

CREATURES OF CONTRACT: A HALF-TRUTH ABOUT LLCs

MOHSEN MANESH*

ABSTRACT

Courts reflexively describe LLCs—the nation’s most popular form of business entity—as “creatures of contract,” the contract being, of course, the LLC agreement that governs the rights and obligations of the parties that own and manage the entity. The judicial reflex to use this maxim is especially pronounced in Delaware, where today LLCs outnumber corporations by more than two to one. And because Delaware LLC law, like its corporate law, enjoys an outsized influence in the business world, courts in other jurisdictions have now predictably embraced the “creatures of contract” maxim, too.

But to describe LLCs as “creatures of contract,” while perhaps a useful shorthand, is simply misleading. LLCs are also creatures of statute. And they are also creatures of equity. This claim is not normative; it is a legal reality.

Therefore, the singular aim of this Article is to puncture the persistent fantasy that LLCs are “creatures of contract.” More accurately, this Article shows that LLCs embody a complex interaction of contract terms, statutory rules, and judge-made doctrine. Thus, LLCs are creatures of contract, statute, and equity.

* Associate Professor, University of Oregon School of Law. The author wishes to express his gratitude to Vice Chancellor J. Travis Laster and Tom Rutledge for their close read and detailed comments to earlier drafts of this article. The author is also grateful to Matthew O’Toole, John W. Noble, Srinivas Raju, Ann Conaway, and other participants at the Delaware Corporate Law Anniversary Symposium in Wilmington for their insights. Finally, the author thanks J.D./M.B.A. candidate Peter Lindholm for his productive research assistance on various topics related to this project.

TABLE OF CONTENTS

I. INTRODUCTION.....	393
II. CREATURES OF CONTRACT.....	399
<i>A. The Judicial Refrain.....</i>	399
<i>B. What Does it Mean?.....</i>	402
III. CREATURES OF STATUTE.....	406
<i>A. Statutory Departures from Contract Law.....</i>	407
1. Formation... ..	407
2. Privity and Binding (Non)Parties.....	410
3. Statute of Frauds.....	414
4. Separate Legal Existence and Limited Liability.....	415
5. Remedies for Breach.....	417
<i>B. Statutory Limits on Contractual Freedom.....</i>	420
1. Unwaivable Jurisdiction of Delaware Courts.....	421
2. Implied Contractual Covenant of Good Faith and Fair Dealing.....	422
IV. CREATURES OF EQUITY.....	425
<i>A. Equitable Departures from Contract Law.....</i>	426
1. Default Fiduciary Duties.....	426
2. Implied Contractual Covenant of Good Faith and Fair Dealing.....	431
3. Aiding and Abetting Liability.....	441
4. Limited Right to Bring Actions for Breach.....	445
<i>B. Equitable Limits on Contractual Freedom.....</i>	447
1. Judicial Power to Narrowly Construe LLC Agreements.....	448
2. Judicial Power to Disregard LLC Agreements.....	453
V. CONCLUSION.....	456
APPENDIX.....	458

I. INTRODUCTION

“The half truths of one generation tend at times to perpetuate themselves in the law as the whole truth of another, when constant repetition brings it about that qualifications, taken once for granted, are disregarded or forgotten.”¹ Chief Justice Cardozo, then sitting on the New York Court of Appeals, wrote these eloquent words in the early 20th century to describe the doctrine of consideration in contract law. But today, these words might well be applied to the most popular form of business entity, the limited liability company (“LLC”).²

The half-truth is this: that LLCs are “creatures of contract.” Courts reflexively use this maxim to describe LLCs, the contract being, of course, the LLC agreement that governs the rights and obligations of the parties that own and manage the entity.³ The judicial reflex to use this maxim is especially pronounced in Delaware,⁴ where today LLCs outnumber corporations by more than two to one.⁵ Undoubtedly, Delaware courts have been spurred in part by the state’s LLC statute, which, like the LLC

¹ *Allegheny Coll. v. Nat’l Chautauqua Cty Bank of Jamestown*, 159 N.E. 173, 174 (N.Y. 1927).

² See, e.g., Rodney D. Chrisman, *LLCs Are the New King of the Hill: An Empirical Study of the Number of New LLCs, Corporations, and LPs Formed in the United States Between 2004-2007 and How LLCs Were Taxed for Tax Years 2002-2006*, 15 *FORDHAM J. CORP. & FIN. L.* 459, 464 (2010) (providing empirical evidence to demonstrate that the LLC “is now undeniably the most popular form of new business entity in America.”); Daniel M. Häusermann, *For a Few Dollars Less: Explaining State to State Variation in Limited Liability Company Popularity*, 20 *U. MIAMI BUS. L. REV.* 1, 6 (2011) (“[S]ince 2004, when LLC formations surpassed incorporations for the first time, the LLC is the most popular business entity in the United States.”); Eric H. Franklin, *A Rational Approach to Business Entity Choice*, 64 *U. KAN. L. REV.* 573, 586 (“LLCs are far and away the most popular legal entity form for new businesses.”).

³ See, e.g., *TravelCenters of Am., LLC v. Brog*, C.A. No. 3751-CC, 2008 WL 5272861, at *2 (Del. Ch. Dec. 5, 2008) (Chandler, C.) (“It is well settled that [LLCs] are primarily creatures of contract, and in this case, the LLC Agreement is the contract.”).

⁴ See *infra* Appendix (identifying instances where Delaware courts have, in a written opinion, described LLCs (or, more generically, “alternative entities”) as a “creature of contract”).

⁵ As of December 31, 2016, the number of domestic Delaware LLCs was more than double the number of domestic Delaware corporations and nearly nine times the number of domestic Delaware limited partnerships:

	Active as of December 31, 2016
LLCs	827,611
Corporations	298,025
Limited Partnerships	90,626

Email, dated June 20, 2017, from Cheryl L. Wyatt, Technical Support Manager, Delaware Secretary of State Division of Corporations (on file with author).

statute of other jurisdictions,⁶ baldly asserts as its guiding policy “to give the maximum effect to the principle of *freedom of contract* and to the enforceability of [LLC] agreements.”⁷ And because Delaware LLC law, like its corporate law, enjoys an outsized influence in the business world,⁸

⁶ See, e.g., ALA. CODE § 10A-5A-1.06(a) (2014); ARK. CODE ANN. § 4-32-1304(a) (West 1993); CAL. CORP. CODE § 17701.07(a) (West 2014); COLO. REV. STAT. ANN. § 7-80-108(4) (West 2016); CONN. GEN. STAT. ANN. § 34-546(b) (West 1997); FL. STAT. ANN. § 605.0111(1) (West 2015); GA. CODE ANN. § 14-11-1107(b) (West 2009); 805 ILL. COMP. STAT. ANN. 180/55-1(b) (West 2017); IND. CODE ANN. 23-18-4 § 13 (West 2013); KAN. STAT. ANN. § 17-76,134(b) (West 2014); KY. REV. STAT. ANN. § 275.003(1) (West 2012); LA. REV. STAT. ANN. § 12:1367(B) (1993); MD. CODE ANN. § 4A-102(a) (West 2012); ME. REV. STAT. ANN. tit. 31, § 1507(1) (2011); MISS. CODE ANN. § 79-29-1201(2) (West 2011); MO. ANN. STAT. § 347.081(2) (West 2004); NEV. REV. STAT. ANN. § 86.286(4)(b) (West 2015); N.C. GEN. STAT. ANN. § 57D-10-01(c) (West 2014); N.H. REV. STAT. ANN. § 304-C:2 (2013); N.J. STAT. ANN. § 42:2C-11(i) (West 2013); N.M. STAT. ANN. § 53-19-65(A) (West 1993); OKLA. STAT. ANN. tit. 18, § 2058(D) (West 2001); S.D. CODIFIED LAWS § 47-34A-114 (2013); VA. CODE ANN. § 13.1-1001.1(C) (2003); WASH. REV. CODE ANN. § 25.15.801(2) (2016); WIS. STAT. ANN. § 183.1302(1) (West 2016). *But see* H. Justin Pace, *Contracting Out of Fiduciary Duties in LLCs: Delaware Will Lead, But Will Anyone Follow?*, 16 NEV. L. J. 1085, 1091 (2016) (noting that although many states’ LLC statutes have adopted the Delaware approach, “allow[ing] for very broad freedom of contract in contracting out of fiduciary duties,” that enforceability of fiduciary waivers outside of Delaware “remains very much in question” because of a variety of factors).

⁷ DEL. CODE ANN. tit. 6, § 18-1101(b) (2018) (emphasis added).

⁸ As is the case for corporate charters, Delaware is the preeminent choice of law for large LLCs. See, e.g., Michelle M. Harner & Jamie Marincic, *The Naked Fiduciary*, 54 ARIZ. L. REV. 879, 901 (2012) (finding that in a dataset of 150 LLCs, in which one or more party is a public company, over half were organized under and governed by Delaware law); Bruce H. Kobayashi & Larry E. Ribstein, *Delaware for Small Fry: Jurisdictional Competition for Limited Liability Companies*, 2011 U. ILL. L. REV. 91, 116 tbl.2 (finding that among closely held LLCs with fifty or more employees that form outside of their home state, more than sixty-one percent are organized under and governed by Delaware law); Mohsen Manesh, *Delaware and the Market for LLC Law: A Theory of Contractibility and Legal Indeterminacy*, 52 B.C. L. REV. 189, 202 (2011) (observing that all fifteen of LLCs that filed for or completed an initial public offering during a six-year period ending March 31, 2010, were chartered in Delaware); Jens Dammann & Matthias Schündeln, *Where are Limited Liability Companies Formed? An Empirical Analysis*, 55 J. L. & ECON. 741, 746 (2012) (finding that among closely held LLCs with 5000 or more employees that form outside of their home state, more than ninety-five percent are organized under and governed by Delaware law); WILLIAM T. ALLEN & REINER KRAAKMAN, COMMENTARIES AND CASES ON THE LAW OF BUSINESS ORGANIZATIONS 68 (5th ed. 2016) (noting that “Delaware dominates the market in out-of-state LLC formations”); Daniel S. Kleinberger, *Two Decades of “Alternative Entities”: From Tax Rationalization Through Alphabet Soup To Contract As Deity*, 14 FORDHAM J. CORP. & FIN. L. 445, 460 (2008) (“Delaware law seems to exert an almost gravitation pull on LLC practice and jurisprudence.” (quoting CARTER G. BISHOP & DANIEL S. KLEINBERGER, LIMITED LIABILITY COMPANIES: TAX AND BUSINESS LAW 14.01[2] (Warren Gorham & Lamont/RIA 1994 & Supp. 2007-2))) (internal quotation marks omitted).

courts in other jurisdictions have now predictably embraced the “creatures of contract” mantra, too.⁹

But to describe LLCs as “creatures of contract,” while perhaps a useful shorthand, is simply misleading. It is a half-truth, but not the whole truth. To be sure, LLCs are creatures of contract. After all, the LLC agreement plays a central role in defining the rights and obligations of the participants within the entity.¹⁰ But LLCs are also creatures of statute.¹¹

⁹ See, e.g., *McArdle v. Wojcicki*, No. 1-14-1229, 2016 WL 5372082, at *2 (Ill. App. 1 Dist. Sept. 23, 2016) (“Limited liability companies are creatures of contract, and the parties have broad discretion to use an LLC agreement to define the character of the company and the rights and obligations of its members.” (quoting *Kuroda v. SPJS Holdings, L.L.C.*, 971 A.2d 872, 880 (Del. Ch. 2009) (Chandler, C.)) (internal quotation marks omitted); *Mizrahi v. Cohen*, No. 3865/10, 2013 WL 238490, at *2 (N.Y. Sup. Ct. Jan. 15, 2013) (“A limited liability company, though analogous to a corporation in some respects, is primarily a creature of contract.”); *Stainless Valve Co. v. Safefresh Techs., LLC*, 753 S.E.2d 331, 335 (N.C. Ct. App. 2013) (“Because the[] default provisions [of the LLC statute] can be changed in virtually any way the parties wish, an LLC is primarily a creature of contract.”); *Torres v. Montano*, No. 30,207, 2012 WL 868941, at *4 (N.M. Ct. App. Feb. 20, 2012) (“Limited liability companies enjoy an arm’s-length relationship with legislatures and courts, because LLCs are primarily creatures of contract.”) (internal quotation marks omitted); *In re Lahood, Bankr. No. 07-81727*, 2009 WL 803558, at *3 (Bankr. C.D. Ill. Mar. 19, 2009) (“Embodying the principle of freedom of contract, a limited liability company is primarily a creature of contract and the limited liability company’s operating agreement governs the conduct of its business and the relations among the members, managers and company.”); *Hamby v. Profile Prods., L.L.C.*, 652 S.E.2d 231, 235 (N.C. 2007) (“[T]he North Carolina Limited Liability Company Act provides . . . default rules, most of which can be varied by the parties forming an LLC. As such, the LLC is primarily a creature of contract, allowing for great flexibility in its organization.”) (internal quotation marks omitted). For a particularly head-spinning use of the mantra, see *Svenningsen v. Ultimate Prof’l Grounds Mgmt., Inc.*, No. 14 Civ. 5161 (NSR), 2017 WL 1234040, at *10 n. 14 (S.D.N.Y. Mar. 31, 2017) (“LLCs are creatures of contract *existing by virtue of state statutory schemes.*”) (emphasis added).

¹⁰ See *Elf Atochem N. Am., Inc. v. Jaffari*, 727 A.2d 286, 291 (Del. 1999) (analogizing the LLC agreement to a LP agreement as the “cornerstone” of the entity and “effectively constitut[ing] the entire agreement among the [parties]”).

¹¹ See, e.g., *Berks v. Cade*, 158 So. 3d 438, 460 (Ala. 2014) (“Because limited liability companies are creatures of statute, operating agreements of limited liability companies . . . incorporate the provisions of the statutes that allow for the creation of such agreements.”) (internal quotations omitted); *Turner v. Andrew*, 413 S.W.3d 272, 275 (Ky. 2013) (“[L]imited liability companies are creatures of statute, controlled by Kentucky Revised Statutes”) (internal quotations omitted); *Weinstein v. Colborne Foodbotics, LLC*, 302 P.3d 263, 266 (Colo. 2013) (“An LLC is an unincorporated, statutorily created business entity.”); *Comm’r of Envtl. Prot. v. State Five Indus. Park, Inc.*, 37 A.3d 724, 744 n.5 (Conn. 2012) (“[L]imited liability companies, like corporations, are creatures of statute.”); *Gasstop Two, LLC v. Seatwo, LLC*, 225 P.3d 1072, 1077 (Wyo. 2010) (“Limited Liability Companies are creatures of statute.”); *Chadwick Farms Owners Ass’n v. FHC LLC*, 207 P.3d 1251, 1259 (Wash. 2009) (“[A] limited liability company is defined by statute.”); *Bell v. Walton*, 861 A.2d 687, 689 (Me. 2004) (“[T]he limited liability company is a creature of statute”); cf. *Joan MacLeod Heminway, The Ties that Bind: LLC Operating Agreements as Binding Commitments*, 68 SMU L. REV. 811, 812

And they are also creatures of equity. This claim is not normative; it is a legal reality.

To persistently obscure this reality risks creating the false impression among practitioners and business participants that an LLC agreement is like any other common law contract,¹² that the concomitant principles of freedom of contract are an inexorable feature of LLCs, and that legislators and the courts play no part in fundamentally shaping the legal rights and obligations of LLC parties. Worse yet, if repeated too frequently, the myth that LLCs are merely “creatures of contracts” might become self-deluding. Judges might actually believe what they say—that the courts’ role in LLC disputes is limited to dispassionately and mechanistically enforcing the express language of an LLC agreement, without regard to broader notions of equity or public policy¹³—thus blinding jurists to the fact that they can and already do play an active role in defining the rights and obligations of LLC parties. What was “taken once for granted,” Justice Cardozo would warn, will be “disregarded or forgotten.”¹⁴

In fact, when courts enforce an LLC agreement, they are not enforcing an ordinary bargained-for agreement; they are instead enforcing the governing instrument of a statutory business entity, crafted in the shadow of statutory and judge-made rules.¹⁵ Acknowledging this fact does

(2015) (“[LLC] agreements exist because of LLC law. The LLC is a creature of late 20th century state statutory law.”).

¹² See Heminway, *supra* note 11, at 812 (observing that “judges, legal scholars, and other commentators with knowledge of the law often assume [LLC] operating agreements are contracts or categorize them, without analysis, as contracts”).

¹³ This judicial belief is typified by the pithy assertion that “[p]arties have a right to enter into good and bad contracts[;] the law enforces both.” *Nemec v. Shrader*, 991 A.2d 1120, 1126 (Del. 2010); *accord* *Emps. Ret. Sys. of St. Louis v. TC Pipelines GP, Inc.*, CA No. 11603–VCG, 2016 WL 2859790, at *7 (Del. Ch. May 11, 2016) (Glasscock, V.C.) (quoting *Nemec v. Shrader* in the context of a LP case).

¹⁴ *Allegheny Coll. v. Nat’l Chautauqua Cty Bank of Jamestown*, 159 N.E. 173, 174 (N.Y. 1927).

¹⁵ As articulated by the leading treatise on Delaware LLCs,

The [LLC] agreement possesses a dual nature. It is at once a contract and also the governing instrument of the Delaware [LLC]. In the first instance, the [LLC] agreement is a contract. [But it] undeniably is a unique type of contract. The special statutory rules that apply to the agreement underscore its distinctiveness.

ROBERT L SYMONDS, JR. & MATTHEW J. O’TOOLE, SYMONDS & O’TOOLE ON DELAWARE LIMITED LIABILITY COMPANIES § 4.01[B] (2d ed. 2017). See also *In re Denman*, 513 B.R. 720, 726 (Bankr. W.D. Tenn. 2014) (rejecting the argument that an LLC agreement is an “executory contract” under the federal bankruptcy code and classifying it instead as “a business formation

not mean that the legislature or the courts must or should take a more regulatory or interventionist role in the internal governance of LLCs.¹⁶ Instead, it simply acknowledges the reality that the freedom of contract—the freedom of LLC parties to define their rights and obligations within the LLC—exists only within confines delineated by the legislature and judiciary. Stated differently, the freedom of contract is not an inexorable feature of LLCs, but a policy choice made by the legislature and the judiciary. It is a policy choice that favors *ex ante* certainty and predictability—through the judicial enforcement of express bargained-for rights and obligations—over *ex post* judicial policing.¹⁷ It is a policy

and governance instrument” that “defines the membership interests and rights that each member holds” in an LLC); Christopher M. Bruner, *The Fiduciary Enterprise of Corporate Law*, 74 WASH. & LEE L. REV. 791, 811 (2017) (“Simply put, the LLC’s degree of contractualism cannot be assessed in isolation from broader political, social, and institutional dynamics; the subject is inherently public.”); Grant M. Hayden & Matthew T. Bodie, *The Uncorporation and the Unraveling of “Nexus of Contracts” Theory*, 109 MICH. L. REV. 1127, 1143 (2011) (arguing that LLCs and other unincorporated entities cannot be described as a “purely contractual relationship” because “[t]he state looms large . . . and the relationships between the firm’s many constituents are largely framed and directed by the exercise of government power”).

¹⁶ Indeed, as I have written elsewhere, there is a strong policy argument in favor of freedom of contract and against equitable intervention by the courts:

[O]ne factor that must be weighed in every case is the central importance of certainty and determinacy in business relationships generally and LLCs in particular. To the extent the courts exercise their . . . equitable power to override the express terms of a particular LLC agreement, the courts undercut the ability of all parties to rely on such agreements. Such uncertainty complicates business planning and promotes costly litigation. It risks undermining parties’ bargained-for risk allocation and the contractual and extra-contractual mechanisms upon which that allocation was based. Put differently, even putting aside Delaware’s statutory mandate, the freedom of contract and the enforceability of bargained-for agreements are intrinsically important values that must be considered in any equitable analysis.

Mohsen Manesh, *Equity in LLC Law?*, 44 FLA. ST. U. L. REV. 93, 131-32 (2016).

¹⁷ See *In re El Paso Pipeline Partners, L.P. Derivative Litig.*, 132 A.3d 67, 101 (Del. Ch. 2015) (Laster, V.C.) (“A contractual alternative entity . . . has many advantages. In theory, obligations and rights can be defined more explicitly and better addressed *ex ante*, rather than leaving issues for *ex post* judicial evaluation.”), *rev’d on other grounds*, *El Paso Pipeline GP Co., v. Brinckerhoff*, 152 A.3d 1248 (Del. 2016); *Gerber v. Enter. Prods. Holdings, LLC*, C.A. No. 5989-VCN, 2012 WL 34442, at *11 (Del. Ch. Jan. 6, 2012) (Noble, V.C.) (“Alternate entity legislation reflects the Legislature’s decision to allow such ventures to be governed without the traditional fiduciary duties, if that is what the partnership agreement or other governing document provides for, and allows conduct that, in a different context, would be sanctioned.”); *R & R Capital, LLC v. Buck & Doe Run Valley Farms, LLC*, C.A. No. 3803-CC, 2008 WL 3846318, at *8 (Del. Ch. Aug. 19, 2008) (Chandler, C.) (“The allure of the [LLC], however, would be eviscerated if the parties could simply petition this court to renegotiate their agreements when relationships sour.”); see also Manesh, *supra* note 8, at 225-34 (illustrating

choice that favors permitting LLC parties the freedom to strike tailored bargains to meet their idiosyncratic needs over the value of applying unwaivable, mandatory rules to all LLCs.¹⁸

Conceding these points would not only bring clarity to the law, it would also highlight the real reasons for contractual primacy in LLCs. It would alert LLC parties as well as jurists and legislators to the active and pervasive role the latter two play in defining the rights and obligations of the participants within the entity. And it would illuminate the potential limits to the freedom of contract in LLCs—where the policy of unrestrained contracting must be balanced against and, in some cases, succumb to other competing policies.

Therefore, the singular aim of this Article, written to mark the 25th anniversary of the Delaware LLC Act (hereinafter the “LLC statute”), is to puncture the persistent fantasy that LLCs are “creatures of contract.” More accurately, this Article shows that LLCs embody a complex interaction of contract terms, statutory rules, and judicial doctrine. Consequently, LLCs are creatures of contract *and* creatures of statute *and* creatures of equity. This is true under Delaware law—the focus of this Article—but to the extent other jurisdictions’ law follow Delaware’s lead, it is true elsewhere, too.

The remainder of this Article proceeds in four parts. Part II explores the usage of the “creatures of contract” maxim in case law. As this part shows, the courts use the maxim to make two descriptive claims: first, that LLCs are essentially contractual entities and, second, that the LLC agreement enjoys primacy over statutory or judge-made rules in defining the rights and obligations of the participants within the entity. Parts III and IV then show how the LLC statute and the equitable power of the courts complicate this simplistic conception of LLCs. Specifically, Part III demonstrates that the LLC statute includes provisions that make the legal relationship of LLC parties incongruent with the relationship of ordinary, common law contract parties. Moreover, Part III shows that the LLC statute includes certain mandatory provisions that effectively limit

how LLCs may exercise the freedom of contract to avoid the uncertainty of *ex post* judicial scrutiny under indeterminate legal standards).

¹⁸ See *Haley v. Talcott*, 864 A.2d 86, 88 (Del. Ch. 2004) (Strine, V.C.) (“A principal attraction of the LLC form of entity is the statutory freedom granted to members to shape, by contract, their own approach to common business ‘relationship’ problems.”); cf. *Dieckman v. Regency GP LP*, C.A. No. 11130–CB, 2016 WL 1223348, at *11 (Del. Ch. Mar. 29, 2016) (Bouchard, C.) (observing that the freedom of contract under alternative entity law “affords commercial parties the advantage of great flexibility to privately order their affairs, but that flexibility can come at a cost[;] investors must be careful to read those agreements and to understand the limitations on their rights they impose”) (internal quotation marks omitted), *rev’d on other grounds*, 155 A.3d 358 (Del. 2017).

the freedom of contract within LLCs. Part IV then demonstrates that the same points are true as a consequence of the equitable power of the courts. Thus, together, Parts III and IV, by demonstrating the indelible marks of the legislature and judiciary on LLCs, debunk the “creatures of contract” myth. Finally, Part V concludes briefly.

II. CREATURES OF CONTRACT

Before considering the inextricable role of the LLC statute and equity in LLCs, this Part first considers the “creature of contract” cliché itself.¹⁹ Part II.A traces the origins and usage of the now common judicial refrain in Delaware case law. Part II.B then explores its meaning. As this discussion shows, courts use the “creatures of contract” refrain to make two related points: first, the relationship among LLC parties is contractual in nature and, second, that the parties’ contract—the LLC agreement—supersedes otherwise applicable statutory rules or equitable principles in determining the parties’ rights and duties.

A. The Judicial Refrain

Given its present-day ubiquity, it is somewhat surprising that the description of LLCs as “creatures of contract” was not commonplace in Delaware case law until 2008,²⁰ some 16 years *after* the state first enacted its LLC statute. Before 2008, the only reference to LLCs as a “creature of contract” in Delaware case law came in a 1994 decision from the state’s Superior Court—and not the more famous Court of Chancery—by then-Judge Steele, addressing whether a Delaware LLC requires Delaware counsel to represent it in a court proceeding.²¹ The expression was not used again in a Delaware judicial opinion for fourteen years.

The real genesis of the expression’s present-day ubiquity in case law is a short 2008 decision by Chancellor Chandler, *TravelCenters of*

¹⁹ See Francis Pileggi, *Chancery Explains that Special Litigation Committee Must Only Include Board Members*, DEL. CORP. & COMM. LITIG. BLOG (June 17, 2016) archived at, <https://perma.cc/XDZ2-777F> (“[M]ost readers will be familiar with the cliché that LLCs are creatures of contract . . .”).

²⁰ See *infra* Appendix.

²¹ *Poore v. Fox Hollow Enters.*, No. C.A. 93A-09-005, 1994 WL 150872, at *2 (Del. Super. Ct. Mar. 29, 1994). Importantly, as described below, then Judge Steele, who would later be appointed as the Chief Justice of the Delaware Supreme Court, championed a purely contractarian view of LLCs. See *infra* note 177 and accompanying text.

America, LLC v. Brog.²² In that decision, addressing the admissibility of certain expert witness testimony, the Chancellor asserted that “limited liability companies are creatures of contract, designed to afford the maximum amount of freedom of contract, private ordering and flexibility to the parties involved.”²³ After *TravelCenters*, Chancellor Chandler began using the expression repeatedly in his opinions,²⁴ such that by the end of 2008—just eight months after his first use—he could conclude confidently that “it is *well settled* that Limited Liability Companies are primarily creatures of contract.”²⁵

Following Chancellor Chandler’s lead, soon other members of the chancery court bench adopted the expression, too.²⁶ By 2010, the chancery court began simply citing to its earlier opinions,²⁷ essentially assuming the “creature of contract” principle to be unassailably true. In all, the Delaware Court of Chancery has used the expression, in some form, in at least thirty written opinions from 2008 through 2017.²⁸ As summed by a recent chancery court decision, “LLCs, as this Court has repeatedly pointed out, are creatures of contract.”²⁹

Unlike the Delaware Court of Chancery, the Delaware Supreme Court did not embrace the “creature of contract” maxim until quite recently. In 2016, the high court adopted the expression for the first time in *El Paso Pipeline GP Co. v. Brinckerhoff*.³⁰ In *El Paso*, an opinion authored by Chief Justice Strine, the high court used the “creatures of

²² C.A. No. 3516-CC, 2008 WL 1746987 (Del. Ch. Apr. 3, 2008) (Chandler, C.).

²³ *Id.* at *1 (internal quotation marks omitted).

²⁴ See *infra* Appendix (identifying examples where Chancellor Chandler began using the expression “creatures of contract” in his opinions).

²⁵ *TravelCenters of Am., LLC v. Brog*, C.A. No. 3751-CC, 2008 WL 5272861, at *2 (Del. Ch. Dec. 5, 2008) (Chandler, C.) (emphasis added).

²⁶ See *infra* Appendix.

²⁷ See, e.g., *Related Westpac LLC v. JER Snowmass LLC*, C.A. No. 5001-VCS, 2010 WL 2929708, at *6 n.30 (Del. Ch. July 23, 2010) (Strine, V.C.); see also *Ross Holding & Mgmt. Co. v. Advance Realty Grp., LLC*, C.A. No. 4113-VCN, 2010 WL 3448227, at *5 n.20 (Del. Ch. Sept. 2, 2010) (Noble, V.C.).

²⁸ See *infra* Appendix (identifying instances where Delaware courts have, in a written opinion, described LLCs (or, more generically, “alternative entities”) as a “creature of contract”).

²⁹ *Henson v. Sousa*, C.A. No. 8057-VCG, 2015 WL 4640415, at *1 (Del. Ch. Aug. 4, 2015) (Glasscock, V.C.).

³⁰ 152 A.3d 1248, 1260 (Del. 2016). Prior to *El Paso*, the Delaware Supreme Court had used the expression “creature of contract” in reference to other legal concepts (such as arbitration and the implied contractual covenant of good faith and fair dealing), but never in reference to LLCs or LPs. See, e.g., *Wood v. Baum*, 953 A.2d 136 (Del. 2008); *Nemec v. Shrader*, 991 A.2d 1120 (Del. 2010).

contract” maxim to describe “alternative entities.”³¹ Although the case involved a limited partnership (“LP”), the term “alternative entity” is widely understood to refer to both LPs and LLCs.³²

But even before *El Paso*, the Delaware Supreme Court had made clear its firmly contract-based conception of LLCs. In the 1999 decision, *Elf Atochem North American, Inc. v. Jaffari*, the high court’s first case squarely addressing the then relatively new form of business entity,³³ the court repeatedly emphasized the principle of freedom of contract in an opinion authored by Chief Justice Veasey.³⁴ Analogizing the LLC to LPs, the court asserted that the “[LLC] agreement is the cornerstone of a [LLC], and effectively constitutes the *entire agreement* among the [members] with respect to the admission of [members] to, and the creation, operation and termination of, the [LLC]”³⁵ Later, in 2010, in *CML V, LLC v. Bax*, authored by Chief Justice Steele, the high court curtly described the LLC as a “contractual entity,”³⁶ in part, to distinguish LLCs from corporations, implying the latter, in contrast to the former, to be creatures of contract, statute, and equity.³⁷ Thus, like the chancery court, the supreme court has long viewed LLCs through a strictly contractual lens, even if the high court did not adopt the “creature of contract” verbiage until only recently.

³¹ *El Paso Pipeline GP Co.*, 152 A.3d at 1259-60.

³² See, e.g., *Elf Atochem N. Am., Inc. v. Jaffari*, 727 A.2d 286, 289-90 (Del. 1999) (referring to LPs and LLC both as types of “alternative entities”); *Related Westpac, LLC v. JER Snowmass, LLC*, C.A. No. 5001-VCS, 2010 WL 2929708, at *8 (Del. Ch. July 23, 2010) (Strine, V.C.) (referring to LLCs as a type of “alternative entity”). The Delaware Supreme Court’s use of the “creature of contract” verbiage in *El Paso* may have particular influence on LP case law, because previously LPs had been described as a “creature of *both statute and contract*.” See *Twin Bridges Ltd. P’ship. v. Draper*, C.A. No. 2351-VCP, 2007 WL 2744609, at *8 (Del. Ch. Sept. 14, 2007) (Parsons, V.C.) (emphasis added); *accord Cantor Fitzgerald, L.P. v. Cantor*, C.A. No. 18101, 2001 WL 1456494, at *5 (Del. Ch. Nov. 5, 2001) (Steele, J.).

³³ *Elf Atochem N. Am. Inc.*, 727 A.2d at 287 (“This is a case of first impression before this Court involving the Delaware [LLC] Act.”).

³⁴ The expression “freedom of contract” or a variant thereof appears seven times in the main body of the *Elf Atochem* opinion and twice more in the footnotes. *Id.* at 290-91, 295-96, n.20.

³⁵ *Id.* at 291.

³⁶ 28 A.3d 1037, 1043 n.20 (Del. 2011) (“[L]imiting derivative standing to members and assignees in a contractual entity like an LLC is not absurd . . .”).

³⁷ *Id.* at 1044-47; see also Manesh, *supra* note 16, at 108-11 (analyzing the reasoning of *CML V*).

B. What Does it Mean?

Having insistently established the judicial belief that LLCs are “creatures of contract,” Delaware courts have been less precise about what exactly that means. At minimum, the expression must mean that the relationship among the participants in an LLC—the LLC entity and its members and managers—is a contractual relationship. As a contractual relationship, the rights and obligations of the LLC parties are defined by contract, namely the agreement governing the LLC.³⁸ The chancery court summed this point neatly in *Fisk Ventures, LLC v. Segal*, where it observed “[c]ontractual language defines the scope, structure, and personality of limited liability companies.”³⁹ Accordingly, the court reasoned “[i]n the context of limited liability companies, which are creatures not of the state but of contract, [the parties’] duties or obligations must be found in the LLC Agreement or some other contract.”⁴⁰

Indeed, because the LLC, as a “creature of contract,” creates an essentially contractual relationship, the LLC agreement is also made subject to the same rules of judicial interpretation and construction applied to all other contractual agreements.⁴¹ Thus, in *Kuroda v. SPJS Holdings, LLC*, the chancery court invoked the “creatures of contract” mantra to assert that the “LLC agreement defines when members of the LLC can be liable for breach of provisions of that agreement. Accordingly, as with any contract, the Court must look to the language of the LLC Agreement to determine the potential liabilities of the parties.”⁴²

³⁸ See *Olson v. Halvorsen*, 986 A.2d 1150, 1161 (Del. 2009) (“The LLC Act[] . . . indicates that an LLC agreement operates like any other . . . contract The LLC Act cannot—and has not—rendered LLC agreements impervious to all other rules and laws relating to contract law.”).

³⁹ *Fisk Ventures LLC v. Segal*, C.A. No. 3017-CC, 2008 WL 1961156, at *1 (Del. Ch. May 7, 2008) (Chandler, C.), *aff’d*, 984 A.2d 124 (Del. 2009) (“affirmed on the basis of and for the reasons assigned by the Court of Chancery”) (emphasis added).

⁴⁰ *Id.* at *8.

⁴¹ See, e.g., *Touch of It. Salumeria & Pasticceria, LLC v. Bascio*, C.A. No. 8602-VCG, 2014 WL 108895, at *4 (Del. Ch. Jan. 13, 2014) (Glasscock, V.C.) (“Pursuant to this Court’s well-established principles of contract interpretation, and recognizing that LLCs are creatures of contract, I must enforce LLC agreements as written.”); *Mickman v. Am. Int’l Processing, LLC*, C.A. No. 3869-VCP, 2009 WL 2244608, at *2 (Del. Ch. July 28, 2009) (Parsons, V.C.) (“LLC agreements are creatures of contract, which should be construed like other contracts. The construction of an LLC agreement, therefore, begins with the language of the agreement.”); see also *Norton v. K-Sea Transp. Partners L.P.*, 67 A.3d 354, 360 (Del. 2013) (explaining in the analogous LP context that because “[LP] agreements are a type of contract” many of the same interpretive principles of contract law apply in interpreting an LP agreement).

⁴² 971 A.2d 872, 880-81 (Del. Ch. 2009) (Chandler, C.); see also *Related Westpac LLC v. JER Snowmass LLC*, C.A. No. 5001-VCS, 2010 WL 2929708, at *6 (Del. Ch. July 23, 2010)

Beyond establishing the contractual nature of the LLC relationship, however, the expression “creature of contract” also seems to convey a correlative implication: namely, the primacy of the contract above other sources of law in defining LLC parties’ respective rights and duties. This primacy, of course, finds voice in the Delaware LLC statute’s express policy giving “maximum effect to the principle of freedom of contract and to the enforceability of [LLC] agreements.”⁴³ Respecting this policy, the chancery court has repeated on numerous occasions the language from *TravelCenters* that, as “creatures of contract,” LLCs “afford the maximum amount of freedom of contract, private ordering and flexibility to the parties involved.”⁴⁴

Delaware courts have understood the primacy of contract to mean that the provisions found in Delaware’s LLC statute are merely default rules, subject to any contrary terms set forth in an LLC agreement.⁴⁵ As the state supreme court explained in *Elf Atochem*, “[t]he basic approach of the Delaware [LLC] Act is to provide members with broad discretion in drafting the [LLC] Agreement and to furnish default provisions when the members’ agreement is silent.”⁴⁶ Thus, where the express terms of an LLC agreement conflict with the LLC statute, the LLC agreement supersedes the statute.⁴⁷ For example, in *R&R Capital, LLC v. Buck & Doe Run Valley Farms, LLC*, the chancery court ruled that where an LLC agreement expressly waives the members’ right to dissolve the LLC, that contractual provision supersedes the statutory right of LLC members the

(Strine, V.C.) (citing the “creature of contract” principle to assert that “[t]he obligations that [one LLC member] owed to [another LLC member] and the LLCs are defined by the terms of the LLCs’ Operating Agreements”).

⁴³ DEL. CODE ANN. tit. 6, § 18-1101(b) (2018).

⁴⁴ *TravelCenters of Am., LLC v. Brog*, C.A. No. 3516-CC, 2008 WL 1746987, at *1 (Del. Ch. Apr. 3, 2008) (Chandler, C.); *accord* *Tulum Mgmt. USA LLC v. Casten*, C.A. No. 11321-VCN, 2015 WL 7269811, at *5 (Del. Ch. Nov. 9, 2015) (Noble, V.C.) (quoting *TravelCenters*); *Fillip v. Centerstone Linen Servs., LLC*, C.A. No. 8712-ML, 2014 WL 793123, at *3 (Del. Ch. Feb. 27, 2014) (Glasscock, V.C.) (same); *CML V, LLC v. Bax*, 6 A.3d 238, 250 (Del. Ch. 2010) (Laster, V.C.) (same); *R&R Capital, LLC v. Buck & Doe Run Valley Farms, LLC*, C.A. No. 3803-CC, 2008 WL 3846318, at *4 (Del. Ch. Aug. 19, 2008) (Chandler, C.) (same).

⁴⁵ *See, e.g., R & R Capital*, 2008 WL 3846318, at *4 (observing that “Delaware’s LLC Act . . . generally provides defaults that can be modified by contract”).

⁴⁶ *Elf Atochem N. Am., Inc. v. Jaffari*, 727 A.2d 286, 291 (Del. 1999).

⁴⁷ *See, e.g., Huatuco v. Satellite Healthcare*, C.A. No. 8465-VCG, 2013 WL 6460898, at *5 (Del. Ch. Dec. 9, 2013) (Glasscock, V.C.) (holding that the express terms of an LLC agreement eliminate the statutory right to judicial dissolution and explaining that “enabling opting out of [a] statutory right altogether[] is consistent with the broad policy of freedom of contract underlying the LLC Act, and comports with the Act’s approach of supplying default provisions around which members may contract if they so choose”).

right to seek judicial dissolution.⁴⁸ Invoking the “creature of contract” maxim, the court reasoned the Delaware LLC statute “generally provides defaults that can be modified by contract” and that such contractual modification was permissible even where the specific statutory provision at issue did not contain a “magical phrase” making it explicit that the statutory provision was merely a default rule.⁴⁹

The primacy of the LLC agreement extends not just over the default provisions of the LLC statute, but also to judge-made equitable principles, most importantly that of fiduciary duty. Ordinarily, where one exercises discretion and control over the management of a business, courts impose on the individual a fiduciary duty.⁵⁰ That judge-made duty, which originates in equity, requires the individual to exercise her control in manner that serves the interests of the business and its owners, rather than her own self-interest.⁵¹ Applying this equitable principle to LLCs,

⁴⁸ *R & R Capital*, 2008 WL 3846318, at *4-5.

⁴⁹ *Id.*

⁵⁰ See Manesh, *supra* note 16, at 96-100.

⁵¹ As Chancellor Allen has explained,

[T]he principle of fiduciary duty, stated most generally, [is] that one who controls property of another may not, without implied or express agreement, intentionally use that property in a way that benefits the holder of the control to the detriment of the property or its beneficial owner. There are, of course, other aspects—a fiduciary may not waste property even if no self interest is involved and must exercise care even when his heart is pure—but the central aspect of the relationship is, undoubtedly, fidelity in the control of property for the benefit of another.

In re USACafes, L.P. Litig., 600 A.2d 43, 48 (Del. Ch. 1991). Elsewhere, Chancellor Allen has also explained the equitable origins of fiduciary duties:

The classic example—the accountability of trustees—demonstrates the reason why chancery takes jurisdiction over fiduciaries. The “fiduciary” duty of a trustee to deal with the trust *res* only for the benefit of the *cestui que trust* and not for his own benefit is a creation of equity. At law a trustee, as the legal owner, may deal with trust property as his own. The rights of a beneficiary are only recognized in equity. Accordingly, an action predicated upon such rights is properly maintained in a court of equity and only a court of equity. A similar rationale underlies Chancery’s traditional jurisdiction over corporate officers and directors. The duties they owe to shareholders with respect to the exercise of their legal power over corporate property supervene their legal rights.

McMahon v. New Castle Assocs., 532 A.2d 601, 604 (Del. Ch. 1987).

Delaware courts have ruled that managers and controlling members owe a fiduciary duty to the LLC and its members.⁵²

But again, the LLC statute makes explicit the primacy of contract over the equitable principle of fiduciary duty. Specifically, the LLC statute provides that:

To the extent that, at law or in equity, a member or manager or other person has duties (including fiduciary duties) to a [LLC] or to another member or manager or to another person . . . , the member's or manager's or other person's duties may be expanded or restricted or eliminated by provisions in [LLC] agreement.⁵³

Invoking the “creature of contract” principle to animate this statutory rule, the chancery court thus held in *Related Westpac LLC v. JER Snowmass LLC* that “[w]hen [LLC parties] cover a particular subject in an express manner, their contractual choice governs and cannot be supplanted by the application of inconsistent fiduciary duty principles that might otherwise apply”⁵⁴ Therefore, the court went on to explain, “[w]hen a fiduciary duty claim is plainly inconsistent with the contractual bargain struck by parties to an LLC . . . agreement, the fiduciary duty claim must fall, otherwise the *primacy of contract law over fiduciary law . . . would be undermined.*”⁵⁵ Cases like *Related Westpac* show that because LLCs are “creatures of contract,” the equitable principles of fiduciary duty, like other rights and duties set forth in the LLC statute, are relegated to mere default rules for LLCs. Where the express terms of an LLC agreement conflict with the LLC statute or principles of equity, the LLC agreement governs, displacing any statutory or equitable rights or duties.⁵⁶

⁵² See Manesh, *supra* note 16, at 100-02 (describing the judicial application of fiduciary duties to LLCs as a relatively new form of business entity).

⁵³ DEL. CODE ANN. tit. 6, § 18-1101(c) (2018).

⁵⁴ C.A. No. 5001-VCS, 2010 WL 2929708, at *8 (Del. Ch. July 23, 2010) (Strine, V.C.); see also *Auriga Capital Corp. v. Gatz Props., LLC*, 40 A.3d 839, 852 (Del. Ch. 2012) (Strine, C.) (“[T]he [LLC] statute allows the parties to an LLC agreement to entirely supplant . . . default [fiduciary] principles or to modify them in part. Where the parties have clearly supplanted default principles in [full or in part], we give effect to their contract choice.”); *In re Atlas Energy*, C.A. No. 4589-VCN, 2010 WL 4273122, at *12 (Del. Ch. Oct. 28, 2010) (Noble, V.C.) (ruling that where a LLC agreement “unambiguously eliminates the traditional fiduciary duties of the [LLC’s managers] . . . the only duties owed by the [managers] are those set forth elsewhere in the LLC Agreement”).

⁵⁵ *Related Westpac LLC*, 2010 WL 2929708, at *8 (emphasis added) (internal quotation marks omitted).

⁵⁶ See *supra* note 54.

So, in sum, when Delaware courts assert that LLCs are “creatures of contract,” the courts appear to be making two related claims about LLCs. First, the relationship of the LLC parties is contractual in nature, with the LLC agreement as the contract that defines the parties’ respective rights and duties.⁵⁷ Second, the contractual relationship enjoys primacy above all else, including the LLC statute and equitable precepts, in defining those rights and duties.⁵⁸

As the next two parts show, neither claim is completely true. Although the relationship between LLC parties may be primarily contractual in nature, both the Delaware LLC statute and the courts’ equitable powers alter that relationship in ways that defy the ordinary common law understanding of what a contract is.⁵⁹ Moreover, both the statute and equity place subtle limits on the freedom of contract, meaning the primacy of the LLC agreement is not absolute.⁶⁰ In short, as the next two parts show, to say that LLC are “creatures of contract” is a misleading half-truth because it elides the integral role of the legislature and the judiciary.

III. CREATURES OF STATUTE

The Delaware LLC Act, first adopted in 1992⁶¹ and annually amended since,⁶² plays a fundamental role in shaping the relationship of the participants within a LLC. As Part III.A explains, the LLC statute does so in numerous respects that depart from ordinary contract law precepts. Moreover, as described in Part III.B, the statute also imposes certain mandatory rules on LLCs, effectively limiting the contractual freedom of LLC parties. To ignore these facts—to insist that LLCs are merely “creatures of contract”—is to ignore the reality that LLCs are also creatures of statute.⁶³

⁵⁷ See *supra* note 38-42 and accompanying text.

⁵⁸ See *supra* note 43-56 and accompanying text.

⁵⁹ See *infra* Parts III.A and IV.A.

⁶⁰ See *infra* Parts III.B and IV.B.

⁶¹ 68 Del. Laws, c. 434 § 1 (1992).

⁶² Since its enactment in 1992, the Delaware LLC statute has been amended annually starting in 1994. See SYMONDS & O’TOOLE, *supra* note 15, at Appendix B.

⁶³ See CML V, LLC v. Bax, 28 A.3d 1037, 1045 (Del. 2010) (Steele, C.J.) (“[W]hen adjudicating the rights, remedies, and obligations associated with Delaware LLCs, courts must look to the LLC Act because it is only the statute that creates those rights, remedies, and obligations.”) (emphasis added); Myron T. Steele, *Judicial Scrutiny of Fiduciary Duties in Delaware Limited Partnerships and Limited Liability Companies*, 32 DEL. J. CORP. L. 1, 5 (2007) (“[L]imited partnerships and limited liability companies, like corporations, are creatures

A. Statutory Departures from Contract Law

In numerous ways, the LLC statute causes LLCs to be incongruent with common law contract norms. Indeed, the statutory departures from contract law addressed below run the gamut, starting with how an LLC is created and ending with the remedies available for breach. Importantly, in highlighting these statutory rules, and their deviations from traditional contract law, the aim is not to suggest these deviations are good or bad policy. Instead, the aim is simply to demonstrate the indelible legislative imprint on LLCs.

1. Formation

Ordinarily, the creation of a contract is a private act—it does not require any particular action or assent on the part of the state. Rather, all that is required to form a contract is an agreement and exchange of consideration between two (or more) parties.⁶⁴ But an LLC cannot be created by a private act. Rather, to form an LLC, the LLC statute requires the filing of a prescribed document—a certification of formation—with the secretary of state⁶⁵ and the payment of a prescribed fee.⁶⁶ Thus, in a very fundamental sense, a LLC is not a “creature of contract” because it cannot be *created* by contract alone. It must be created through formal action, as dictated by statute, in coordination with the state, namely the filing of a certification of formation.⁶⁷

of statute . . .”); *cf.* Heminway, *supra* note 11, at 828 (concluding that a “[LLC] agreement is a statutory form of contract, rather than a common law contract—one with its own legal rules”). It is, of course, ironic that the Delaware Supreme Court would in its *CML V* decision concede the central importance of the statute to the LLC, because the holding of *CML V* itself is premised on the view that LLCs are a “contractual entity.” See *CML V*, 28 A.3d at 1043 n.20.

⁶⁴ See RESTATEMENT (SECOND) OF CONTRACTS § 17 (AM. LAW INST. 1981) (“[T]he formation of a contract requires a bargain in which there is a manifestation of mutual assent to the exchange and a consideration.”); *accord* Ramone v. Lang, C.A. No. 1592-N, 2006 WL 905347, at *10 (Del. Ch. Apr. 3, 2006) (Strine, V.C.) (citing Wood v. State, No. 307,2002, 2003 WL 168455, at *2 (Del. Jan. 23, 2003)).

⁶⁵ See DEL. CODE ANN. tit. 6, § 18-201(a), (b) (2018); Elf Atochem N. Am., Inc. v. Jaffari, 727 A.2d 286, 288 (Del. 1999) (“The certificate of formation is a relatively brief and formal document that is the first statutory step in creating the LLC as a separate legal entity.”).

⁶⁶ See DEL. CODE ANN. tit. 6, § 18-1105(a)(3) (2018) (requiring the payment of a \$70 fee upon the filing of a LLC certificate of formation); DEL. CODE ANN. tit. 6, § 18-1105(a) (2018) (“No document required to be filed under this chapter shall be effective until the applicable fee required by this section is paid.”) (emphasis added).

⁶⁷ See SYMONDS & O’TOOLE, *supra* note 15, § 4.05 (“[T]he [LLC] cannot exist prior to the filing of the certificate of formation.”).

To be sure, even before a certification of formation is filed, LLC parties may assent to a contract dictating the rules of internal governance for the LLC,⁶⁸ and in this respect, one might insist on the “creature of contract” maxim. But again, the LLC statute complicates this view. Under that LLC statute, any contract made before the LLC is created is not, strictly speaking, an “LLC agreement.”⁶⁹ By statute, an “LLC agreement” is an “agreement . . . of the member or members as to the affairs of a [LLC] and the conduct of its business.”⁷⁰ Yet, because no LLC exists until a certificate of formation has been filed, there can be no LLC “member or members” to speak of, and therefore the contract fails the statutory definition of an LLC agreement.⁷¹ Stated differently, the statutory definition of an LLC agreement requires the preexistence of a duly formed LLC.

Just as the parties cannot create an LLC by contract alone, neither can the parties’ contract ensure the entity continues to exist for whatever term bargained for by the parties. Instead, to avoid premature termination of the LLC, the parties must ensure that the LLC pays an annual tax to the state.⁷² Otherwise, the LLC’s existence risks being terminated administratively.⁷³

Even after the LLC is formed, however, and even assuming the entity remains in good standing, the nature of the LLC agreement defies common law contract principles. Ordinarily, a contract requires an agreement among at least two parties. There cannot be a legally enforceable contract with just one party.⁷⁴ After all, an “agreement” requires at least two parties to *agree*. And for an agreement to qualify as

⁶⁸ See DEL. CODE ANN. tit. 6, § 18-201(d) (2018) (providing that an LLC agreement may be entered into before the filing of a certificate of formation).

⁶⁹ See SYMONDS & O’TOOLE, *supra* note 15, § 4.05 (“Under the [Delaware LLC] Act, the admission of a person as a member . . . cannot precede the formation of the company . . .”).

⁷⁰ DEL. CODE ANN. tit. 6, § 18-101(7) (2018).

⁷¹ See SYMONDS & O’TOOLE, *supra* note 15, § 4.05 (articulating this interpretation of the LLC statute without endorsing it).

⁷² See DEL. CODE ANN. tit. 6, § 18-1107(b) (2018) (imposing an annual tax of \$300 as of 2017).

⁷³ See *id.* § 18-1108(a) (“The certificate of formation of a domestic [LLC] shall be canceled if the [LLC] shall fail to pay the annual tax due under § 18-1107 of this title for a period of 3 years . . .”).

⁷⁴ See RESTATEMENT (SECOND) OF CONTRACTS § 9 (AM. LAW INST. 1981) (“There must be at least two parties to a contract, a promisor and a promisee, but there may be any greater number.”).

a contract, the agreement must also involve an exchange of consideration between the parties.⁷⁵

But the LLC statute expressly contemplates the possibility of an enforceable agreement involving just one party. Specifically, to accommodate single-member LLCs, the LLC statute provides a “[LLC] agreement of a [LLC] having only 1 member shall not be unenforceable by reason of there being only 1 person who is a party to the [LLC] agreement.”⁷⁶ Thus, the LLC statute explicitly authorizes a scenario that would be “an absurdity” in the ordinary contract setting: an enforceable agreement made by only one party.⁷⁷

A defender of the “creature of contract” notion might note that even in a single-member LLC, there are in fact two parties to the LLC agreement: the LLC member and the LLC entity. While perhaps true, that fact does not resolve the lack of consideration involved in single-member LLCs, where the sole member’s obligations under the LLC agreement, if any, are effectively only enforceable by that member at her sole discretion and, therefore, illusory.⁷⁸

But even setting aside the lack-of-consideration problem in single-member LLCs, the notion that the LLC, as an entity, is a party to the LLC agreement raises its own statutory peculiarities. As the next part notes, under the LLC statute, the fact that an LLC is a party to, and therefore, bound by the LLC agreement is based not upon common law contract principles of assent, but upon statutory dictate.

⁷⁵ See *id.* § 17 (“[T]he formation of a contract requires a bargain in which there is a manifestation of mutual assent to the exchange and a consideration.”).

⁷⁶ DEL. CODE ANN. tit. 6, § 18-101(7) (2018).

⁷⁷ See *In re Denman*, 513 B.R. 720, 724-25 (Bankr. W.D. Tenn. 2014) (observing that “[a]pplying contract logic, the single member LLC seemingly becomes an absurdity” because “[a] single member LLC . . . can satisfy neither the mutual assent element nor the exchange of consideration element of contract law”); accord SYMONDS & O’TOOLE, *supra* note 15, § 4.09[B] (“[A] [LLC] agreement to which there is only one party is to be treated as a ‘contract’ even though outside this unique statutory context it might not be viewed as a contract at all. This rule of enforceability departs from the general contract law principle requiring mutuality of obligation.”). Reflecting the basic premise that an agreement requires more than just one party, in 1992, Delaware’s original LLC statute defined an LLC agreement to be an agreement among two or more members. 68 Del. Laws, c. 434 § 1 (1992) (“‘Limited liability company agreement’” means a written agreement of the *members* . . .”) (emphasis added).

⁷⁸ See 17A AM. JUR. 2D *Contracts* § 125 (“Illusory promises cannot serve as consideration for a contract An ‘illusory promise’ is one which . . . by its terms makes performance optional or entirely discretionary on the part of the promisor. In other words, a promise is illusory when it fails to bind the promisor, who retains the option of discontinuing performance.”); see also SYMONDS & O’TOOLE, *supra* note 15, § 4.09[B] (observing that the LLC’s statutory rule enabling the legal enforceability of an LLC agreement with only a single member “departs from the general contract law principle requiring mutuality of obligation”).

2. Privity and Binding (Non)Parties

Under ordinary common law contract principles, only the parties to a contract owe legal duties arising under the contract.⁷⁹ And one only becomes a party to a contract if she objectively manifests her assent to the contract's terms.⁸⁰ Absent such assent, one is not bound to the contract. Lacking privity of contract, a nonparty has no rights against and owes no obligations to the contract parties.⁸¹

Here again, the LLC statute departs from the basic contract law norms. Under the statute, a LLC, as an entity, "is bound by its [LLC] agreement whether or not the [LLC] executes the [LLC] agreement."⁸²

⁷⁹ See, e.g., *EEOC v. Waffle House, Inc.*, 534 U.S. 279, 294 (2002) ("It goes without saying that a contract cannot bind a nonparty."); *Gotham Partners, L.P. v. Hallwood Realty Partners, L.P.*, 817 A.2d 160, 172 (Del. 2002) ("It is a general principle of contract law that only a party to a contract may be sued for breach of that contract." (quoting *Wallace v. Wood*, 752 A.2d 1175, 1180 (Del. Ch. 1999) (Steele, V.C.)) (internal quotation marks omitted); *Am. Legacy Found. v. Lorillard Tobacco Co.*, 831 A.2d 335, 343 (Del. Ch. 2003) (Lamb, V.C.) ("[A] fundamental principal of contract law provides that only parties to a contract are bound by that contract."); 17A AM. JUR. 2d *Contracts* § 400 ("Ordinarily, only parties to contracts are bound by their provisions or liable for their breach."). Admittedly, there are exceptions to this general rule, but those exceptions are not relevant for the purposes of the present discussion. See, e.g., RESTATEMENT (SECOND) OF CONTRACTS § 302 (AM. LAW INST. 1981) (describing the rights of a nonparty that is an intended third-party beneficiary of the contract parties); RESTATEMENT (SECOND) OF TORTS § 766 (AM. LAW INST. 1979) (describing the liability of a nonparty that tortiously interferes with the relationship of the contract parties).

⁸⁰ See RESTATEMENT (SECOND) OF CONTRACTS § 17 (AM. LAW INST. 1981) (identifying the requirement of assent). To be sure, "[o]ne does not have to be a signatory to a contract . . . to become bound by it." *Am. Legacy Found.*, 831 A.2d at 343-44. But for an individual to become a party to an agreement, and therefore bound to the agreement, that individual must "either expressly or implicitly adopt[] the agreement." *Id.* at 344; see also 17A AM. JUR. 2d *Contracts* § 400 ("Parties to a contract cannot impose any liability on one who . . . is a stranger to the contract, and in order to bind a third person contractually, an expression of assent by such person is necessary A person is not made a party to a contract merely by being named and described in it."). Applying this basic contract law principle to LLC agreements would mean that, in the absence of the LLC statute, "the [LLC] agreement can have the effect of binding a person who has not signed a writing agreeing to be bound thereby, . . . [only] if that person otherwise has manifested an intent to be so bound." SYMONDS & O'TOOLE, *supra* note 15, § 4.04[A] (emphasis added).

⁸¹ See, e.g., 17A AM. JUR. 2d *Contracts* § 400 ("A contract cannot bind a nonparty Parties to a contract cannot impose any liability on one who, under its terms, is a stranger to the contract, and in order to bind a third person contractually, an expression of assent by such person is necessary."); *id.* § 404 ("In general, only the parties to a contract or those in privity with the parties have rights under the contract A nonparty to a contract has no remedy for breach of the contract"); *id.* § 405 ("The doctrine of privity of contract requires that only parties to a contract may bring suit to enforce it.").

⁸² DEL. CODE ANN. tit. 6, § 18-101(7) (2018); see *Seaport Vill. Ltd. v. Seaport Vill. Operating Co.*, C.A. No. 8841-VCL, 2014 WL 4782817, at *1 (Del. Ch. Sept. 24, 2014) (Laster,

This statutory provision, adopted by the state legislature in 2002,⁸³ essentially codifies one of the Delaware Supreme Court’s rulings in *Elf Atochem v. Jaffari*, where the court held that an LLC was bound to the terms of its LLC agreement, which was made a month after the LLC was formed, despite the fact that an authorized agent of the LLC never signed that agreement to bind the LLC as a party thereto.⁸⁴ The court concluded that it was immaterial that the LLC, as an entity, never assented to the agreement, reasoning that “[i]t is the members who are the real parties in interest. The LLC is simply their joint business vehicle.”⁸⁵ Left unanswered by the high court, and now by the statute, is how this rule—contractually binding the LLC despite the lack of assent by the LLC—comports with the dignity of the LLC as a “separate legal entity.”⁸⁶ Indeed, commentators have described it as a “counterintuitive statutory rule”⁸⁷ and one that “departs from general common law rules pertaining to contracts.”⁸⁸ Elaborating on these points, one scholar has noted that “[f]or students of contract law, the conclusion that a non-party is bound by a contract does not seem to be an obvious result.”⁸⁹

Of course, it is not just the LLC, as an entity, that is statutorily bound to the LLC agreement, despite the lack of assent to its terms. Members, managers, and assignees of a membership interest also suffer this indignity. In 2005,⁹⁰ the Delaware legislature further amended the LLC statute to provide that “[a] member or manager of a [LLC] or an assignee of a [LLC] interest is bound by the [LLC] agreement whether or not the member or manager or assignee executes the [LLC] agreement.”⁹¹ Thus,

V.C.) (“By statute, a [LLC] is a party to its own [LLC] agreement, regardless of whether the [LLC] executes its own [LLC] agreement.”) (emphasis added).

⁸³ See 73 Del. Laws, c. 289 §2 (2002).

⁸⁴ *Elf Atochem N. Am., Inc. v. Jaffari*, 727 A.2d 286, 293 (Del. 1999).

⁸⁵ *Id.*

⁸⁶ DEL. CODE ANN. tit. 6, § 18-201(b) (2018) (“A [LLC] formed under this chapter shall be a separate legal entity . . .”).

⁸⁷ Francis Pileggi, *Chancery Non-Signatory LLC Members Bound By Operating Agreement*, DEL. CORP. & COMM. LITIG. BLOG (Sept. 25, 2014), at <https://tinyurl.com/y7rezxf6>.

⁸⁸ SYMONDS & O’TOOLE, *supra* note 15, § 4.09[A]. However, as the authors go on to recognize, consistent with the thesis of this Article, a “[LLC] agreement is . . . no ordinary contract . . ., as it is specifically governed by the [Delaware LLC] Act and serves as the governing instrument of the [LLC].” *Id.*

⁸⁹ Joan Heminway, *More on LLCs as Non-Signatories of Operating Agreements . . .*, BUS. L. PROF BLOG (Sept. 29, 2014), at <https://tinyurl.com/yaekhkoe>. As Professor Heminway has noted elsewhere, other jurisdictions have not followed Delaware law on this issue. See Heminway, *supra* note 11, at 818-19.

⁹⁰ 73 Del. Laws, c. 295 §1 (2005).

⁹¹ DEL. CODE ANN. tit. 6, § 18-101(7) (2018).

by statute, the same rule that applies to the LLC entity also applies to LLC managers, members, and assignees of a membership interest in the LLC. In this respect, the statute eliminates a core element of the common law of contracts—the requirement of assent—from LLC agreements.⁹²

For managers, this statutory rule is particularly problematic. Unlike the LLC entity, which arguably “is simply. . . a joint business vehicle” of the LLC members,⁹³ the manager may have no ownership interest in the LLC. Yet, by being merely named as “manager” in the member’s LLC agreement, the individual so designated becomes bound by statute to the LLC agreement, without any requirement of that individual’s assent or even knowledge of the agreement’s existence or terms therein.⁹⁴ Indeed, this statutory rule is so counterintuitive given traditional contract law norms that in practice LLC parties frequently have the individual designated as manager explicitly agree to the terms of the LLC agreement, even though such assent is strictly unnecessary by statute.⁹⁵

In the absence of express assent, the best explanation a leading treatise can offer to justify the statutory rule binding the manager to the LLC agreement is that the manager’s assent to its terms is implicit in the manager’s acceptance of her appointment as manager.⁹⁶ Yet even this explanation proves unsatisfying. For one, the LLC statute does not require an individual to “accept” her appointment as manager to be bound by the LLC agreement.⁹⁷ All that is statutorily required is that the individual is named as “manager” by the LLC agreement.⁹⁸ Moreover, even when an individual formally accepts her appointment as manager, she may not be

⁹² See *In re Denman*, 513 B.R. 720, 725 (Bankr. W.D. Tenn. 2014) (reasoning that an LLC agreement, to which parties may become statutorily bound, is not a contract because, “under contract law, parties cannot be deemed to be parties to a contract without their assent”).

⁹³ *Elf Atochem N. Am., Inc. v. Jaffari*, 727 A.2d 286, 293 (Del. 1999).

⁹⁴ Under DEL. CODE ANN. tit. 6, § 18-101(10) (2018), a person becomes manager of a LLC if the person “is named as a manager” in or “designated as a manager” pursuant to the LLC agreement. And under DEL. CODE ANN. tit. 6, § 18-101(7) (2018), the person so named or designated as manager “is bound by the [LLC] agreement whether or not the . . . manager . . . executes the . . . agreement.” Thus, there is no requirement that the person named or designated as manager assent or even know of the LLC agreement’s existence or terms.

⁹⁵ See SYMONDS & O’TOOLE, *supra* note 15, § 4.03[B][2] (“Not infrequently, . . . even though by operation of law a manager is bound by the [LLC] agreement, the [manager] may be asked to agree explicitly in writing to the terms of the [LLC] agreement.”).

⁹⁶ See *id.* (“[T]he assent to appointment as [manager], by the person named or designated as a manager of a [LLC], is an implicit condition to that person’s becoming a manager.”).

⁹⁷ See DEL. CODE ANN. tit. 6, § 18-101(7) (2018).

⁹⁸ Under DEL. CODE ANN. tit. 6, § 18-101(10) (2018), all that is required to gain manager status is that the person “is named as a manager” in or “designated as a manager” pursuant to the LLC agreement.

aware of the terms or even existence of the LLC agreement to which she is now statutorily bound, straining any notion of assent.

As noted above, like managers, LLC members and assignees of a membership interest are statutorily bound to an LLC agreement without actually executing the agreement or otherwise assenting to its terms.⁹⁹ Thus, the same issues described above for managers potentially present themselves for members and assignees, too.

But it gets worse for managers and assignees. Under traditional contract law principles, to modify the terms of an existing contract requires the mutual assent of the parties bound by that contract.¹⁰⁰ Under the default rules of the LLC statute, however, only members (and not non-members, like managers and assignees of a membership interest) are entitled to vote on any amendments to an LLC agreement.¹⁰¹ Thus, the contract terms that managers and assignees are statutorily bound to may be changed at any time by the members of an LLC, again without the assent of the managers and assignees, who will also be bound to those changed terms.¹⁰²

Of course, there is a reasonable explanation for all of these statutory rules binding nonparties to an LLC agreement, even in the absence of their express assent to its terms: such rules are necessary to promote order and

⁹⁹ See *id.* § 18-101(7).

¹⁰⁰ SYMONDS & O'TOOLE, *supra* note 15, § 4.06[A][3][b] (“Under Delaware law, in the absence of a contract term governing amendments, the consent of all parties generally is required to amend a contract.”).

¹⁰¹ See DEL. CODE ANN. tit. 6, § 18-302(f) (2018) (“If a [LLC] agreement does not provide for the manner in which it may be amended, the [LLC] agreement may be amended with the approval of all of the members.”). However, Section 18-302(f) of the Delaware statute applies only to Delaware LLCs formed on or after January 1, 2012. For LLCs formed before that date, the Delaware LLC statute is silent as to the nature of consent required to amend an existing LLC agreement, and the leading treatise suggests that ordinary contract principles would apply, requiring the consent of all parties, including any non-member parties, such as managers and assignees. See SYMONDS & O'TOOLE, *supra* note 15, § 4.06[A][3][b].

¹⁰² As the leading Delaware LLC treatise has explained:

Section 18-302(f) [of the Delaware LLC statute] makes clear that non-members who are parties to a [LLC] agreement (including managers, assignees and others who are parties) have no right to vote on amendments to that agreement unless such right is provided in the agreement. This default rule arguably represents a departure from the otherwise applicable standard [under contract law], and undoubtedly creates significant risk for these non-members.

SYMONDS & O'TOOLE, *supra* note 15, § 4.06 [A][3][a].

accountability in the governance of LLCs.¹⁰³ And that may be sound policy. But that policy is operationalized with statutory rules that deviate LLCs from traditional contract law principles. The same holds true for the LLC statute's treatment of the statute of frauds, as described below.

3. Statute of Frauds

Ordinary contracts may be made in writing, orally, or even implicitly through conduct.¹⁰⁴ Regardless of how an agreement is reached, so long as there is objective manifestation of assent by the parties and an exchange of consideration, their agreement is contractually enforceable.¹⁰⁵ Strangely, however, until 1995, Delaware's LLC statute departed from this basic principle of contract law. Instead, the original LLC statute required an LLC agreement to be in writing, thus mandating a singular method for parties to manifest their assent.¹⁰⁶ It was only after amendments to the LLC statute in 1995¹⁰⁷ and 2007¹⁰⁸ that conformed LLCs to the rest of contract law by enabling parties to form an LLC agreement in writing, orally, or implicitly through conduct.¹⁰⁹

Yet, contract law has long had another rule dealing with certain types of agreements made orally or implicitly, in the absence of a writing. In particular, in the ordinary contract setting, an agreement that is incapable of full performance within one year of its making is subject to the statute of frauds.¹¹⁰ The statute of frauds generally provides that such

¹⁰³ *Cf. id.* § 4.03[B][2] (explaining that “sound policy reasons (such as promotion of order and accountability) support[] the proposition that a manager of a [LLC] must be bound . . . by the entity’s governing instrument”).

¹⁰⁴ *See* RESTATEMENT (SECOND) OF CONTRACTS § 4 (AM. LAW INST. 1981) (“A promise may be stated in words either oral or written, or may be inferred wholly or partly from conduct.”); *id.* § 19(1) (“The manifestation of assent may be made wholly or partly by written or spoken words or by other acts or by failure to act.”).

¹⁰⁵ *See id.* § 17.

¹⁰⁶ *See* DEL. CODE ANN. tit. 6, § 18-101(7) (as in effect prior to Aug. 1, 1995) (“‘Limited liability company agreement’ means a *written* agreement of the members”) (emphasis added).

¹⁰⁷ 70 Del. Laws, c. 75, § 3 (1995) (authorizing an LLC agreement to be “written or oral”).

¹⁰⁸ 76 Del. Laws, c. 105, § 1 (2007) (authorizing an LLC agreement to be written, oral, or implied).

¹⁰⁹ *See* DEL. CODE ANN. tit. 6, § 18-101(7) (2018) (defining an LLC agreement to mean “any agreement . . . *written, oral or implied*, of the member or members”) (emphasis added); *Olson v. Halvorsen*, 986 A.2d 1150, 1161 (Del. 2009) (“[T]he LLC Act, like many other contracts, treats LLC agreements by permitting oral, written, or implied agreements.”).

¹¹⁰ *See* DEL. CODE ANN. tit. 6, § 2714(a) (2018); *see also* RESTATEMENT (SECOND) OF CONTRACTS § 130 (AM. LAW INST. 1981); *Olson*, 986 A.2d at 1159 (“Only if the parties cannot

an agreement is unenforceable unless the agreement is evidenced by an adequate writing signed by the party against whom its enforcement is sought.¹¹¹ Originally aimed to prevent the enforcement of alleged agreements that may have been the product of fraud or perjured testimony, the statute of frauds has a rich history in contract law.¹¹²

But here again, the LLC statute departs from ordinary contract law. In 2010, the Delaware General Assembly amended the LLC statute to provide that LLC agreements, unlike all other contracts, are not subject to the statute of frauds.¹¹³ The amendment effectively reversed the decision in *Olson v. Halvorson*, in which both the Delaware Court of Chancery¹¹⁴ and the Delaware Supreme Court¹¹⁵ held that LLC agreements are, in fact, subject to the statute of frauds.¹¹⁶ After all, the supreme court reasoned, an LLC agreement is a contract. “[A] LLC agreement operates like any other oral, written, or implied contract, i.e., it requires compliance with the statute of frauds.”¹¹⁷ In this respect, the *Olson* decision conformed LLCs to traditional contract law norms. But the LLC statute now diverges from the rest of contract law. Unlike ordinary contracts, LLC agreements are exempt from the statute of frauds.¹¹⁸

4. Separate Legal Existence and Limited Liability

Assuming the LLC is validly formed in compliance with the LLC statute, a new person is brought into being. That person, the LLC entity, is not a natural person of course, but a juridical person that may exist in perpetuity, separate and apart from its owners. Thus, the LLC statute enables LLC parties to do something that cannot be done by private agreement alone. By statute, the filing of a LLC’s certificate of formation creates a “separate legal entity” that has the power and capacity to enter

possibly perform the agreement within one year does the statute of frauds apply and require a writing, signed by the charged party.”).

¹¹¹ See DEL. CODE ANN. tit. 6, § 2714(a) (2018); RESTATEMENT (SECOND) OF CONTRACTS § 131 (AM. LAW INST. 1981).

¹¹² See 2 E. ALLAN FARNSWORTH, FARNSWORTH ON CONTRACTS § 6.1, at 93-99 (2d ed. 1998) (describing the history of the statute of frauds); see also *Olson*, 986 A.2d at 1159 (observing that the Delaware statutory of frauds was enacted by the state legislature over a century ago).

¹¹³ DEL. CODE ANN. tit. 6, § 18-101(7) (2018).

¹¹⁴ *Olson v. Halvorsen*, 982 A.2d 286, 291 (Del. Ch. 2008) (Lamb. V.C.).

¹¹⁵ *Olson*, 986 A.2d at 1159-61.

¹¹⁶ See DEL. CODE ANN. tit. 6, § 2714(a) (2018).

¹¹⁷ *Olson*, 986 A.2d at 1161.

¹¹⁸ DEL. CODE ANN. tit. 6, § 18-101(7) (2018) (“A [LLC] agreement is not subject to any statute of frauds . . .”).

into contracts, undertake obligations, hold title to assets, transact business, sue and be sued, all in its own name.¹¹⁹

The LLC's separate legal existence means, in part, that the members of an LLC are afforded limited liability.¹²⁰ By statutory decree, "the debts, obligations and liabilities of a [LLC], whether arising in contract, tort or otherwise, shall be solely the debts, obligations and liabilities of the [LLC], and no member or manager . . . shall be obligated personally for any such debt, obligation or liability of the [LLC]."¹²¹ Limited liability is a benefit that LLC parties simply could not contract for privately.¹²² Limited liability exists solely because the statute bestows it. Absent the LLC statute, the relationship among members and managers would likely be characterized as a general partnership¹²³ or an agency,¹²⁴ in either case creating the risk for the members of personal liability for the debts and obligation of the business.¹²⁵

Separate legal existence, potentially perpetual life, and limited liability—these are all "core attributes of the LLC."¹²⁶ Yet, even the chancery court has recognized, these attributes are distinctly non-contractual.¹²⁷ Contracting parties cannot create a separate legal person

¹¹⁹ *Id.* § 18-201(b) ("A [LLC] formed under this chapter shall be a separate legal entity.").

¹²⁰ *See, e.g.,* Feeley v. NHAOCG, LLC, 62 A.3d 649, 667 (Del. Ch. 2012) (Laster, V.C.) ("When making consensual commitments to third parties via contract, . . . LLCs are typically treated as separate legal entities such that only the . . . LLC is obligated to perform and liable for default The same principles apply when [LLCs] incur tort obligations through non-consensual transactions.").

¹²¹ DEL. CODE ANN. tit. 6, § 18-303(a) (2018).

¹²² *See In re Carlisle Etcetera LLC*, 114 A.3d 592, 605 (Del. Ch. 2015) (Laster, V.C.) (describing "separate legal existence, potentially perpetual life, and limited liability" as "core attributes of the LLC . . . that contracting parties cannot grant themselves by agreement" and that are made available only by the state); Hayden & Bodie, *supra* note 15, at 1137 ("The role of limited liability has long been a *bête noire* for contractarians, since it is clearly an aspect of the corporation that is not contractual.").

¹²³ *See* Rev. UNIF. PARTNERSHIP ACT § 202 (1997) [hereinafter RUPA] (describing how a general partnership is formed).

¹²⁴ *See* RESTATEMENT (THIRD) OF AGENCY §1.01 (AM. LAW INST. 2006) (describing how an agent-principal relationship is formed).

¹²⁵ *See* RUPA, *supra* note 123, § 306 (defining the personal liability of partners for the obligations of the partnership); RESTATEMENT (THIRD) OF AGENCY §§ 6.01, 6.02, 6.03, 7.03, 7.04 (AM. LAW INST. 2006) (defining the personal liability of a principal for the acts of her agent).

¹²⁶ *In re Carlisle Etcetera LLC*, 114 A.3d at 605-06.

¹²⁷ *Id.*

with perpetual life and a shield of limited liability by private agreement alone.¹²⁸ These features require the Delaware LLC statute.

5. Remedies for Breach

Under common law contract principles, the underlying aim of remedies for breach is compensatory.¹²⁹ Specifically, the goal is to protect the expectation interest of the non-breaching party “in having the benefit of [her] bargain” by awarding the non-breaching party compensation in the form of money damages in the amount necessary to “put [her] in as good a position as [s]he would have been had the contract been performed.”¹³⁰

Two corollary contract law doctrines stem from this general principle. First, the courts will not enforce contractual provisions that are aimed at punishing or penalizing the breaching party, rather than compensating the non-breaching party for the lost benefit of the bargain.¹³¹ This doctrinal ban against so-called penalty provisions is a distinctive feature of contract law.¹³² And it is consonant with the principle underlying contract law remedies, namely to compensate, rather than punish, in the event of a breach.¹³³

Second, the non-breaching party to a contract is not ordinarily entitled to specific performance or an injunction against the breaching party as a remedy for breach. Instead, the ordinary contract law remedy,

¹²⁸ See RESTATEMENT (SECOND) OF CONTRACTS, Introductory Note to Chapter 16 (AM. LAW INST. 1981) (“The traditional goal of the law of contract remedies has not been compulsion of the promisor to perform his promise but compensation of the promisee for the loss resulting from breach.”).

¹²⁹ *Id.*

¹³⁰ *Id.* §§ 344, 347; accord *Genencor Int’l, Inc. v. Novo Nordisk A/S*, 766 A.2d 8, 11 (Del. 2000) (“It is a basic principle of contract law that remedy for a breach should seek to give the non-breaching party the benefit of its bargain by putting that party in the position it would have been but for the breach.”).

¹³¹ See RESTATEMENT (SECOND) OF CONTRACTS § 355 (AM. LAW INST. 1981) (barring the recovery of punitive damages for breach of contract); *id.* § 356(1) (“A [contract] term fixing unreasonably large liquidated damages is unenforceable . . . as a penalty.”); see also *Del. Bay Surgical Servs., P.C. v. Swier*, 900 A.2d 646, 650 (Del. 2006) (“[A] ‘penalty’ is a sum inserted into a contract that serves as a punishment for default, rather than a measure of compensation for its breach [I]f a [contract] provision is considered a penalty, it is void as against public policy and recovery is limited to actual damages”).

¹³² In contrast to contract law, tort law—to take one example—allows punitive or exemplary damages under appropriate circumstances. See RESTATEMENT (SECOND) OF TORTS § 908(2) (AM. LAW INST. 1979).

¹³³ See RESTATEMENT (SECOND) OF CONTRACTS § 356 cmt. a (AM. LAW INST. 1981) (“The central objective behind the system of contract remedies is compensatory, not punitive.”).

as described above, is monetary damages.¹³⁴ Monetary damages are historically a legal remedy, as distinguished from the equitable remedies of specific performance or an injunction against breach.¹³⁵ Under ordinary contract law principles, equitable remedies are not available unless the legal remedy of monetary damages would be somehow inadequate to compensate for the non-breaching party's expectation interest.¹³⁶ And even then, any equitable remedy is granted only upon the discretion of the court.¹³⁷ A court is never compelled to grant equitable relief.

Both contract law doctrines, the ban against penalties and discretionary nature of equitable remedies, are bedrock features of contract law. Like the statute of frauds, both doctrines have a rich history¹³⁸—and both are cast aside by the LLC statute.¹³⁹

Instead, the LLC statute purports to authorize a LLC agreement to include enforceable penalty provisions as well as provisions that mandate specific performance or an injunction against breach.¹⁴⁰ Specifically, the statute provides that a LLC agreement “may provide that [a] member who fails to perform in accordance with, or to comply with the terms and conditions of, the [LLC] agreement shall be subject to specified penalties

¹³⁴ See, e.g., *Morabito v. Harris*, C.A. No. 1463-K, 2002 WL 550117, at *3 (Del. Ch. Mar. 26, 2002) (Chandler, C.) (“[T]oday a damages remedy is routinely available, but specific performance is considered extraordinary, awarded on a discretionary basis by courts of equity.”).

¹³⁵ See 3 FARNSWORTH, *supra* note 112, § 12.4, at 159-64 (describing the historical preference in contract law for the legal remedy of money damages over equitable remedies).

¹³⁶ See RESTATEMENT (SECOND) OF CONTRACTS § 359(1) (AM. LAW INST. 1981) (“Specific performance or an injunction will not be ordered if damages would be adequate to protect the expectation interest of the injured party.”).

¹³⁷ See *id.* § 357(1) (“[S]pecific performance of a contract duty will be granted *in the discretion of the court . . .*”) (emphasis added); see also *AQSR India Private, Ltd. v. Bureau Veritas Holdings, Inc.*, C.A. No. 4021-VCS, 2009 WL 1707910, at *7 (Del. Ch. June 16, 2009) (Strine, V.C.) (“It is a basic principle of contract law, however, that to be entitled to specific performance, which is an equitable remedy that rests in the discretion of the court”); *Morabito*, 2002 WL 550117, at *3 (“[T]here is no ‘entitlement’ to specific performance, even when a contract breach involving unique goods is admitted. Specific performance is available when it is equitable”).

¹³⁸ See 3 FARNSWORTH, *supra* note 112, § 12.4, at 159-65 (describing the history and limitations of equitable remedies for breach of contract); *id.* § 12.18, at 298-300 (describing the history of the doctrinal ban against contractual penalty provisions).

¹³⁹ See *CML V, LLC v. Bax*, 6 A.3d 238, 251 (Del. Ch. 2010) (Laster, V.C.) (recognizing that the Delaware LLC statute’s authorization of contractually “specified penalties or specified consequences” represents “a departure from the contract law rule against penalty clauses”); Kleinberger, *supra* note 8, at 8 (arguing that “[t]he Delaware LLC Act . . . by expressly authorizing an LLC agreement to provide for ‘specified penalties or specified consequences’ . . . is at odds with hundreds of years of contract law”).

¹⁴⁰ See *CML V*, 6 A.3d at 251 (observing that the Delaware LLC statute represents “a departure from the contract law rule against penalty clauses”).

or specified consequences”¹⁴¹ The statute also includes a nearly identical provision applicable to the manager of an LLC.¹⁴² Although the statute is explicit that “penalties” are enforceable, the other “specified consequences” language indicates that so too are contractual provisions that entitle a non-breaching party to an equitable remedy.¹⁴³ In the ordinary contract context, provisions purporting to create a contractual right to equitable remedies have faced judicial hostility because such provisions conflict with the equitable discretion of the courts to grant such remedies.¹⁴⁴ But as a statutory matter at least, such provisions are enforceable in LLCs.¹⁴⁵

¹⁴¹ DEL. CODE ANN. tit. 6, § 18-306 (2018).

¹⁴² *Id.* § 18-405.

¹⁴³ *Cf.* Kleinberger, *supra* note 8, at 468 (observing that the statutory language authorizing an LLC agreement to stipulate “specified consequences” for breach might include specifying the equitable remedy of disgorgement).

¹⁴⁴ *See* United BioSource LLC v. Bracket Holding Corp., C.A. No. 12886-CB, 2017 WL 2256618, at *3 (Del. Ch. May 23, 2017) (Bouchard, C.) (observing that because “the parties’ ‘irreparable damage’ stipulation . . . is not controlling . . . the inquiry before the Court remains the appropriateness of specific performance as a form of relief”); Kan. City S. v. Grupo TMM, S.A., No. Civ. A. 20518-NC, 2003 WL 22659332, at *5 (Del. Ch. Nov. 4, 2003) (Chandler, C.) (noting that “a contractual stipulation as to the irreparable nature of the harm that would result from a breach cannot limit this Court’s discretion to decline to order injunctive relief” and that “[i]f the facts plainly do not warrant a finding of irreparable harm, this Court is not required to ignore those facts, especially since the parties cannot confer subject matter jurisdiction upon a court”); *see also* 3 FARNSWORTH, *supra* note 112, § 12.6, at 178-79 (“Because the restraints on the availability of equitable relief have been viewed as limitations on the court’s jurisdiction, it is generally supposed that the parties cannot enlarge the availability of specific performance or injunction”); Stephen L. Ascher & Andrew J. Lichtman, *Availability Of Specific Performance To Jilted M&A Parties*, LAW360 (July 22, 2016), at <https://tinyurl.com/y9vl9zyu> (concluding that a “specific performance stipulation in [an] M&A agreement[] . . . is far from conclusive; courts generally give them at least some weight . . . but [the] Delaware and New York courts have given little deference to such provisions”); Michael Frisch, *Contracting For Irreparable Harm*, LAW360 (June 2, 2014), at <https://www.law360.com/articles/543397/contracting-for-irreparable-harm> (“[I]n most jurisdictions, the nonbreaching party is likely to find itself disappointed if the facts do not line up in support of an injunction regardless of what the parties agreed to in the contract.”); Kleinberger, *supra* note 8, at 468 (“Generally courts have resisted contractual attempts to mandate equitable relief.”).

¹⁴⁵ *But see* AM Gen. Holdings LLC v. Renco Grp., Inc., C.A. No. 7668-VCN, 2015 WL 9487922, at *3 (Del. Ch. Dec. 29, 2015) (Noble, V.C.). In *Am General*, the Chancery Court curiously declined to grant an equitable remedy despite the express terms of the LLC agreement entitling the parties to such a remedy. Specifically, the LLC agreement provided that

[t]he parties hereto agree that any party [hereto] shall be entitled to specific performance in addition to any other appropriate relief or remedy. Such party may . . . apply to a court of competent jurisdiction for . . . injunctive or such other relief as such court may deem just and proper in order to enforce this

B. Statutory Limits on Contractual Freedom

Despite the explicit policy set forth in the LLC statute “to give the maximum effect to the principle of freedom of contract,”¹⁴⁶ the statute also makes explicitly clear that this freedom is not an immutable right, but a privilege that may be at any time legislatively “altered . . . or repealed.”¹⁴⁷ Moreover, the LLC statute—by including a number of mandatory, rather than merely default, rules—likewise makes clear that even the “maximum” freedom to contract currently afforded by the statute is not an “absolute” freedom.

Indeed, several of the statutory rules outlined in Part III.A above may be considered mandatory rules for LLCs in the sense that (i) such rules are not part of the common law of contracts, yet apply to LLCs, and (ii) LLC parties cannot contractually avoid the application of those rules to their LLC.¹⁴⁸ The very existence of these mandatory rules should undermine the fantasy that LLC are “creatures of contract” unconcerned with mandatory statutory rules.

To date, no court has hazarded a comprehensive list of the mandatory statutory rules applicable to LLCs. But the Delaware Supreme Court has characterized any such mandatory rules as “likely to be those intended to protect third parties, not necessarily the contracting members”

Agreement or prevent any violation hereof and, to the extent permitted by applicable law, each party waives any objection to the imposition of such relief.

Id. at *2. In declining the motion for a preliminary injunction, Vice Chancellor Noble explained that

[p]arties sometimes . . . agree that contractual failures are to be deemed to impose the risk of irreparable harm. Such an understanding can be helpful when the question of irreparable harm is a close one. Parties, however, cannot in advance agree to assure themselves (and thereby impair the Court’s exercise of its well-established discretionary role in the context of assessing the reasonableness of interim injunctive relief) the benefit of expedited judicial review through the use of a simple contractual stipulation that a breach of that contract would constitute irreparable harm.

Id. at *3. Notably, the court, perhaps taking its lead from the parties’ briefings, never referenced or squared its ruling with Sections 306 and 405 of the LLC statute, which purports to make enforceable such contractual stipulations for equitable relief.

¹⁴⁶ DEL. CODE ANN. tit. 6, § 18-1101(b) (2018).

¹⁴⁷ *Id.* § 18-1106 (“All provisions of this chapter may be altered from time to time or repealed and all rights of members and managers are subject to this reservation.”).

¹⁴⁸ Examples include the statutory rules relating to the formation and maintenance of an LLC and who is bound to an LLC agreement. See *infra* Part III.A.1 and Part III.A.2.

of the LLC.¹⁴⁹ Again, some of the rules outlined in Part III.A above—particularly those concerned with the formation and maintenance of an LLC—fit this characterization. But at least two mandatory rules found in the LLC statute deal only with the relationship among the LLC contract parties.

1. Unwaivable Jurisdiction of Delaware Courts

The first mandatory rule relates to the jurisdiction of the Delaware courts to resolve any disputes among the members of an LLC. Although an LLC agreement may stipulate that Delaware courts have exclusive jurisdiction, the agreement is statutorily barred from stipulating exclusive jurisdiction in the courts of another, non-Delaware jurisdiction.¹⁵⁰ In the language of the LLC statute, a LLC agreement “may not waive [a member’s] right to maintain a legal action or proceeding in the courts of the State of Delaware with respect to matters relating to the organization or internal affairs of a [LLC].”¹⁵¹ Thus, the jurisdiction of Delaware courts to resolve disputes among the members of a domestic LLC is a mandatory rule.¹⁵²

No comparable rule exists for contracts in other settings. For example, a contract may be governed by the laws of Delaware, but stipulate that the courts of New York have exclusive jurisdiction to resolve any disputes arising therefrom. Of course, there again may be a sound policy reason for a mandatory rule barring LLC parties from this choice. It might well be that prohibiting exclusive jurisdiction in courts outside of

¹⁴⁹ *Elf Atochem N. Am., Inc. v. Jaffari*, 727 A.2d 286, 292 (Del. 1999).

¹⁵⁰ See DEL. CODE ANN. tit. 6, § 18-109(d) (2018). The Delaware legislature amended § 18-109(d) of the Delaware LLC statute in 2000 in response to the Delaware Supreme Court’s decision in *Elf Atochem*. In *Elf Atochem*, the high court ruled that § 18-109(d), as then written, did not explicitly bar an LLC agreement from vesting exclusive jurisdiction in the courts of another, non-Delaware jurisdiction, and that interpreting the earlier statutory language in that way would conflict with “the overall policy of the Act to give maximum effect to the parties’ freedom of contract.” 727 A.2d at 296. See also *Baker v. Impact Holding, Inc.*, C.A. No. 4960-VCP, 2010 WL 1931032, at *2 (Del. Ch. May 13, 2010) (Parsons, V.C.) (recounting the legislative history of § 18-109(d)).

¹⁵¹ DEL. CODE ANN. tit. 6, § 18-109(d) (2018). The sole exception set forth in this provision is that an LLC agreement may include terms compelling arbitration in a “specified jurisdiction” outside of Delaware. *Id.*

¹⁵² See *City of Providence v. First Citizens BancShares, Inc.*, 99 A.3d 229, 239 (Del. Ch. 2014) (Bouchard, C.) (“[I]n 2000, the [Delaware] General Assembly explicitly amended § 18-109(d) of the [LLC] Act to prevent a Delaware LLC from *mandating* a foreign court as the exclusive forum for intra-entity disputes asserted by its non-manager members”) (emphasis added).

Delaware will “center interpretive litigation in Delaware courts with the expectation of uniformity” in the state’s LLC law.¹⁵³ But this aim at uniformity does little (perhaps nothing) “to protect third parties,” and it comes at the expense of contractual freedom for the participants within the LLC.¹⁵⁴

2. Implied Contractual Covenant of Good Faith and Fair Dealing

The second mandatory rule relates to the implied contractual covenant of good faith and fair dealing. The LLC statute makes it explicitly clear that an LLC agreement “may not eliminate the implied contractual covenant.”¹⁵⁵ Thus, the implied contractual covenant is another mandatory rule that is imposed by the LLC statute. And it is a mandatory rule that affects only the internal affairs of the LLC; only the parties to a contract are bound by the implied covenant.¹⁵⁶ Therefore, it is another mandatory rule that cannot be accurately characterized as “protect[ing] third parties.”

Even so, supporters of the “creature of contract” notion might defend the statutory imposition of the implied covenant on two grounds. First, to the extent the implied covenant is a mandatory rule, the LLC statute is merely codifying the common law of contracts. The common law has, after all, long imposed on all contracts an implied duty of good faith and fair dealing.¹⁵⁷ And because all contracts are necessarily incomplete—no contract can address every aspect of every possible

¹⁵³ *Elf Atochem*, 727 A.2d at 292; *R & R Capital, LLC v. Buck & Doe Run Valley Farms, LLC*, C.A. No. 3803-CC, 2008 WL 3846318, at *5 (Del. Ch. Aug. 19, 2008) (Chandler, C.) (“[S]ection 18-109 ensures that Delaware retains ultimate jurisdiction over its limited liability companies . . .”).

¹⁵⁴ Instead, by encouraging or “center[ing] interpretive litigation in Delaware courts,” the LLC statute does seem to foster the creation of learning and network effects of Delaware law, which might attract more businesses to organize their LLCs in the state. *See Manesh, supra* note 8, at 211-16.

¹⁵⁵ DEL. CODE ANN. tit. 6, § 18-1101(c) (2018).

¹⁵⁶ *See Gerber v. Enter. Prods. Holdings, LLC*, 67 A.3d 400, 421 (Del. 2013) (“We reject [the plaintiff’s] argument that the implied covenant applies to nonparties to the contract. Both the [Delaware] Superior Court and Court of Chancery have held that the implied covenant only binds parties to the contract.”).

¹⁵⁷ *See* RESTATEMENT (SECOND) OF CONTRACTS § 205 (AM. LAW INST. 1979).

situation¹⁵⁸—the doctrine is in some sense an unwaivable rule that applies to every contract, no matter how carefully drafted.¹⁵⁹

Second, one might argue, the implied covenant is not a mandatory rule at all, but instead actually a default rule. As the Delaware courts have repeatedly made clear, the implied covenant is merely a contractual “gap-filler,” applicable only where the parties to a contract fail to expressly address a particular issue that is now the subject of their dispute.¹⁶⁰ Most notably, in *Nemec v. Shrader*, the Delaware Supreme Court stated that “[t]he implied covenant of good faith and fair dealing involves . . . inferring contractual terms to handle developments or contract gaps that . . . neither party anticipated.”¹⁶¹ Consistent with this gap-filler function, the *Nemec* court added that “one generally cannot base a claim for breach of the implied covenant on conduct authorized by the agreement.”¹⁶² Thus, as a mere “gap filler,” the implied covenant may be better conceived of as a default rule, rather than mandatory; it applies only where the parties’ express agreement fails to address a relevant issue.¹⁶³

¹⁵⁸ See also *Amirsaleh v. Bd. of Trade of N.Y., Inc.*, C.A. No. 2822-CC, 2008 WL 4182998, at *1 (Del. Ch. Sept. 11, 2008) (Chandler, C.) (“No contract, regardless of how tightly or precisely drafted it may be, can wholly account for every possible contingency.”); Mohsen Manesh, *Express Terms and the Implied Contractual Covenant of Delaware Law*, 38 DEL. J. CORP. L. 1, 20 (2013) (“No contract can address every aspect of every possible situation Instead, all contracts will have gaps—matters as to which the contract does not expressly articulate the parties’ expectations.”). As explained by two Delaware jurists:

[T]he human mind cannot foresee every potential situation that could arise after contracting. All contracts necessarily will be incomplete. But assuming that drafters could anticipate all future states of the world, a fully complete contract still would be beyond the parties’ power. After all, contracting is costly. Trying to identify, negotiate, and draft language to address every eventuality would take so much time and require such a large investment of resources that the deal itself would never happen.

Leo E. Strine, Jr., & J. Travis Laster, *The Siren Song of Unlimited Contractual Freedom* in RESEARCH HANDBOOK ON PARTNERSHIPS, LLCs AND ALTERNATIVE FORMS OF BUSINESS ORGANIZATIONS 17 (Robert W. Hillman & Mark J. Loewenstein eds., 2015).

¹⁵⁹ See *Gerber*, 67 A.3d at 419 (“Express contractual provisions always supersede the implied covenant, but even the most carefully drafted agreement will harbor residual nooks and crannies for the implied covenant to fill.”); Manesh, *supra* note 158, at 42 (“Because no contract can address every aspect of every possible situation, what is unsaid in the contract must be left to the parties’ good faith and reason. *This is* the reasonable expectation that courts protect and fulfill with the Implied Covenant.”).

¹⁶⁰ See *Allen v. El Paso Pipeline GP Co.*, C.A. No. 7250-VCL, 2014 WL 2819005, at *10-*11 (Del. Ch. June 20, 2014) (Laster, V.C.), *aff’d*, 2015 WL 803053 (Del. 2015).

¹⁶¹ 991 A.2d 1120, 1125-26 (Del. 2010).

¹⁶² *Id.*

¹⁶³ Elsewhere, I have described the implied covenant as a rebuttal presumption:

But even if this characterization of the implied covenant as a mere default rule is correct—and, as will be explained below, there are reasons to contest it¹⁶⁴—the LLC statute goes on to impose a second mandatory rule relating to the implied covenant. Specifically, an LLC agreement “may not limit or eliminate liability for any act or omission that constitutes a bad faith violation of the implied contractual covenant of good faith and fair dealing.”¹⁶⁵ This statutory provision has two consequences of note. First, it suggests, by negative implication, that one may act in good faith, but still breach the implied covenant. This doctrinal point is undoubtedly true¹⁶⁶—a party may breach the implied covenant by acting arbitrarily or unreasonably thereby frustrating the reasonable expectations of the other party¹⁶⁷—even if Delaware courts have sometimes failed to recognize it.¹⁶⁸ Second, and more relevant to the present discussion, it imposes another

[T]he Implied Covenant operates as a gap filler—a legal presumption that when parties enter into a contract, they do not expect to be treated arbitrarily or unreasonably, to be deceived or exploited. It is a presumption that, in the absence of an express agreement reflecting a contrary expectation, the parties to a contract reasonably expect to be dealt with honestly and with reason.... But ... the Covenant is ultimately a rebuttable presumption. It is a doctrine of contract, subject to and limited by the parties' ex ante expectations. So, ... the Implied Covenant may not be invoked to contradict the express terms of a bargained-for agreement.

Manesh, *supra* note 158, at 51-52.

¹⁶⁴ See *infra* Part IV.A.2.

¹⁶⁵ DEL. CODE ANN. tit. 6, § 18-1101(e) (2018).

¹⁶⁶ See *Allen v. El Paso Pipeline GP Co.*, C.A. No. 7250-VCL, 2014 WL 2819005, at *10 (Del. Ch. June 20, 2014) (Laster, V.C.) (observing that “satisfying the implied covenant [does not] necessarily require that a party have acted in subjective good faith”), *aff'd*, 2015 WL 803053, at *1 (Del. 2015) (“affirmed on the basis of *and for the reasons* assigned by the Court of Chancery”) (emphasis added).

¹⁶⁷ See *Nemec*, 991 A.2d at 1126 (“We will only imply contract terms when the party asserting the implied covenant proves that the other party has acted arbitrarily or unreasonably, thereby frustrating the fruits of the bargain that the asserting party reasonably expected . . . [.] assess[ing] the parties' reasonable expectations at the time of contracting”); *accord Dieckman v. Regency GP LP*, 155 A.3d 358, 367 (Del. 2017); see also Manesh, *supra* note 158, at 48 (“[U]nder Delaware law, a party can breach the Implied Covenant without scienter when it exercises its contract rights arbitrarily or unreasonably.”).

¹⁶⁸ See *ASB Allegiance Real Estate Fund v. Scion Breckenridge Managing Member, LLC*, 50 A.3d 434, 442, 444 (Del. Ch. 2012) (Laster, V.C.) (ruling that “[t]he elements of an implied covenant claim remain those of a breach of contract claim” and that “[p]roving a breach of contract claim does not depend on the breaching party's mental state” despite “references in Delaware case law to the implied covenant turning on the breaching party having a culpable mental state”), *rev'd on other grounds*, 68 A.3d 665, 669 (Del. 2013); Manesh, *supra* note 158, at 46-47 (questioning the “mercurial relevance that a party's subjective motivations play in the courts' application of the Implied Covenant”).

mandatory rule for LLCs: that certain bad faith conduct is unexcusable. There is no such rule for ordinary contracts.¹⁶⁹

Both mandatory rules, relating to the unwaivable jurisdiction of the Delaware courts and the implied covenant of good faith and fair dealing, reveal that the “freedom of contract” available under the LLC statute is different than the freedom of contract afforded under ordinary contract law. To be sure, in some respects the freedom for LLCs is more expansive—enforcing penalty provisions and rights to equitable remedies, for example. But in other respects, that freedom is restricted by statute in ways that are alien to the common law.

IV. CREATURES OF EQUITY

Like the Delaware LLC statute, the equitable powers of the Delaware courts also fundamentally shape the relationship of the participants in a LLC. To be clear, “equity” here refers to not just the doctrines and remedies historically applied by courts of equity, including the Delaware Court of Chancery.¹⁷⁰ It also refers to equity in the broader sense, meaning the power vested in all courts “to do right and justice” by exercising judicial discretion in how the law is interpreted and applied.¹⁷¹

As Part IV.A explains, the courts have exercised their equitable powers in ways that have caused the relationship between parties within an LLC to depart from ordinary contract law precepts. Moreover, as described in Part IV.B, the courts' equitable powers may be and have been used to effectively limit the freedom of contract for LLCs. In sum, this discussion shows that just as LLCs are creatures of contract and creatures of statute, they are also creatures of equity.

¹⁶⁹ For example, in other non-LLC settings, contracts can and often do limit a party's liability for breach to a maximum dollar amount. But such a term would be unenforceable under the LLC statute, which prohibits even a “limit” on liability for a bad faith breach of the implied covenant. In contrast, under ordinary contract law, such terms are generally enforceable, subject only to the doctrine of unconscionability. See RESTATEMENT (SECOND) OF CONTRACTS § 356 cmt. d (AM. LAW INST. 1979).

¹⁷⁰ See Manesh, *supra* note 16, at 96-98 (describing briefly the historical distinction between law and equity).

¹⁷¹ See Schoon v. Smith, 953 A.2d 196, 205 (Del. 2008) (“[T]he final object of equity is to do right and justice.”); see also William T. Quillen & Michael Hanrahan, *A Short History of the Delaware Court of Chancery—1792-1992*, 18 DEL. J. CORP. L. 819, 821 (1993) (“[E]quity is a moral sense of fairness based on conscience.”).

A. *Equitable Departures from Contract Law*

Asserting their equitable powers, Delaware courts have fundamentally shaped the rights of LLC members to hold accountable the managers of an LLC for misusing their control over the business and assets of the entity. And the courts have done so in ways that have made the legal relationship between LLC participants unlike a traditional contractual relationship.

The first and most prominent example of this judicial pattern of equitable intervention has been the Delaware courts' insistence that those who exercise control over an LLC owe the LLC and its owners traditional fiduciary duties of loyalty and care, even in the absence of express contract terms in the LLC agreement imposing such duties. Three other examples stem not directly from LLC precedents, but from the closely related law governing LPs.¹⁷² In the LP context, Delaware courts have expanded the scope of the implied contractual covenant of good faith and fair dealing as well as potential liability for aiding and abetting, while limiting the standing of owners to hold the entity's managers accountable for breach of a contractual obligation—all in ways that depart from ordinary contract law precepts. And every indication suggests that these LP precedents would apply with equal force in any case involving an LLC.¹⁷³

1. Default Fiduciary Duties

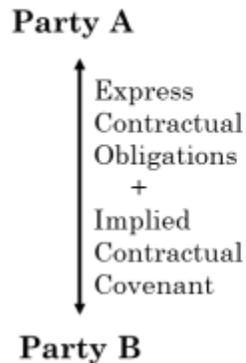
Under ordinary contract law precepts, the legal relationship of the parties to a contract is defined by the terms of their agreement. In this respect, a contractual relationship differs from the relationship, for example, of shareholders and directors in a corporation. In a corporation, the rights and obligations of the participants are defined in part by the express terms of the corporate contract—the corporation's articles and

¹⁷² Delaware LP law is in many respects identical to its LLC law. In fact, Delaware's LLC statute was modeled on the state's LP statute, including its express commitment to the "freedom of contract." See *Elf Atochem N. Am., Inc. v. Jaffari*, 727 A.2d 286, 290-92 (Del. 1999) (noting the similarities between LPs and LLCs).

¹⁷³ Then Vice Chancellor Strine has noted that "in the absence of developed LLC case law, [the chancery] court has often decided LLC cases by looking to analogous provisions in limited partnership law." *Bay Ctr. v. Emery Bay PKI*, C.A. No. 3658-VCS, 2009 WL 1124451, at *9 n.43 (Del. Ch. Apr. 20, 2009). Likewise, Vice Chancellor Laster has observed that "[t]he field of limited partnership law is particularly fertile [to draw analogies for LLCs] When a manager-managed [LLC] has passive members, those members are often treated much like a limited partner under the LP Act." *Obeid v. Hogan*, C.A. No. 11900-VCL, 2016 WL 3356851, at *6 n.4 (Del. Ch. June 10, 2016).

bylaws—and in part by judicially implied equitable principles of fiduciary duty. Contract parties, by contrast, do not owe each other fiduciary duties.¹⁷⁴ The only judicially implied duty owed by contract parties is, as discussed above, the implied contractual covenant of good faith and fair dealing.¹⁷⁵ Thus, the legal obligations of the contract parties may be depicted as follows:

Contract



Consistency with these contract law principles would, therefore, dictate that the participants in an LLC are not subject to judicially implied fiduciary duties. Rather, the rights and obligations of LLC parties are defined solely by reference to the LLC agreement and implied contract covenant of good faith and fair dealing. On this view, fiduciary duties are inapplicable to LLC parties unless the parties' LLC agreement expressly

¹⁷⁴ See *McMahon v. New Castle Assocs.*, 532 A.2d 601, 605 (Del. Ch. 1987) (Allen, C.) (holding, in a dispute involving a real property lease, that “the relationship between the parties is a straightforward commercial relationship arising from contract” and, therefore, “the relationship is not ‘fiduciary’ in the traditional sense”); *Cheese Shop Int'l, Inc. v. Steele*, 303 A.2d 689, 690 (Del. Ch. 1973) (Short, V.C.) (holding, in a dispute involving a trademark license, that “while the contract between [the parties] reveals a quantum of trust placed in [defendant], such trust does not render [defendant] a fiduciary [because] absent here is a dependency on or superiority of the one alleged to be a fiduciary”), *rev'd on other grounds*, 311 A.2d 870 (Del. 1973); see also Ann E. Conaway & Peter I. Tsolfias, *Challenging Traditional Thought: No Default Fiduciary Duties in Delaware Limited Liability Companies after Auriga*, 13 J. BUS. & SEC. L. 1, 2, 4-5 (2012) (arguing that “fiduciary duties are unnecessary in the LLC business form” because “[c]ontract law does not impose fiduciary duties between parties”).

¹⁷⁵ See *supra* note 157 and accompanying text.

imposes such duties. Indeed, this was the view subscribed by some,¹⁷⁶ including most notably former Chief Justice Steele,¹⁷⁷ the originator of the “creature of contract” maxim in Delaware LLC case law.¹⁷⁸

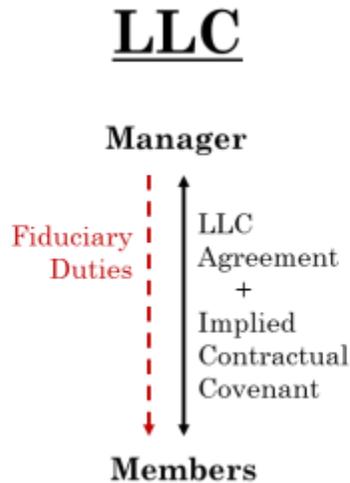
But Delaware courts have all but uniformly rejected this “purely contractual” view of LLCs. Instead, the law is well settled that, consistent with traditional principles of equity, those who exercise control over an LLC—typically, the LLC’s manager—owe the LLC members a fiduciary duty.¹⁷⁹ Thus, in contrast to typical contract parties, the legal relationship of LLC parties may be depicted as follows:

¹⁷⁶ See Conaway & Tsoflias, *supra* note 174, at 6 (“[F]reedom of contract’ signifies to a reviewing court that a Delaware LLC is a bargained-for, contractual entity”); Nicole M. Sciotto, Note, *Opt-In vs. Opt-Out: Settling the Debate over Default Fiduciary Duties in Delaware LLCs*, 37 DEL. J. CORP. L. 531, 555 (2012) (“LLCs are ‘creatures of contract’ whose relationships must be governed solely by the LLC agreement’s terms”).

¹⁷⁷ See Myron T. Steele, *Freedom of Contract and Default Contractual Duties in Delaware Limited Partnerships and Limited Liability Companies*, 46 AM. BUS. L.J. 221, 242 (2009) (arguing that “courts should analyze LLC agreements by the parties’ agreement alone” without reference to default equitable principles); see also Q&A with Chief Justice Myron T. Steele of the Delaware Supreme Court, PRAC. L.J. (Dec. 1, 2012), <http://us.practicallaw.com/3-515-1049> (“Those who advocate for default fiduciary duties . . . miss the fact that the LLC . . . statute’s explicit policy is to maximize contractual freedom. The way to maximize contractual freedom is to look at . . . the contract . . . [LLC parties’] entire relationship is driven by the terms of the contract.”).

¹⁷⁸ See *supra* note 21 and accompanying text.

¹⁷⁹ See, e.g., *Auriga Capital Corp. v. Gatz Props., LLC*, 40 A.3d 839, 851 (Del. Ch. 2012) (Strine, C.) (“[B]ecause the LLC Act provides for principles of equity to apply, because LLC managers are clearly fiduciaries, and because fiduciaries owe the fiduciary duties of loyalty and care, the LLC Act starts with the default that managers of LLCs owe enforceable fiduciary duties.”); *Feeley v. NHAOCG, LLC*, 62 A.3d 649, 661 (Del. Ch. 2012) (Laster, V.C.) (“Delaware [LLC Act] contemplates that equitable fiduciary duties will apply by default to a manager or managing member of a Delaware LLC.”); *Phillips v. Hove, C.A. No. 3644-VCL*, 2011 WL 4404034, at *24 (Del. Ch. Sept. 22, 2011) (Laster, V.C.) (“Unless limited or eliminated in the entity’s operating agreement, the member-managers of a Delaware [LLC] owe traditional fiduciary duties to the LLC and its members.”); *Kelly v. Blum, C.A. No. 4516-VCP*, 2010 WL 629850, at *10 (Del. Ch. Feb. 24, 2010) (Parsons, V.C.) (“[U]nless the LLC agreement in a manager-managed LLC explicitly expands, restricts, or eliminates traditional fiduciary duties, managers owe those duties to the LLC and its members and controlling members owe those duties to minority members.”); *In re Atlas Energy Res., LLC, C.A. No. 4589-VCN*, 2010 WL 4273122, at *6 (Del. Ch. Oct. 28, 2010) (Noble, V.C.) (“[I]n the absence of explicit provisions in a [LLC] agreement to the contrary, the traditional fiduciary duties owed by corporate directors and controlling shareholders apply in the [LLC] context.”); *Bay Ctr. Apartments Owner, LLC, v. Emery Bay PKI, LLC, C.A. No. 3658-VCS*, 2009 WL 1124451, at *8 (Del. Ch. Apr. 20, 2009) (Strine, V.C.) (holding that “in the absence of a contrary provision in the LLC agreement, the manager of an LLC owes the traditional fiduciary duties of loyalty and care to the members of the LLC”).



Then-Chancellor Strine forcefully justified this judge-made rule in *Auriga v. Gatz Properties*, writing that “[t]he [LLC] statute incorporates equitable principles. Those principles view the manager of an LLC as a fiduciary and subject the manager as a default principle to the core fiduciary duties of loyalty and care.”¹⁸⁰ Indeed, when on appeal, the Delaware Supreme Court, led then by Chief Justice Steele, questioned the chancellor’s conclusion,¹⁸¹ the Delaware legislature acted promptly to amend the LLC statute, confirming that equitable principles of fiduciary duty to LLCs.¹⁸²

Yet, Delaware courts have gone further in exercising their equitable powers to impose fiduciary duties in LLCs. Where the manager of an LLC is not a natural person, but instead an entity (for example, another LLC), Delaware courts have imported the doctrine of *USACafes*,¹⁸³ which originated in LP case law,¹⁸⁴ to hold that in addition to the manager-entity, the natural-person controller(s) of the manager-entity owes fiduciary

¹⁸⁰ 40 A.3d at 852.

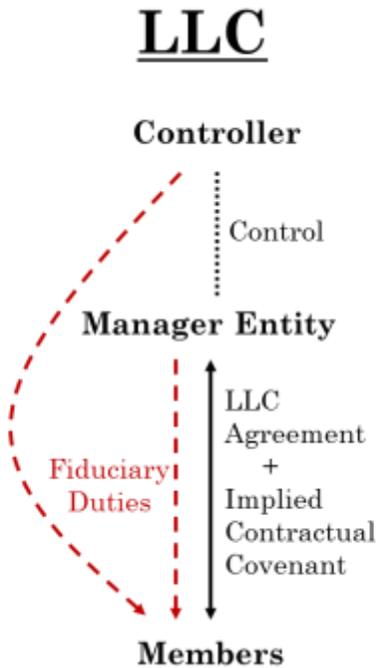
¹⁸¹ *Gatz Props., LLC v. Auriga Capital Corp.*, 59 A.3d 1206, 1218 (Del. 2012); see also Mohsen Manesh, *Damning Dictum: The Default Duty Debate in Delaware*, 39 J. CORP. L. 35, 43-49 (2013) (discussing the chancery and supreme court opinions in *Auriga*).

¹⁸² See H.R. 126, 147th Gen. Assemb., Reg. Sess. (Del. 2013) (providing that “the rules of law and equity relating to fiduciary duties” apply as the default rules); see also Manesh, *supra* note 181, at 64-68 (discussing the context behind and effects of the 2013 amendment to the LLC statute).

¹⁸³ *In re USACafes, L.P. Litig.*, 600 A.2d 43, 48-49 (Del. Ch. 1991) (Allen, C.).

¹⁸⁴ See Mohsen Manesh, *The Case Against Fiduciary Entity Veil Piercing*, 72 BUS. LAW. 61, 64-71 (2017) (describing the origins and expansion of the holding in *USACafes*).

duties directly to the members of the LLC.¹⁸⁵ Thus, where the manager of an LLC is itself an entity, the legal relationship of parties may be depicted as follows:



To be sure, the application of fiduciary duties to the ultimate controller of the manager-entity of an LLC is consistent with equitable principles that burden control with fiduciary responsibility.¹⁸⁶ But it conflicts with contract law principles because it imposes such duties on a natural-person controller who is not formally a party to the LLC agreement; rather it is the manager-entity and the LLC members that are the contract parties.¹⁸⁷ Therefore, imposing fiduciary duties onto the natural-person controllers of a manager-entity arguably disregards the express terms of the LLC

¹⁸⁵ See *Bay Ctr. Apartments Owner, LLC v. Emery Bay PKI, LLC*, C.A. No. 3658-VCS, 2009 WL 1124451, at *9-10 (Del. Ch. Apr. 20, 2009) (Strine, V.C.) (applying *USACafes* in the context of an LLC); *Feeley v. NHAOCG, LLC*, 62 A.3d 649, 671 (Del. Ch. 2012) (Laster, V.C.) (same); see also Manesh, *supra* note 184, at 68-71 (describing the doctrinal expansion of *USACafes*).

¹⁸⁶ See *supra* note 51 and accompanying text.

¹⁸⁷ See Manesh, *supra* note 184, at 79-81 (describing the conflicts of fiduciary duties imposed under *USACafes* with principles of contract law).

agreement.¹⁸⁸ After all, pursuant to the express terms of the LLC agreement, the LLC members contractually agreed that it is an entity, and not the unnamed controllers of the entity, that is the manager of the LLC; it is the entity that is their fiduciary.¹⁸⁹

Thus, the imposition of default fiduciary duties on LLC managers as well as those who may exercise control over a manager-entity reflects a judicial choice made by the Delaware courts about the rights and obligations of LLC participants. This choice, although consistent with traditional principles of equity, is simply incongruent with a strictly contractual vision of LLCs.

2. Implied Contractual Covenant of Good Faith and Fair Dealing

Even if Delaware courts impose fiduciary duties on LLCs as a default matter, the reality is that LLC parties, exercising the freedom of contract, can and often do waive such duties in the terms of their LLC agreement.¹⁹⁰ And such contractual waivers are routinely enforced by

¹⁸⁸ As I have argued elsewhere:

[T]o the extent that the [LLC] is primarily a contractual relationship, consent is relevant. Surely, if parties may agree to modify or eliminate the content of fiduciary duties [in an LLC agreement], then parties may also agree as to who owes such duties. In an arrangement where the parties have agreed that it is an entity that stands in a fiduciary position [as LLC manager], and not the unnamed persons that may control the [manager] entity, one might reasonably question why the courts do not defer to this agreement—what injustice or wrong justifies the intervention of equity to impose onto the nonparty controllers of a [manager] entity the obligations and liabilities of the [manager] entity, despite the parties' express agreement?

Id. at 79-80.

¹⁸⁹ *See id.* at 76 (“Where the [LLC] agreement vests control of the business in another entity, the [LLC’s] investors have, in essence, contractually agreed that it is that entity that is their fiduciary; it is that entity that will be liable to them for any breach of duty”); *cf.* Paige Capital Mgmt., LLC v. Lerner Master Fund, LLC, C.A. No. 5502-CS, 2011 WL 3505355, at *30 (Del. Ch. Aug. 8, 2011) (Strine, C.) (asking rhetorically, in the context a LP with a corporate general partner, “why [are] the investors in the limited partnership not required, in the absence of a reason for veil piercing, to look solely to the entity they knew was their fiduciary for relief?”).

¹⁹⁰ *See, e.g.,* Wood v. Baum, 953 A.2d 136, 139, 141 (Del. 2008) (LLC agreement eliminating all liability associated with fiduciary duties, other than for “fraudulent or illegal conduct”); CNL-AB LLC v. E. Prop. Fund I SPE (MS Ref) LLC, C.A. No. 6137-VCP, 2011 WL 353529, at *9 (Del. Ch. Jan. 28, 2011) (Parsons, V.C.) (LLC agreement permitting the managing member to act in its “sole and absolute discretion . . . without consideration of any other obligation or duty, fiduciary or otherwise”); *In re* Atlas Energy Res., LLC, C.A. No. 4589-VCN, 2010 WL 4273122, at *12 (Del. Ch. Oct. 28, 2010) (Noble, V.C.) (LLC agreement

Delaware courts, despite the equitable concerns such waivers might raise.¹⁹¹ Yet, as noted above, one duty that is statutorily unwaivable for LLCs—and that, therefore, remains always available to the courts and LLC members—is the implied contractual covenant of good faith and fair dealing.¹⁹²

Delaware courts frequently assert that the implied covenant is a “narrow,”¹⁹³ “limited and extraordinary legal remedy,”¹⁹⁴ a “most chary”¹⁹⁵ and “cautious [judicial] enterprise,”¹⁹⁶ applied “sparingly,”¹⁹⁷

explicitly eliminating all fiduciary duties owed by officers and directors of a publicly traded LLC); *Fisk Ventures LLC v. Segal*, C.A. No. 3017-CC, 2008 WL 1961156, at *9 (Del. Ch. May 7, 2008) (Chandler, C.) (LLC agreement eliminating all fiduciary duties by explicitly limiting the parties’ duties to those “expressly set forth” therein); *see also* Peter Molk, *How Do LLC Owners Contract Around Default Statutory Protections?*, 42 J. CORP. L. 503, 505, 507, 522-27 (2017) (providing evidence showing that fiduciary waiver or modification is common among privately held LLCs); *cf. In re El Paso Pipeline Partners, L.P. Derivative Litig.*, 132 A.3d 67, 101 (Del. Ch. 2015) (Laster, V.C.) (observing in the LP context that “[a]lthough the contractual flexibility could be used to provide investors with greater protection, in practice the [alternative entity] agreements establish litigation standards that are more defendant-friendly than traditional fiduciary duty standards.”).

¹⁹¹ *See, e.g., Norton v. K-Sea Transp. Partners L.P.*, 67 A.3d 354, 367 (Del. 2013) (“While we understand [the plaintiff’s] frustration, the [LP agreement’s] provisions control.”); *Dieckman v. Regency GP LP*, C.A. No. 11130-CB, 2016 WL 1223348, at *2, 11 (Del. Ch. Mar. 29, 2016) (Bouchard, C.) (“I recognize it may seem harsh to shield a conflicted transaction from judicial review . . . however, it always must be kept in mind [in the alternative entity context] that the express policy of this State is to give maximum effect to the principle of freedom of contract.”); *Gerber v. EPE Holdings, LLC*, C.A. No. 3543-VCN, 2013 WL 209658, at *2, 10 (Del. Ch. Jan. 18, 2013) (enforcing the terms of an LP agreement that displaced default fiduciary duties and stating in dicta that “[i]t is not difficult to understand [the plaintiff’s] skepticism and frustration, but his real problem is the contract that binds him and his fellow limited partners”).

¹⁹² *See supra* notes 155-169 and accompanying text.

¹⁹³ *E.g., E.I. DuPont de Nemours & Co. v. Pressman*, 679 A.2d 436, 438 (Del. 1996) (“Our holding here reinforces and reaffirms . . . the narrow and carefully crafted nature of the [Implied] Covenant.”); *accord* *Emps. Ret. Sys. of St. Louis v. TC Pipelines GP, Inc.*, No. 291, 2016, 2016 WL 7338592, at *2 (Del. Dec. 19, 2016) (“[T]he implied covenant is narrowly applied . . .”).

¹⁹⁴ *E.g., Nemec v. Shrader*, 991 A.2d 1120, 1128 (Del. 2010) (“[T]he covenant is a limited and extraordinary legal remedy.”).

¹⁹⁵ *E.g., Allied Capital Corp. v. GC-Sun Holdings, L.P.*, 910 A.2d 1020, 1035 (Del. Ch. 2006) (Strine, V.C.) (“[C]ourts should be most chary about implying a contractual protection when the contract could easily have been drafted to expressly provide for it.”).

¹⁹⁶ *E.g., Cincinnati SMSA L.P. v. Cincinnati Bell Cellular Sys. Co.*, 708 A.2d 989, 992 (Del. 1998) (“[I]mplying obligations based on the covenant of good faith and fair dealing is a cautious enterprise.”); *accord* *Emps. Ret. Sys. of St. Louis v. TC Pipelines GP, Inc.*, CA No. 11603-VCG, 2016 WL 2859790, at *6 (Del. Ch. May 11, 2016) (Glasscock, V.C.) (“The Courts apply the implied covenant of good faith and fair dealing cautiously . . .”).

¹⁹⁷ *E.g., Bay Ctr. Apartments Owner, LLC, v. Emery Bay PKI, LLC*, C.A. No. 3658-VCS, 2009 WL 1124451, at *7 (Del. Ch. Apr. 20, 2009) (Strine, V.C.) (“Delaware courts rightly employ the implied covenant sparingly . . .”).

“conservatively”¹⁹⁸ and only in “rare” cases.¹⁹⁹ But in a series of cases involving publicly traded LPs, the courts have predictably²⁰⁰ begun to wield the unwaivable, judicially-defined doctrine more aggressively, in ways that appear to depart from its application in the ordinary contract law setting.²⁰¹

Of course, cases concerning publicly traded LPs involve circumstances that are the most likely to implicate a court’s sense of equity and justice. The agreements governing these publicly traded businesses bear all the hallmarks of contracts of adhesion: prolix and confusing, often unread and unnegotiated, offered on a take-it-or-leave-it basis, and frequently stuffed full of terms that favor the drafting party (the LP’s general partner and its affiliates) at the expense of sometimes unsophisticated public investors.²⁰² And, unsurprisingly, these agreements routinely contain terms that eliminate the fiduciary duty of loyalty owed by the LP’s general partner, replacing that equitable duty with less rigorous contract terms.²⁰³

¹⁹⁸ *E.g.*, *Kuroda v. SPJS Holdings, L.L.C.*, 971 A.2d 872, 888 (Del. Ch. 2009) (Chandler, C.) (“[T]he implied covenant can only be used conservatively [and] . . . is only rarely invoked successfully.”).

¹⁹⁹ *E.g.*, *Cincinnati SMSA*, 708 A.2d at 992 (noting that judicial use of the Implied Covenant to imply terms into a contract “should be rare and fact-intensive”).

²⁰⁰ *See Strine & Laster, supra* note 158, at 26 (predicting that when “judges [are] faced with cases where faithful adherence to the broad exculpatory and safe harbor provisions of alternative entity agreements would seem to excuse unfair self-interested behavior . . . [they] will be tempted to wield the implied covenant as a substitute for . . . fiduciary duties . . .”); *Manesh, supra* note 8, at 248 (predicting that “Delaware courts, pressed by the repeated challenges of aggrieved investors and compelling fact patterns, may eventually be forced to broaden the standards defining the implied contractual covenant to achieve equitable results in . . . [LLC cases].”).

²⁰¹ *See* Mark J. Loewenstein, *Freedom of Contract for Alternative Entities in Delaware: Myth or Reality?*, in *RESEARCH HANDBOOK ON PARTNERSHIPS, LLCs AND ALTERNATIVE FORMS OF BUSINESS ORGANIZATIONS* 33-35 (Robert W. Hillman & Mark J. Loewenstein eds., 2015) (noting the Delaware courts use of the implied covenant of good faith in alternative entity cases to achieve equitable results); Douglas M. Branson, *Alternative Entities in Delaware — Reintroduction of Fiduciary Concepts by the Backdoor?*, in *RESEARCH HANDBOOK ON PARTNERSHIPS, LLCs AND ALTERNATIVE FORMS OF BUSINESS ORGANIZATIONS* 56, 64-67 (Robert W. Hillman & Mark J. Loewenstein eds., 2015) (same).

²⁰² *See Strine & Laster, supra* note 158, at 11-13, 23-24; *see also* Mohsen Manesh, *Legal Asymmetry and the End of Corporate Law*, 34 *DEL. J. CORP. L.* 465, 482-84 (2009) (questioning the assumptions underlying the contractual conception of LLCs and limited partnerships for publicly traded firms).

²⁰³ *See Dieckman v. Regency GP LP*, 155 A.3d 358, 363-64, 366 (Del. 2017) (“One freedom often exercised in the MLP context is eliminating any fiduciary duties a partner owes to others in the partnership structure.”); *Morris v. Spectra Energy Partners (DE) GP, LP, C.A. No. 12110-VCG*, 2017 WL 2774559, at *6 (Del. Ch. June 27, 2017) (Glasscock, V.C.) (observing that the contractual elimination of all default fiduciary duties “is typical in modern

Typically, these less-rigorous contract terms permit the LP to engage in a conflicted transaction with its general partner or the general partner's affiliates if the general partner obtains a so-called "special approval."²⁰⁴ "Special approval" is defined to mean the approval of individuals who are nominally independent of the general partner, but who in practice often have significant relationships with affiliates of the general partner.²⁰⁵ These "special approval" provisions are frequently coupled with so-called "conclusive presumption" provisions, which assert that if the general partner follows a specified procedure to procure the "special approval," then the general partner is "conclusively presumed" to have acted in good faith.²⁰⁶

alternative entities"); *In re El Paso Pipeline Partners, L.P. Derivative Litig.*, 132 A.3d 67, 101 (Del. Ch. 2015) (Laster, V.C.) ("Although the contractual flexibility could be used to provide investors with greater protection, in practice the agreements establish litigation standards that are more defendant-friendly than traditional fiduciary duty standards."); Mohsen Manesh, *Contractual Freedom under Delaware Alternative Entity Law: Evidence from Publicly Traded LPs and LLCs*, 37 DEL. J. CORP. L. 555, 574-96 (2011) (reporting empirical evidence showing that 88% of publicly traded LLCs and limited partnerships fully eliminate or exculpate the fiduciary duties of their managers); Strine & Laster, *supra* note 158, at 12 (observing, from a judicial perspective, that "[a]mong the hallmarks of these agreements [governing publicly traded LLCs and limited partnerships] are broad waivers of all fiduciary duties").

²⁰⁴ See, e.g., *Dieckman*, 155 A.3d at 363-64; *El Paso Pipeline GP Co. v. Brinckerhoff*, 152 A.3d 1248, 1257 (Del. 2016); *Allen v. Encore Energy Partners, L.P.*, 72 A.3d 93, 102-03 (Del. 2013); *Gerber v. Enter. Prods. Holdings, LLC*, 67 A.3d 400, 410 (Del. 2013); *Norton v. K-Sea Transp. Partners L.P.*, 67 A.3d 354, 362-63 (Del. 2013); *Morris*, 2017 WL 2774559, at *7; *In re Energy Transfer Equity L.P. Unitholder Litig.*, C.A. No. 10093-VCL, 2017 WL 782495, at *11 (Del. Ch. Feb. 28, 2017) (Glasscock, V.C.); *In re Kinder Morgan, Inc. Corp. Reorganization Litig.*, C.A. No. 10093-VCL, 2015 WL 4975270, at *6 (Del. Ch. Aug. 20, 2015) (Laster, V.C.); *Gerber v. EPE Holdings, LLC*, C.A. No. 3543-VCN, 2013 WL 209658, at *2 (Del. Ch. Jan. 18, 2013) (Noble, V.C.); *Lonergan v. EPE Holdings LLC*, 5 A.3d 1008, 1020 (Del. Ch. 2010) (Laster, V.C.); *Brinckerhoff v. Tex. E. Prods. Pipeline, Co.*, 986 A.2d 370, 389-90 (Del. Ch. 2010) (Laster, V.C.); *In re Atlas Energy Res., LLC*, C.A. No. 4589-VCN, 2010 WL 4273122, at *7 (Del. Ch. Oct. 28, 2010) (Noble, V.C.); *Brickell Partners v. Wise*, 794 A.2d 1, 3 (Del. Ch. 2001) (Strine, V.C.).

²⁰⁵ See, e.g., *Dieckman*, 155 A.3d at 364-65 (describing relationships between members of the committee charged with considering the special approval and affiliates of the general partner); *In re Energy Transfer Equity L.P. Unitholder Litig.*, 2017 WL 782495, at *5 (same); *In re El Paso Pipeline Partners*, C.A. No. 7141-VCL, 2015 WL 1815846, at *2-3 (Del. Ch. Apr. 20, 2015) (Laster, V.C.) (same); Sandra K. Miller & Karie Davis-Nozemack, *Toward Consistent Fiduciary Duties for Publicly Traded Entities*, 68 FLA. L. REV. 263, 282 (2016) ("A review of recent litigation reveals that parties with ties to the MLP's sponsor or its affiliates may heavily populate GP boards.").

²⁰⁶ See, e.g., *Brinckerhoff v. Enbridge Energy Co.*, 159 A.3d 242, 260-61 (Del. 2017); *Allen*, 72 A.3d at 103; *Gerber*, 67 A.3d at 410-11; *Norton*, 67 A.3d at 366; *Morris*, 2017 WL 2774559, at *7; *Dieckman v. Regency GP LP*, C.A. No. 11130-CB, 2016 WL 1223348, at *3 (Del. Ch. Mar. 29, 2016) (Bouchard, C.); *Lonergan*, 5 A.3d at 1022; *Brinckerhoff*, 986 A.2d at 389-90.

The principal intent of these contract provisions is unambiguously clear: to insulate conflict-of-interest transactions involving the general partner or its affiliates from any judicial scrutiny and, thus, quickly and decisively defeat any legal challenge brought by the LP's public investors.²⁰⁷ But, employing the implied covenant, the Delaware courts have firmly reasserted their equitable role to police against the abuse of these contractual rights by the controllers of a LP.²⁰⁸

First, in *Brinckerhoff v. Texas Eastern Products Pipeline Co.*, Vice Chancellor Laster observed that "special approval" provisions do not entirely insulate a conflicted transaction from any judicial scrutiny, writing that

[w]hile I agree that those provisions establish a weighty defense, the syllogism of "if [special] approval, then judgment for the defendants" does not automatically follow. [Such an] absolutist interpretation of a special approval provision . . . is much too simplistic. At a minimum, the approval must have been given in compliance with the implied covenant of good faith and fair dealing, which a partnership agreement may not eliminate.²⁰⁹

A few months later, in *Lonergan v. EPE Holdings*, the Vice Chancellor confirmed that "the implied covenant constrains the Special Approval processes."²¹⁰ In particular he elaborated that plaintiffs could successfully challenge a conflict-of-interest transaction if the individuals granting the special approval on behalf of the general partner "acted arbitrarily or in bad faith" in breach of the implied contractual covenant.²¹¹

²⁰⁷ See, e.g., *Dieckman*, 155 A.3d at 361 ("The partnership agreement's conflict resolution provision is a powerful tool in the general partner's hands because it can be used to shield a conflicted transaction from judicial review."); *Miller & Davis-Nozemack*, *supra* note 205, at 271 ("MLP agreements are often drafted to maximize the GP's control and to minimize the limited partners' remedies.").

²⁰⁸ As I have previously argued, the judicial construction of express contract terms to identify "gaps" and imply terms using the implied covenant necessarily involves the court's exercise of its equitable discretion and judicial notions of fairness, reasonableness, and good faith. See generally *Manesh*, *supra* note 158, at 18-44.

²⁰⁹ 986 A.2d at 390.

²¹⁰ 5 A.3d at 1021.

²¹¹ See *id.* (observing that to make a cognizable claim "the plaintiff would need to allege particularized facts from which this Court could infer that the members of the Audit Committee acted arbitrarily or in bad faith"); see also *Emps. Ret. Sys. of St. Louis v. TC Pipelines GP, Inc.*, CA No. 11603-VCG, 2016 WL 2859790, at *7 n.48 (Del. Ch. May 11, 2016) (*Glasscock*, V.C.) (observing that the plaintiff could make a cognizable implied covenant claim if the plaintiff

Later, in *Gerber v. Enterprise Products Holdings, LLC*, Vice Chancellor Noble added that the general partner could breach the implied contractual covenant not just in the manner that the “special approval” was obtained; the general partner could also breach the implied covenant with its initial decision to seek a “special approval” if that decision was made in bad faith in order to take opportunistic advantage of the “special approval” process to prevent judicial scrutiny of an otherwise unfair transaction.²¹²

Importantly, however, the chancery court in *Gerber* also held that any such claim of bad faith that the plaintiff might bring was precluded by the LP agreement’s “conclusive presumption” provision, under which the general partner was “conclusively presumed by the terms of the contract to have acted in good faith.”²¹³ The chancery court recognized the inequitable consequences of this holding.²¹⁴ Nonetheless, the court reasoned that the result was compelled by the limited scope of the implied covenant as a mere “gap filler,” applicable only when the parties’ express

alleged facts suggesting the general partner had bribed the independent committee charged with considering a special approval), *aff’d*, 2016 WL 7338592, at *2 (Del. Dec. 19, 2016) (“If a plaintiff is to invoke [the implied covenant], the plaintiff must plead some specific facts suggesting that the Conflicts Committee process was tainted in some specific way by unanticipated behavior, such as the example of bribery the Vice Chancellor pointed to, or other factors bearing on whether the Conflicts Committee process fulfilled its evident contractual purpose.”).

²¹² See *Gerber v. Enter. Prods. Holdings, LLC*, C.A. No. 5989–VCN, 2012 WL 34442, at *11 (Del. Ch. Jan. 6, 2012) (Noble, V.C.) (“[The] GP had discretion as to whether it would use the Special Approval process to take advantage of the contractual duty limitations provided by [the LP agreement and, therefore] had a duty, under the implied covenant, to act in good faith if it took advantage of the Special Approval process.”).

The high court in *Gerber* confirmed that a general partner could breach the implied contractual covenant by acting in bad faith, not just in the process through which the “special approval” was obtained, but also in the initial decision to seek a “special approval”. See *Gerber v. Enter. Prods. Holdings, LLC*, 67 A.3d 400, 423 (Del. 2013) (“*The selection and carryout of the Special Approval process must satisfy . . . the duty [of good faith and fair dealing] under the implied covenant.*”) (emphasis added); *accord Dieckman*, 155 A.3d at 361 (ruling that “[t]he implied covenant is well-suited to imply contractual terms” where “[t]he partnership agreement does not address how the general partner must conduct itself *when seeking the safe harbor[]*” of a special approval) (emphasis added); see also *In re Kinder Morgan, Inc. Corp. Reorganization Litig.*, C.A. No. 10093–VCL, 2015 WL 4975270, at *9 (Del. Ch. Aug. 20, 2015) (Laster, V.C.) (recognizing, in dicta, that a general partner may breach the implied covenant by selecting conflicted individuals to serve on the committee charged with considering the general partner’s request for a special approval).

²¹³ *Gerber*, 2012 WL 34442, at *12-13.

²¹⁴ See *id.* at *13 (“The facts of this case take the reader and the writer to the outer reaches of conduct allowable under [Delaware law]. It is easy to be troubled by the allegations.”).

agreement fails to address a particular matter.²¹⁵ To address the potential conflict between a contractual provision creating a “conclusive presumption” of good faith and the implied covenant’s statutorily unwaivable status, the court explained straightforwardly:

[H]ow can a section of the [LP agreement] preclude a claim for breach of the implied covenant when [Delaware’s LP statute, like its LLC statute,] provides that a “partnership agreement may not eliminate the implied contractual covenant of good faith and fair dealing?” The answer is that although the covenant of good faith and fair dealing may sound like some grandiose principle, it is a gap-filler In *Nemec v. Shrader*, the [Delaware] Supreme Court explained that the implied covenant is a limited remedy meant to address gaps in a contract. The Supreme Court rejected the notion that “where [a contracting party is] expressly empowered to act . . . [it] can breach the implied covenant if it exercises that contractual power arbitrarily or unreasonably.” Thus, under Delaware law . . . [a LP] agreement may not validly state that “the implied covenant is not part of this agreement,” but if a [LP] agreement simply has no gaps, then the implied covenant will never apply to that agreement.²¹⁶

Applying the “gap-filler” conception of the implied covenant to the parties’ LP agreement, the court concluded that that “conclusive presumption” filled any gaps that might otherwise be filled by judicially implied obligations of good faith and fair dealing.²¹⁷

²¹⁵ See *id.* at *12 (“[The implied covenant] is a gap-filler, and may not be used to infer language that contradicts a clear exercise of an express contractual right.”).

²¹⁶ *Id.* at *13 n.58.

²¹⁷ See *id.* at *13. In particular, the Vice Chancellor explained:

The [LP agreement] provides that if [the general partner] follows a specific procedure, then any gaps that may appear in the [LP agreement] will be filled with a conclusive presumption of good faith. When [the general partner] caused [the LP] to undertake the [challenged transaction], it followed that specific procedure in deciding whether to take advantage of the Special Approval process. Thus, any possible gap that [plaintiff] might be able to find in the use of the Special Approval process will be filled with a conclusive presumption of good faith. There can be no claim that [the general partner] breached the implied covenant.

Id. at *13 n.58.

Although the chancery court's interpretation of the "conclusive presumption" provision was arguably consistent with Delaware contract law precedents,²¹⁸ most notably *Nemec*,²¹⁹ it had the effect of neutering the only contractually unwaivable protection available to investors and the courts to ensure accountability and equity in LLCs. Thus, it was quite noteworthy when the Delaware Supreme Court in *Gerber* reversed the lower court on appeal,²²⁰ suggesting the implied covenant is *more* than a mere "gap filler," at least in the alternative entity context. Specifically, the high court in *Gerber* rejected the chancery court's ruling "that under *Nemec*, the implied covenant is merely a 'gap filler' that by its nature must always give way to, and be trumped by, an 'express' contractual right that covers the same subject matter."²²¹ Instead, the high court explained, because the LP statute (like the LLC statute) prohibits an entity agreement from waiving the implied covenant, even express contract terms creating a "conclusive presumption" of good faith in compliance with the implied covenant cannot preclude judicial scrutiny.²²²

Although our Opinion in *Nemec* characterized the implied covenant as a "gap filler" . . . our *Nemec* Opinion was not intended to be, nor should it be read, as an open-ended invitation to scriveners of partnership agreement to "fill the gap" by employing "express" contractual provision that manifestly contravene [state's LP statute].²²³

Having sidestepped the insulating effect of the "conclusive presumption" provision, the supreme court then invoked the implied covenant to rule that the general partner's alleged actions breached the

²¹⁸ Indeed, in two subsequent decisions, the chancery court followed its interpretation in *Gerber* before that interpretation was overruled by the Delaware Supreme Court on appeal. See *In re Encore Energy Partners LP Unitholder Litig.*, C.A. No. 6347-VCP, 2012 WL 3792997, at *14-15 (Del. Ch. Aug. 31, 2012) (Parsons, V.C.); *In re K-Sea Transp. Partners LP Unitholders Litig.*, C.A. No. 6301-VCP, 2012 WL 1142351, at *9-10 (Del. Ch. Apr. 4, 2012) (Parson, V.C.).

²¹⁹ See *supra* notes 160-163 and accompanying text.

²²⁰ See *Gerber v. Enter. Prods. Holdings, LLC*, 67 A.3d 400, 404 (Del. 2013).

²²¹ *Id.* at 420 n.48.

²²² See Loewenstein, *supra* note 201, at 38 ("It is difficult to articulate what additional language the [LP agreement at issue in *Gerber*] could have included to avoid the applicability of the implied covenant."); Branson, *supra* note 201, at 67 (summarizing *Gerber* to mean that "despite the careful drafting and the thinking behind it, [the conclusive presumption provision] did not neutralize the good faith component of the implied covenant, which still exists, compliance with the contractual procedure regardless").

²²³ *Gerber*, 67 A.3d at 420 n.48.

implicit terms of the governing LP agreement.²²⁴ This facet of the *Gerber* ruling was itself novel. Under Delaware contract law precedents, a court will invoke the implied covenant to imply “only those terms that the parties would have agreed to during their original negotiations if they had thought to address them.”²²⁵ As summarized by *Gerber*:

Under Delaware law, a court confronting an implied covenant claim asks whether it is *clear* from what was expressly agreed upon that the parties who negotiated the express terms of the contract would have agreed to proscribe the act later complained of as a breach of the implied covenant of good faith—had they thought to negotiate with respect to that matter.²²⁶

This type of “hypothetical bargain” analysis might make sense in the ordinary contract setting, where an agreement is negotiated between two arms-length parties. But it is ill-fitted where the contract at issue (namely, the governing instrument of a publicly traded entity) is an unnegotiated contract-of-adhesion drafted by, and largely for the benefit of, one party (namely, the general partner and its affiliates).²²⁷ In such circumstances, there are *no* negotiations between the general partner and the myriad public investors who ultimately become party to the agreement.²²⁸ And to the extent one could imagine any such negotiations, the most likely scenario would be one in which the public investors would have agreed to practically any terms the proposed by the general partner.²²⁹ Nonetheless, applying the “hypothetical bargain” analysis to the LP agreement at issue, the high court was able to “*confidently* conclude” that had the parties to the LP agreement expressly addressed the actions the plaintiff alleged

²²⁴ *See id.* at 423-25.

²²⁵ *Id.* at 418.

²²⁶ *Id.* (emphasis added).

²²⁷ Perhaps recognizing the ill-fit of the usual hypothetical bargain analysis as applied to publicly traded LPs, the state supreme court subtly switched course in *Dieckman v. Regency GP*, to focus instead on the “apparent intentions and reasonable expectations of the parties” based on the governing agreement’s express terms. *See Dieckman v. Regency GP LP*, 155 A.3d 358, 367 (Del. 2017).

²²⁸ *But see* *Emps. Ret. Sys. of St. Louis v. TC Pipelines GP, Inc.*, CA No. 11603-VCG, 2016 WL 2859790, at *7 (Del. Ch. May 11, 2016) (Glasscock, V.C.) (noting, in the context of a publicly traded LP, that the implied covenants’ temporal focus is “the time the [LP agreement] was *negotiated*”) (emphasis added).

²²⁹ *See* *Miller & Davis-Nozemack*, *supra* note 205, at 317 (“Given the extent to which MLP partnership agreements protect management, one wonders whether MLP investors understand the governance risks they assume when they invest in an MLP.”).

were undertaken by the general partner, “the parties would *certainly* have agreed” to prohibit such actions.²³⁰

The source of the high court’s confidence and certainty was not obvious. But its desire to achieve equity in the case before it was plain.²³¹ By liberating the implied covenant from *Nemec*’s mere “gap-filler” characterization, the high court in *Gerber* reinvigorated the doctrine and then assertively wielded it to sustain the plaintiff’s claims alleging abuse of power by the LP’s controllers.

More recently, in *Dieckman v. Regency GP LP*,²³² the Delaware Supreme Court further chipped away at the doctrinal limitations of the implied covenant created by *Nemec*. In particular, the *Nemec* court held that “[t]he implied covenant only applies to developments that could not be anticipated, not developments that the parties simply failed to consider.”²³³ By limiting the implied covenant to only unforeseeable situations, the effect of *Nemec* was to make the doctrine inapplicable to situations that were foreseeable at the time of contracting, but were left unaddressed by the express terms of the agreement.²³⁴ The problem with this facet of *Nemec* is that it “imposes on [contract] parties an unrealistic burden of expression[,] require[ing] parties, at the time of the contract’s formation, to address *ex ante* all foreseeable situations.”²³⁵

In *Dieckman*, the high court retreated from this apparent limitation of *Nemec*. Instead, the *Dieckman* court explained that contract terms may be judicially implied under the implied covenant to address even foreseeable situations where “the parties must have intended [the terms] and have only failed to express them because they are too obvious to need expression. Stated another way some aspects of the deal are so obvious to the participants that they never think, or see no need, to address them.”²³⁶ The effect of this ruling, like in *Gerber*, was to further unshackle the implied covenant, making it applicable more broadly. Under *Dieckman*, the doctrine may now be used to judicially imply contract terms not only to deal with unforeseeable situations; it may also be invoked to imply terms to deal with situations that were perfectly foreseeable at the time of contracting, if the relevant terms were so obvious that “it goes without

²³⁰ *Gerber*, 67 A.3d at 422-23 (emphasis added).

²³¹ *See id.* at 422 (describing the defendant’s alleged actions as “arbitrary, unreasonable” and “manifestly unfair”).

²³² 155 A.3d 358 (Del. 2017).

²³³ *Nemec v. Shrader*, 991 A.2d 1120, 1126 (Del. 2010).

²³⁴ *See Manesh, supra* note 158, at 49-50 (criticizing this facet of *Nemec*).

²³⁵ *Id.*

²³⁶ 155 A.3d at 368.

saying.”²³⁷ Moreover, again like *Gerber*, the high court in *Dieckman* then proceeded to use the newly aggrandized doctrine to again sustain the investor’s claim against the alleged abuse of power by the controllers of the LP.²³⁸

It is too early to tell whether *Gerber* and *Dieckman* portend broader doctrinal shifts for the implied covenant in Delaware contract law generally, or whether their holdings are limited to the implied covenant as applied in alternative entities. In either case, it is clear that a judicial sense of equity has caused the high court to expand the unwaivable doctrine in alternative entity cases in ways that were hitherto novel for Delaware contract law more generally. In this respect, the implied covenant as applied in both *Gerber* and *Dieckman*, belie a traditional contractual conception of alternative entities.

3. Aiding and Abetting Liability

Even while a reinvigorated implied contractual covenant of good faith and fair dealing might enable LLC members to more readily challenge managerial self-dealing, the implied covenant applies to only contract parties.²³⁹ This doctrinal limitation means that the manager of an LLC is subject to the implied covenant, but if the manager is an entity, then the natural-person controller of the manager-entity, who is not formally a party to the LLC agreement, is not subject to the implied contractual covenant of good faith. And although the natural-person controller would, under *USACafes* (discussed above), owe a fiduciary duty directly to the LLC and its members,²⁴⁰ where the LLC agreement, as is common, eliminates fiduciary duties,²⁴¹ then the natural-person controller owes no such duties.

Unable to assert a claim for breach of fiduciary duty, a LLC member might instead state a claim for secondary liability against the natural-person controller for aiding and abetting a breach of contract on the part

²³⁷ See Manesh, *supra* note 158, at 30 (explaining that contract parties may fail to include a relevant term in their express agreement for a variety of reasons including because “the parties, hoping to avoid an unmanageably prolix agreement, thought the term too obvious to articulate—it ‘goes without saying,’ they figured”).

²³⁸ See *Dieckman*, 155 A.3d at 368-69.

²³⁹ See *supra* note 156 and accompanying text.

²⁴⁰ See *supra* notes 183-185 and accompanying text.

²⁴¹ See *supra* note 190 and accompanying text.

of the manager-entity.²⁴² But, under ordinary contract law principles, courts do not recognize a cause of action for aiding and abetting a breach of contract.²⁴³

This judicially created limitation on aiding and abetting liability makes contractual obligations different than fiduciary obligations. Where there has been a breach of a fiduciary obligation, Delaware courts have long recognized a separate cause of action against any third party that may have aided and abetted the breach.²⁴⁴ But where a nonparty to a contract assists a contract party's breach of her contractual obligations, the courts bar any aiding-and-abetting claims.²⁴⁵ Instead, any such aiding-and-abetting claim is subsumed, and therefore redundant of, a claim for tortious interference with a contractual relationship.²⁴⁶ Unfortunately, a claim for tortious interference may be more difficult to make than a claim for aiding and abetting.²⁴⁷

²⁴² See, e.g., *Allen v. El Paso Pipeline GP Co.*, C.A. No. 7250-VCL, 2014 WL 2819005, at *18-19 (Del. Ch. June 20, 2014) (Laster, V.C.) (involving a claim for aiding and abetting a breach of contract where the underlying LP agreement has eliminated all default fiduciary duties); *Gerber v. EPE Holdings, LLC*, C.A. No. 3543-VCN, 2013 WL 209658, at *11 (Del. Ch. Jan. 18, 2013) (Noble, V.C.) (same).

²⁴³ See, e.g., *Feeley v. NHAOCG, LLC*, 62 A.3d 649, 658 (Del. Ch. 2012) (Laster, V.C.) (“When dealing with commercial contracts, rather than entity agreements, Delaware law does not recognize the concept of aiding and abetting a breach of contract.”); *accord Allen*, 2014 WL 2819005, at *18 (“Delaware law generally does not recognize a claim for aiding and abetting a breach of contract.”), *aff’d*, 2015 WL 803053, at *1 (Del. 2015); *Gerber*, 2013 WL 209658, at *11 (“Delaware law does not recognize a claim for aiding and abetting a breach of contract.”).

²⁴⁴ See, e.g., *Penn Mart Realty Co. v. Becker*, 298 A.2d 349, 351 (Del. Ch. 1972) (Short, V.C.) (“[O]ne who knowingly joins with any fiduciary, including corporate officials, in a breach of his obligation is liable to the beneficiaries of the trust relationship.”).

²⁴⁵ See *supra* note 243 and accompanying text.

²⁴⁶ The overlap between the two causes of action is manifest. “To succeed on a claim for tortious interference with contractual relations, one must establish the elements of ‘(1) a contract, (2) about which defendant knew, and (3) an intentional act that is a significant factor in causing the breach of such contract (4) without justification (5) which causes injury.’” *Renco Grp., Inc. v. MacAndrews AMG Holdings LLC*, C.A. No. 7668-VCN, 2015 WL 394011, at *9 (Del. Ch. Jan. 29, 2015) (Noble, V.C.). Similarly, the elements of a claim for aiding and abetting are (1) the existence of a duty, (2) the breach of that duty, (3) a defendant who knowingly participated in the breach, and (4) damages to the plaintiff resulting from the concerted action of the defendant and obligor of the breached duty. See *Gotham Partners, L.P. v. Hallwood Realty Partners, L.P.*, 817 A.2d 160, 172 (Del. 2002) (articulating the elements of aiding and abetting liability in the context of a breach of fiduciary duty).

²⁴⁷ As explained by the Delaware Court of Chancery:

[W]here . . . a defendant [accused of tortious interference of contract] is affiliated with the party accused of breaching a contract, a plaintiff must adequately plead that the non-party [defendant] was not pursuing in good faith the legitimate profit seeking activities of the affiliated enterprises, or was motivated by some malicious or other bad faith purpose to injure the plaintiff.

Yet, Delaware courts *do* recognize a cause of action for aiding and abetting a breach of contract—“as odd as that sounds”²⁴⁸—in the alternative entity context.²⁴⁹ Specifically, in LP cases, the courts have allowed aiding and abetting claims where the governing entity agreement imposes a fiduciary-like obligation—what has been called a “contractually adopted fiduciary duty”²⁵⁰—that displaces and supersedes the default fiduciary duty that would otherwise apply at common law.²⁵¹ Although this precedent developed in the LP context,²⁵² it has more recently been applied to LLCs, too.²⁵³ Thus, where a general partner or LLC manager breaches a “contractually adopted fiduciary duty,” then any third party that knowingly participated in that breach may be liable for aiding and abetting

This is because a party to a contract cannot tortiously interfere with its own contractual relations, and affiliates can be understood to share in the contractual interest. Generally speaking, the standard for finding liability for controllers must be high or every-day consultation or direction between parent corporations and subsidiaries about contractual implementation would lead parents to be always brought into breach of contract cases.

Renco Grp., Inc., 2015 WL 394011, at *9; *see also* *Matthew v. Laudamiel*, C.A. No. 5957–VCN, 2014 WL 5904716, at *2 (Del. Ch. 2014) (Noble, V.C.) (“As a general matter, establishing an aiding and abetting claim would likely be less difficult than demonstrating tortious interference with contractual relations.”); *Morris v. Spectra Energy Partners (DE) GP, LP*, C.A. No. 12110–VCG, 2017 WL 2774559, at *17–18 (Del. Ch. June 27, 2017) (Glasscock, V.C.) (dismissing a tortious interference claim brought against the controller of an LP’s general partner).

²⁴⁸ *Feeley*, 62 A.3d at 659 (ruling that a LLC member’s complaint against the controller of the LLC’s manager-entity pleads a valid claim for aiding and abetting the manager-entity’s breach of the LLC agreement).

²⁴⁹ *See, e.g., Gotham Partners, L.P.*, 817 A.2d at 172–73; *Gerber v. Enter. Prods. Holdings, LLC*, 67 A.3d 400, 425 (Del. 2013); *Allen v. El Paso Pipeline GP Co.*, C.A. No. 7250–VCL, 2014 WL 2819005, at *19 (Del. Ch. June 20, 2014) (Laster, V.C.), *aff’d*, 2015 WL 803053, at *1 (Del. 2015).

²⁵⁰ *See generally* D. Gordon Smith, *Contractually Adopted Fiduciary Duty*, 2014 U. ILL. L. REV. 1783 (criticizing the references to “contractually adopted fiduciary duty” in Delaware case law). Delaware courts have variously referred to such duties as “contractual fiduciary duties,” *Gotham Partners, L.P.*, 817 A.2d at 175, “contractually adopted fiduciary duties,” *Gatz Props., LLC v. Auriga Capital Corp.*, 59 A.3d 1206, 1213 (Del. 2012), and “contractually measured fiduciary duties,” *Allen*, 2014 WL 2819005, at *19.

²⁵¹ *See, e.g., Gotham Partners, L.P.*, 817 A.2d at 173 (“[W]here a corporate General Partner fails to comply with a contractual standard of fiduciary duty that supplants traditional fiduciary duties and the General Partner’s failure is caused by its directors and controlling stockholder, the directors and controlling stockholders remain liable [for aiding and abetting the breach].”) (internal quotation marks omitted); *Allen*, 2014 WL 2819005, at *18 (observing that if “the scope of the fiduciary duty [is] established by contract” then “a third party could aid and abet a breach of the contractually measured fiduciary duty”).

²⁵² *See supra* note 249 and accompanying text.

²⁵³ *See Feeley*, 62 A.3d at 658.

the breach.²⁵⁴ Such liability attaches despite the fact that the underlying breach was of a *contractual* obligation—defined and imposed by the governing entity agreement—and not a judicially implied fiduciary obligation.

The stated rationale for the alternative entity exception to the general rule against liability for aiding and abetting breach of contract is that the alternative rule—the one applied in ordinary contract cases—would, if applied to alternative entities, promote injustice.²⁵⁵ “[T]o hold that there is no claim for aiding and abetting the breach of a fiduciary duty created by a contract . . . would deprive a partnership and its partners of claims against those who encourage or otherwise collaborate with a partner which breaches [contractually-created] fiduciary duties for which all partners contracted.”²⁵⁶ While such reasoning certainly has equitable salience, it results in another judicially-created divergence from the common law of contracts. It does so by muddling the distinction between contractual and fiduciary duties, equating the two for purposes of secondary liability. Indeed, in this respect, the alternative entity exception to the general rule against liability for aiding and abetting a breach of contract rejects yet another aspect of *Nemec* as applied to alternative entities, namely the primacy of contract over fiduciary duties. As the *Nemec* court plainly stated, “[i]t is a well-settled principle that where a dispute arises from obligations that are expressly addressed by contract, *that dispute will be treated as a breach of contract claim*. . . . [A]ny fiduciary claims arising out of the same facts that underlie the contract obligations would be foreclosed”²⁵⁷ Yet, despite this “well settled

²⁵⁴ Predictably, the alternative entity exception to the general rule against liability for aiding and abetting a breach of contract has given rise to its own complexities, namely when does a contractual duty qualify as a contractually adopted fiduciary duty? Compare *Gerber*, 67 A.3d at 404 (denying motion to dismiss a plaintiff’s claim for aiding and abetting a breach of a contractually defined obligation of good faith where the relevant LP agreement includes a blanket waiver of fiduciary duties), with *Allen*, 2014 WL 2819005, at *19 (holding that a contractually defined obligation of good faith is *not* a contractually adopted fiduciary duty where the relevant LP agreement also includes a blanket waiver of fiduciary duties). See also *Miller & Davis-Nozemack*, *supra* note 205, at 304 (“It may be difficult to distinguish an agreement’s purely contractual language from language that amounts to a contractual fiduciary duty.”).

²⁵⁵ See *Renco Grp., Inc. v. MacAndrews AMG Holdings LLC*, C.A. No. 7668–VCN, 2015 WL 1830476, at *3 (Del. Ch. Apr. 20, 2015) (Noble, V.C.) (“[W]ithout aiding and abetting liability, deep pocket controllers could avoid liability while the contracting party which they controlled might be rendered unable to pay any judgment.”).

²⁵⁶ *Fitzgerald v. Cantor*, No. CIV. A. 16297–NC, 1999 WL 182573, at *1 (Del. Ch. Mar. 25, 1999) (Steele, V.C.).

²⁵⁷ *Nemec v. Shrader*, 991 A.2d 1120, 1129 (Del. 2010); see also *Madison Realty Partners 7, LLC v. Ag ISA, LLC*, No. CIV. A. 18094, 2001 WL 406268, at *6 (Del. Ch. Apr.

principle,” where the contract is the governing agreement of an alternative entity, the breach of a fiduciary-like contractual obligation is not “treated as a breach of contract claim.” Instead, it is effectively treated as a breach fiduciary duty claim for purposes of attaching secondary liability onto any third party that knowingly participated in the breach.

4. Limited Right to Bring Actions for Breach

One final aspect that highlights the divergence between the relationship among LLC parties versus the relationship among ordinary contract parties is the limited right of a party to an LLC agreement to bring an action against another party that has breached the agreement. Basic contract law provides that when one party to a contract breaches her contractual obligations, the nonbreaching party to the contract is entitled to a remedy for breach and may bring suit against the breaching party to secure that remedy.²⁵⁸ Again, the privity of contract entitles a nonbreaching party to make the claim against the breaching party for breach.²⁵⁹

Yet, the principle of contractual privity is seemingly inoperative for LLCs. Specifically, where one party to an LLC agreement (for example the LLC’s manager) breaches the agreement, a nonbreaching party (for example a member of the LLC) is not necessarily entitled to bring an action for breach. Instead, Delaware courts apply to LLCs the corporate law distinction between direct and derivative claims.²⁶⁰ Where the breach causes a “direct” injury to a complaining LLC member—meaning the breach harms the member in a manner that is independent and separate from any harm the breach cause the LLC entity—then the member may bring a direct action for breach.²⁶¹ But where the breach causes a

17, 2001) (Jacobs, V.C.) (“[I]f the dispute relates to obligations expressly treated by contract, it will be governed by contract principles.”) (internal quotation marks omitted).

²⁵⁸ See RESTATEMENT (SECOND) OF CONTRACTS § 346(1) (AM. LAW INST. 1981) (“The injured party [to a contract] has a right to damages for any breach by a party against whom the contract is enforceable unless the claim for damages has been suspended or discharged.”).

²⁵⁹ See 17A AM. JUR. 2d *Contracts* § 405 (“The doctrine of privity of contract requires that only parties to a contract may bring suit to enforce it.”).

²⁶⁰ See *Elf Atochem N. Am., Inc. v. Jaffari*, 727 A.2d 286, 293 (Del. 1999) (“The derivative suit is a corporate concept grafted onto the limited liability company form.”); *Kelly v. Blum*, C.A. No. 4516-VCP, 2010 WL 629850, at *9 (Del. Ch. Feb. 24, 2010) (Parsons, V.C.) (reasoning that because “[c]ase law governing corporate derivative suits is equally applicable to suits on behalf of an LLC” the court may “look to corporate case law to determine the proper method for distinguishing between derivative actions” in the LLC context).

²⁶¹ See *Tooley v. Donaldson, Lufkin & Jenrette, Inc.*, 845 A.2d 1031, 1033 (Del. 2004) (articulating the two-part test distinguishing derivative and direct claims); *Dietrichson v. Knott*,

derivative, rather than direct, injury—meaning that it is the LLC that suffered a direct harm and the complaining LLC member only suffered an indirect injury arising from the pro rata reduction in the value of his ownership interest in the LLC—then the nonbreaching member is not entitled to bring a lawsuit for breach unless she can plead demand futility.²⁶² Successfully pleading demand futility is itself an onerous burden.²⁶³ But even if a LLC member is able to successfully overcome the demand requirement, the member's derivative claim may be quashed in other ways by the manager of the LLC,²⁶⁴ effectively precluding the member from seeking a remedy.

Typically, the limitations on derivative lawsuits are thought of in the context of a LLC member's claim for breach of *fiduciary* duty brought against the manager of the LLC.²⁶⁵ Yet, in *El Paso Pipeline v. Brinckerhoff*, the Delaware Supreme Court made clear, in the analogous LP context, that the distinction between direct and derivative claims, and the limitations applicable to claims that are judicially assigned to the latter category, apply even when the alleged breach is of a strictly *contractual* duty.²⁶⁶ Thus in *El Paso*, the high court ruled that the plaintiff-investor lacked standing to bring an action against the LP's general partner for breaching the governing LP agreement, despite the fact that the plaintiff had produced a "record [of] evidence suggesting bad faith conduct by the

No. 11965–VCMR, 2017 WL 1400552, at *3 (Del. Ch. Apr. 19, 2017) (Montgomery-Reeves, V.C.) (applying the *Tooley* test in the LLC context); *Kuroda v. SPJS Holdings, L.L.C.*, 971 A.2d 872, 887 (Del. Ch. 2009) (Chandler, C.) (“Delaware law is clear that direct claims are available only where the member has suffered damage that is independent of any damage suffered by the limited liability company.”).

²⁶² See, e.g., *Wood v. Baum*, 953 A.2d 136, 140-44 (Del. 2008) (applying demand futility in the context of a LLC derivative claim); *Dietrichson*, 2017 WL 1400552, at *4 (same); *Lola Cars Intern. Ltd. v. Krohn Racing, LLC*, C.A. Nos. 4479-VCN, 4886-VCN, 2009 WL 4052681, at *7 (Del. Ch. Nov. 12, 2009) (same).

²⁶³ See, e.g., *Wood*, 953 A.2d at 140-41 (“To satisfy [the demand futility] test, a plaintiff must comply with stringent requirements of factual particularity . . .”).

²⁶⁴ See, e.g., *Obeid v. Hogan*, C.A. No. 11900-VCL, 2016 WL 3356851, at *16 (Del. Ch. June 10, 2016) (describing the use of a special litigation committee to review and dismiss derivative litigation in the context of a manager-managed LLC); cf. *El Paso Pipeline GP Co. v. Brinckerhoff*, 152 A.3d 1248, 1250-52 (Del. 2016) (describing how a merger may eliminate the standing of investors to bring a derivative claim in the context of a publicly traded LP).

²⁶⁵ See, e.g., *Wood*, 953 A.2d 139-42 (dismissing LLC member's suit, alleging breach of fiduciary duties, for failure to plead demand futility); *Dietrichson*, 2017 WL 1400552, at *4-5 (same); *Lola Cars Int'l Ltd.*, 2009 WL 4052681, at *8 (ruling that LLC member's suit, alleging breach of fiduciary duties, satisfies the demand excusal standard).

²⁶⁶ *El Paso Pipeline GP Co.*, 152 A.3d at 1259-62 (holding that a breach of contract claim against the general partner of a LP is a derivative claim); see also *Gerber v. EPE Holdings, LLC*, C.A. No. 3543-VCN, 2013 WL 209658, at *13 (Del. Ch. Jan. 18, 2013) (Noble, V.C.) (same).

persons controlling [the] limited partnership.”²⁶⁷ The court determined that the plaintiff’s claims were derivative, not direct, and, therefore, subject to the limitations applied to derivative lawsuits.²⁶⁸

The rules distinguishing direct and derivative suits and limiting the right of LLC members to proceed derivatively are not dictated by the LLC statute or by any contractual terms or doctrines. Instead, these rules are judge-made interventions on the relationship of LLC parties. And the consequence is once again that the rights of LLC parties fundamentally diverge from those of parties to an ordinary contract.

B. Equitable Limits on Contractual Freedom

Taken collectively, the equitable departures from contract law described in Part IV.A above have an indeterminate effect on the rights and protections afforded to LLC members vis-à-vis managers. On one hand, the judicial application of default fiduciary duties and the expansion of the implied contractual covenant provide LLC members with additional legal tools to hold managers accountable for misusing their control over the LLC. On the other hand, the limits placed on the standing of LLC members to bring a suit where the underlying claim is considered derivative and not direct burden members’ ability deploy these legal tools to ensure managerial accountability. What all of these equitable departures have in common, however, is to effectively force intra-LLC litigation between the owners and managers of a LLC to look more like intra-corporate litigation, where there exists a set of unwaivable mandatory rules (deriving largely from the fiduciary duty of loyalty) always available to courts to police against the abuse of managerial control, but where courts also police against the abuse of shareholder lawsuits by placing limits on derivative standing.

There is, however, another resemblance between corporations and LLCs. Both are subject to the maxim “that inequitable action does not become permissible simply because it is legally possible.”²⁶⁹ These famous words derive from Delaware corporate law, where, as already noted, significant aspects of fiduciary duty, and the concomitant equitable power of the courts to police against the managerial abuse of power, are unwaivable and not subject to contracting. But these words might also be aptly applied to Delaware LLCs.

²⁶⁷ *El Paso Pipeline GP Co.*, 152 A.3d at 1251.

²⁶⁸ *Id.* at 1265.

²⁶⁹ *Schnell v. Chris-Craft Indus., Inc.*, 285 A.2d 437, 439 (Del. 1971).

For LLCs, the law clearly and explicitly states that, to the maximum extent possible, LLC parties are entitled to judicial enforcement of their LLC agreement. Yet, when faced with palpably unjust circumstances, Delaware courts retain the equitable discretion “to do right and justice” by declining to enforce the express terms that the parties agreed to.²⁷⁰

A court may do so by exercising its interpretative powers, construing the express terms of an LLC agreement narrowly. Or, in extraordinary cases, a court may do so by exercising its constitutionally vested equitable power to disregard the express terms of an agreement and instead enforce an equitable right or duty. In either case, even if these powers are seldom used by the courts, the effect is the same: the judicial power to do equity limits the freedom of contract and the enforceability of LLC agreements.

1. Judicial Power to Narrowly Construe LLC Agreements

The judicial power to do equity in LLCs manifests itself in how Delaware courts sometimes narrowly construe the express terms of an LLC agreement.²⁷¹ By narrowly construing an LLC agreement, the court effectively limits the legal enforceability of what the parties expressly agreed to in favor of some other default rule that the court implicitly finds to be more palatable.

The application of the implied contractual covenant, discussed in Part IV.A above, illustrates the judicial power to do equity through the strict construction of LLC agreements. Where the express terms of an LLC agreement are construed narrowly, the court may find a “gap” in the agreement, thus enabling the court to imply terms that comport with judicial notions of good faith and fair dealing.

A strict construction of LLC agreements not only leaves room for the implied contractual covenant to operate. It also enables the courts to enforce statutory default rules, where the court believes such default rules

²⁷⁰ Professor Loewenstein has similarly observed that, despite the state’s professed commitment to the freedom of contract, the Delaware state courts will sometimes exercise interpretative or judicial discretion to achieve equitable results in the alternative entity cases. See Loewenstein, *supra* note 201, at 32-35; Mark J. Loewenstein, *Fiduciary Duties and Unincorporated Business Entities: In Defense of the “Manifestly Unreasonable” Standard*, 41 TUL. L. REV. 411, 427 (2005).

²⁷¹ See Loewenstein, *supra* note 201, at 33-35 (noting the Delaware court’s narrow construction of the express terms of an LP agreement in *Miller v. American Real Estate Partners, L.P.*, to achieve an equitable result); Loewenstein, *supra* note 270, at 427 (noting the Delaware court’s narrow interpretation of the express terms of an LP agreement in *Werner v. Miller Technology* to achieve an equitable result).

to be more equitable than what the parties expressly agreed to. For example, in *Haley v. Talcott*, then-Vice Chancellor Strine narrowly construed the express terms of an LLC agreement that provided for a “detailed exit mechanism” so as to not preclude application of the default statutory rule permitting judicial dissolution.²⁷² Despite acknowledging that the “contract-law foundations” of LLC law, “grounded on principles of freedom of contract[,] . . . bear[] on the propriety of ordering [judicial] dissolution,”²⁷³ the Vice Chancellor nonetheless ordered dissolution, reasoning that the “exit mechanism [set forth in the LLC agreement] fails as an adequate remedy . . . because it does not equitably effect the separation of the parties.”²⁷⁴ Of course, the consequence of reaching an equitable result was that the court did not enforce the express terms that the parties had agreed to.²⁷⁵

Haley applied a strict construction of an LLC agreement in order to enforce a statutory default rule the court believed to be more equitable under the circumstances. But Delaware courts will also sometimes apply a strict construction to enforce judge-made fiduciary duties in lieu of an LLC agreement’s express terms. The judicial preference to enforce fiduciary duties over the express terms of an LLC agreement is reflected in the judge-made rule that an enforceable contractual waiver of a fiduciary duty must be explicit and unambiguous.²⁷⁶ This rule means that

²⁷² 864 A.2d 86, 96-98 (Del. Ch. 2004).

²⁷³ *Id.* at 93, 96.

²⁷⁴ *Id.* at 98. In particular, the court explained that the bargained for “exit mechanism” would, if enforced, “penalize” the petitioning party by removing the party from the LLC, but not relieving the party of his obligation under a personal guaranty he had earlier made on behalf of the LLC. *Id.* at 97-98. The court did not explain, however, why such a “penalty” would be problematic given that the LLC statute specifically authorizes penalty provisions. See *supra* Part III.A.5. In this respect, *Haley* is consistent with the chancery court’s subsequent decision in *AM General*, discussed above, where the court declined to enforce a provision in an LLC agreement entitling any party to equitable remedies for any breach by another party, despite the fact that the LLC statute specifically authorizes such a provision. See *supra* note 145.

²⁷⁵ See Loewenstein, *supra* note 270, at 428 n.98 (“The exit provision [in *Haley*] was unconditional and, aside from equitable considerations, the court cited no reason why the provision should not apply While noting the contractual nature of a [LLC], the court interestingly failed to enforce the agreement of the parties.”).

²⁷⁶ See, e.g., *Feeley v. NHAOCG, LLC*, 62 A.3d 649, 664 (Del. Ch. 2012) (Laster, V.C.) (“Drafters of a limited liability company agreement ‘must make their intent to eliminate fiduciary duties plain and unambiguous.’” (quoting *Bay Ctr. Apartments Owner, LLC v. Emery Bay PKI, LLC*, C.A. No. 3658-VCS, 2009 WL 1124451, at *9 (Del. Ch. Apr. 20, 2009) (Strine, V.C.)); *Paige Capital Mgmt., LLC v. Lerner Master Fund, LLC*, C.A. No. 5502-CS, 2011 WL 3505355, at *31 (Del. Ch. Aug. 8, 2011) (Strine, C.) (“Although Delaware’s [LP statute] permits the waiver of fiduciary duties, such waivers must be set forth clearly”); *Kelly v. Blum*, C.A. No. 4516-VCP, 2010 WL 629850, at *10 n.70 (Del. Ch. Feb. 24, 2010) (Parsons, V.C.) (“Having been granted great contractual freedom by the LLC Act, drafters of or parties to an LLC

unless LLC parties express their intent to contractually displace default fiduciary duties with sufficient clarity, the court will enforce default fiduciary duties rather than what the parties perhaps intended to be bound to. Thus, in *In re Atlas Energy Resources, LLC*, the chancery court narrowly construed the express terms of an LLC agreement waiving all conflicts of interest between the publicly-traded LLC and its controlling unitholder so as to not also waive the duty of loyalty as it applies to a conflict of interests between the *controlling unitholder and the LLC's public unitholders*.²⁷⁷ To justify this interpretation of the LLC agreement's express terms, the court explained that it was "especially wary" of enforcing a contract provision to eliminate traditional fiduciary duties in the context of a publicly traded LLC "without sufficient evidence within the contractual language of the parties' intent to do so."²⁷⁸

Closely related to the courts' use of strict construction to avoid enforcing an LLC agreement's express terms is the court's use of *contra proferentem*. This judge-made doctrine requires the court to interpret ambiguity in the express terms of a contract against the drafting party—most commonly, in the LLC context, the manager or controller of the LLC—and in favor of the non-drafting party—typically the LLC's investors. In practice, the doctrine essentially means that the court may avoid enforcing the express terms of an LLC agreement, as intended by the manager or controller of the LLC, where there is any indication of ambiguity.²⁷⁹ *Contra proferentem* becomes particularly important where

agreement should be expected to provide . . . clear and unambiguous provisions when they desire to expand, restrict or eliminate the operation of traditional fiduciary duties."); *Sonet v. Timber Co., L.P.*, 722 A.2d 319, 322 (Del. Ch. 1998) (Chandler, C.) ("[P]rinciples of contract preempt fiduciary principles where the parties to a limited partnership have made their intentions to do so plain.").

²⁷⁷ 2010 WL 4273122, at *8-9 (Del. Ch. Oct. 28, 2010) (Noble, V.C.).

²⁷⁸ *Id.* at *7.

²⁷⁹ *Contra proferentem* is commonly applied in the closely analogous LP context where the relevant governing agreement is drafted by the general partner (or its affiliates) and offered to LP investors without the opportunity to negotiate the agreement's terms. See *Dieckman v. Regency GP LP*, 155 A.3d 358, 366 (Del. 2017) ("[I]n the case of an ambiguous partnership agreement of a publicly traded [LP], ambiguities are resolved as with publicly traded corporations, to give effect to the reading that best fulfills the reasonable expectations an investor would have had from the face of the agreement."); *Norton v. K-Sea Transp. Partners, L.P.*, 67 A.3d 354, 360 (Del. 2013) ("If the contractual language at issue is ambiguous and if the limited partners did not negotiate for the agreement's terms, we apply the *contra proferentem* principle . . ."); *Morris v. Spectra Energy Partners (DE) GP, LP, C.A. No. 12110-VCG*, 2017 WL 2774559, at *13 (Del. Ch. June 27, 2017) (Glasscock, V.C.) ("[B]ecause of the nature of [alternative] entities and their broad contractual freedoms, coupled with the unitholders' limited bargaining power and the fact that the unitholders' sole protections flow from the text of the [entity's governing agreement], ambiguities should be resolved in favor of the unitholder."); *In*

the governing agreement explicitly and unambiguously eliminates default fiduciary duties, leaving LLC members with only the protections (if any) found in the agreement's express terms.²⁸⁰

For example, consider *Morris v. Spectra Energy Partners*, another case involving a publicly traded LP.²⁸¹ Familiarly, the LP agreement in *Morris* waived all default fiduciary duties and included provisions permitting conflicted transactions between the LP and affiliates of the general partner upon a "special approval" and, moreover purported to create a "conclusive presumption" of good faith if the general partner followed a specified procedure to obtain the "special approval."²⁸² Rather than relying on the implied covenant of good faith to avoid the insulating effect of the "conclusive presumption" provision,²⁸³ the court instead employed *contra proferentem*, ruling that the highly protective "conclusive presumption" conflicted with another less protective provision of the governing LP agreement that only created a rebuttable presumption of good faith on the part of the general partner.²⁸⁴ The general partner argued that the two provisions were, in fact, not in conflict; rather, the "conclusive presumption" provision was intended to afford the general partner *additional protection* from judicial review of any "special approval" if the general partner followed the contractually specified

re Energy Transfer Equity L.P. Unitholder Litigation, C.A. No. 10093-VCL, 2017 WL 782495, at *10 (Del. Ch. Feb. 28, 2017) (Glasscock, V.C.) ("[W]hen interpreting the contractual language of a limited partnership agreement, if, but only if, the contractual terms are ambiguous and the limited partners did not negotiate for such terms, I may invoke the principle of *contra proferentem* and construe the ambiguous terms against the drafter."); *In re* Kinder Morgan, Inc. Corp. Reorganization Litig., C.A. No. 10093-VCL, 2014 WL 5667334, at *3 (Del. Ch. Nov. 5, 2014) (Laster, V.C.) ("Where a limited partnership agreement was drafted exclusively by the general partner, the court will interpret ambiguities against the drafter, rather than examine extrinsic evidence.") (citations omitted); *In re* Nantucket Island Assocs. Ltd. P'ship Unitholders Litig., 810 A.2d 351, 361 (Del. Ch. 2002) (Strine, V.C.) (applying *contra proferentem* to interpret ambiguity in a limited partnership agreement "drafted almost exclusively by the[] founding general partners—or perhaps more accurately, by the lawyers for the[] founding general partners").

²⁸⁰ Cf. *Brinckerhoff v. Enbridge Energy Co.*, 159 A.3d 242, 206-61 (Del. 2017) (observing in the LP context that "[p]recisely because [Delaware LP law] allows [LP agreements] . . . to eliminate fiduciary duties, it is essential that unitholders be able to hold the GP accountable for not complying with the terms of the LPA").

²⁸¹ See *Morris*, 2017 WL 2774559.

²⁸² *Id.* at *6-7.

²⁸³ See *supra* notes 209-238 and accompanying text (discussing cases using the implied contractual covenant to limit the insulating effect of "conclusive presumption" provisions).

²⁸⁴ *Morris*, 2017 WL 2774559, at *3, 13,17-18, 22-23, 25-26.

procedure.²⁸⁵ But Vice Chancellor Glasscock rejected the general partner's argument, reasoning:

To the extent there is any ambiguity . . . because of the nature of [alternative entities like LPs and LLCs] and their broad contractual freedoms, coupled with the [investors'] limited bargaining power and the fact that the [investors'] sole protections flow from the text of the [agreement governing the entity], ambiguities should be resolved in favor of the [investors].²⁸⁶

Thus, by invoking *contra proferentem*, the chancery court interpreted the LP agreement's "conclusive presumption" provision to be inoperative.²⁸⁷ And in doing so, the court was able to conclude that the plaintiff-investor had made sufficient allegations showing that, in procuring the "special approval," the general partner had acted in bad faith in breach of the general partner's express contractual obligations.²⁸⁸

Finally, even where the express terms of a governing agreement appear to be facially unambiguous, and therefore not subject to *contra proferentem*, the courts may still apply a miserly interpretation to limit the legal effect of the agreement's express terms. Consider *Brinckerhoff v. Enbridge Energy Co.*, one last case involving a publicly traded LP.²⁸⁹ Again, the LP agreement in *Brinckerhoff* included a provision purporting to create a "conclusive presumption" of good faith by the general partner:

The General Partner may consult with [any] consultants and advisors selected by it, and any act taken or omitted *in reliance* upon the opinion . . . of such [advisors] as to matters that the General Partner *reasonably believes* to be within such [advisor's] professional or expert competence shall be *conclusively presumed to have been done or omitted in good faith . . .*²⁹⁰

²⁸⁵ *Id.* at *11-12.

²⁸⁶ *Id.* at *14.

²⁸⁷ *Id.* at *33-32, 39, 41.

²⁸⁸ *Id.* at *16.

²⁸⁹ 159 A.3d 242, 248 (Del. 2017).

²⁹⁰ *Id.* at 260-61 (emphasis added).

Invoking this contract term, the general partner in *Brinckerhoff* argued that its reliance on the fairness opinion of its financial advisor in approving an allegedly conflicted, unfair deal entitled the general partner to a “conclusive presumption” of good faith, thus nullifying the plaintiff-investor’s claim brought against the general partner.²⁹¹ The Delaware Supreme Court, however, again ruled the “conclusive presumption” provision to be inoperative—but this time not because the provision conflicted with some other aspect of the LP agreement, but instead based on the express language of the provision itself.²⁹² Specifically, the high court held the plaintiff-investor’s allegations, highlighting problems in the process employed by the general partner and its financial advisor, raised doubts as to whether the general partner had “reasonably believed” the fairness opinion as well as whether the general partner had, in fact, “relied” on the opinion at all.²⁹³ One marquee law firm, frequently involved in the drafting of agreements governing publicly traded alternative entities, noted that “the Supreme Court’s . . . failure to give effect to [the conclusive presumption] provision” was “troubling.”²⁹⁴

But what cases like *Brinckerhoff*, *Morris*, *Altas*, and *Haley* reveal is that the freedom of contract—no matter how expertly exercised—is always subject to the equitable discretion of the courts. Whether through a strict construction of an agreement’s express terms or the application of *contra proferentem* to resolve ambiguity, when compelled by equity, the courts can and do avoid enforcing the express terms of an LLC agreement, at least as intended by the manager or controller of the LLC. This interpretative power effectively places a judicial limit on the freedom of contract within LLCs, lessening the ability of LLC parties to potentially exploit that freedom.

2. Judicial Power to Disregard LLC Agreements

Of course, the judicial use of interpretative discretion to reach equitable results is not new or unique to the LLC context; courts have long

²⁹¹ *See id.*

²⁹² *See id.* at 261.

²⁹³ *See id.*

²⁹⁴ *The Delaware Supreme Court “Changes Course” in Evaluating MLP Investor Bad Faith Claims by Adopting Somewhat Lower and “More Traditional” Pleading Standard in Brinckerhoff v. Enbridge Energy Company, Inc.*, BAKER BOTTS (Mar. 29, 2017), <http://www.bakerbotts.com/ideas/publications/2017/03/the-delaware-supreme-court>.

used such “covert tools” in ordinary contract cases.²⁹⁵ But the Delaware Chancery Court’s equitable power to wholly disregard the express terms of an LLC agreement provides one final and unique example of how courts may limit the freedom of contract in LLCs.

Unlike most other states, the equitable powers of the Delaware Court of Chancery are vested by the state’s constitution. Moreover, the Delaware Supreme Court has held, in *Dupont v. Dupont*, that these equitable powers, because they are constitutionally vested, cannot be divested by any act of the Delaware legislature.²⁹⁶ Applied to the LLC context, *Dupont* means that neither the LLC statute, nor an LLC agreement authorized by the statute, may preclude the chancery court from exercising its constitutionally-vested equitable powers in LLC cases.²⁹⁷ These powers include the power to recognize fiduciary relationships and enforce fiduciary duties, even where an LLC agreement purports to modify or eliminate such duties.²⁹⁸

To date, the chancery court has only once exercised its constitutionally unwaivable equitable powers in the LLC context, in *In re Carlisle Etcetera LLC*.²⁹⁹ It did so in *Carlisle* to disregard not the express terms of an LLC agreement, but instead the express terms of the LLC statute.³⁰⁰ Specifically, the LLC statute recognizes that only a LLC “member or manager” may seek judicial dissolution of an LLC, conspicuously omitting any reference to an assignee of an LLC interest.³⁰¹ Despite this express statutory language, Vice Chancellor Laster ruled that an LLC interest assignee may nonetheless seek judicial dissolution as an

²⁹⁵ Loewenstein, *supra* note 270, at 414 (“[C]ourts traditionally have been leery of deferring to the agreement that parties strike when unfairness seems palpable. In those instances, courts will imply strained rules of interpretation to reach a ‘just’ result. They will employ . . . ‘covert tools’ to reach the end that they desire.” (quoting Karl N. Llewellyn, Book Review, 52 HARV. L. REV. 700, 703 (1939))).

²⁹⁶ See *Dupont v. Dupont*, 85 A.2d 724, 728-30 (Del. 1951).

²⁹⁷ See Manesh, *supra* note 16, at 117-28 (arguing that, under the reasoning of *In re Carlisle Etcetera LLC*, the Delaware LLC statute cannot abridge the Delaware Chancery Court’s constitutionally protected equitable powers, including the power to recognize fiduciary relationships and enforce fiduciary duties in LLC); see also Lyman Johnson, *Delaware’s Non-Waivable Duties*, 91 B.U. L. REV. 701, 709 (2011) (making the same argument prior to *Carlisle*).

²⁹⁸ See Johnson, *supra* note 297, at 718; Manesh, *supra* note 16, at 108 (“The upshot of Johnson’s analysis is that, despite Delaware’s embrace of freedom of contract, as a constitutional matter, Delaware courts retain their traditional equitable power to recognize fiduciary relationships and impose fiduciary standards. That power means that Delaware courts need not blithely defer to terms in an LLC agreement purporting to limit or eliminate fiduciary duties.”).

²⁹⁹ 114 A.3d 592 (Del. Ch. 2015) (Laster, V.C.).

³⁰⁰ See *id.* at 601 (ruling that the Delaware LLC statute did not limit the power of the chancery court to equitably dissolve an LLC).

³⁰¹ DEL. CODE ANN. tit. 6, § 18-802 (2018).

equitable matter.³⁰² To support this conclusion, the Vice Chancellor reasoned that the judicial power to dissolve a solvent business is itself a power that originated in equity.³⁰³ Therefore, the Vice Chancellor concluded, as a state constitutional matter, the LLC statute cannot limit the court's traditional equitable power to order dissolution in circumstances where justice dictated.³⁰⁴ In so ruling, *Carlisle* also rejected the chancery court's prior precedent, *R&R Capital, LLC v. Buck & Doe Run Valley Farms, LLC*,³⁰⁵ which, as described in Part II.B,³⁰⁶ held that an LLC agreement may eliminate the court's equitable power to order dissolution of an LLC. By rejecting *R & R Capital*, the Court of Chancery in *Carlisle* thus also implicitly recognized that, like the LLC statute, the express terms of an LLC agreement cannot limit the Delaware courts' constitutional power to do equity.³⁰⁷

Admittedly, *Carlisle* is the only extant LLC precedent where the chancery court has explicitly relied on its constitutionally vested equitable powers. But the chancery court has in a subsequent decision recognized *Carlisle* as binding authority.³⁰⁸ And the reasoning of *Carlisle* may be

³⁰² *Carlisle*, 114 A.3d at 607.

³⁰³ *See id.* at 601-02.

³⁰⁴ *See id.* (ruling that if the LLC statute was interpreted to curtail the traditional equitable powers of the chancery court then it “would raise serious constitutional questions” under *Dupont* because the LLC statute would unconstitutionally “divest this court of a significant aspect of its traditional equitable jurisdiction”).

³⁰⁵ *See id.* at 605 (“This court has held [in *R & R Capital*] that the parties to an LLC agreement can waive by contract the right to seek statutory dissolution In my view, the ability to waive dissolution under [the LLC statute] does not extend to a party's standing to seek dissolution in equity.”).

³⁰⁶ *See supra* notes 48-49 and accompanying text.

³⁰⁷ *See Manesh, supra* note 16, at 113-14 (“If *Carlisle* is correct . . . then . . . [u]nder the state's constitution, the chancery court's traditional equitable powers—including the power to grant derivative standing, order dissolution, or to recognize fiduciary relationships and enforce fiduciary duties—cannot be limited by the LLC statute or a private agreement authorized by that statute.”); *see also* *Huatuco v. Satellite Healthcare and Satellite Dialysis of Tracy, LLC*, C.A. No. 8465-VCG, 2013 WL 6460898, at *1 n.2 (Del. Ch. Dec. 9, 2013) (Glasscock, V.C.) (questioning “[w]hether [LLC] parties may, by contract, divest this Court of its authority to order a dissolution in *all* circumstances, even where it appears manifest that equity so requires”), *aff'd*, 93 A.3d 654 (Del. 2014) (unpublished table decision); Jason C. Jowers & Meghan A. Adams, *The Increasing Role of Equity in Delaware LLC Litigation*, 2015 BUS. L. TODAY 1, 1 (“Based on *Carlisle*, the Court of Chancery may use its equitable powers to dissolve a Delaware LLC even where neither the operating agreement nor the LLC Act expressly permits such dissolution.”).

³⁰⁸ *See* *Trusa v. Nepo*, C.A. No. 12071-VCMR, 2017 WL 1379594, at *8 (Del. Ch. Apr. 13, 2017) (Montgomery-Reeves, V.C.) (citing *Carlisle* to support the court's assertion that “this Court, as a court of equity, has the power to order the dissolution of a solvent company” but that “[g]iven its extreme nature . . . equitable dissolution is a remedy that should be granted sparingly”).

readily applied by the Court of Chancery in a future LLC case where equity dictates the court to override the express terms of an LLC agreement and apply fiduciary duties or another traditionally equitable right or remedy.³⁰⁹

Thus, the constitutionally vested power of the chancery court places a final, important, and far-reaching equitable limit on “the principle of freedom of contract and . . . the enforceability of [LLC] agreements.”³¹⁰ Where equitable circumstances compel it to do so, the chancery court retains its discretion to apply equitable rights and remedies, rather than enforce the express terms that the LLC parties agreed to.³¹¹ More importantly, even if the chancery court seldom asserts its constitutional power to override the express terms of an LLC agreement where compelled by equity, the very existence of a contractually unwaivable judicial power “to do right and justice” places a prophylactic limit on the freedom of contract, deterring LLC parties from even testing the limits of what the courts will countenance from a perspective of equity.

V. CONCLUSION

Vice Chancellor Laster recently observed in *Obeid v. Hogan* that LLCs are “primarily” creatures of contract.³¹² “The adverb ‘primarily,’” he wrote is necessary because it “recognizes the critical but sometimes overlooked non-contractual dimensions of the entity.”³¹³ This Article has cataloged several of these “non-contractual dimensions”—dimensions that spring from both the Delaware LLC statute and from the equitable power of the judiciary. And this Article has shown that these “non-contractual dimensions” are not just narrow or trivial; they are pervasive and fundamental to the identity of the LLC as a business entity.

Thus, to speak of LLCs as mere “creatures of contract” is only a half truth that denies the whole truth about LLCs. To be sure, LLCs are primarily “creatures of contract.” But the freedom of contract in LLCs

³⁰⁹ Indeed, Delaware courts already use their equitable discretion to disregard the express terms of LLC agreements, even without explicitly relying on their constitutional right to do so. *See, e.g.,* *Haley v. Talcott*, 864 A.2d 86, 96-98 (Del. Ch. 2004) (Strine, V.C.); *AM Gen. Holdings LLC v. Renco Grp., Inc.*, C.A. No. 7668-VCN, 2015 WL 9487922, at *3 (Del. Ch. Dec. 29, 2015) (Noble, V.C.).

³¹⁰ DEL. CODE ANN. tit. 6, § 18-1101(b) (2018).

³¹¹ *See* Manesh, *supra* note 16, at 95 (“*Carlisle* suggests that [as a state constitutional matter] Delaware courts retain the equitable power to apply fiduciary standards or recognize other equitable rights or duties, despite the statutorily mandated freedom of contract.”).

³¹² C.A. No. 11900-VCL, 2016 WL 3356851, at *5 (Del. Ch. June 10, 2016).

³¹³ *Id.* at *5 n.2.

exists only within a framework and confines dictated by the legislature and the judiciary. Courts, legislators, practitioners, and business parties should not “take[] [this fact] for granted” lest it be “disregarded or forgotten.”³¹⁴

³¹⁴ *Allegheny Coll. v. Nat’l Chautauqua Cty Bank of Jamestown*, 159 N.E. 173, 174 (N.Y. 1927).

APPENDIX

Using the Westlaw database, the table below identifies each instance where the Delaware state courts have in a written opinion described LLCs (or, more generically, “alternative entities”) as a “creature of contract.” This table includes opinions in which the court cited to an earlier precedent and specifically quoted in that citation the “creature of contract” language found in the earlier precedent. This table was updated as of December 2017.

Case	Date	Court	Judge	Opinion Excerpt
Poore v. Fox Hollow Enterprises, 1994 WL 150872	Mar. 29, 1994	Superior	Steele	Although the statute treats an LLC as a partnership for federal income tax purposes, an LLC is largely a creature of contract -with management, economic, voting and other rights and obligations being primarily specified in the LLC agreement.
Travelcenters of America, LLC v. Brog, 2008 WL 1746987	Apr. 3, 2008	Chancery	Chandler	On the contrary, limited liability companies are creatures of contract , “designed to afford the maximum amount of freedom of contract, private ordering and flexibility to the parties involved.”
Fisk Ventures, LLC v. Segal, 2008 WL 1961156	May 7, 2008	Chancery	Chandler	The sine qua non of pleading an actionable breach is demonstrating that there was something to be breached in the first place. In other words, before the Court can start worrying about whether or not there was a breach, the Court needs to determine that there was a duty. In the context of limited liability companies, which are creatures not of the state but of contract , those duties or obligations must be found in the LLC Agreement or some other contract.

R&R Capital, LLC v. Buck & Doe Run Valley Farms, LLC, 2008 WL 3846318	Aug. 19, 2008	Chancery	Chandler	As this Court has noted, “Limited Liability Companies are creatures of contract , ‘designed to afford the maximum amount of freedom of contract, private ordering and flexibility to the parties involved.’” Delaware’s LLC Act leaves to the members of a limited liability company the task of “arrang[ing] a manager/investor governance relationship;” the Act generally provides defaults that can be modified by contract.
<i>In re</i> Seneca Investments, LLC, 970 A.2d 259	Sept. 23, 2008	Chancery	Chandler	An LLC is primarily a creature of contract , and the parties have wide contractual freedom to structure the company as they see fit.
Travelcenters of America, LLC v. Brog, 2008 WL 5272861	Dec. 5, 2008	Chancery	Chandler	It is well settled that Limited Liability Companies are primarily creatures of contract , and in this case, the LLC Agreement is the contract.
Fisk Ventures, LLC v. Segal, 2009 WL 73957	Jan. 13, 2009	Chancery	Chandler	“Limited Liability Companies are creatures of contract , ‘designed to afford the maximum amount of freedom of contract, private ordering and flexibility to the parties involved.’” Delaware’s LLC Act thus allows LLC members to “‘arrange a manager/investor governance relationship;’ the LLC Act provides defaults that can be modified by contract” as deemed appropriate by the LLC’s managing members.

Spellman v. Katz, 2009 WL 418302	Feb. 6, 2009	Chancery	Noble	Moreover, “[w]hen the issue before the Court involves the interpretation of a contract, summary judgment is appropriate only if the contract in question is unambiguous.” The same is true when the interpretation of an limited liability company agreement is in dispute, as the Delaware limited liability company is a creature of contract . A threshold inquiry on a motion for summary judgment in a dispute over a limited liability company agreement, therefore, becomes whether the agreement contains an ambiguity. “A contract [or limited liability company agreement] provision is ambiguous only when it is fairly susceptible to two or more reasonable interpretations.”
Mickman v. American International Processing, LLC, 2009 WL 891807	Apr. 1, 2009	Chancery	Parsons	LLCs generally are created on a less formal basis than corporations and are basically creatures of contract .

Kuroda v. SPJS Holdings, LLC, 971 A.2d 872	Apr. 15, 2009	Chancery	Chandler	Limited liability companies are creatures of contract , and the parties have broad discretion to use an LLC agreement to define the character of the company and the rights and obligations of its members. Among other things, a company's LLC agreement defines when members of the LLC can be liable for breach of provisions of that agreement. Accordingly, as with any contract, the Court must look to the language of the LLC Agreement to determine the potential liabilities of the parties.
Mickman v. American International Processing, LLC, 2009 WL 2244608	July 28, 2009	Chancery	Parsons	LLC agreements are creatures of contract , which should be construed like other contracts. The construction of an LLC agreement, therefore, begins with the language of the agreement.
Julian v. Julian, 2009 WL 2937121	Sept. 9, 2009	Chancery	Parsons	LLCs are creatures of contract . Indeed, the Delaware Limited Liability Company Act specifically requires the existence of a limited liability company agreement
Kelly v. Blum, 2010 WL 629850	Feb. 24, 2010	Chancery	Parsons	Generally, in Delaware, a merger of an LLC must be approved "by members who own more than percent of the then current percentage or other interest in the profits" of that company. Because LLCs are creatures of contract , however, parties may impose additional requirements for a merger, as they did in this case through the 2008 LLC Agreement.

Kuroda v. SPJS Holdings, LLC, 2010 WL 925853	Mar. 16, 2010	Chancery	Chandler	In my earlier opinion in this case, I noted that “[l]imited liability companies are creatures of contract , and the parties have broad discretion to use an LLC agreement to define the character of the company and the rights and obligations of its members.”
Related Westpac LLC v. JER Snowmass LLC, 2010 WL 2929708	July 23, 2010	Chancery	Strine	<i>Citing:</i> Fisk Ventures LLC v. Segal et al., 2008 WL 1961156, at *8 (Del. Ch. May 7, 2008) (“In the context of limited liability companies, which are creatures ... of contract , those duties or obligations [among parties] must be found in the LLC Agreement or some other contract.”); TravelCenters of Am., LLC v. Brog, 2008 WL 1746987, at *1 (Del.Ch. Apr.3, 2008) (“Limited Liability Companies are creatures of contract , ‘designed to afford the maximum amount of freedom of contract, private ordering and flexibility to the parties involved.’”)
Ross Holding and Management Company v. Advance Realty Group, LLC, 2010 WL 3448227	Sept. 2, 2010	Chancery	Noble	<i>Citing:</i> In re Seneca Inv. LLC, 970 A.2d 259, 261 (Del. Ch. 2008) (“An LLC is primarily a creature of contract , and the parties have wide contractual freedom to structure the company as they see fit.”).

<i>In re</i> Atlas Energy Resources, LLC, 2010 WL 4273122	Oct. 28, 2010	Chancery	Noble	“Limited Liability Companies are creatures of contract , ‘designed to afford the maximum amount of freedom of contract, private ordering and flexibility to the parties involved.’ “One aspect of this flexibility is that parties to a limited liability agreement can contractually expand, restrict, modify, or fully eliminate the fiduciary duties owed by the company or its members, subject to certain limitations.
CML V, LLC v. Bax, 6 A.3d 238	Nov. 3, 2010	Chancery	Laster	LLCs “are creatures of contract , ‘designed to afford the maximum amount of freedom of contract, private ordering and flexibility to the parties involved.’”
DFG Wine Holdings, LLC v. Eight Estates Wine Holdings, LLC, 2011 WL 4056371	Aug. 31, 2011	Chancery	Noble	A limited liability company, of course, is a creature of contract , and a limited liability company agreement may grant members inspection rights that are “in addition to and separate from” the statutory inspection right. . . .
Zimmerman v. Crothall, 2012 WL 707238	Mar. 27, 2012	Chancery	Parsons	Because Adhezion is an LLC, it is governed by the contractual terms of its Operating Agreement. See <i>Kuroda v. SPJS Hldgs., L.L.C.</i> , 971 A.2d 872, 880 (Del.Ch.2009) (“Limited liability companies are creatures of contract , and the parties have broad discretion to use an LLC agreement to define the character of the company and the rights and obligations of its members.”).

Costantini v. Swiss Farm Stores Acquisition LLC, 2013 WL 4758228	Sept. 5, 2013	Chancery	Glasscock	However, LLCs are creatures of contract , and our law provides broad latitude for LLCs to allocate the rights and responsibilities of its members.
Zimmerman v. Crothall, 2013 WL 5630992	Oct. 14, 2013	Chancery	Parsons	<i>Citing</i> In re Seneca Invs. LLC, 970 A.2d 259, 261 (Del. Ch.2008) (“An LLC is primarily a creature of contract [, over which DGCL governs where the parties to the contract so declare.]”).
Touch of Italy Salumeria & Pasticceria, LLC v. Bascio, 2014 WL 108895	Jan. 13, 2014	Chancery	Glasscock	Pursuant to this Court’s well-established principles of contract interpretation, and recognizing that LLCs are creatures of contract , I must enforce LLC agreements as written.
Phillip v. Centerstone Linen Services, LLC, 2014 WL 793123	Feb. 27, 2014	Chancery	Glasscock	In Delaware, limited liability companies “are creatures of contract , designed to afford the maximum amount of freedom of contract, private ordering and flexibility to the parties involved.”
<i>In re</i> Interstate General Media Holdings, LLC, 2014 WL 1697030	Apr. 25, 2014	Chancery	Parsons	It is well-settled under Delaware law that LLCs are creatures of contract rather than statute, and that those who form LLCs are given great latitude in defining their rights and obligations by mutual agreement. Based on that freedom, the parties to the LLC Agreement were free to craft whatever procedure they wished to govern IGM’s dissolution. That freedom included the ability to proscribe the use of judicial dissolution altogether as a means to dissolve the Company.

Durham v. Grapetree, LLC, 2014 WL 1980335	May 16, 2014	Chancery	Glasscock	“Limited liability companies are creatures of contract , and the parties have broad discretion to use an LLC agreement to define the character of the company and the rights and obligations of its members.”
CSH Theatres v. Nederlander of San Francisco Associates, 2015 WL 1839684	Apr. 21, 2015	Chancery	Parsons	Limited liability companies are creatures of contract , and the Delaware Limited Liability Company Act states that “[i]t is the policy of this chapter to give the maximum effect to the principle of freedom of contract.” The drafters of an LLC agreement can modify the traditional duties of care and loyalty or displace them altogether, but they cannot eliminate the implied covenant of good faith and fair dealing.
Henson v. Sousa, 2015 WL 4640415	Aug. 4, 2015	Chancery	Glasscock	LLCs, as this Court has repeatedly pointed out, are creatures of contract . The members can specify certain rights as they find appropriate in the LLC agreement.
Tulum Management USA LLC v. Casten, 2015 WL 7269811	Nov. 9, 2015	Chancery	Noble	Although LLCs are “ creatures of contract ” and therefore provide maximum flexibility to the contracting parties, “[t]he same policy reasons supporting indemnification for corporate actors apply to actors for other entities, including LLCs.”

RED Capital Investment, LP v. RED Parent LLC, 2016 WL 612772	Feb. 11, 2016	Chancery	Noble	<i>Citing</i> Mickman v. Am. Int'l Processing, L.L.C., 2009 WL 2244608, at *2 (Del. Ch. July 28, 2009) ("LLC agreements are creatures of contract , which should be construed like other contracts. The construction of an LLC agreement, therefore, begins with the language of the agreement.")
Obeid v. Hogan, 2016 WL 3356851	June 10, 2016	Chancery	Laster	It is frequently observed that LLCs "are creatures of contract ," which they primarily are. The Delaware Limited Liability Company Act (the "LLC Act") provides that "[i]t is the policy of this chapter to give maximum effect to the principle of freedom of contract and to the enforceability of limited liability company agreements."
El Paso Pipeline GP Company, LLC v. Brinckerhoff, 152 A.3d 1248	Dec. 20, 2016	Supreme	Strine	Such a rule would essentially abrogate Tooley with respect to alternative entities merely because they are creatures of contract .
Sehoy Energy LP v. Haven Real Estate Group Fund, LP, 2017 WL 1380619	Apr. 17, 2017	Chancery	Glasscock	Such a rule would essentially abrogate Tooley with respect to alternative entities merely because they are creatures of contract .
Aloha Power Company, LLC v. Regensis Power, LLC, 2017 WL 6550429	Dec. 22, 2017	Chancery	Montgomery-Reeves	Limited liability company agreements are creatures of contract , which should be construed like other contracts.
