

\*86 864 A.2d 86

Court of Chancery of Delaware,  
New Castle County.

**Matthew James HALEY, Plaintiff,**  
**v.**  
**Gregory L. TALCOTT, and Matt &**  
**Greg Real Estate, LLC, Defendants.**

**C.A. No. 098-S.**

Submitted: Oct. 28, 2004.

Decided: Dec. 16, 2004.

**Background:** Member of limited liability company (LLC) who owned 50% of the LLC brought action seeking dissolution. Member moved for summary judgment.

**Holding:** Court of Chancery, New Castle County, Strine, Vice Chancellor, held that it was not reasonably practicable for LLC, which owned property leased to restaurant, to carry on its business in conformity with LLC agreement.

Dissolution of limited liability company ordered.

West Headnotes

[1] Limited Liability Companies ☞49

241E ----  
241Ek49 Conversion, Merger, and  
Dissolution.

Even if there are no facts under which a Limited Liability Company (LLC) could carry on business in conformity with the LLC Agreement, the remedy of judicial dissolution remains discretionary. 6 Del.C. § 18-802.

[2] Limited Liability Companies ☞49

241E ----  
241Ek49 Conversion, Merger, and  
Dissolution.

Purpose of statute allowing judicial dissolution of a Limited Liability Company (LLC) is to provide an avenue of relief when an LLC cannot continue to function in accordance with its chartering agreement. 6 Del.C. § 18-802.

[3] Limited Liability Companies ☞49

241E ----  
241Ek49 Conversion, Merger, and  
Dissolution.

It was not "reasonably practicable" for Limited Liability Company (LLC), which owned property leased to restaurant, to carry on its business in conformity with LLC agreement, and thus Chancery Court would exercise its discretion and order dissolution of LLC; LLC had two 50% members, members were engaged in a joint venture to operate restaurant, member seeking dissolution was supposed to operate restaurant and share in its profits pursuant to a contract that established a relationship more similar to a partnership than an employer/employee relationship, member seeking dissolution was forbidden by other member to enter restaurant, members were at a deadlock concerning LLC's business strategy, restaurant had a very favorably lease, and, though LLC agreement had an exit provision, exit provision would not relieve member seeking dissolution from his personal guarantee on loan that was secured by mortgage on LLC's property. 6 Del.C. § 18-802.

[4] Limited Liability Companies ☞2

241E ----  
241Ek2 Constitutional and Statutory  
Provisions.

The Delaware Limited Liability Company Act is grounded on principles of freedom of contract. 6 Del.C. § 18-101 et seq.

[5] Corporations ☞612

101 ----  
101XV Dissolution and Forfeiture of  
Franchise  
101k611 Proceedings to Enforce Dissolution or  
Forfeiture  
101k612 In General.

[See headnote text below]

[5] Joint Ventures ☞1.14

224 ----  
224k1.14 Commencement, Duration and  
Termination of Relation.

A court's authority to order dissolution of a joint venture corporation with two 50% stockholders

remains discretionary and may be influenced by the particular circumstances. 8 Del.C. § 273.

\*87 John A. Sergovic, Jr., Sergovic & Ellis, P.A., Georgetown, DE, for Plaintiff.

James D. Griffin, and Alix K. Robinson, Griffin & Hackett, P.A., Georgetown, DE, for Defendants.

#### OPINION

STRINE, Vice Chancellor.

Plaintiff Matthew James Haley has moved for summary judgment of his claim seeking dissolution of Matt and Greg Real Estate, LLC ("the LLC"). Haley and defendant Gregory L. Talcott are the only members of the LLC, each owning a 50% interest in the LLC. Haley brings this action in reliance upon § 18-802 of the Delaware Limited Liability Company Act which permits this court to "decree dissolution of a limited liability company whenever it is not reasonably practicable to carry on the business in conformity with a limited liability company agreement." (FN1) The question before the court is whether dissolution of the LLC should be granted, as Haley requests, or whether, as Talcott contends, Haley is limited to the contractually-provided exit mechanism in the LLC Agreement.

Haley and Talcott have suffered, to put it mildly, a falling out. There is no rational doubt that they cannot continue to do business as 50% members of an LLC. But the path to separating their interests is complicated by a second company, Delaware Seafood, also known as the Redfin Seafood Grill ("Redfin Grill"), a restaurant \*88 that, at the risk of slightly oversimplifying, was owned by Talcott and, before the falling out, operated by Haley under an employment contract that gave him a 50% share in the profits. The LLC owns the land that the Redfin Grill occupies under an expired lease. The resolution of the current case and the ultimate fate of the LLC therefore critically affect the continued existence of a second business that one party owns and that the other bitterly contends, in other litigation pending before this court, wrongly terminated him.

The question before the court is essentially how the interests of the members of the LLC are to be separated. Haley asserts that summary judgment is appropriate because it is factually undisputed that it is not reasonably practicable for the LLC to carry on business in conformity with a limited liability company agreement (the "LLC Agreement") that calls

for the LLC to be governed by its two members, when those members are in deadlock. Therefore, urges Haley, the LLC should be judicially dissolved immediately. Such an end will force the sale of the LLC's real property, which is likely worth, at current market value, far more than the mortgage that the LLC must pay off if it sells.

In response, Talcott stresses that the LLC Agreement provides an alternative exit mechanism that allows the LLC to continue to exist, and argues that Haley should therefore be relegated to this provision if he is unhappy with the stalemate. In other words, Talcott argues that it is reasonably practicable for the LLC to continue to carry on business in conformity with its LLC Agreement because the exit mechanism creates a fair alternative that permits Haley to get out, receiving the fair market value of his share of the property as determined in accordance with procedures in the LLC Agreement, while allowing the LLC to continue. Critically, the exit provision would allow Talcott to buy Haley out with no need for the LLC's asset (i.e., the land) to be sold on the open market. The LLC could continue to exist and own the land (with its favorable mortgage arrangement) and Talcott, as owner of both entities, could continue to offer the Redfin Grill its favorable rent.

But the problem with Talcott's argument is that the exit mechanism is not a reasonable alternative. A principle attraction of the LLC form of entity is the statutory freedom granted to members to shape, by contract, their own approach to common business "relationship" problems. If an equitable alternative to continued deadlock had been specified in the LLC Agreement, arguably judicial dissolution under § 18-802 might not be warranted. In this case, however, Talcott admits that the exit mechanism provides no method to relieve Haley of his obligation as a personal guarantor for the LLC's mortgage. Haley signed an agreement with the lender personally guaranteeing the entire mortgage of the LLC (as did Talcott) in order to secure the loan. Without relief from the guaranty, Haley would remain personally liable for the mortgage debt of the LLC, even after his exit. Because Haley would be left liable for the debt of an entity over which he had no further control, I find that the exit provision specified in the LLC Agreement and urged by Talcott is not sufficient to provide an adequate remedy to Haley under these circumstances.

With no reasonable exit mechanism, I find that Haley is entitled to exercise the only practical

deadlock-breaking remedy available to him, and one that is also alluded to in the LLC Agreement, (FN2) the right to \*89 seek judicial dissolution. Haley argues, convincingly, that the analysis under § 18-802 for an evenly-split, two-owner LLC ordinarily should parallel the analysis under 8 *Del. C.* § 273, which enables this court to order the judicial dissolution of a joint venture corporation owned by deadlocked 50% owners. Because Haley has demonstrated an indisputable deadlock between the two 50% members of the LLC, and that deadlock precludes the LLC from functioning as provided for in the LLC Agreement, I also grant Haley's motion for summary judgment and order dissolution of Matt and Greg Real Estate, LLC.

#### I. *Factual Background* (FN3)

Haley and Talcott each have a 50% interest in Matt & Greg Real Estate, LLC, a Delaware limited liability company they formed in 2003. The creation of the company, however, is only a recent event in the history between the parties.

Haley and Talcott have known each other since the 1980s. In 2001 Haley was the manager of the Rehoboth location of The Third Edition, a restaurant owned by Talcott that also had a location in Washington, D.C. In 2001, Haley found the location for what would become the Redfin Grill. Talcott contributed substantial start-up money and Haley managed the Redfin Grill without drawing a salary for the first year.

The structure of the agreements between the parties forming the Redfin Grill is complex and the subject of additional litigation before this court. (FN4) For reasons that are not relevant, Haley and Talcott chose to create and operate the Redfin Grill as an entity solely owned by Talcott, with Haley's rights and obligations being defined by a series of contracts. Those agreements, all dated November 30, 2001, included an Employment Agreement, a Retention Bonus Agreement, and a Side Letter Agreement (together, the "Employment Contract"), as well as an Agreement regarding an option to purchase real estate (the "Real Estate Agreement"). (FN5)

\*90 The Employment Contract, although structured as an agreement between an employer and an employee, makes clear that the parties were operating the business as a joint venture. The Employment Contract specified that Haley reported to Talcott and that Talcott had the right to reevaluate and revise Haley's decisions, but indicated that "such

action is not anticipated." (FN6) It also provided that Haley's "bonus" would be one half of the net profits of the Redfin Grill, after the initial loan from Talcott was repaid. (FN7) Moreover, Talcott would materially breach the Employment Contract, and Haley could end his employment for cause, if Talcott amended Haley's duties such that his position as "Operations Director" became one of "less dignity, responsibility, importance or scope." (FN8) The Employment Contract further clarified Haley's importance to the enterprise by awarding him one half of any proceeds from any sale of the Redfin Grill. (FN9) Finally, the Employment Contract limited Talcott's ability to remove Haley from his active role:

[N]otwithstanding the language in the Employment Agreement relating to termination, individually, I [Talcott] will assure you that the Employment Agreement will not be terminable under any circumstances unless an event occurs that would entitle you payment of a Retention Bonus as set forth in the Retention Bonus Agreement that is part of this transaction. Such an event would be a "Business Sale" .... (FN10)

The Employment Contract therefore establishes a relationship more similar to a partnership than a typical employer/employee relationship.

The equivalent nature of the parties' contributions is further confirmed by the Real Estate Agreement. In that agreement, Talcott granted Haley the right to participate in an option to purchase the property where the Redfin Grill was situated which is located at 1111 Highway One in Bethany Beach, Delaware (the "Property"). (FN11) Talcott had obtained the option personally when the Redfin Grill first leased the Property from the then-owner in February of 2001. Talcott provided this valuable right to participate for the nominal price of \$10.00. The agreement provided that if the option were exercised, Haley would shoulder 50% of the burden of the purchase, and would be either a 50% owner of the land or a 50% owner of the entity formed to hold the land.

From late 2001 into 2003, under Haley's supervision, the Redfin Grill grew into a successful business. By the second year of its existence, the start-up money had been repaid to Talcott with interest, both parties were drawing salaries (Talcott's substantially smaller since he was not participating in day-to-day management), and the parties each received approximately \$150,000 in profit sharing.

In 2003, the parties formed Matt & Greg Real Estate, LLC to take advantage of the option to purchase the Property that was the subject of the Real Estate Agreement. The option price was \$720,000 and the new LLC took out a mortgage from County Bank in Rehoboth Beach, Delaware, for that amount, exercised the option, and obtained the deed to the Property on or about May 23, 2003. Importantly, both Haley and Talcott, individually, signed personal \*91 guaranties for the entire amount of the mortgage in order to secure the loan. The Redfin Grill continued to operate at the site, paying the LLC \$6,000 per month in rent, a payment sufficient to cover the LLC's monthly obligation under the mortgage. Thus by mid-2003, the parties appeared poised to reap the fruits of their labors; unfortunately, at that point their personal relationship began to deteriorate.

Haley, having managed the restaurant from the time it opened in May 2001, and having formalized his management position in the Employment Contract, apparently believed that the relationship would be reformulated to provide him a direct stock ownership interest in the Redfin Grill at some point. The reasons underlying that belief are not important here, but in late October they caused a rift to develop between the parties. On or about October 27, 2003, the conflict that had been brewing between the parties led to some kind of confrontation. (FN12) As a result, Talcott sent a letter of understanding to Haley dated October 27, 2003, purporting to accept his resignation and forbidding him to enter the premises of the Redfin Grill.

Haley responded on November 3, 2003 with two separate letters from his counsel to Talcott. In the first, Haley asserts that he did not resign, and that he regarded Talcott's October 27, 2003 letter of understanding as terminating him without cause in breach of the Employment Contract. Haley goes on to express his intent to pursue legal remedies, an intent that he acted upon in the related case in this court.

In his second November 3, 2003 letter, Haley purported to take several positions expressly as a 50% member in the LLC including: 1) rejecting the new lease proposed by Talcott for the Redfin Grill; 2) voting to revoke any consent to possession by the Redfin Grill and terminating any lease by which the Redfin Grill asserts the right to possession; and 3) voting that the Property be put up for sale on the open market.

Of course, as a 50% member, Haley could not force the LLC to take action on these proposals because Talcott opposed them. As a result, the pre-existing status quo continued by virtue of the stalemate--a result that Talcott favored. The Redfin Grill's lease has expired and, as a consequence, the Redfin Grill continues to pay \$6,000 per month to the LLC in a month-to-month arrangement. The \$6,000 rent exceeds the LLC's required mortgage payment by \$800 per month, so the situation remains stable. With only a 50% ownership interest, Haley cannot force the termination of the Redfin Grill's lease and evict the Redfin Grill as a tenant; neither can he force the sale of the Property, land that was appraised as of June 14, 2004 at \$1.8 million. In short, absent intervention by this court, Haley is stuck, unless he chooses to avail himself of the exit mechanism provided in the LLC Agreement.

That exit mechanism, like judicial dissolution, would provide Haley with his share of the fair market value of the LLC, including the Property. Section 18 of the LLC Agreement provides that upon written notice of election to "quit" the company, the remaining member may elect, in writing, to purchase the departing member's interest for fair market value. If the remaining member elects to purchase the departing member's interest, the parties may agree on fair value, or have the fair value determined by three arbitrators, one chosen by each member and a third chosen \*92 by the first two arbitrators. The departing member pays the reasonable expenses of the three arbitrators. Once a fair price is determined, it may be paid in cash, or over a term if secured by: 1) a note signed by the company and personally by the remaining member; 2) a security agreement; and 3) a recorded UCC lien. Only if the remaining member fails to elect to purchase the departing member's interest is the company to be liquidated. (FN13)

The LLC agreement describes additional details regarding the term and interest rate of any installment payments and defines penalty, default, and acceleration terms to be contained in the securing note. Although these details are not critical to a comparison between a contractual separation under the LLC Agreement and a judicial dissolution, they demonstrate the level of detail that the parties considered in crafting the exit mechanism. But despite this level of detail, the exit provision does not expressly provide a release from the personal guaranties that both Haley and Talcott signed to secure the mortgage on the Property. Nor does the exit provision state that any member dissatisfied with

the status quo must break an impasse by exit rather than a suit for dissolution.

Rather than use the exit mechanism, Haley has simultaneously sought: 1) dissolution of the LLC; and 2) relief in an employment litigation filed against Talcott and Redfin Grill, a case also pending in this court. Haley does not view himself as being obligated by the LLC Agreement to be the one who exits; moreover, he would bear the cost of the exit mechanism and that mechanism, as will be discussed, would not release him from the guaranty.

As a tactical move, Talcott--on the same day as this suit was filed--putatively reinstated Haley as a manager of the Redfin Grill, but with no duties and only \$1.00 per year in pay. Talcott claims, however, to recognize Haley's right to 50% of the Redfin Grill profits. It appears that Talcott took this step as a method to preempt relief being granted to Haley by a court in lawsuits that Talcott knew were likely to be imminently filed by Haley. Despite the so-called "reinstatement," Talcott and Haley have not had any direct business contact since October 2003.

Haley has moved on since leaving the Redfin Grill in an active capacity, and now operates another restaurant in Lewes, Delaware. Despite his shift in focus, Haley continues to be interested in the Redfin Grill, and has expressed his desire to buy Talcott out of both the LLC and the Redfin Grill itself if given the opportunity. Talcott, by urging the exit remedy provided in the LLC Agreement, has expressed his desire to buy Haley out of the LLC and has no interest in selling the Redfin Grill. Haley continues to refuse to use the exit mechanism.

Pragmatically, the current impasse arises because we have two willing buyers and no willing sellers. Haley alleges that, given this practical dilemma, and his evident inability to effect his desired direction for the LLC, judicial dissolution is his only practicable remedy.

## II. Procedural History

Haley first filed suit over a year ago. (FN14) Although some efforts at resolution were \*93 made by the parties, Haley moved for summary judgment on June 4, 2004. The matter was briefed and argument occurred on August 25, 2004 by teleconference. After argument, the parties again attempted to resolve the matter, requesting and receiving additional time from the court to do so, but again their negotiations proved unfruitful. The court,

by letter dated October 28, 2004, considered Haley's motion for summary judgment submitted and now decides the motion.

## III. Legal Analysis

### A. Procedural Framework

Haley alleges that pursuant to 6 *Del. C.* § 18-802 the court should exercise its discretion and dissolve the LLC because it is not reasonably practicable for it to continue the business of the company in conformity with the LLC Agreement. Section 18-802 provides in its entirety:

On application by or for a member or manager the Court of Chancery may decree dissolution of a limited liability company whenever it is not reasonably practicable to carry on the business in conformity with a limited liability company agreement. (FN15)

Haley argues that dissolution is required because the two 50% managers cannot agree how to best utilize the sole asset of the LLC, the Property, because no provision exists for breaking a tie in the voting interests, and because the LLC cannot take any actions, such as entering contracts, borrowing or lending money, or buying or selling property, absent a majority vote of its members. Because this circumstance resembles corporate deadlock, Haley urges that 8 *Del. C.* § 273 provides a relevant parallel for analysis.

[1] The standard Haley must meet to succeed on a motion for summary judgment is clearly established. Haley must establish that no genuine issue of law or of fact exists and that he is entitled to judgment as a matter of law. (FN16) In examining the record, I must draw every rational inference in Talcott's favor. (FN17) Here, even if I find that there are no facts under which the LLC could carry on business in conformity with the LLC Agreement, the remedy of dissolution, by analogy to 8 *Del. C.* § 273, remains discretionary. (FN18)

Here, the key facts about the parties' ability to work together are not rationally disputable. Therefore, my decision on the motion largely turns on two legal issues: 1) if the doctrine of corporate deadlock is an appropriate analogy for the analysis of a § 18-802 claim on these facts; and 2) if so, and if action to break the stalemate is necessary to permit the LLC to function, whether, because of the contract-law foundations of the Delaware LLC Act, Haley should

