



Court of Chancery Addresses Validity of Entity Action

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In *Feeley v. NHAOCG*, C.A. No. 7304-VCL (Del. Ch. Oct. 12, 2012), the Delaware Court of Chancery addressed several important issues regarding the validity of actions taken in violation of a Delaware limited liability company's operating agreement. The court also indicated that, in certain instances, otherwise unauthorized acts may be ratified by a course of conduct or a later grant of authority. Finally, the court provided significant guidance on the application of Section 144 of the Delaware General Corporation Law, confirming that the common law rules displaced by that statute are inapplicable to Delaware limited liability companies, despite the absence of an analog in the Delaware Limited Liability Company Act.

The *Feeley* case arose from a control dispute involving an overly complicated venture. In 2009, Christopher J. Feeley, a real estate professional, and Andrea Akel, a financial analyst, began to explore forming a real estate company. For initial funding, Akel turned to her father, George Akel, a real estate developer, who then turned to David Newman, also a real estate investor, who contacted Daniel Hughes, also a real estate investor, according to the opinion. In January 2010, the parties formed Oculus Capital Group, a Delaware limited liability company, to operate the business. Oculus' initial members, each having a 50 percent membership interest, were NHAOCG (which counted Newman, Hughes and George Akel as its members) and Ak-Feel (which counted Andrea Akel and Feeley as its members, although Feeley held 55 percent of the membership interests and served as its managing member).

At its formation, Oculus designated Ak-Feel as its initial managing member, and it entered into an employment agreement with Feeley pursuant to which he served as president and chief executive officer. By the end of 2011, the NHA faction wanted to separate from Feeley. NHA sent Feeley a letter advising him that Oculus did not intend to renew his employment agreement. Then, in early 2012, Newman and George Akel notified Feeley that NHA was terminating him as president and CEO of Oculus. Absent from these communications was any explanation as to how NHA purported to take these actions. But that did not stop NHA from advising third parties that Feeley had been terminated and was no longer authorized to represent Oculus, according to the opinion. On the same day that Feeley was purportedly terminated, NHA's counsel sent Feeley yet another letter advising him that NHA was removing Ak-Feel as managing member of Oculus and installing NHA in that position. In other words, after purporting to cause Oculus to fire Feeley, NHA essentially acknowledged it had no authority to take the action.

Pointing to this key deficiency, Feeley filed suit, seeking to block the removal of Ak-Feel as Oculus' managing member. At that point, NHA essentially conceded its lack of authority, and the parties entered into a stipulation to resolve the control dispute and reach a settlement. But the settlement discussions failed, and Feeley again filed suit, seeking declarations that he is the president and CEO, and Ak-Feel is the managing member, of Oculus (the control disputes) and that NHA's letter seeking to replace Ak-Feel, its letter terminating Feeley and its representations to third parties regarding Feeley's removal resulted in breaches of Oculus' operating agreement and were invalid (the authorization disputes).

After reciting the prerequisites for finding a case or controversy sufficient to issue a declaratory judgment, the court found that the control disputes were rendered moot by the parties' control stipulation. The authorization disputes, however, remained live. Specifically, whether NHA breached Oculus' operating agreement when it attempted to take control of the company gave rise to a controversy involving the rights of Ak-Feel and Oculus (the parties seeking relief), and NHA had an interest in contesting that claim, because a finding of breach could give rise to liability on its part. While the control stipulation resolved which parties remained in control of Oculus (thus mooting those claims), it did not resolve whether NHA had breached Oculus' operating agreement and could be held liable for damages. Ruling on the pleadings, the court found that, under the plain language of the operating agreement, Oculus was managed by its managing member, and the provisions of that agreement, read as a whole, made clear that only the managing member had the authority to remove and replace Ak-Feel as managing member or Feeley as president and CEO.

First, the court found that by purporting to remove Feeley as president and CEO, NHA acted without authority and breached the plain language of the operating agreement. The court indicated that NHA's actions in violation of the Oculus operating agreement were unauthorized and void. In earlier cases involving Delaware corporations, a finding that an action is void has led to a finding that it is not susceptible to cure

through ratification by the board or less than all of the stockholders. But the court, in addressing one of NHA's arguments designed to defeat judgment on the pleadings, suggested that certain acts not expressly authorized by a limited liability company agreement could be ratified. NHA argued that Feeley's employment agreement with Oculus was not signed by Ak-Feel, on behalf of Oculus, but was rather signed by Newman, who was acting for Oculus. This, NHA claimed, demonstrated that a party other than the managing member appointed Feeley — and that a party other than the managing member could remove him. The court concluded that Newman's signature constituted extrinsic evidence and thus could not be used to contradict the plain meaning of the operating agreement. "Regardless," the court stated, "the only reasonable inference from the pleadings is that if Newman's action was unauthorized, the members unanimously ratified it by having Feeley serve as president and CEO of Oculus for over two years." To this point, the court referenced the provision of the operating agreement permitting the members, by unanimous action, to authorize a party other than a member to bind Oculus. The court then stated that "as managing member, Ak-Feel could ratify Newman's actions by exercising its authority [to appoint officers]," suggesting that the managing member itself could ratify certain acts that were previously not expressly authorized under the agreement.

Second, the court found that NHA's attempt to remove Ak-Feel as managing member was likewise in violation of the specific provisions of the Oculus operating agreement. On this point, NHA articulated an interesting basis supporting its authority to remove Ak-Feel. The operating agreement provided that Ak-Feel could be removed by unanimous consent of Oculus' members — and NHA claimed that Ak-Feel had also consented to its own removal. Under Ak-Feel's operating agreement, Feeley was the managing member, and only he could authorize it to act. But the provision of Ak-Feel's operating agreement describing the powers of officers stated that the "members [of Ak-Feel] hereby agree that initially Christopher Feeley shall be chief executive officer and Andrea Akel shall be the chief operations officer, and that Andrea Akel, as member and chief operations officer, may execute agreements on behalf of [Ak-Feel] which are or have been authorized pursuant to the terms of [Ak-Feel's operating agreement] if the managing member is unavailable to do so."

NHA claimed that Feeley's conflict of interest regarding whether to remove Ak-Feel as managing member of Oculus disabled him from voting on the matter and, accordingly, rendered him "unavailable." The court rejected this argument, noting that it was reminiscent of the "venerable common law rule" that rendered corporate directors having an interest in a transaction incapable of voting on it. The court noted that Section 144 of the Delaware General Corporation Law displaced this common law rule and confirmed that nothing in the Delaware Limited Liability Company Act suggested that the Delaware Legislature sought to reintroduce into a new and highly flexible act a rigid common law rule. The court then stated that it was "even less likely that the [Delaware] General Assembly sought to reject Section 144(b)'s specific authorization of voting by interested parties in favor of the abandoned common law approach." Finally, the court noted that contracting parties certainly structure their agreements to adopt that common law approach.

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