a motion for summary judgment and stated that the "reasonably practicable" test is a mixed question of both law and fact, and a trial was necessary to resolve all of the facts involved. The court did, however, note that based on case precedent, in situations involving a deadlock it is "exceedingly likely" that the court would ultimately order dissolution of the LLC.[166]

In contrast to *Fisk Ventures and Eric Burke*, the Court of Chancery denied a petition for dissolution in *Seneca Investments LLC v. Tierney.*[167] The petitioner, who was the former chief executive officer of the LLC, sought judicial dissolution of the LLC, claiming that for years the LLC had not: "(1) had a business plan; (2) made an investment; (3) sought or received additional capital; (4) sought to sell any shares; (5) had a shareholders' meeting; (6) had a meeting of the board of directors; or (7) sought to hire an employee or manager who could conduct any business on behalf of the corporation."[168] The LLC had in fact held three assets passively for a number of years.

The charter in *Seneca* had been set up to be governed by the DGCL, subject to certain express exceptions. In fact, the purpose of the LLC under its charter was "to engage in any lawful act or activity for which corporations may be organized under the [DGCL]."[169] The petitioner's petition for dissolution was therefore argued under both section 18-802 of the LLC Act and section 226(a)(3) of the DGCL.

In the court's section 18-802 analysis, it first noted that judicial dissolution has been granted "where there was a 'deadlock' that prevented the corporation from operating"[170] and where the defined purpose of the entity was fulfilled or impossible to carry out. In *Seneca*, there was no claim of a deadlock, so the court's focus was on whether it was impracticable for the LLC to fulfill its purpose as it was stated in its charter. The petitioner had shown no facts to meet the "reasonably practicable" standard under section 18-802; the petitioner had only alleged that the LLC was a functioning

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163. *Id.*

164. *Id.* at *5.

165. C.A. No. 3322-CC, 2009 WL 1130388 (Del. Ch. Apr. 14, 2009).

166. The court referred to Haley v. Talcott, 864 A.2d 86 (Del. Ch. 2004), which involved a deadlocked LLC, and the court ultimately ordered dissolution of the entity.

167. C.A. No. 3624-CC, 2008 WL 4329230 (Del. Ch. Sept. 23, 2008).

168. *Id.* at *2.

169. *Id.* at *1.

170. *Id.* at *2.

passive instrumentality holding title to assets, which the court noted was "both lawful and common."[171] The petitioner had also attempted to argue that dissolution was proper under section 18-802 because the LLC had failed to comply with certain provisions of its LLC agreement, including making certain distributions and providing certain reports. The court felt that this approach was misplaced and noted that the "role of [the] Court in ordering dissolution under § 18-802 is limited, and the Court of Chancery will not attempt to police violations of operating agreements by dissolving LLCs."[172] Under these circumstances, the court found that granting judicial dissolution under section 18-802 was not warranted.

Because of the LLC agreement's incorporation of corporate principles, the court then turned to section 226(a)(3) of the DGCL to decide whether to appoint a custodian or receiver for the LLC due to abandonment of the LLC's business and a subsequent failure to dissolve.[173] The court concluded that the reference to the corporation's "business" under section 226(a)(3) meant the business of the LLC set forth in the purpose clause of its charter. It is lawful for a corporation to function as a passive holding company, which was consistent with the purpose set forth in the LLC's charter. In addition to serving as a passive holding company, the LLC was in the process of pursuing various legal claims, which was another "acceptable, and common, corporate function."[174] The court stated that it would be possible for a corporation facing a petition for dissolution to file nonmeritorious counterclaims to avoid judicial dissolution; however, that scenario was not present. Furthermore, the court found that a failure to have a business plan or to make new investments was not enough to show that the LLC had abandoned its business, as its stated purpose was to function as a passive holding company. As sufficient facts were not shown by the petitioner, the court dismissed the petition for dissolution of the LLC.

In *In re Arrow Investment Advisors, LLC,*[175] the Delaware Court of Chancery reviewed another set of facts and granted a motion to dismiss a petition for judicial dissolution. The petitioner seeking judicial dissolution of an LLC was a co-founder of the LLC who had previously been removed from its management by the other two co-founders. The purpose of the LLC as stated in its LLC agreement was to act as "an investment adviser to certain investment funds a*nd for such other lawful business as the Management Committee chooses to pursue.*"[176] The petitioner had been removed from the management committee of the LLC after disputes arose among the members of the committee over the management and strategic direction of the LLC.

Due to financial difficulties for the LLC in 2008, the LLC had sent a report to its members showing that the LLC was operating at a loss and notifying the members that the management committee had decided to explore new investment strategies for the LLC. After receiving this notification, the petitioner filed the petition seeking judicial dissolution of the LLC. The basis for the petition was that the management committee had poorly managed the LLC and had therefore impeded the LLC's business plan, goals, and objectives. The petition was very short and was viewed by the court as not containing a lot of support. The LLC sought to dismiss the petition, asserting that no facts had been set forth

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171. *Id.* at *3.

172. *Id.*

173. Section 226(a)(3) of the DGCL provides for the appointment of a custodian or receiver when "[t]he corporation has abandoned its business and has failed within a reasonable time to take steps to dissolve, liquidate or distribute its assets." DGCL § 226(a)(3).

174. *Seneca*, 2008 WL 4329230, at *5.

175. C.A. No. 4091-VCS, 2009 WL 1101682 (Del. Ch. Apr. 23, 2009).

176. *Id.* at *1 (emphasis added by court).

to infer that it was not reasonably practicable to carry on the business of the LLC as contemplated by section 18-802 of the LLC Act.

In analyzing whether judicial dissolution was appropriate, the court noted the extraordinary nature of judicial dissolution as a remedy. Judicial dissolution is not an appropriate remedy merely when profitability has not been as expected, as this is common in a capitalistic system that encourages risk-taking activity. Instead, judicial dissolution is to be used only in situations where an LLC's management has "become so dysfunctional or its business purpose so thwarted that it is no longer practicable to operate the business, such as in the case of a voting deadlock or where the defined purpose of the entity has become impossible to fulfill."[177]

In addressing the petitioner's arguments, the court first noted that an allegation that the LLC is not meeting its business plan is not the same as an allegation that it is no longer reasonably practical to carry on the business of the LLC in accordance with its LLC agreement. The court also disagreed with the petitioner's argument that the purpose set forth in the LLC agreement should be read narrowly, as this was clearly not the intent in light of the broad language in the LLC agreement allowing the LLC to pursue any lawful business chosen by the management committee. The petitioner argued that broad purpose clauses needed to be read narrowly to avoid section 18-802 from becoming superfluous; however, the court did not find this argument persuasive. The court acknowledged that there could be circumstances where judicial dissolution would be appropriate even when an entity had a broad purpose, if the facts supporting dissolution were persuasive.[178] Such a situation could arise "upon a strong showing that a confluence of situationally specific adverse financial, market, product, managerial, or corporate governance circumstances [exist making] it nihilistic for the entity to continue."[179]

The petitioner also argued that due to breaches of fiduciary duties by the current members of the management committee, judicial dissolution was appropriate. The court rejected this argument on two specific grounds. First, the court found that the petitioner had failed to allege any specific facts demonstrating a reasonable inference that fiduciary duties had been breached. Second, because many fiduciary duty claims are derivative claims, such claims must comply with the procedural requirements for derivative claims. In this case, none of those requirements had been met, including that the petitioner first make a demand on the management committee to address the alleged wrongs. "The purpose of demand is, in part, to give corporate managers an opportunity to address alleged wrongs without subjecting the entity to costly litigation."[180] The demand rule had an important function that should not be bypassed with a judicial dissolution petition.

In order for a petitioner to successfully bring a judicial dissolution petition based on breaches of fiduciary duties, she must show that "(1) she has proven the fiduciary breaches in a plenary action; and (2) there remains a rational basis for a dissolution remedy notwithstanding the remedy granted in the plenary action."[181] The LLC agreement required disputes to be handled first through arbitration. Since Delaware policy favors alternative dispute resolution, the petitioner was required to first attempt to handle his fiduciary duty concerns through the LLC agreement's dispute mechanisms.

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177. *Id.* at *2.

178. In fact, even with a broad purpose provision in an LLC agreement, the Delaware Court of Chancery granted a petition for judicial dissolution. *See* Harris v. RHH Partners, LP, C.A. No. 1198-VCN, 2010 WL 322993 (Del. Ch. Jan. 27, 2010).

179. *Arrow*, 2009 WL 1101682, at *3.

180. *Id.* at *4.

181. *Id.* at *5.

In summary, "[d]issolution is an extreme remedy to be applied only when it is [no] longer reasonably practicable for the company to operate in accordance with its founding documents, not as a response to fiduciary or contractual violations for which more appropriate and proportional relief is available."[182] Finding no basis for judicial dissolution, the court dismissed the petitioner's motion.

On a motion to dismiss, the Delaware Court of Chancery again discussed the standard for judicial dissolution under section 18-802 of the LLC Act in *Lola Cars International Limited v. Krohn Racing, LLC*.[183] In *Lola Cars*, the plaintiff and defendant had formed a Delaware LLC. Despite the fact that the plaintiff held a majority equity interest in the LLC, the members agreed to an equal representation on the board of the LLC of one director each. The defendant's director was also the chief executive officer of the LLC.

The relationship between the plaintiff and the defendant soured, and, among the multitude of claims made by the plaintiff, the plaintiff brought a claim seeking judicial dissolution of the LLC based on an allegation that the LLC could no longer realize its stated business purpose. The defendant moved to dismiss the plaintiff's petition for judicial dissolution, arguing that insolvency alone does not support judicial dissolution and that the plaintiff's alleged facts do not support the conclusion that the LLC cannot attain its business purpose.

The court relied upon the reasoning in *Fisk*[184] to determine if the reasonable practicability standard of section 18-802 had been met: "1) whether the members' vote is deadlocked at the Board level; 2) whether there exists a mechanism within the operating agreement to resolve this deadlock; and 3) whether there is still a business to operate based on the company's financial condition."[185] While noting that no one factor is dispositive and that not all *Fisk* factors must be present, the court found that all three of such factors existed. First, the court found a deadlock among the parties on whether to replace the chief executive officer. There was a potentially irreconcilable conflict between the parties, which would likely render the LLC unable to pursue the business objectives set forth in the LLC agreement. Second, the court concluded that there was not a mechanism for resolving the deadlock. The court arrived at this conclusion notwithstanding that the LLC agreement set forth a buy-out mechanism in the event of a dispute because such mechanism was voluntary. Third, the court expressed doubt as to whether the LLC could continue to operate based on its financial condition. The relevant inquiry was whether it is reasonably practicable to continue the business of the LLC and "not whether the company cannot possibly continue its business in [accordance] with its Operating Agreement."[186] In addition to the *Fisk* factors, the court also was persuaded by allegations of mismanagement, disloyalty, and poor performance.

The defendant also argued that the LLC agreement provided specific circumstances where the LLC could be terminated and since judicial dissolution was not specifically listed, it therefore was a contractually unavailable remedy. The court found the terms of the LLC agreement did not contain the exclusive means by which the LLC could be terminated and therefore judicial dissolution had not been contractually eliminated. The court denied the defendant's motion to dismiss the action for judicial dissolution. The court did not address whether a member's or manager's statutory right to petition for judicial dissolution could be contractually eliminated.

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182. *Id.* at *1.

183. C.A. Nos. 4479-VCN, 4886-VCN, 2009 WL 4052681 (Del. Ch. Nov. 12, 2009).

184. Fisk Ventures, LLC v. Segal, C.A. No. 3017-CC, 2009 WL 73957 (Del. Ch. Jan. 13, 2009).

185. *Lola Cars*, 2009 WL 405281, at *5 (quoting *Fisk Ventures*, 2009 WL 73957, at *4).

186. *Id.* at *6.

C. Winding Up Upon Cause Shown

Section 18-803(a) of the LLC Act provides that "upon cause shown," the Court of Chancery "may wind up [a] limited liability company's affairs" and "in connection therewith, may appoint a liquidating trustee."[187] In *Spellman v. Katz (In re KSA, L.L.C.),*[188] the Court of Chancery examined the circumstances that constitute "cause shown" to authorize the court to appoint a liquidating trustee to wind up the affairs of an LLC under the LLC Act. The plaintiff and defendant in the case were each doctors who had formed the LLC to construct a medical office building. The relationship between the plaintiff and defendant deteriorated. The plaintiff eventually initiated suit to either have the LLC dissolved pursuant to section 18-802 of the LLC Act or, in the alternative, have an order issued under section 18-803(a) to appoint a liquidating trustee for the LLC. The plaintiff argued that the LLC had already been dissolved pursuant to its LLC agreement, which provided for the LLC to be dissolved and wound up as soon as the construction of the medical building was completed and a certificate of occupancy was issued with respect to each condominium unit therein.

Although neither party denied that the express preconditions for dissolution set forth in the LLC agreement had been met, the defendant argued that dissolution and winding up of the LLC was not proper because the LLC agreement did not accurately reflect the intent of the parties. The defendant argued that neither party had intended for the LLC to be dissolved upon completion of the medical building. The court found the defendant's arguments to be unpersuasive, as it found the LLC agreement to be unambiguous and thus would not overlook the plain meaning of the provision by considering parol evidence in its interpretation. Based on the plain meaning of the LLC agreement and the lack of dispute among the parties as to the facts involved, the court found that the LLC had been dissolved by the express will of the members and it was then necessary to wind up the LLC's affairs. The court granted the plaintiff's motion for summary judgment on the issue of dissolution.

The court then turned to the plaintiff's section 18-803(a) argument for the appointment of a liquidating trustee. On dissolution, the LLC agreement required the parties to select jointly a person to wind up the LLC's affairs. Because of the animosity between the two members, it seemed very unlikely that they could agree on such an appointment. Due to this inability, the court concluded that "cause" existed to support its appointment of a liquidating trustee pursuant to section 18-803 of the LLC Act.

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187. LLC Act §18-803(a).

188. C.A. No. 1838-VCN, 2009 WL 418302 (Del. Ch. Feb. 6, 2009).