IN THE SUPERIOR COURT OF THE STATE DELAWARE

IN AND FOR NEW CASTLE COUNTY

GED O'NEILL,	)	
	)	C.A. No. N13C-02-189 JTV
Plaintiff,	)	
	)	
v.	)	
	)	
AFS HOLDINGS, LLC., a Delaware limited liability company, ARROW GLOBAL GUERNSEY LIMITED, a company incorporated in Guernsey, and SALLIE MAE, INC., a Delaware corporation,	)	
	)	
Defendants.	)	

Submitted: September 5, 2013
Decided: January 15, 2014

Thomas E. Hanson, Esq., Morris James, LLP, Wilmington, Delaware. Attorney for Plaintiff.

Kelly E. Farnan, Esq., and Katharine C. Lester, Esq., Richards, Layton & Finger, P.A., Wilmington, Delaware. Attorneys for Defendants.

Upon Consideration of Defendants'
Motion to Dismiss or, in the Alternative, to Strike
GRANTED in Part
DENIED in Part

VAUGHN, President Judge

OPINION

The plaintiff, Ged O'Neill ("O'Neill") has filed this action against defendants AFS Holdings, LLC ("AFSH"), Arrow Global Guernsey Limited ("AGGL"), and Sallie Mae, Inc., ("Sallie Mae") (collectively referred to as "Defendants") seeking a declaratory judgment and compensatory and exemplary damages in connection with a July 16, 2008 earn out agreement (the "Earn Out Agreement") and a November 27, 2008 amended agreement (the "Amended Agreement").

The Defendants have filed a motion to dismiss the complaint under Civil Rules 12(b)(1) and 12(b)(6), or in the alternative, to strike a portion of the complaint under Civil Rule 12(f).

FACTS

In September 2005, Arrow Financial International, LLC ("AFI") was created as a joint venture between Langenlewy, L.P. ("Langenlewy") and Arrow Financial Services, LLC ("AFS"), a debt purchaser owned by Sallie Mae. AFI's membership interest was held 75% by AFSH and 25% by Langenlewy. AFI, along with certain of its subsidiaries, operated under the trade name Arrow Global. Arrow Global's business model centered around purchasing distressed consumer receivables and engaging with outside collection agencies and law firms to collect the unpaid debt. Defendant Sallie Mae is a guarantor under the Earn Out Agreement.

In July 2007, Arrow Global hired O'Neill, a UK solicitor with experience in commercial law, as Commercial Director for the company. On July 17, 2007, O'Neill and Arrow Global memorialized the terms of O'Neill's employment in an employment agreement which provided for a salary, bonuses and long-term

compensation ("Long-Term Compensation") upon the occurrence of certain events. One triggering event for the payment of Long-Term Compensation was the sale of AFI. Upon such sale, the Long-Term Compensation would equal 5% of the equity value of AFI.

In late 2007, Sallie Mae decided to sell both AFS and AFI. In anticipation of such sale, Sallie Mae and AFSH entered into two agreements, one with Langenlewy, a Purchase and Sale of Limited Liability Company Interests (the "Purchase and Sale Agreement") and one with O'Neill, the Earn Out Agreement. The Purchase and Sale Agreement stated that in the event of a sale transaction involving AFI or a substantial part of its assets (defined in the Purchase and Sale Agreement as a "Transaction"), AFSH would purchase Langenlewy's membership interest in AFI at a modified price.

The Earn Out Agreement, entered into by AFSH, Sallie Mae and O'Neill provided that O'Neill would waive his rights to Long-Term Compensation in exchange for a closing payment at the close of the sale (the "Closing Payment") and three deferred payments (the "Deferred Payments") calculated at the end of certain performance periods. The performance periods commenced on January 1, 2008 and respectively ended on December 31, 2009 (the "First Performance Period"), December 31, 2010 (the "Second Performance Period") and December 31, 2011 (the "Third Performance Period"). The Earn Out Agreement required AFSH to make the Deferred Payments to O'Neill on February 1, 2010, January 31, 2011 and January 31, 2012. Section 2.2.2 of the Earn Out Agreement provides that the Deferred Payments were to be calculated as the sum of a certain minimum payment, as set forth in the Earn Out Agreement, and a Performance-Based Payment, based on a comparison of

actual "Collections"[1] made on certain accounts, portfolios and loans to certain target amounts.

In connection with the Collections , AFSH ensured that any purchaser of AFI and AFS would be obligated to provide O'Neill and Sallie Mae with certain reporting, access and audit rights, as follows:

> Buyer [AFSH] shall cause, and shall insure that, the agreements providing for any Transaction [sale of AFI or its assets] shall require the purchaser or acquirer under any such Transaction . . . to cause (a) to be prepared and delivered to Executive [O'Neill] and Guarantor [Sallie Mae] sufficient details of all Collections after the end of each quarter . . . and (b) to provide Executive and his representatives and Guarantor and its representative with reasonable access to, and reasonable and customary audit rights with respect to, the books and records of such entity relating to such of the Portfolios and Loans set forth in Exhibits A and B as may be owned or controlled by such entity. After the closing of any Transactions . . . Buyer shall take all actions necessary to have prepared and delivered on a timely basis the information specified in clause (a) and to provide the access and audit rights specified in clause (b).[2]

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[1] Section 2.2.1(b) of the Earn Out Agreement defines Collections as:
with respect to any Performance Period the sum . . . of (I) gross cash receipts collected during such Performance Period in respect of the portfolios listed in Exhibit A attached hereto (the "Portfolios"), which are all of the portfolios acquired by the Company and its subsidiaries on or before April 30, 2008, calculated in accordance with the collections recognition policies set forth in Exhibit C attached hereto. . . .

[2] Section 2.2.4 of the Earn Out Agreement.

The Earn Out Agreement further stated:

> Notwithstanding the provisions of Section 2.2.2 and 2.2.4, if following any such Transaction or Relevant Transaction [sale of AFI or its assets] Seller [Langenlewy] is not provided such reporting, access and audit rights in all material respects, as such rights are described in Section 2.2.4, and Seller [Langenlewy] has provided written notice to Buyer [AFSH] and/or transferee (with a copy to Guarantor [Sallie Mae]) of such failure to be so provided such rights and Buyer [AFSH] and /or transferee has not corrected such failure within 90 days of receipt of such notice, then until such rights are provided and complied with in all material respects, each installment of Deferred Purchase Prices affected by such failure shall be calculated and paid with the Performance Based Payment equal to the Maximum Performance Payment, without regard to the Achievement Percentage.[3]

Finally, the Earn Out Agreement provided a maximum amount payable to O'Neill equaling $2,230,769 for the Closing Payment and the Deferred Payments, and specifically $1,653,846 for the Deferred Payments alone.[4]

Instead of the joint sale of both AFS and AFI, Sallie Mae forced the sale of AFI only. To assist with the sale of AFI, the Royal Bank of Scotland Special Opportunities Fund agreed to finance a management buyout thorough Arrow Global Guernsey Holdings Limited ("AGGHL"). AGGHL purchased stock of Arrow

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[3] Section 2.2.5 of the Earn Out Agreement.

[4] Section 2.3 of the Earn Out Agreement.

Global's UK entities and AGGL purchased the non-performing loans previously held by a US subsidiary of AFI.

On November 27, 2008, prior to the buyout, AGGL entered into the Amended Agreement with O'Neill and several other entities. The Amended Agreement confirmed that the buyout constituted a Transaction under both the Purchase Agreement and the Earn Out Agreement, set the Earn Out Agreement closing date as the closing date of the Transaction and provided that AGGL assumed the deferred payment obligations of AFSH to O'Neill.

The Transaction closed on January 21, 2009, and AFSH made the closing payment to O'Neill in the amount of $576,923.08. On February 1, 2010, AGGL made the first required Deferred Payment to O'Neill. The second required Deferred Payment was made to O'Neill in February 2011.

On October 17, 2011, O'Neill contacted AGGL to inquire about his reasonable and customary audit rights of the books and records of AGGL, Arrow Global Ltd. and Strzala sp.zo.o under section 2.2.4 of the Earn Out Agreement and to serve notice that he was exercising those rights. AGGL responded and arranged for an audit to take place on March 7, 2012, after the end of the Third Performance Period, when the final figures would be available for all three Performance Periods. On March 7, 2012, O'Neill met with various employees of AGGL and Arrow Global Ltd. to perform the described audit. However, the parties could not agree on the proper nature and scope of the audit, and the audit was not completed.

_____O'Neill filed the Complaint on February 21, 2013 in which he asserted three claims for relief. Count I of the Complaint seeks a declaratory judgment that the

Defendants have failed to provide reporting, access and audit rights required under section 2.2.4 of the Earn Out Agreement within 90 days as required under section 2.2.5. Count II alleges that Defendants breached their obligations under the agreements by refusing to provide contractually obligated access and audit rights to O'Neill. Count III alleges that Defendants have breached the implied covenant of good faith and fair dealing by engaging in business practices which had the effect of reducing the amount of O'Neill's compensation. Under Counts II and III, as I understand them, O'Neill seeks additional compensation for Performance-Based Payments under section 2.2.2 of the Earn Out Agreement, and, in addition, compensation under section 2.2.5, for payments referred to therein as "Maximum Performance Payments." He also seeks exemplary damages.

STANDARD OF REVIEW

"[T]he governing pleading standard in Delaware to survive a motion to dismiss is reasonable 'conceivability.'"[5] The Court will limit its review of the motion to dismiss to the well-pleaded allegations in the complaint, but will draw all reasonable factual inferences in favor of the non-moving party.[6] In considering Defendants' motion to dismiss, the court must deny the motion unless the plaintiff could not recover under any reasonably conceivable set of circumstances.[7] This

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[5] *Cent. Mortg. Co. v. Morgan Stanley Mortg. Capital Hldgs, LLC*, 27 A.3d 531, 537 (Del. 2011).

[6] *Doe v. Cahill*, 884 A.2d 451, 458 (Del. 2005).

[7] *Cent. Mortg. Co.*, 27 A.3d at 536.

"conceivability" pleading standard asks whether there is any, even a remote, possibility of recovery.[8]

DISCUSSION

Defendants move to dismiss O'Neill's claims alleging breach of contract and breach of implied covenant of good faith and fair dealing, and for declaratory judgment, under Superior Court Civil Rule 12(b)(6) for failure to state a claim upon which relief can be granted, or under Superior Court Civil Rule 12(b)(1) for lack of subject matter jurisdiction. Defendants also move to dismiss O'Neill's exemplary damages prayer for relief arguing that O'Neill is expressly forbidden by language in the Earn Out Agreement from seeking this type of damages. Finally, Defendants move to strike specific portions of O'Neill's Complaint regarding a certain settlement agreement for containing impertinent, immaterial and scandalous information.

Defendants contend that O'Neill's declaratory judgment and breach of contract claims pertaining to section 2.2.5 should be dismissed because O'Neill does not have rights under that section. They contend that section 2.2.5 gives rights to the "Seller," and that it does so unambiguously. The Seller is defined in the recitals of the Earn Out Agreement as Langenlewy in a paragraph which refers to the Purchase and Sale Agreement. Langenlewy was a seller in the Purchase and Sale Agreement, but was not a party to the Earn Out Agreement. Langenlewy, the Defendants contend, is the party who has rights under section 2.2.5. O'Neill is referred to in the Earn Out Agreement as the "Executive." Since there is no mention of the "Executive" in

[8] *Id*. at 537.

section 2.2.5, they contend, the section has no application to O'Neill.

The Defendants are literally correct that section 2.2.5 refers to "Seller" and not "Executive." O'Neill's response, however, is that the use of the word "Seller" in section 2.2.5 is a drafting error, that the intent of the parties to the Earn Out Agreement was that section 2.2.5 give rights to him, and that but for the drafting error section 2.2.5 would have referred to "Executive," not "Seller." In fact, O'Neill contends that section 2.2.5 was lifted from the Purchase and Sale Agreement, and that when inserted in the Earn Out Agreement, through error it was not edited to refer to Executive instead of Seller to bring it into consistent whole with the Earn Out Agreement.

When the agreement is viewed as a whole, it is clear that the purpose of the Earn Out Agreement was to provide for new compensation to be given to O'Neill in place of the "Long-Term Compensation" given to him in the previous agreement. Section 2.2.5 refers to section 2.2.4 and purports to give inspection and potential compensation rights "[n]otwithstanding" section 2.2.4. I am satisfied that the words "Seller" and "Deferred Purchase Price" in section 2.2.5, in the midst of section 2 which otherwise seems to address only O'Neill's compensation, renders section 2.2.5 ambiguous.

Defendants further contend that even if O'Neill is correct in his belief that the failure to refer to "Executive" in section 2.2.5 is merely a drafting error, O'Neill has not properly plead a claim for reformation. Defendants further contend that O'Neill must plead a claim for reformation in order to obtain relief and that this Court lacks equitable jurisdiction to hear a claim for reformation.

O'Neill contends in response that reformation is not required; that the relief which he seeks may be obtained through contract interpretation; that to the extent a claim for reformation may be found to be necessary, he has adequately pled such a claim; that this Court has jurisdiction over reformation claims which seek only money damages; and that the court has jurisdiction over his claims.

Apart from O'Neill's claim for declaratory relief, he seeks only money damages. He does not ask this Court to grant him any equitable relief. At this point in the proceedings, I am not persuaded that an order or judgment of reformation is necessary or that the relief which O'Neill seeks cannot be obtained through construction of the Earn Out Agreement. Therefore, the Defendants motion to dismiss the complaint on this grounds will be denied.

The Defendants also move to dismiss Count III. They contend that the complaint fails to allege a specific implied covenant, fails to provide factual support for an implied covenant, and is barred by the statute of limitations.

To state a claim for breach of the implied covenant of good faith and fair dealing, O'Neill "must allege a specific implied contractual obligation, a breach of the obligation by the defendant, and resulting damage to the plaintiff."[9] "General allegations of bad faith conduct are not sufficient."[10] Because the implied covenant has a narrow purpose, it is only rarely invoked successfully.[11]

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[9] *Fitzgerald v. Cantor,* 1998 WL 842316, at *1 (Del. Ch. Nov. 10, 1998).

[10] *Kuroda v. SPJS Holdings, L.L.C.*, 971 A.2d 872, 888 (Del. Ch. 2009).

[11] *Id.*

Bearing in mind that the test on a motion to dismiss is one of conceivability, I find that O'Neill sufficiently alleges an implied covenant to operate Arrow Global in compliance with applicable statutory and regulatory law. He also alleges a breach of that alleged implied covenant by such alleged activities as opening thousands of accounts with more than one service, failure to maintain accurate records of the status of accounts, engaging in "short suing," suing debtors in wrong courts, and failing to keep accurate records of the status of accounts. He also alleges damages resulting therefrom. I am satisfied that O'Neill has sufficiently pled an implied covenant of good faith and fair dealing and a violation thereof to allow the claim to survive the pleading stage of the action.

With respect to the statute of limitations, the Defendants contend that O'Neill had notice of the deficiencies and business practices of which he complains during his employment at Arrow Global, a time prior to the complaint which exceeds the limitations period. However, I conclude that this contention would require me to make findings of fact which are beyond the scope of a motion to dismiss. Moreover, the statute of limitations is an affirmative defense which should be pled in an answer.[12]

_____The Defendants also move to dismiss O'Neill's claim for exemplary damages. They contend that O'Neill's exemplary damage request is barred by an express contractual waiver agreed to by the parties in the Earn Out Agreement. Section 7.6.1

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[12] Del. Super. Ct. Civ. R. 12(b); *See Kaplan v. Jackson*, 1994 WL 45429, at *2 (Del. Super. Jan. 20, 1994).

of the Earn Out Agreement prohibits any claim for exemplary or consequential damages.[13] O'Neill contends that the waiver of exemplary damages provision does not apply to his breach of implied covenant claim. He also alleges it does not apply because the alleged conduct of the Defendants was not only a breach of contract, but willfully wrong and malicious, tortious in nature, and violated regulatory and statutory laws. He also contends that the Defendants have themselves disregarded section 7.6.1 by requesting a jury trial, notwithstanding that section 7.6.2 provides that any trial will be by a judge without a jury. The Defendants, however, have since dropped that request. Notwithstanding O'Neill's contentions, I find that section 7.6.1 is a waiver of any claim for exemplary damages arising out of the contract and that all of the claims which O'Neill has pled arise out of the contract. Therefore, the Defendants motion to dismiss O'Neill's claim for exemplary damages will be granted.

Finally, the Defendants move to strike paragraphs 40 through 42 of the complaint and Exhibit D to the complaint. Superior Court Civil Rule 12(f) allows a party to move the court to strike from any pleading "redundant, immaterial, impertinent or scandalous matter."[14] Motions to strike "are not favored and are granted sparingly, and then only if clearly warranted, with doubt being resolved in

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[13] Section 7.6.1 of the Earn Out Agreement:
Notwithstanding any provision of this Agreement to the contrary, the parties to this Agreement expressly waive and forego any right to recover punitive, exemplary, lost profits, consequential or similar damages in any arbitration, lawsuit, litigation or proceeding arising out of or resulting from controversy or claim arising out of or relating to this Agreement or the transactions contemplated hereby.

[14] Del. Super. Ct. Civ. R. 12(f).

favor of the pleadings." [15]

The Defendants contend that the material included in paragraphs 40 - 42 and Exhibit D, which pertain to O'Neill's termination, is included only to disparage the Defendants. Defendants assert that these statements place Defendants in a "derogatory light" and should be stricken as immaterial, impertinent and scandalous. Additionally, Defendants contend that O'Neill included the statements as a way to relitigate his termination and circumvent an out-of-court settlement between the parties.

"The test employed in determining whether to strike is: 1) whether the challenged averments are relevant to an issue in the case and 2) whether they are unduly prejudicial."[16] Delaware courts have articulated the meaning of the terms immaterial, impertinent, and scandalous to help address the merits of a motion to strike:

> A matter is immaterial if it has no essential or important relationship to the claim for relief or the defenses being pleaded, or a statement of unnecessary particulars in connection with and descriptive of that which is material. A matter is impertinent if it contains statements that do not pertain, and are not necessary, to the issues in question. A matter is scandalous if it improperly casts a derogatory light on someone, most typically on a party to the action.[17]

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[15] *Belfint, Lyons and Shuman v. Potts Welding & Boiler Repair Co., Inc.* 2005 WL 2746332, at *2 (Del. Super. Aug. 26, 2005)

[16] *Shaffer v. Davis*, 1990 WL 81892 , at *4 (Del. Super. June 12, 1990).

[17] *Quereguan v. New Castle Cnty.*, 2010 WL 2573856, at *5 (Del. Ch. June 18, 2010) (internal quotations omitted) (quoting *Salem Church (Del.) Assocs. v. New Castle Cnty.*, 2004

The paragraphs in question may have some relevance in setting forth that the claims which O'Neill brings now were not released in a settlement agreement entered into in February 2011, and they may have some relevance by way of background in connection with O'Neill's claims of breach of contract and breach of the implied covenant of good faith and fair dealing. I am also satisfied that Exhibit D is relevant to O'Neill's claims. If either party seeks to conduct discovery or otherwise relitigate issues not relevant to O'Neill's claims in this action, application can be made to the Court for an appropriate order. I am not persuaded that either the paragraphs in issue in the complaint or Exhibit D are unduly prejudicial to the Defendants.

CONCLUSION

For the foregoing reasons, Defendants' Motion to Dismiss or, in the Alternative, Strike is ***granted in part*** with regard to O'Neill's "exemplary" damages prayer for relief and ***denied in part*** with regard to O'Neill's remaining claims.

IT IS SO ORDERED.

/s/ James T. Vaughn, Jr.

oc: Prothonotary
cc: Order Distribution
File

WL 1087341, at *2 (Del. Ch. May 6, 2004)).