9-8-2008

Order on Motions for Partial Summary Judgment (JESSEE MAHOE, LLC)

Alice D. Bonner
Superior Court of Fulton County

IN THE SUPERIOR COURT OF FULTON COUNTY
STATE OF GEORGIA

JESSEE MAHONE, LLC,

Plaintiff,

v.

PAUL V. VIERA, JR., individually and as Managing Member of Earnest Holdings, LLC, and EARNEST HOLDINGS, LLC,

Defendants.

Civil Action File No. 2007CV138625

ORDER ON MOTIONS FOR PARTIAL SUMMARY JUDGMENT

Counsel appeared before the Court on August 21, 2008, to present oral arguments on the following cross motions for partial summary judgment: (1) Plaintiff's Motion for Partial Summary Judgment as to Count I (Declaratory Judgment), filed April 23, 2008; and (2) Defendants' Motion for Partial Summary Judgment, filed June 30, 2008. After reviewing the record of the case, the briefs submitted on the motions, and the arguments presented by counsel, the Court finds as follows:

FACTS

Plaintiff Jessee Mahone, LLC ("Mahone") brought this suit against Earnest Holdings, LLC ("Earnest Holdings"), and its Managing and majority Member, Paul V. Viera ("Mr. Viera"). Mahone, also a Member of Earnest Holdings, alleges that Mr. Viera and Earnest Holdings breached certain contractual obligations and engaged in tortuous conduct toward him. Additionally, Mahone seeks a declaratory judgment[1] that certain amendments[2] to the

1. Count I in the Complaint and Count V in the Amended Complaint seek declaratory judgment on several issues, including a determination that the amendments are null and void.

2. At issue are eight (8) separate actions purpotedly taken by written consent of a Super Majority-in-Interest of Earnest Holdings, which are attached as Exhibits B1-8 to Plaintiff's Motion for Partial Summary Judgment. Defendants argue that not all of the actions are

Earnest Holdings Operating Agreement are invalid because they were not adopted pursuant to the terms of the Operating Agreement. The parties filed their cross motions on this issue. In addition, Defendants move for summary judgment on Plaintiffs' breach of fiduciary duty claim against Mr. Viera.

STANDARD

A court should grant a motion for summary judgment pursuant to O.C.G.A. § 9-11-56 when the moving party shows that no genuine issue of material fact remains to be tried and that the undisputed facts, viewed in the light most favorable to the non-movant, warrant summary judgment as a matter of law. Lau's Corp., Inc. v. Haskins, 261 Ga. 491, 491 (1991).

The internal affairs of a corporation, such as actions involving officers and directors, shall be regulated by the law of the state of incorporation. Diedrich v. Miller & Meier & Assoc., Architects & Planners, Inc., 254 Ga. 734, 735 (1985).

DECLARATORY JUDGMENT

Plaintiff's Complaint seeks a declaratory judgment under O.C.G.A. § 9-4-2(a). Defendants challenge Plaintiff's standing to seek a declaratory judgment arguing that there is no "actual controversy" in this case and that a declaratory judgment would be "fruitless." First, Defendants argue that the amendments, entered into over a series of years from 2001-2007, have been fully authorized, executed, filed, and acted upon; therefore, Mahone's rights have already been fixed on the issue of amendments. Second, Defendants argue that

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"amendments" and that some are written consents pursuant to a specific provision of the Operating Agreement such as with Exhibit B3, which increases the amount of compensation paid to the Managing Member under Section 6.9. The Court, like Plaintiff, shall refer to each such action as an amendment, adopting the number of the corresponding exhibit, for purposes of ease and clarity for this Order. Such terminology, however, is not a legal conclusion about the effect or intent of the action.

Mahone, with a 10% interest in Earnest Holdings, does not hold an ownership interest great enough to prevent a super-majority approval even if the Court determined that additional notice procedures were required under the Operating Agreement. Virginian Ry. Co. v. System Fed'n. No. 40, 300 U.S. 515 (1937).

The questions posed to the Court about amendments ultimately seek clarification about the approval procedures required under certain provisions of the Operating Agreement which would govern both past and future actions. The rights of the parties in their legal relationship are uncertain due to the parties' differing interpretation of key provisions in the Operating Agreement. Therefore, the Court concludes that issues raised with respect to the amendments present an actual controversy regarding the parties' rights and obligations that is the appropriate subject of a declaratory judgment.

OPERATING AGREEMENT

In determining the parties' rights under the Operating Agreement, the Court must first identify the relevant rules of contract construction. "The construction which will uphold a contract in whole and in every part is to be preferred, and the whole contract should be looked to in arriving at the construction of any part." O.C.G.A. §13-2-2 (4). In addition, extrinsic evidence is inadmissible and the meaning of the provisions shall be determined by the Court on the face of the Operating Agreement. O.C.G.A. §§ 13-2-1, 2(1); Eagle Industries, Inc. v. DeVilbiss Health Care, Inc., 702 A.2d 1228 (Del. Supr. 1997).

A. Notice Requirement

Plaintiff's interpretation of the Operating Agreement is that Section 7.2 modifies any section that requires Member consent, approval, or a vote.[3] Section 7.2 titled "Meetings"

3. The Operating Agreement alternately refers to Member action as "approve," "consent," or "vote."

outlines the procedures for calling, noticing, hosting, participating in, and voting at a meeting of the Members. Under Section 7, Earnest Holdings is not required to hold meetings and Section 7.2(i) titled "Action by Members Without a Meeting" establishes the procedures for voting via written consents.

> Any action required or permitted to be taken at a meeting of the Members may be taken without a meeting if one or more written consents, setting forth the action so taken or to be taken, is signed by a Majority-in-Interest of the Members, and written notice of any such action is given by the Managing member to the Members no less than two (2) business days prior to the effective date of the action. The Managing Member shall include such consent in the Company's records. The written consent of such Members has the same force and effect as a meeting vote of the Members and may be described as such in any document or instrument.

Plaintiff's position is that every action requiring Member approval must be done in accordance with Section 7 either through a meeting or with written consent pursuant to Section 7.2(i). Because the amendments at issue in this motion were approved via written consents, Plaintiff argues that Earnest Holdings was required to provide every Member, including Jessee Mahone, notice of the amendment two (2) business days before its effective date. It is undisputed that Plaintiff did not receive[4] and did not waive its rights to receive such notice, and so Plaintiff urges the Court to declare that the amendments are null and void.

Defendants, on the other hand, argue that Section 7.2 is a stand alone provision that governs meetings and actions to be taken at a meeting and only implicates those actions

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4. Notice of the amendments was not provided to Jessee Mahone two (2) business days in advance of the effective date of action in accordance with Section 7.2 (i). In March, 2004, Earnest Holdings provided Members with notice of amendments numbered 5, 6, and 7 after the effective date of each such amendment. In addition, Earnest Holding sent notice to Members in July, 2007 of amendment 8, after it was executed. Similarly, on April 2, 2008, Earnest Holdings provided notice to Members of amendment 9, which was executed on April 4, 2008, but made effective on January 1, 2008. Amendment 9, is not specifically discussed in these motions, but would be required to follow the same procedures determined necessary by this Court to amend under the terms of the Operating Agreement.

requiring approval by a Majority-in-Interest of the Members.[5] Defendants argue that provisions in the Operating Agreement requiring approval of a Super-Majority-in-Interest[6] of the Members are not bound by the procedural requirements in Section 7.2(i). Section 13.2, titled "Amendments" states that "[e]xcept as otherwise specifically provided herein, this Agreement may be amended or modified from time to time only by a written instrument approved by a Super Majority-in-Interest of the Members." In addition, other provisions in the Operating Agreement, such as Section 6.9 and 6.1 allow the terms to be modified upon the approval or consent of a Super Majority-in-Interest.[7] The amendments at issue all involve provisions requiring approval by a Super Majority-in-Interest and therefore, Defendants argue, are not modified by the notice requirements required in Section 7.2(i).

Pursuant to its Operating Agreement Earnest Holdings is not required to hold meetings, thus the Agreement contemplated actions to be taken by alternative means. Section 7.2(i), one of the alternative mechanisms, authorizes actions taken by written consents signed by a Majority-in-Interest with advance notice to Members, but does not govern all alternative actions by Members. The language of Section 7.2 "signed by a Majority-in-Interest" is not reconcilable with the language in other provisions requiring a Super

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5. "'Majority-in-Interest' of the Members at any particular time means the Member or Members owning at such time more than fifty percent (50%) of the Units owned by the Members entitled to vote with respect to the particular matter involved."

6. "'Super Majority-in-Interest' of the Members at any particular time means the Member or Members owning at such time more than eighty percent (80%) of the Units owned by the Members entitled to vote with respect to the particular matter involved."

7. Section 6.9 "Compensation" states that "compensation shall not exceed in the aggregate $100,000 per annum without the consent of a Super Majority-in-Interest of the Members." Section 6.1 "Management and Control" states that "the Managing Member shall not have the power or authority to do any of the following, without the prior approval a Super Majority-in-Interest of the Members."

Majority-in-Interest. If Section 7.2(i) was intended to establish the procedures for Super Majority-in-Interest approvals in addition to Majority-in-Interest approvals, then the Operating Agreement could have stated so. To hold otherwise reads language and terms into the Operating Agreement that are not apparent from the face of the document. For example, compare Section 13.2, which specifically states that the Operating Agreement "may be amended or modified...**only** by a written instrument approved by a Super Majority-in-Interest..." with Section 7.2(i) which provided that actions "required or permitted to be taken at a meeting" may be taken with written consents signed by a Majority-in-Interest. (emphasis added) These sections state different standards for approval (Super Majority-in-Interest v. Majority-in-Interest) and different mechanisms (written instruments v. signed written consents). Therfore, the Court concludes that Section 7.2(i) does not modify provisions requiring approval by a Super Majority-in-Interest.

Holding that Section 7.2(i) does not modify all actions to be taken by Members does not render the section meaningless. For example, Section 6.2 states that a Managing Member vacancy "shall be filled by appointment by a Majority-in-Interest of the Members." which would require that either (i) a meeting be held, or (ii) written consents be obtained pursuant to Section 7.2(i).

The requirement for additional approval and notice procedures for Member actions requiring a Majority-in-Interest is a standard risk mitigation mechanism. The additional procedures including notice to all Members for votes that require a simple Majority-in-Interest decrease the risks to minority Members of losing control over the company (and their investments). With actions requiring a Super-Majority, the additional procedures required with Majority-in-Interest votes are not as necessary because obtaining an additional 30% voting interest in the company is itself the procedural barrier to the action, not notice to

Members. This is not to say that even with these procedural safeguard against loss of control, that a minority Member will not actually lose control (i.e., the ability to influence management) over the company. Member action approval and procedural provisions are intended to mitigate these risks, but clearly as demonstrated with the facts presented in this case, cannot completely remove the control risk associated with minority member status. The only complete safeguard against loss of control is sufficient ownership interest percentages.

B. Amendments 1, 2, & 3

Amendments 1, 2, and 3 increase the amount of compensation paid to the Managing Member. Amendments 1 and 2, state "I consent to amend," but otherwise appear to be mere consents executed under Section 6.9, which allows for compensation to be increased with the "consent of a Super Majority-in-Interest". Amendment 3 uses the word "approve" and is on a document titled "Approval of Super Majority-in-Interest of the Members." Whether Amendments 1, 2 and 3 were executed pursuant to Section 13.2 as an "amendment" or pursuant to Section 6.9 is not determinative because both provisions require approval by a Super Majority-in-Interest. Therefore, Earnest Holdings was not required to follow the notice procedures in Section 7.2(i) for amendments 1, 2, and 3.

C. Amendments 4 & 5

Amendments 4 and 5 modified Section 7.6 "Additional Members". Plaintiff highlights language in Section 7.6[8] which states that "Jessee Mahone, LLC (only so long as Wendell

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8. Section 7.6 Additional Members.

> Upon the consent of a Super Majority-in-Interest of the Members, the Managing member shall have authority and shall be permitted to admit additional Members, and issue to such Members Units, on such terms and conditions as the Managing Member shall deem appropriate. ... Upon the admittance of additional Members, all Ownership Percentages of the Members and Assignees shall be diluted proportionately. Notwithstanding the foregoing, ...Jessee Mahone, LLC (only so long as Wendell M. Starke is living) shall be entitled to

M. Starke is living) ***shall be entitled to vote*** their respective Units **and** shall be taken into account for purposes of determining Super Majority-in-Interest consent...." (emphasis added). Plaintiff argues that the phrase "shall be entitled to vote" gives Jessee Mahone the limited right to cast a vote on the issue of admitting new members for so long as Wendell Starke is living. Plaintiff claims that the amendments are void because Jessee Mahone was denied the opportunity to vote on the amendments to a section in which it was guaranted voting rights. Defendants, on the other hand, argue that the phrase is a recognition of voting power and a limitation on that right, not an absolute right or requirement to cast a vote.

This issue would be determinative of the Court's decision only if Plaintiff were challenging action taken under the original Section 7.6 of the Operating Agreement. Instead, Plaintiff challenges the amendment to Section 7.6 and Earnest Holdings' subsequent actions taken pursuant to the revised section. The question before the Court on the cross motions for declaratory judgment asks whether the amendments to Section 7.6 are valid or invalid. The amendments state that they are approvals pursuant to Section 6.1, which allows the Managing Member to take actions contrary to the Operating Agreement with approval of a Super Majority-in-Interest. Whether the amendments are approvals pursuant to Section 6.1 or "amendments" pursuant to Section 13.2 is not determinative for purposes of the motion before the Court because both provisions require approval by a Super Majority-in-Interest. Therefore, Earnest Holdings was not required to follow the notice procedures in Section 7.2(i) for amendments 4 and 5.

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vote their respective Units and shall be taken into account for purposes of determining Super Majority-in-Interest consent under this Section 7.6.

D. Amendments 6, 7, 8, & 9

The Court, having found above that Section 13.2 requires approval by a Super Majority-in-Interest and therefore is not subject to the notice requirements established in Section 7.2(i), finds that Earnest Holdings was not required to follow the notice procedures in Section 7.2(i) for amendments 6, 7, 8, and 9.

E. Conclusion

The procedures in Section 7.2 do not modify the specific provisions in Sections 13.2, 6.1, 6.9, and 7.6, or any other provision requiring approval by a Super Majority-in-Interest. This interpretation respects the plain language of the contract, gives meaning and importance to all sections of the Operating Agreement, and reflects the parties' freedom of contract to structure the terms of this legal relationship as negotiated. Plaintiff's Motion for Declaratory Judgment that the Amendments are null and void is hereby **DENIED**.

Defendants sought a partial summary judgment declaring that the amendments are valid and enforceable. Plaintiff raised a limited objection to this motion on the grounds that discovery is not complete and there are outstanding issues with regard to the validity and enforceability of the amendments as executed, which Plaintiff argues, require additional analysis beyond the question of whether or not Mahone was entitled to notice. Additionally, new defendants[9] challenged the propriety of Plaintiff's petition for declaratory judgment, but did not object to Defendants' motion, on the same grounds that discovery has not yet been completed and questions of fact remain. Therefore, the Court shall refrain from ruling on Defendants' motion for declaratory judgment and shall hold Defendants' motion open for

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9. Matthew Bronfman, EP Management Pool, LLC, and Bronfman Associates III's were added to this case as new defendants pursuant to an Order of this Court dated June 18, 2008 granting Plaintiff's motion for leave to file an amended complaint naming the aforementioned parties.

supplemental briefing until ten (10) days after the close of discovery. The Court considers Defendants' motion fully briefed and argued; however, counsel may submit supplemental briefs containing new evidence and arguments on the issues discussed herein.

FIDUCIARY DUTY CLAIMS

Defendants' motion also sought summary judgment on Plaintiff's breach of fiduciary duty claims. Under Section 6.4 of the Operating Agreement, the Managing Member shall "exercise his duties with the same care and attention as a reasonable person would use in the prudent conduct of business," but owes no other fiduciary duties to the Members. Defendants argue that the same allegations form the basis of both Plaintiff's breach of fiduciary duty claims and breach of contract claims in violation of Delaware law. See, Blue Chip Capital Fund II LP v. Tubergen, 906 A.2d 827, 834 (Del. Ch. 2006); BAE Sys. North Am., Inc. v. Lockheed Martin Corp., 2004 Del. Ch. LEXIS 119, *28 (Del. Ch. Aug. 3, 2004). Plaintiff, on the other hand, argues that a second line of cases controls and that the breach of contract and fiduciary duties claims should proceed simultaneously. See, RJ Assocs. v. Health payors' Org. Ltd. Pshp., 1999 WL 550350 (1999 Del. Ch. July 16, 1999) (allowing breach of contract and breach of fiduciary duty claims to proceed simultaneously); see also, In Re Fruehauf Trailer Corp., v. Shriss W. Street, 369 B.R. 817, 830-831 (2007); Cantor Fitzgerald, L.P. v Cantor, 724 A.2d 571 (1998).

Plaintiff also argues that their breach of fiduciary duty claims are based upon self-dealing transactions such as loans, which are in addition to claims arising from the alleged breach of the Operating Agreement. Plaintiff petitions this Court for additional time to conduct discovery on these issues and requests that the Court refrain from ruling on the claim until after discovery is concluded. Therefore, the Court shall not rule on Defendants' motion for summary judgment on the breach of fiduciary duty claims and shall hold that

motion open for supplemental briefing until ten (10) days after the close of discovery. The Court considers Defendants' motion fully briefed and argued; however, counsel may submit supplemental briefs containing new evidence and arguments on the issues presented in Defendants' motion.

SO ORDERED this 8 day of Sept., 2008.

Alice D. Bonner
ALICE D. BONNER, SENIOR JUDGE
Superior Court of Fulton County
Atlanta Judicial Circuit

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