

Delaware LLC and Partnership Law Update

May 12, 2025

Delaware Court of Chancery Decision Demonstrates Limitations on the Scope of the Implied Covenant of Good Faith and Fair Dealing

In [*Khan, et al. v. Warburg Pincus, LLC, et al.*](#), C.A. No. 2024-0523-LWW (Del. Ch. April 30, 2025), the Delaware Court of Chancery held, on a motion to dismiss, that an amendment provision in a limited liability company agreement (an “LLC Agreement”) left no gap to fill with the implied covenant of good faith and fair dealing. In addition, because the LLC Agreement eliminated fiduciary duties, the court found that there was not an implied term in the LLC Agreement restricting the controlling parties from amending the LLC Agreement in a manner that furthers their own interests, noting that the implied covenant of good faith and fair dealing is not a substitute for traditional fiduciary duties. The court’s ruling highlights that the implied covenant of good faith and fair dealing has limited application, particularly when the parties to an LLC Agreement have eliminated fiduciary duties.

WP CityMD TopCo LLC (the “Company”), an urgent medical care provider, was capitalized into classes of units, with certain affiliated private equity funds holding 60% of the ownership of the Company through Class A Units (the “WP Investors”) and other unitholders holding a minority ownership of the Company through Class B Units (the “Minority Investors”). In late 2021 and 2022, the WP Investors negotiated a merger of the Company with Village Practice Management Company LLC (“Village”), pursuant to which the WP Investors would receive consideration in cash and the Minority Investors would receive consideration in a combination of cash and equity in Village (the “Merger”). As negotiated, the terms of the Merger violated certain existing Minority Investor protections in the LLC Agreement of the Company (the “Operating Agreement”), which required that each class of unitholders receive the same type of consideration in this type of transaction in accordance with the Operating Agreement’s distribution waterfall, and which empowered Minority Investors to elect to participate in such a transaction on the same terms as the WP Investors.

Consequently, the WP Investors sought to amend the Operating Agreement to permit the Merger, including the negotiated merger consideration, notwithstanding these restrictions. The amendment provision in the Operating Agreement required that such amendment be approved by a majority of the Minority Investors, as a class of unitholders whose rights would be adversely affected by the amendment. The amendment was approved by such vote, and the Merger was consummated in January 2023. In March 2024, the primary controller of Village after the Merger filed a \$12.4 billion goodwill impairment charge with respect to Village, effectively devaluing the equity in Village received as merger consideration solely by the Minority Investors. The Minority Investors subsequently brought an action against the WP Investors for, among other things, breach of the implied covenant of good faith and fair dealing in negotiating away the Minority Investors’ rights under the Operating Agreement and coercing the Minority Investors into approving the amendment to permit disparate consideration for different classes of interests.

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Underscoring the implied covenant's character as a gap-filling mechanism, the Court of Chancery held that the Operating Agreement had no gap to fill with respect to the WP Investors' negotiation of disparate merger consideration and implementation of an amendment of the Operating Agreement to permit the disparate merger consideration. The court held that no gap existed because the Operating Agreement expressly contemplated amendments to the Operating Agreement that adversely affect specific classes of unitholders. In addition, the Operating Agreement both expressly eliminated the WP Investors' fiduciary duties and provided that the WP Investors were permitted to act in their own interests. Because the Operating Agreement contained an explicit provision for amendments that adversely affect the Minority Investors and because the WP Investors were authorized to act in their own interests, the Operating Agreement contained no gap or implied term that would prevent the WP Investors from taking those steps.

Finally, the court briefly discussed the Minority Investors' argument that any release contained in the letters of transmittal was unenforceable for lack of separate consideration. In *dicta*, the court noted that the facts of this case differ from *Cigna Health & Life Insurance Co. v. Audax Health Solutions, Inc.*, 107 A.3d 1082 (Del. Ch. 2014), because *Cigna* concerned a corporation and implicated a provision of the Delaware General Corporation Law that is not applicable to limited liability companies. Ultimately, however, the Court determined that it did not need to decide whether the releases in the letters of transmittal were enforceable because the Court dismissed the complaint on other grounds.