IN THE COURT OF CHANCERY OF THE STATE OF DELAWARE

PAIGE CAPITAL MANAGEMENT, LLC, PAIGE OPPORTUNITY PARTNERS, L.P., PAIGE OPPORTUNITY MASTER FUND, LTD, PAIGE GP, LLC, MICHELE PAIGE and CHRISTOPHER PAIGE,

Plaintiffs,

v.

LERNER MASTER FUND, LLC, and BROOKLYN NY HOLDINGS LLC,

Defendants.

Civil Action No. 5502-CS

LERNER MASTER FUND, LLC,

Counterclaim/Third-Party Plaintiff,

v.

PAIGE CAPITAL MANAGEMENT, LLC, PAIGE OPPORTUNITY PARTNERS, L.P., PAIGE OPPORTUNITY MASTER FUND, LTD, PAIGE GP, LLC, MICHELE PAIGE and CHRISTOPHER PAIGE,

Counterclaim/Third-Party Defendants.

MEMORANDUM OPINION

Date Submitted: May 25, 2011
Date Decided: August 8, 2011

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STRINE, Chancellor.

I. Introduction

This is a dispute between a hedge fund manager and the hedge fund's seed investor. The hedge fund manager had achieved some success working for other established investment firms and hoped to strike out on her own.

She bargained with the seed investor for it to invest in the first investment fund she had ever managed on her own. The idea was that the seed investor would benefit not only from the gains on its investment, but would also share some of the fees that would be generated when the "Hedge Fund" found additional investors.

To facilitate the investment, the hedge fund manager and the seed investor negotiated a specific contract governing their relationship. That contract was executed by the seed investor and the seed investor also signed on to the Limited Partnership Agreement (the "Partnership Agreement") that would govern all investors in the Fund, because investors in the Fund were, as a formal matter, limited partners in the partnership that was the Hedge Fund.

In the specifically negotiated Revenue Sharing Agreement (the "Seeder Agreement"), the seed investor was generally precluded from withdrawing its capital for three years upon penalty of paying an identified sum of liquidated damages and could only withdraw without cost if the hedge fund manager committed a breach of fiduciary duty, lost a key individual, failed to abide by risk covenants, or materially breached the Seeder Agreement. After that time, the Seeder Agreement permitted the seed investor to withdraw without the payment of any fee.

The seed investor made its investment on October 31, 2007. During the first year or so of the investment, the hedge fund manager kept the fund invested mostly in cash or other short-term instruments, concluding that the distressed and special situation investments in which the fund was to specialize were too expensive. The hedge fund manager also made no progress in obtaining other investors.

About a year into the three-year period, the seed investor began to evaluate all of its investments in hedge funds given the weakened state of the market. It held several meetings with the hedge fund manager and came away concerned about her ability to secure other investors for the fund and her investment strategy. After some period of reflection, the seed investor informed the hedge fund manager that it would likely withdraw all of its capital at the end of the three-year lock up period in the Seeder Agreement but that if acceptable terms could be negotiated, it would prefer to withdraw sooner.

No such terms were reached and when the third anniversary of the investment approached, the seed investor, after trying once more in vain to reach a business solution to the problem, sent formal notice of its intention to withdraw its entire investment as of October 31, 2010 — the end of the three-year investment period. In response, the hedge fund manager refused to return the seed investor's capital, arguing that it was entitled to raise the "Gates" contained in the generally applicable Partnership Agreement. The "Gate Provision" enabled the hedge fund manager to restrict a withdrawal of capital if it would result in more than 20% of the total assets of the Hedge Fund being withdrawn in any six-month period. Because the hedge fund manager had never secured any other

outside investor in the Fund, the seed investor's $40 million investment comprised over 99.9% of the Fund's invested capital. The only other investor was the hedge fund manager herself, and she had only $40,000 invested, a sum that paled in comparison to the management fees she would receive by keeping the seed investor's capital locked up. Furthermore, there was no basis to conclude that the hedge fund manager's invested capital was put at risk by the return of the seed investor's capital. Rather, the Gates were erected solely for the self-interested benefit of the hedge fund manager as manager, and not for the benefit of the Fund's investors.

Litigation arose. Claims proliferated.

The central issue is contractual, however, and involves whether the hedge fund manager could use the Gate Provision in the Partnership Agreement to lock up the seed investor. In this decision, I find that the hedge fund manager was not contractually entitled to raise the Gates. The Partnership Agreement is a general agreement that specifically contemplates agreements like the Seeder Agreement between the hedge fund manager and the seed investor. When pertinent principles of contract law are considered, the terms of the Seeder Agreement setting forth the conditions and time frame under which the seed investor could withdraw must be read as exclusive and as excluding any application of the Gates, which would undercut the specifically negotiated withdrawal arrangements in the Seeder Agreement. That finding is also consistent with the expectation created by the hedge fund manager and her representatives during negotiations, when she made clear that the Partnership Agreement contemplated specific bargains with particular large investors like the seed investor and thus that the specific

deal embodied in the Seeder Agreement was in essence, the deal. Therefore, as a matter of contract law, I conclude that the hedge fund manager's refusal to honor the withdrawal request and return the seed investor's capital in full was a violation of the Seeder Agreement and a breach of contract.

Alternatively, even if the Gates were potentially applicable, I conclude that it was a breach of fiduciary duty for the hedge fund manager to use the Gates solely for a selfish reason. The only rational reason for the failure to take down the Gates was to enable the manager to continue to receive management fees for as long as possible. The manager's purported rationale was based on the manager's unconvincing assertion that the Gates in the Partnership Agreement are not only designed to protect the Fund and its investors from harm, but also as a contractual provision intended to guarantee a cash flow to the manager for a longer period of time. But that is a rationale that was never advanced in the contractual negotiations. The discretion granted to the hedge fund manager to determine whether to waive the Gates is a fiduciary authority that must be used for the benefit of those whom the Hedge Fund is intended to benefit, and not for the selfish interest of the manager. Because the decision to use the Gates was a selfish one, inimical to the interests of the Fund's 99.9% investor and not intended to, nor needed to, protect the minor investment of the hedge fund manager herself, it was a breach of the duty of loyalty.

For these reasons, I order a remedy requiring the immediate return to the seed investor of all of its capital and of an award of interest to compensate it for the delay.

Because the hedge fund manager and the seed investor have brought several other claims, I also dispose of those.

II. Factual Background

These are the facts as I find them after trial.

A. The Formation Of The Hedge Fund

After establishing a stellar academic record at some of our nation's leading higher education institutions, Michele Paige, a Yale-trained lawyer, decided to embark on a career in investing. She had some success, beginning her career with Icahn Associates before leaving for an opportunity to work at a large hedge fund, King Street. Her progress coincided with a hot time in the investment industry, as so-called "sophisticated investors," a class that legally included not just wealthy individuals but also pension funds and universities, sought to deploy their capital in investment funds of various kinds that promised to employ active trading strategies to beat the market, deliver "alpha," and thus defy the ECMH/CAPM odds.

Michele Paige wanted to take advantage of this and to be her own boss by creating a hedge fund of her own with its own investors. Thus, in May 2006, Michele Paige left her job at King Street to create her own hedge fund.

To that end, Michele Paige created a series of entities that would serve as the vehicle for the formation of the Hedge Fund that she would manage. Thus, she created Paige Capital Management, LLC, the investment manager for the Hedge Fund, Paige Opportunity Partners, L.P. and Paige Opportunity Master Fund, Ltd., the entities that

would serve as the "offshore" and "onshore" halves of the Hedge Fund,[1] and Paige GP, LLC ("Paige General Partner"), which served as the general partner of the "onshore" Fund. Together with her husband who was also a Yale-trained lawyer, Christopher Paige, Michele controlled the Paige entities and the Hedge Fund they comprised. Each of the Paige entities and each of the Paiges themselves are plaintiffs and counterclaim defendants in this case (collectively, the "Paiges").

B. <u>The Paiges Negotiate An Agreement For The Lerner Fund To Be Their Seed Investor</u>

Creating a hedge fund on paper, however, is the comparatively easy part.

The market space that Michele Paige wished to enter was one focusing on distressed and special situation investments. Indeed, Michele Paige hoped to raise enough capital to be an activist investor who could influence issuers to take value-maximizing action. These goals required that the Hedge Fund raise a large amount of capital to succeed, and Michele Paige herself was intent on raising billions, not merely millions, in funds to invest.

To embark on that successfully, a nascent fund manager needs an initial investor who will provide a base of core capital for operations and also give the hedge fund manager some lent credibility. In exchange for taking that risk, a seed investor can be rewarded with a share of the management and incentive fees that the hedge fund manager

[1] Separate onshore and offshore funds were created because certain investors preferred investing in one over the other for tax reasons. But, the funds were operated and invested in the same manner to whatever extent possible and Paige Capital Management, i.e., Michele Paige, served as the investment manager for both of the funds. Tr. at 22-23 (Michele Paige). The parties focus their energy almost exclusively on addressing the operation of the onshore fund and the Partnership Agreement that governs its operation. This opinion, therefore, will be similarly focused, but my conclusions apply equally to the Lerner Fund's capital invested in both funds.

makes on top of the investment return on its capital. In the fall of 2007, the Paiges entered into negotiations with Brooklyn NY Holdings LLC, an entity that managed the fortune of the Lerner family (the "Lerner Fund"). The Lerner family's wealth was created in the first instance by Alfred Lerner, a founder of MBNA, which was later sold to Bank of America. After his death, Alfred Lerner's son, Randy Lerner, took control of the Lerner Fund, and serves as among other things, the owner of the Cleveland Browns, which his father had owned since that venerable name was revived after a short period of dormancy when Cleveland was given a new NFL franchise in 1999.

The negotiations with the Lerner Fund centered on the drafting and execution of the Seeder Agreement that outlined the special terms of the Lerner Fund's seed investment. The relationship between the Seeder Agreement and the Partnership Agreement for the onshore portion of the Hedge Fund is central to the parties' competing positions in this case. The importance of the relationship between the two Agreements was not lost on the parties during the negotiations. The Lerner Fund sought to have a provision in the Seeder Agreement that acknowledged that the Seeder Agreement was amending the Partnership Agreement to ensure the primacy of the Seeder Agreement.[2]

The Paiges did not agree to that provision, instead insisting that the Seeder Agreement contain a provision stating that the Seeder Agreement "shall not be deemed to amend in any manner" the Partnership Agreement.[3] But, on October 18, 2007, Michele

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[2] JX-24 (Lerner Fund draft of Seeder Agreement (October 22, 2007)) (containing a provision that stated that the Seeder Agreement did not amend the Partnership Agreement "except as expressly provided for herein.").
[3] JX-2 ("Revenue Sharing Agreement" (October 31, 2007)) ("Seeder Agreement") § 9.8.

Paige sent an email to the Lerner Fund explaining the relationship between the Seeder Agreement and the offering documents generally applicable to all investors, such as the Partnership Agreement. In that email, the Paiges wrote:

> Also, we're making it clear in [the Seeder Agreement] that we're not amending the offering docs [(like the Partnership Agreement)] because the offering docs expressly permit agreements like [the Seeder Agreement] & thus, [the Seeder Agreement] doesn't conflict with the offering docs. (Technically, [the Seeder Agreement] is more like a side letter than an amendment. Frankly, I don't know why this distinction matters, so I'd leave it to the lawyers.).[4]

Her counsel sent a similar communication, assuring the Lerner Fund that the Seeder Agreement was permitted by the Partnership Agreement and creating the reasonable impression that it was understood that the terms in the Seeder Agreement governed the specific relationship between the Paiges and the Lerner Fund.[5] Consistent with that communication, the Partnership Agreement provided that the Paiges could "waive or modify" the Partnership Agreement's provisions for "certain large or strategic investors" in three areas: withdrawal fees; management fees; and incentive allocation.[6]

On October 31, 2007, the Lerner Fund and the Paiges executed both the Seeder Agreement and the Partnership Agreement and the Lerner Fund invested $40,000,000 in the Hedge Fund. At that time, the Hedge Fund had investments totaling $40,040,000,

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[4] JX-22 (email from Michele Paige to Ben Alimansky (October 18, 2007)). Although the email was sent from Michele Paige's email account, Christopher Paige wrote it. Tr. at 248-249 (Michele Paige).

[5] JX-29 (email from Michael Wolf to Daniel Berick and others (October 24, 2007)) ("The reductions in management fee and incentive allocation are permitted by the terms of the [P]artnership [A]greement without requiring an amendment. In some ways, the [Seeder Agreement] is no different than a side letter.").

[6] Partnership Agreement §§ 8.02(d), 4.04, 6.01(b).

comprised of the Lerner Fund's $40,000,000 investment and a $40,000 investment by Michele Paige. These initial investments turned out to be the only ones ever made in the Hedge Fund and the Lerner Fund and Michele Paige remain the Hedge Fund's only two investors today.

Although I will save a detailed discussion of the contractual provisions of the Seeder and Partnership Agreements for my analysis of the parties' contract claims, for purposes of understanding the factual background, some key points of the Agreements must be noted now. The basic premise of the Seeder Agreement was that the Lerner Fund agreed to "lock up" its capital in the Hedge Fund for three years and bear the additional risk associated with investing a large amount of money in an unproven fund in exchange for more favorable investment terms. What the Lerner Fund got was a share of the gross management and incentive fees that the Paiges earned,[7] as well as a reduction in the management and incentive fees that it had to pay itself,[8] and was granted extensive information rights.[9]

But, in exchange for that share in the upside, the Lerner Fund was prohibited by the Seeder Agreement from withdrawing its capital without triggering a severe liquidated damages provision until October 31, 2010, three years after the Agreement's execution. This limitation had a safe harbor that allowed the Lerner Fund to withdraw in the first three years if the Paiges breached their fiduciary duties, materially breached the Seeder

[7] Seeder Agreement § 5.1.
[8] Seeder Agreement §§ 4.1, 4.2.
[9] *See, e.g.,* Seeder Agreement § 8.2.

Agreement, or in certain other limited circumstances.[10] The liquidated damages amount was substantially higher than the amounts set forth in the Partnership Agreement for early withdrawals.[11]

As I discuss in more detail later, I find no basis to conclude that the Paiges told the Lerner Fund that the Gate Provision in the Partnership Agreement could be used to restrict the Lerner Fund from withdrawing at the end of the three-year lock up period in the Seeder Agreement.

C. The Hedge Fund Initiates Operations But No Forward Progress Occurs

During the first year of the Lerner Fund's investment, there was little interaction between the Paiges and the Lerner Fund. But nor, apparently, was there much positive action of any kind at the Hedge Fund.

On the investment front, Michele Paige was convinced that despite a slowdown in the equity markets and a substantial tightening in the debt markets, the United States had not hit bottom and that there was going to be an even greater crash.[12] Michele Paige wanted to husband the Fund's capital to deploy at that time. As a result, 2007 and much of 2008 passed with very little deployment of the Fund's capital.

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[10] The Seeder Agreement also allows the Lerner Fund to withdraw its entire investment before the third anniversary of the Agreement if Michele Paige is no longer involved with the Hedge Fund, the Hedge Fund fails to properly recruit a Chief Operating Officer, or the Hedge Fund fails to comply with certain risk covenants. Seeder Agreement §§ 6.4(a), (b), (d).

[11] *Compare* Seeder Agreement § 8.10(c) (calling for payment of 10% of the Lerner Fund's investment if the Lerner Fund withdraws its investment in the first year) *with* Partnership Agreement § 8.02(a)(ii) (calling for payment of 5% of the investor's investment if the investor withdraws its investment in the first year).

[12] JX-65 (Paige Capital Management Quarterly Investment Letter (April 15, 2008)) ("Despite recent volatility, we believe debt and equity securities remain overvalued.").

On another key front — the recruitment of other investors — the Paiges made no progress at all. By the time the Lerner Fund was signed up, the economy was already in difficulty and it was a challenging time to raise money for hedge funds. But whether it was the economy or the inability of Michele Paige and her team to impress institutional investors with their promise or some other cause, the result itself is undeniable, which is that the Paiges did not raise any additional capital. As a result, the Lerner Fund's $40,000,000 investment remained over 99.9% of the Fund's invested capital.

D. In Late 2008, The Lerner Fund Meets With The Paiges As Part Of A Reassessment Of Its Overall Investment Strategy

In the second half of 2008, about a year into the three-year lock up period established by the Seeder Agreement, Randy Lerner decided to reevaluate the Lerner Fund's overall investment strategy. Lerner wanted to move the Lerner Fund away from its initial concept of building a "portfolio of multiple strategies that would include hedge funds and private equity involvements."[13] Instead, Lerner wanted to emphasize owning operating companies and keeping the Lerner Fund's other capital in more liquid cash and cash-related instruments. The Paiges claim that the Lerner Fund was experiencing severe financial distress as of that time because the family had retained a substantial block of Bank of America stock it had received when MBNA was sold to Bank of America and the value of that stock had decreased from $40.56 per share at the beginning of 2008 to $14.08 per share by the end of 2008. Although I find this claim to have no substantial basis, for reasons I later discuss, I have little doubt that the decline in Bank of America's

[13] Tr. at 1240 (Lerner).

value and the general market conditions led the Lerner Fund to look closely at its investments and to review whether they were prudent. But, I find no reliable basis to conclude that the Lerner Fund was in emergency mode or faced a liquidity or solvency crisis.

As part of that process of portfolio review, Lerner and two of his employees at the Lerner Fund, Murray Rabinowitz and Robert Bolandian, met with the various fund managers with whom the Lerner Fund had invested.

In late 2008, representatives of the Lerner Fund met with Michele Paige four times. These were information gathering meetings that were not contentious. But the meetings instilled doubt in the Lerner Fund as to the Paiges' ability to make the Hedge Fund a success. In particular, the Lerner Fund representatives left the meetings with less confidence in Michele Paige's acumen as an investor. As noted, Michele Paige had largely kept the Fund in cash, and according to the Lerner Fund she was unable to articulate in the meetings how she was going to execute her investment strategy in the market conditions facing the Fund. As important, the Lerner Fund came away from the meetings realizing not only that the Paiges had not secured any additional investors, but also that they did not have any good prospects for doing so.

As to this topic, a delicate but inescapable point arises. Although Wall Street is hardly Milan in terms of fashion, there is a certain expectation of a crisp, professional appearance, especially for those who have not proven themselves over the long term. Likewise, there is a certain expectation about clarity, focus, and confidence in substantive presentation. The Paiges came across as more professorial than professional to the

Lerner Fund representatives, and Michele Paige, as the key person, in particular emerged as someone who was clearly very bright in an academic sense, but not so clearly equipped to handle all the tasks necessary to run a hedge fund. In particular, Randy Lerner, Rabinowitz, and Bolandian all perceived that in a challenging marketplace, a nascent fund manager like Michele Paige was going to have great trouble raising funds because her presentation skills were not up to what they felt the market was likely to expect.[14] In other words, because part of what a fund manager has to do is sell, and because Michele Paige was not perceived as good at presenting herself effectively and her human capital was the product, the Lerner Fund questioned whether it would ever gain as a seed investor from continuing with the Paiges. This sales concern was, of course, rational because the premise of its investment was that it would gain if the Hedge Fund secured other investors, and Michele Paige gave them no basis to believe this was a reasonable prospect in the coming years.

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[14] *See, e.g.,* JX-695 (email from Randy Lerner to Michael Martin and Robert Bolandian (November 15, 2008)) ("Paige. Here I'm concerned. I've met with them. And a couple of times with the head woman. Probably more than anything here is that I don't feel that they have the personalities to promote themselves to build a serious asset base. Clearly they're talented, educated people but as independent free-standing investors, I'm concerned."); Tr. at 686 (Rabinowitz) ("I also developed a contradictory notion. On the one hand, she seemed arrogant about her ability to attract and manage a large amount of capital. At the same time, she seemed incredibly lacking in confidence. She struggled to maintain eye contact. She shifted in her chair. She avoided answering questions directly.*"); id.* at 537 (Bolandian) ("Her communication skills were certainly not up to par anywhere near what a portfolio manager, hedge fund manager should be. We've been in front of plenty of hedge fund managers over time. There were certain quirks and mannerisms that were -- that sat outside the bounds of normal business interactions, therefore suggesting that if she came anywhere close to doing those types of things in front of potential investors, the immediate answer would be no.").

E. A Detour To The Gutter

Regrettably, but unavoidably, this decision must address an issue that was literally discovered during discovery in this case. At all the meetings in the autumn of 2008 and thereafter between representatives of the Lerner Fund and the Paiges, the representatives of the Lerner Fund behaved professionally and treated the Paiges with decency and respect.

But during discovery, the Lerner Fund produced emails from its files. As it happens, the key person at the Lerner Fund dealing with the investment with the Paiges was Robert Bolandian. During the course of the meetings in the fall of 2008, Bolandian began to come back to the office and engage in inappropriate and derogatory email banter about Michele Paige's appearance with certain of his male office colleagues.[15] These comments were of an insulting sexual nature. When considered from an objective perspective, the emails make Bolandian, not Michele Paige, look bad, but had to be hurtful for Michele Paige and her husband to read when they emerged in document production. By any reasonable measure, the comments are immature and degrading and the sort of thing that an adolescent bully seeking to ingratiate himself with his male buddies who are equally lacking in self-awareness and deeply, but perhaps not consciously, insecure might send.[16]

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[15] *See, e.g.*, JX-88 (email from Ron Mann to Bolandian and others (December 3, 2008)); JX-94 (email from Ron Mann to Bolandian (January 13, 2009)).

[16] I do not believe repeating the content of the emails is fair to the Paiges, although their own litigation strategy has featured them time and again. Suffice it to say that I have read them, and can best describe them as repulsive and strikingly devoid of wit. Put simply, Lorne Michaels, or even Jason Friedberg, will not be ringing up Bolandian looking to employ him.

Without in any way excusing these emails, I do pause to address an argument that the Paiges make about them. The Paiges seek to portray the emails as evidence that the Lerner Fund was inspired by personal antipathy to injure Michele Paige and that this explains its behavior toward its investment in the Hedge Fund. A careful reading of the entire record does not support that inference.

That Bolandian behaved like a boor (and a boar)[17] and that others, as we shall see, at times chimed in, does not mean that he, and certainly not the Lerner Fund's leader, Randy Lerner, took action regarding the Lerner Fund's investment in the Hedge Fund for personal reasons. To the contrary, the causal direction of this behavior seems to run in the other direction. To the extent that Bolandian interacted with Michele Paige, and even Christopher Paige, and came to regard them as not clear communicators, sloppy dressers, reluctant to share information, and not likely to yield profits for the Lerner Fund, he expressed his frustration through inappropriate crude banter with his office buddies.

This is not to excuse in any way Bolandian's wrongful behavior. But it was not a motivating factor for the Lerner Fund. If Michele Paige had been securing new investors for the Fund and had undertaken an investment plan promising good returns, Bolandian's view of her appearance or her diffidence in dealings with him would not have mattered. The bottom line concern for even Bolandian was the bottom line. In fact, people who behave like Bolandian will often do business with anyone who serves their selfish ends.

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[17] I am sure that the thought that Bolandian should lose one of the attributes of a boar has crossed the Paiges' mind.

F. The Lerner Fund Communicates Its Concerns To The Paiges And The Parties Begin To Discuss A Termination Of Their Relationship

After the four meetings in the fall of 2008 between the Lerner Fund and the Paiges, the Lerner Fund thought it would be more productive to put its concerns about the Paiges into writing rather than retread the same topics at meetings that the Lerner Fund increasingly viewed as leading nowhere. On January 20, 2009, the Lerner Fund sent a memorandum to the Paiges outlining the concerns that the Lerner Fund had developed over the course of its fall meetings with the Paiges.[18] In that memorandum, the Lerner Fund outlined three primary concerns. First, the Lerner Fund communicated that it was concerned that "the duration of opportunities [the Hedge Fund] seeks to pursue in the distressed/bankruptcy arena may exceed the remaining term of [the Lerner Fund's] investment period."[19] In other words, the Lerner Fund was worried that at the end of the three-year investment term the money in the Hedge Fund would be invested in long-term instruments and unavailable for withdrawal if the Lerner Fund chose to withdraw its capital at that time. Second, the Lerner Fund communicated its concern that the Hedge Fund had "not yet committed serious capital to the types of deep distressed/bankruptcy opportunities it hopes to identify and pursue."[20] Finally, the Lerner Fund communicated its concern that the Paiges had not been able to raise any outside capital and its

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[18] JX-95 (Memorandum from the Lerner Fund to the Paiges (January 20, 2009)).
[19] *Id.* at LMF-PAIGE 00002993.
[20] *Id.*

conclusion that the Paiges would be unlikely to successfully raise capital given the investment climate at that time.[21]

The Paiges responded to the Lerner Fund's memorandum in a letter dated January 26, 2009.[22] In that letter, the Paiges failed to respond meaningfully to the concerns raised by the Lerner Fund. Instead, the letter mischaracterizes the issues raised by the Lerner Fund and dodges the Lerner Fund's concerns and requests rather than addressing them head on.[23] Fairly read, the letter was a rather snide, contentious response that displayed a striking insensitivity, inconsistent with the normal way one would communicate with a valued client.

As a result, the Paiges' response to the Lerner Fund did nothing to assuage the Lerner Fund's concerns. Rather, the letter helped solidify the Lerner Fund's belief that the Paiges were "not [] particularly good steward[s] of [its] capital"[24] and its realization

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[21] *Id.* at LMF-PAIGE 00002994.

[22] JX-99 (Letter from the Paiges to the Lerner Fund (January 26, 2009)).

[23] For instance, in the portion of its memorandum dealing with its concerns about the Paiges' ability to redeem its capital at the end of its investment period, the Lerner Fund expressed its concern that there was a "growing likelihood that [the Paiges] will not be able to redeem [the Lerner Fund's] investment using third party capital." JX-95. In other words, the Lerner Fund was concerned that the Paiges would invest the capital that the Lerner Fund had contributed in illiquid investments that could not be easily unwound if the Lerner Fund wished to redeem and exit the Hedge Fund especially because the Paiges were unable to attract any other investors and thus, no new capital was coming in the door that could be kept more liquid and used to satisfy any redemption requests. Rather than address either of the two concerns embedded in that portion of the Lerner Fund's memorandum the Paiges retorted that they do not "repay old investors with new investors' money – that would make us a Ponzi scheme, not a hedge fund." JX-99 at LMF-PAIGE 00003363. In response to the Lerner Fund's assertion that it would be difficult for the Paiges to raise additional capital given the then-current economic environment, the Paiges outlined their fundraising efforts to date and then suggested that if the Lerner Fund was concerned that the Hedge Fund did not have adequate capital, the Lerner Fund itself should invest an additional $60 million. *Id.* at LMF-PAIGE 00003365.

[24] Tr. at 705 (Rabinowitz).

that its goal in entering into the Seeder Agreement — participating in the upside of a growing business — was unlikely to be realized because the Paiges would be unable to attract any new investors. It was after the Paiges sent the January 26, 2009 letter that the Lerner Fund decided it did not intend to stay invested in the Hedge Fund after the expiration of the three-year lock up period contained in the Seeder Agreement. In fact, Rabinowitz drafted a reply letter to the Paiges, that although he never sent, reflected the Lerner Fund's decision that it "intend[ed] to redeem its capital upon [the] conclusion of the three year investment period."[25] Instead of sending the letter that Rabinowitz had drafted, Lerner instructed Bolandian and Rabinowitz to set up a meeting with the Paiges and "express very, very clearly that . . . it [is] not our intention to go beyond the three-year period."[26]

On February 17, 2009, Bolandian and Rabinowitz met with the Paiges. Michele Paige secretly recorded the meeting. In advance of the meeting, the inappropriate internal emails at the Lerner Fund about Michele Paige continued.[27] But, the tone of the meeting was civil. At that meeting, the Lerner Fund stated, as planned, that the "relationship is going to come to a natural end" but that it "wanted to give [the Paiges] as much heads up as humanly possible."[28] The Lerner Fund expressed its desire to "have kind of a collaborative effort" moving forward about how to proceed with the remainder of the investment term, to which Christopher Paige replied, "Okay. We can work on

[25] JX-100.
[26] Tr. at 1255 (Lerner).
[27] JX-104 (email from Bolandian to Ron Mann (February 17, 2009)).
[28] JX-105 (transcript of audio recording of February 17, 2009 meeting (February 17, 2009)) at 2.

that."[29] With regards to the timing of the Lerner Fund's planned exit, there were various exchanges in the meeting in which the Paiges manifested an understanding that the Lerner Fund wished to exit the Hedge Fund sooner rather than later but was prepared to stay for the three-year investment period if no mutually agreeable exit plan could be reached before then. For instance, after joining the meeting, Christopher Paige asked the Lerner Fund: "In other words you would like to get out if we could arrange for you to get out quicker you'd be happier. Is that right?"[30] Bolandian responded "Yes" and Christopher Paige said "Okay that's fine. We can work on that."[31] When one of the Paiges' employees raised questions about the timing of the Lerner Fund's planned exit, Michele Paige stated that "I think they're open to staying *for the three years* is that correct?" to which Bolandian replied, "right."[32] Michele Paige then clarified that it was her understanding that the Lerner Fund was "open to staying *for the three years* but if but if [sic] they can get out earlier we can accommodate them."[33]

The meeting transcript thus reflects a general understanding by the Paiges that the Lerner Fund was free to withdraw its capital after three years. Neither the Paiges nor the Lerner Fund raised the issue of the Gates at the meeting. In fact, the terms of the parties' Agreements were not discussed at the meeting at all and there was no intimation by the Paiges that anything would stand in the way of the Lerner Fund withdrawing all of its invested capital after three years. The overall tone of the meeting was collegial, and

[29] *Id.* at 4.
[30] *Id.*
[31] *Id.*
[32] *Id.* at 7 (emphasis added).
[33] *Id.* (emphasis added).

Bolandian and Rabinowitz left after the parties agreed to talk a week later and "keep going back and forth until something works for both sides."[34] But, as soon as Bolandian and Rabinowitz had left the meeting, Christopher Paige declared that the Paiges were now in "litigation mode."[35]

G. <u>Throughout The Rest Of 2009, The Lerner Fund Continues To Remind The Paiges Of Their Intention To Redeem At The End Of The Three-Year Investment Period</u>

After the parties' meeting in February 2009, Bolandian became increasingly frustrated with the Paiges as business partners,[36] and soon lost hope that the Paiges and the Lerner Fund would be able to work out an early exit for the Lerner Fund from the Hedge Fund. Yet again, employees of the Lerner Fund, including Bolandian, allowed their frustration with the Paiges to spill over into inappropriate email traffic.[37] On March 16, Bolandian shared his thoughts with Lerner in an email, stating that the Paiges "most likely, internally made up their minds that they want to keep the money and not negotiate a deal."[38] In that same email, Bolandian told Lerner that he had made it "very clear to [the Paiges] to be ultra respectful of our liquidity needs."[39] Going forward, Bolandian suggested that he would be "as annoying as possible in terms of micromanaging" if the Paiges were not going to cooperate with the Lerner Fund's efforts to negotiate an early

[34] *Id.* at 8.
[35] *Id.* at 10.
[36] Tr. at 572 (Bolandian) ("[The Paiges] would not cooperate in any sense of the word in order to have conversations and/or meet.").
[37] JX- 107 (email from Ron Mann to Bolandian (March 5, 2009)).
[38] JX-111 (email from Bolandian to Lerner (March 16, 2009)).
[39] *Id.*

exit from the Hedge Fund.[40] But, Lerner rejected Bolandian's idea and instead instructed Bolandian to take a "hands-off" approach to dealing with the Paiges.[41]

After that, Bolandian communicated with the Paiges via email to remind them of the Lerner Fund's desire to redeem at the end of the three-year term and asked that the Paiges be mindful of the liquidity required to redeem the Lerner Fund at that point when making their investment decisions.[42] Bolandian's emails to the Paiges reminding them to be mindful of the Hedge Fund's liquidity with regard to the Lerner Fund's planned redemption were genial. But, throughout the remainder of 2009, Bolandian and others at the Lerner Fund continued the stream of inappropriate internal emails about Michele and Christopher Paige.[43] At one point, in August 2009, Randy Lerner himself got involved, and although not nearly as graphic as some of the emails sent by his subordinates, his inappropriate email is nonetheless indicative of the frat house attitude that permeated the staff of the Lerner Fund and the frustration they were all feeling about being unable to exit the investment with the Paiges.[44] For the most part, that environment remained

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[40] *Id.*
[41] Tr. at 1256 (Lerner); *see also* JX-148 (email from Bolandian to Lerner (August 25, 2009)) ("I know you wanted to take a hands-off approach with [the Paiges] . . . .").
[42] *See, e.g.,* JX-780 (email from Bolandian to Christopher and Michele Paige (April 6, 2009)) ("Please continue to be careful with our capital, being mindful of our liquidity and duration concerns, such that you will be in a position to distribute cash per our redemption at the end of our contract."); JX-141 (email from Bolandian to Christopher and Michele Paige (July 7, 2009)) ("Once again, just a reminder to be mindful of our liquidity needs as our redemption date approaches.").
[43] JX-121; JX-124; JX-145; JX-131; JX-147.
[44] JX-148 (email from Lerner to Bolandian (August 25, 2009)).

contained internally at the Lerner Fund, and in their meetings with the Paiges, the Lerner Fund's representatives were never anything but professional.[45]

H. Michele Paige's Investment Strategy In 2009 And Her Reasons For Pursuing It

Throughout this litigation, Michele Paige has insisted that the Lerner Fund sought to withdraw its capital from the Hedge Fund not because the Fund had poor prospects, but because the Lerner Fund was under severe economic stress as a result of the collapse in the value of the Lerner Fund's stake in Bank of America. According to Michele Paige, this was confided in her by Bolandian and Rabinowitz at another in-person meeting in the spring of 2009 at the Lerner Fund's offices. During that meeting — the date of which Michele Paige could not specify — she claims that Bolandian and Rabinowitz revealed to her the dire liquidity needs of the Lerner Fund and the fact that the Lerner Fund might need access to the capital it had invested in her Hedge Fund at a moment's notice.

As of that date, most of the Hedge Fund had been kept in very liquid positions with no big upside because Michele Paige believed the market had not bottomed. She claims that she was ready to enter the fray in spring of 2009 and to actually deploy the

[45] But, in April and October 2009, Bolandian emailed his friend at JPMorgan about Michele Paige. JX-134 (email from Bolandian to Robert Blanch (April 29, 2009)); JX-151 (email from Bolandian to Robert Blanch (October 23, 2009)). At trial, Bolandian explained that the person he emailed was not merely a business contact at JPMorgan but was also his best friend. Tr. at 489 (Bolandian). Bolandian's emails to his friend at JPMorgan represent a particularly improper example of Bolandian's poor judgment about the appropriate content of work email at the Lerner Fund and serve as yet another cautionary tale about the perils of emailing. In their post-trial briefs, the Paiges do not argue that Bolandian's emails constituted defamation, but instead argue that that they manifested contractual bad faith in that they evidenced that the Lerner Fund was undermining the Paiges' effort to attract new investors. *See, e.g.,* Pl. Op. Pre-Tr. Br. at 17; Pl. Op. Post-Tr. Br. at 25. In light of the fact that the Paiges failed to present any reliable evidence indicating that JPMorgan was ever a serious prospect to invest with the Hedge Fund and that Bolandian's communication with his friend interfered with that prospect, I cannot conclude that the Paiges suffered any harm from Bolandian's email to his friend at JPMorgan.

capital of the Hedge Fund in the type of distressed and other risky investments that would yield the superior returns the Fund promised. But she claims she balked because of her concern for the Lerner Fund.

By stark contrast, the Lerner Fund denied that the meeting occurred at all.

I conclude that the meeting likely did not occur. It is true that Bolandian initially testified in his deposition that he recalled another meeting, saying "we met in our office, I am not sure if it was March of '09."[46] Bolandian had originally testified at his deposition that he "believe[d]" the meeting was in March of 2009 but later used the errata sheet to change "believe" to "am not sure if" to "clarify the record" and "conform to the facts."[47]

There are several reasons I find that Michele Paige is likely incorrect in asserting that there was an additional in-person meeting at which Bolandian and Rabinowitz confided to her about the supposedly dire circumstances of the Lerner Fund. For starters, Rabinowitz testified that the Lerner Fund possessed no record of any in-person meeting with Michele Paige between February 17, 2009 and January 2010, and that the only context in which liquidity was ever discussed was the Lerner Fund's desire for the Paiges to maintain sufficient liquidity in the Hedge Fund to accommodate the Lerner Fund's redemption at the end of the three-year period. Consistent with that, Bolandian has no recollection of a meeting where the substance of what Michele Paige insists was conveyed was said. He and the other Lerner Fund witnesses, including Randy Lerner, deny that the Lerner Fund ever experienced a credit or liquidity crisis. Moreover, I find

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[46] Bolandian Dep. at 141.
[47] Tr. at 1169 (Bolandian).

them to be credible in saying that they never communicated any such thing to Michele Paige, and certainly not in the spring of 2009. By that time, relations between the Lerner Fund and the Paiges were strained and they had no confidence in her judgment. Given that, it seems highly unlikely that they entrusted the Paiges with what would be very sensitive information that the Lerner Fund was experiencing financial distress. Not only that, the Paiges did not submit evidence at trial showing that the Lerner Fund was experiencing a financial crisis.

Furthermore, there are no corroborating documents evidencing that this meeting occurred, where it occurred, or precisely when it occurred. That is in contrast to other meetings, about which there was a good deal of email traffic. And, of course, at the prior meeting, the Paiges had even made a surreptitious tape recording.[48] If this was such a piquant period in their relations and the meeting was as sensitive as Michele Paige describes, the absence of any written communications from her or Christopher Paige is striking. Reticence in written communication is not their trademark; nor that of their counterparts at the Lerner Fund.[49]

At bottom, therefore, I cannot find that the meeting occurred only by relying on Michele Paige's say so. I find that problematic for a few reasons. As a general matter, it is difficult to credit Michele Paige's testimony on most subjects. Perhaps because the

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[48] At that meeting the Lerner Fund stated that it was open to staying the full three years and made no mention of a liquidity crisis. *See, e.g.,* JX-105 at 7 ("Michele Paige: Well I think they're open to staying for the three years is that correct? Robert Bolandian: Right.").

[49] In fact, after the February 17, 2009 meeting, Christopher Paige was in "litigation mode." Tr. at 1096. One thing that Christopher Paige did as part of being in "litigation mode" was to create documents that would support the Paiges' position in the event of litigation. *Id.*

subject matter of this case is so important to her, her emotions about the case seemed to lead her to testify in exaggerated, hyperbolic terms,[50] often using simple questions from her counsel as a jumping off point to extensive rambling statements. The length of her statements was often not correlated with an ability to set forth a convincing recitation of factual events, with a clear narrative about who did and said what and when. Given these realities and her strong self-interest, Michele Paige's testimony alone is not something I tend to find sufficient, in general, to prove a contested fact. This is not to distinguish her entirely from many of the Lerner Fund witnesses, Bolandian in particular. But it is to say that in general, this is a case where one puts more weight on the documentary evidence than on the self-interested testimony of either side. And as to the issue at hand, this is a subject where Michele Paige is the only witness who recalls the events she contends transpired, with only weak support from even her loyal husband and co-plaintiff Christopher who "think[s]" she told him about it.[51] But, Christopher Paige prepared a March 14, 2010 letter to the Lerner Fund that goes through, in great detail, the history of the parties' dealings and specifically how those dealings have harmed the Paiges as well

[50] For instance, Michele Paige testified that it was her desire to run the Hedge Fund until she was 99 years old. Tr. at 18 (Michele Paige) ("It was a dream of mine that I wanted to start my own fund, run it until I was 99."); *id*. at 40 (Michele Paige) ("I told them I wanted to invest and I wanted -- that this was my dream. That I wanted to continue doing these vehicles for, you know, until I was 99."); *id.* at 158 (Michele Paige) ("I told them I wanted to do this until I was 99. It was my dream.").

[51] *Id.* at 1098 (Christopher Paige) ("I think I may have even walked her [to the meeting], but yes, I think she told me about it."). Christopher Paige also testified that he recalled an email being sent about the meeting, but that the email could not be found during discovery. *Id.* at 1099.

as a timeline that he prepared for litigation, and in neither of those documents does Christopher Paige mention this supposed meeting.[52]

Michele Paige's credibility is further undermined because her description at trial of why she undertook the investment strategy she did — attributing it to her concern for the Lerner Fund and its supposed liquidity crisis — is undercut by her own writings and by the credible testimony of her own sister.

Despite the fact that the Paiges only had one outside investor, they prepared investment letters that were disseminated to "Friends and Fellow Investors."[53] Those letters give a different perspective than Michele Paige's testimony on why she kept the Fund out of the market. Throughout 2009, Michele Paige believed that the market was on the verge of a downward adjustment that would create unprecedented opportunities in the distressed debt market and said so in her letters to the Paiges' investors.[54] Rather than pursuing the distressed debt investment strategy that was to be the Paiges' hallmark, therefore, Michele Paige caused the Hedge Fund to remain invested mostly in cash, and waited. But, as Christopher Paige stated in a proposed investment letter in January 2010, "[the Paiges] simply underestimated how powerful and long-lasting this government-induced speculation would be . . . . As loyal readers know, we have been expecting an unprecedented distressed debt cycle, which many now believe will never come to pass."[55]

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[52] JX-1004; JX-1225.
[53] *See, e.g.,* JX-870 (Paige Capital Management investor letter (July 15, 2009)).
[54] *See, e.g., id.* ("In short, the combined wealth of North America, Western Europe and developed Asia is about to go on sale at once-in-a-lifetime prices.").
[55] JX-967. That Michele Paige's real reason for not investing more heavily in 2009 was that she, like so many others, simply misjudged the market, rather than a meeting with the Lerner Fund is

At trial, Michele Paige's sister, who worked at Paige Capital Management from 2007 through October 2009 and again for several months in 2010, testified credibly about her understanding of Michele's view of the marketplace in 2009 and confirmed that she understood that the reason that Michele Paige did not invest heavily in 2009 was that she could "get things cheaper if she waited."[56] In fact, Jessica Paige testified that Michele had never told her about the meeting with the Lerner Fund until after this litigation was under way,[57] and that she doubted the veracity of Michele's story.[58]

For all these reasons, Michele Paige's claim that a meeting in the spring of 2009 caused her to secretly change her investment strategy without telling anyone else at the Hedge Fund about her true motivations for doing so is not one that I find convincing.

That said, I also do not ignore the reality that to the extent that Michele Paige was slow to enter the market for illiquid investments in 2007, 2008 and through much of 2009, it was also likely the case that the closer she got to the end of the three-year lock up period in the Seeder Agreement, the more she had to consider the Hedge Fund's lack of other outside investors as a factor in her investment strategy in light of the Lerner Fund's stated intention to withdraw its capital in full at the expiration of that period. But the major reason that Michele Paige had not invested any of the Lerner Fund's capital in the

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also supported by the fact that despite claiming to be totally open with her team at Paige Capital Management, Michele Paige never told anyone about the meeting in the spring of 2009. JX-105 ("Michele Paige: No no I am very open with them. To the extent that every conversation that we have I tell them exactly what we had I don't want them to think I am holding back anything or not telling them anything . . . .").

[56] Tr. at 1182 (Jessica Paige).

[57] *Id.* at 1172-75 (Jessica Paige).

[58] *Id.*

kind of investments that were intended to be the core categories for the Hedge Fund was her deep belief that a deepening of the recession was going to happen. From the inception of the Hedge Fund to well into 2009, she kept waiting for an even lower bottom before investing.

I. The Parties Meet Again In Early 2010 And Attempt To Find A Way To Amicably Unwind Their Relationship

In January 2010, the Lerner Fund reached out to the Paiges and attempted to find a business solution that would allow for an early withdrawal of its capital before filing a formal notice that it planned to redeem its investment on October 31, 2010, the end of the three-year lock up period. To that end, Bolandian and Rabinowitz met with Michele and Christopher Paige at the Lerner Fund's offices. At that meeting, the Lerner Fund offered to pay the Paiges the management fees that the Paiges would collect on the Lerner Fund's capital between January and October (the end of the three-year lock up) if the Paiges would allow the Lerner Fund to withdraw its capital immediately. The Lerner Fund gave the Paiges until February 5, 2010 to respond to its offer before it would formally submit its withdrawal notice.[59]

On February 5, Michele Paige emailed Bolandian but did not accept or reject the Lerner Fund's offer explicitly, and instead informed him that the Paiges "will agree to dissolve the [Hedge Fund] for the financial terms specified in our original agreements."[60] Almost a month later, on March 1, 2010, Michele Paige sent Bolandian the Paiges' draft agreement that would implement their proposal to permit the Lerner Fund to withdraw

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[59] JX-160 (email from Bolandian to Lerner (January 15, 2010)).
[60] JX-161 (email from Michele Paige to Bolandian (February 5, 2010)).

from the Hedge Fund "according to the terms specified in our previous agreements."[61] The proposed agreement that the Paiges sent called for the Lerner Fund to pay 5% of its total capital balance in the Hedge Fund plus legal and accounting fees in order to withdraw its money immediately.[62] That 5% figure represented the sum of the fees required for an early withdrawal in the third year under the Partnership Agreement (2%)[63] and the liquidated damages that were the remedy for a violation of the three-year lock up in the Seeder Agreement (3%).[64] In other words, the Paiges believed that their Agreements with the Lerner Fund required it to pay *both* the early withdrawal fee in the Partnership Agreement and the liquidated damages in the Seeder Agreement in order to effect an early withdrawal of its capital. The Lerner Fund did not like the Paiges' offer. Randy Lerner thought that it was "time to just let this thing go and provide [the Paiges] with a withdrawal notice."[65] Therefore, on March 11, 2010, the Lerner Fund sent the Paiges formal notice of its intention to withdraw all of its capital from the Hedge Fund on October 31, 2010.[66] In the cover letter enclosing the notice, the Lerner Fund stated that it was providing the notice "well in advance of October 31 in order to allow you sufficient time to take such actions with respect to the composition of the [Hedge Fund's] portfolios

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[61] JX-176 (email from Michele Paige to Bolandian (March 1, 2010)).
[62] *Id.* at 3, § 3(a).
[63] *See* Partnership Agreement § 8.02(a)(ii).
[64] *See* Seeder Agreement § 8.10(c).
[65] Tr. at 1258 (Lerner).
[66] JX-182 (Withdrawal Notice and Cover Letter (March 11, 2010)).

as may be necessary or appropriate in order to satisfy the withdrawal and redemption in full in cash on a timely basis."[67]

J. The Paiges React Rashly To The Redemption Notice And The Parties' Relationship Deteriorates Into Litigation

On March 14, 2010, in response to the withdrawal request, the Paiges sent the Lerner Fund a letter drafted by Christopher Paige (the "March 2010 Letter").[68] In that letter, Christopher Paige, in a purported attempt to settle the parties' dispute, uses nine single-spaced typed pages to summarize the history of the parties' dealings, and the weakness of the Lerner Fund's position. The March 2010 Letter was a hostile screed rather than a healing, conciliatory overture. In the letter, Christopher Paige suggested that the Paiges would take unilateral action harmful to the Lerner Fund if it did not accede to the Paiges' settlement demands. For instance, in the March 2010 Letter, the Paiges surface for the first time the prospect of using the Gate Provision in the Partnership Agreement to tie up the Lerner Fund's investment and to mire them in lengthy litigation:

> "[The Lerner Fund] should remember that our right to raise the [G]ates ensures that we will continue to manage your money throughout the litigation. Similarly, you should remember that you will be responsible for your pro rata share of the [Hedge Fund's] legal expenses, so — in a very real sense — you will be paying our attorneys' fees as well as your own.
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> . . . .
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> . . . [W]e are fully prepared to litigate this matter to the bitter end because we will continue to manage your money, and collect management and incentive fees, until this matter is resolved many years hence. The

[67] *Id.*
[68] JX-1004 (Letter from the Paiges to the Lerner Fund (March 14, 2010)) ("March 2010 Letter").

> economic reality, therefore, is that you cannot win because you will spend more litigating than we're fighting over.
>
> If this matter is not resolved quickly, we will mitigate our damages by investing the portfolio in the high risk, long-term, illiquid, activist securities in which we specialize, and we will turn the matter over to the [Hedge Fund's] attorneys with instructions to spend whatever it takes to defend the [Hedge Fund]. (*Please remember that you are responsible for your pro rata share of the [Hedge Fund's] expenses*.)."[69]

In threatening to raise the Gates, the Paiges never identified a justification for using the Gates in view of the Hedge Fund's investment portfolio. The only motivation for raising the Gates was to enable the Paiges to continue to receive the management fees payable under the Seeder Agreement for a longer period. The record is devoid of any basis to believe that a redemption by the Lerner Fund would impair Michele Paige's modest investment in the Hedge Fund. That is, the only way that a decision on the Gates could harm any investor in the Fund was if the Gates were raised, preventing that investor from withdrawing its capital when it desired. A decision that the Gates were not applicable or would not be employed by the Paiges did not threaten any harm to any investor in the Hedge Fund. But it did mean that the Paiges would not receive as large a management fee and would have to find new investors, or new jobs, relatively soon.

At trial, the parties hotly contested the admissibility of the March 2010 Letter. In an opinion dated May 5, 2011, I admitted the letter into evidence. In that opinion, I described two types of threats that the letter could be read as making: first, that the Paiges would "engage in improper, frivolous and delaying litigation tactics effectively using the Lerner Fund's own money, thus thwarting the ability of the Lerner Fund to get

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[69] March 2010 Letter (emphasis added).

justice;"[70] and second, that the Paiges would "invest[] the Lerner Fund's money, not to advance the best interests of the Hedge Fund or its investors, but solely to aid the self-interest of the Paiges in tying up the Lerner Fund's investment and ensuring that the Paiges could draw their management fees for the longest time possible."[71] Whether those threats constituted a breach of the Paiges' fiduciary duties is a question I will address in my analysis below, but for now, the key point is that the Paiges' March 2010 Letter, a letter which Randy Lerner found to be "personally threatening" and "predatory,"[72] led the Lerner Fund to believe that its "money was at risk."[73]

The day after receiving the March 2010 Letter, Bolandian emailed Michele Paige asking for "a list of [the Hedge Fund's] current position, and the most recent custodian statement."[74] The Lerner Fund wanted to "satisfy [itself] that the funds were, in fact, intact and basically looked for a heightened level of information to assuage [its] concerns."[75]

On March 16, at around five p.m., the Paiges responded that they would "prepare the information you requested."[76] But, less than three hours later, the Paiges changed their mind. In a second email sent at around eight p.m. on March 16, the Paiges informed

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[70] *Paige Capital Mgmt., LLC v. Lerner Master Fund, LLC*, 2011 WL 1707346, at *3 (Del. Ch. May 5, 2011).
[71] *Id.*
[72] Tr. at 1259 (Lerner).
[73] *Id.*
[74] JX-194 (email from Bolandian to Michele Paige (March 15, 2010)).
[75] Tr. at 727 (Rabinowitz).
[76] *Id.* (email from Michele Paige to Bolandian (March 16, 2010)).

Bolandian that they could not provide the Lerner Fund with the information it sought because "[the Lerner Fund's] request is unreasonable, and we cannot comply."[77]

About two months later, on May 18, 2010, the Paiges filed the first complaint in this lawsuit, seeking: 1) a declaratory judgment that the Partnership Agreement's Gate Provision allowed them to restrict the Lerner Fund's ability to withdraw all of its capital on October 31, 2010 notwithstanding the existence of the Seeder Agreement;[78] and 2) a declaratory judgment that they were entitled to indemnification from the Hedge Fund for the prosecution of their lawsuit.[79] Three days later, on May 21, 2010, the Lerner Fund filed a Summons with Notice in New York state court.[80] In that action, the Lerner Fund sought damages "in excess of $40,000,000" for "fraud and breach of fiduciary duty in connection with the [Paiges'] misrepresentations and omissions in their solicitation of funds from [the Lerner Fund] for investment purposes, and [the Paiges'] subsequent misuse of [the Lerner Fund's] funds."[81]

After the Lerner Fund filed the Summons with Notice in New York, but before it answered the Paiges' complaint in this case, the Lerner Fund continued to pursue the information it sought from the Paiges. On July 15, the Lerner Fund, via its counsel, Boies, Schiller & Flexner LLP, sent the Paiges a letter, through the Paiges' outside counsel, in which the Lerner Fund outlined its position in the dispute and its take on the

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[77] JX-194.
[78] Original Compl. ¶ 41.
[79] *Id.* ¶ 42.
[80] JX-208 (Summons with Notice filed in the Supreme Court of the State of New York (May 21, 2010)).
[81] *Id.*

events that had transpired to date.[82] In that letter, the Lerner Fund stated that "the Paiges, in breach of their legal obligations, have repeatedly refused [the Lerner Fund's] requests for information regarding the [Hedge Fund's] balances and portfolio positions,"[83] and that the Paiges had also failed to provide the Lerner Fund with 2009 audited financial statements for the Hedge Fund.[84] That letter ended with the Lerner Fund warning the Paiges that it saw "no value in continuing the fruitless discussions that [the parties] have had, and will proceed instead to a speedy judicial resolution and a judgment against [the Paiges]."[85]

But despite the Lerner Fund's apparent decision that a resort to litigation was the only way to vindicate its rights described in the July 15 letter, the Lerner Fund continued to try to get the information that it felt entitled to by the terms of the Seeder Agreement. To that end, Boies Schiller worked with the Paiges' outside counsel to arrange a time when the Lerner Fund could inspect the Paiges' books and records.[86] The parties settled on July 29, 2010 as the date on which the Lerner Fund, along with its advisor from Ernst & Young, could come inspect the Paiges' books and records at the Paiges' office.[87]

But, when the representatives of the Lerner Fund arrived at the Paiges' offices on July 29, accompanied by Ernst & Young but unaccompanied by counsel, they were met

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[82] JX-1090 (Letter from the Lerner Fund's counsel to the Paiges' counsel (July 15, 2010)).
[83] *Id.* at 2.
[84] *Id.*
[85] *Id.*
[86] *See* JX-1091 (email from the Lerner Fund's outside counsel to the Paiges' outside counsel (July 23, 2010)).
[87] *Id.* (confirming a date of July 29, 2010 for a books and records inspection at the Paiges' office).

by the Paiges' litigation counsel, refused access to the offices, and given 70 pages of documents that were "generally irrelevant," such as copies of Michele Paige's driver's license and passport, and a general ledger for Paige Capital Management showing, for instance, payment for utilities and lunches.[88]

The Lerner Fund never pursued the New York action after filing the Summons with Notice. But, on July 30, 2010, the Lerner Fund filed its answer and counterclaims in this court. The Lerner Fund's counterclaims contain four counts: 1) breach of contract against the Paiges for failing to honor their obligations under their agreements with the Lerner Fund by refusing to allow the Lerner Fund to withdraw all of its investment, violating their fiduciary duties, and not honoring the Lerner Fund's information rights; 2) a declaratory judgment count to enforce the Lerner Fund's right to withdraw all of its money without application of the withdrawal restrictions found in the Partnership Agreement, i.e., the Gate Provision; 3) breach of fiduciary duty against the Paiges; and 4) a claim for judicial dissolution under 6 *Del. C.* § 17-802 on the ground that it is no longer reasonably practicable to carry on the Hedge Fund's "business in conformity with the [P]artnership [A]greement."[89]

K. <u>This Case Is Covered By The Media And The Paiges Amend Their Complaint</u>

On October 8, 2010, a website called HedgeFund.net, which bills itself as a "leading source for hedge fund performance, news and information,"[90] published an article entitled "Cleveland Browns Owner [(Randy Lerner)] to Hedge Fund: Give My

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[88] Tr. at 736 (Rabinowitz); JX-1096.
[89] 6 *Del. C.* § 17-802.
[90] HEDGEFUND.NET, http://www.hedgefund.net (last visited July 25, 2011).

$40M Back."[91] In that article, an attorney from Boies Schiller provided information regarding the case and the Lerner Fund's claims. For instance, the article states that the "[The Lerner Fund] also lost confidence in the [H]edge [F]und because it wasn't getting the documentation that had been promised [, a Boies Schiller attorney] said."[92]

On November 24, 2010, the Paiges filed an amended complaint with a defamation count, alleging that statements in the Summons with Notice filed in New York and the statements made by the Lerner Fund's counsel to HedgeFund.net were defamatory.[93] The amended complaint also accused the Lerner Fund of violating the implied covenant of good faith and fair dealing in the Seeder Agreement by having requested that the Paiges allow it to withdraw its capital before the end of the three-year lock up if suitable arrangements could be made.[94] When October 31, 2010 arrived, the Paiges applied the Gates to the Lerner Fund, and returned only 20% of the Lerner Fund's investment. No intervening event had arisen to change the reality that the only justification for using the Gates was to ensure that the Paiges would continue to receive management fees for a

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[91] JX-229.

[92] *Id.* at 1.

[93] JX-208 (Summons with Notice (May 21, 2010)).

[94] The amended complaint contains eight counts. Count I seeks a declaratory judgment that the Paiges are entitled to apply the Gate Provision in the Partnership Agreement to the Lerner Fund's capital. Count II seeks a declaratory judgment that the Paiges are entitled to indemnification and advancement of their expenses of the litigation. Count III seeks a declaratory judgment that the Paiges are entitled to indemnification for any losses suffered as a result of this litigation. Count IV is a claim for breach of the Hedge Fund agreements by the Lerner Fund by attempting to withdraw its money early without paying the proper termination fees. Count V is a claim for breach of the Lerner Fund's alleged oral agreement to help find a replacement seed investor for the Paiges. Count VI is for breach of the implied covenant of good faith and fair dealing claiming that the Lerner Fund prevented the Paiges from enjoying the benefit of their bargain by improperly dealing with them regarding its planned withdrawal. Count VII is for breach of fiduciary duty against the Lerner Fund. And Count VIII is for defamation.

longer period of time. No rationale based on the best interests of the Hedge Fund's investors qua investors existed, and it was solely the Paiges' own self-interest that motivated the decision to erect the Gates.

III. Analysis

The parties' claims have proliferated since the filing of the Paiges' original complaint seeking a declaratory judgment relating to the interpretation of the Partnership and Seeder Agreements on May 18, 2010. But, at its heart, this remains a case about the interpretation of those Agreements. Many of the other claims either fall away or are influenced by a determination of the issue of whether the Paiges' decision to gate the Lerner Fund's capital was: 1) within its contractual authority under the Partnership Agreement in light of the parties' execution of the Seeder Agreement; and 2) whether that decision complied with the fiduciary duties owed by the Paiges to the Lerner Fund as an investor of the Hedge Fund.

Because of the centrality of these questions, I analyze them first before resolving the parties' various other claims. And, as is standard in the examination of a business law case challenging the actions of a fiduciary, I first determine whether the fiduciary had the legal authority to make the decision in question, the source of the legal authority in this case being a contract. After doing that, I determine whether, assuming there was proper legal authority, that authority was used in conformity with the fiduciary duties owed by the fiduciary.[95]

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[95] *See, e.g., Sample v. Morgan*, 914 A.2d 647, 664 n.54 (Del. Ch. 2007) (quoting Adolphe A. Berle, *Corporate Powers As Powers In Trust,* 44 HARV. L. REV. 1049, 1049 (1931)) ("That the

A. The Parties' Contract Claims

The parties' relationship in this case is governed primarily by two agreements: the generic Partnership Agreement that any investor in the Hedge Fund would sign; and the separately negotiated Seeder Agreement between the Paiges and the Lerner Fund that contained the specific terms under which the Lerner Fund would provide the Hedge Fund with its seed capital. There are two main issues about the interpretation of those Agreements in this case: 1) whether the withdrawal provisions, i.e., the Gates, in the Partnership Agreement apply at all to the Lerner Fund in light of the separately negotiated Seeder Agreement; and 2) whether the Paiges breached the Seeder Agreement in a way so as to allow the Lerner Fund to withdraw its investment immediately without penalty. The resolution of both of those issues is governed by New York law.[96]

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operation of Delaware corporate law depends importantly on the subjection of action in conformity with legal rules to equitable principles has long been understood. In an historically-important article, Adolphe Berle captured thusly the two fundamental inquiries that determine the propriety of any corporate action: '[I]n every case, corporate action must be twice tested: first, by the technical rules having to do with the existence and proper exercise of the power; second, by equitable rules somewhat analogous to those which apply in favor of a cestui que truest to the trustee's exercise of wide powers granted to him in the instrument making him a fiduciary.'").

[96] The Seeder Agreement is governed by New York law. Seeder Agreement § 9.3. Therefore, the issue of whether the Seeder Agreement was breached thereby permitting a penalty-free withdrawal is governed by New York law. Similarly, the parties agree that the issue of whether the Seeder Agreement supersedes the withdrawal provisions of the Partnership Agreement should also be determined by New York law because it is in essence an exercise in determining the effect of the Seeder Agreement on the Partnership Agreement. Pl. Op. Br. at 21 n.15 (stating that New York law governs the question of whether the Gate Provision has been superseded or amended by the Seeder Agreement); Def. Op. Br. at 47 (citing New York law in support of its argument that the Seeder Agreement superseded the Gate Provision in the Partnership Agreement).

1. The Key Terms Of The Seeder And Partnership Agreements Relating To Withdrawals

Article VIII of the Partnership Agreement deals with "Withdrawals from Capital Accounts and Retirements."[97] Section 8.02 of the Partnership Agreement addresses "Withdrawal Procedures" and establishes a system whereby limited partners may withdraw their funds from the Hedge Fund only on certain dates and only in certain amounts, and establishes fees for early withdrawals. Specifically, § 8.02(a)(ii) sets forth the general procedure for withdrawal for limited partners owning class two interests, like the Lerner Fund, and the fees associated with an early withdrawal.[98] That section provides that:

> (ii) A Limited Partner owning Class Two Interests may withdraw all or any portion of a particular capital contribution for a Class Two Interest as of the last business day of the calendar month occurring on or after the three-year anniversary of the date of such capital contribution and on each six month anniversary thereafter; provided, however, that a Limited Partner may withdraw all or any portion of a Class Two Interest prior to the three-year anniversary of the date of such capital contribution upon the payment of a withdrawal fee, payable to the Partnership according to the following schedule: (i) 5% of the withdrawal proceeds for withdrawal prior to the one-year anniversary of the date of such capital contribution, (ii) 3% of the withdrawal proceeds for withdrawals on or after the one-year anniversary of the date of such capital contribution and prior to the two-year anniversary of the date of such capital contribution and (iii) 2% of the withdrawal proceeds for withdrawals on or after the two-year anniversary of the date [sic] such capital contribution and prior to the three-year

[97] Partnership Agreement art. VIII.

[98] The only difference between class one and class two interests are the withdrawal procedures and the incentive allocation. Class one interests are shorter term interests that pay a higher incentive allocation but can withdraw without any fees after one year. *See* Partnership Agreement §§ 6.01(b), 8.02(a)(i). Class two interests are longer term interests that pay a lower incentive allocation but pay withdrawal fees for the first three years. *See* Partnership Agreement §§ 6.01(b), 8.02(a)(ii).

> anniversary of the date of such capital contribution. All withdrawal fees are payable to the [Hedge Fund].[99]

Section 8.02(a)(ii), therefore, allows limited partners like the Lerner Fund to withdraw their capital from the Hedge Fund at any time, but forces them to pay an early withdrawal fee that gets less expensive the longer the capital is left in the Fund and eventually allows for penalty-free withdrawal after the three-year anniversary of the initial capital contribution. But, the Partnership Agreement also contains another limitation on a limited partner's ability to withdraw. Section 8.02(b) of the Partnership Agreement contains the so-called Gate Provision that restricts the total amount of capital that can be withdrawn from the fund at any given time. Specifically, the Gate Provision provides:

> In all cases, if as of any withdrawal date, withdrawal requests are received that, when combined with all other withdrawal requests, would result in a withdrawal of more than 20% of the total value of the [Hedge Fund]'s net assets (the "Threshold Level"), [Paige] General Partner will reduce on a pro-rata basis the amounts requested to be withdrawn to such extent as is necessary to ensure that the Threshold Level is not exceeded and will carry forward the balance of withdrawal requests to the next earliest withdrawal date of the [Hedge Fund] and, if necessary, for successive withdrawal dates until each request has been satisfied in full (the "Gate[s]"). Withdrawal requests which have been carried forward from an earlier withdrawal date (and which have not been withdrawn by the Limited Partner) will have priority over subsequent requests.[100]

The effect of the Gate Provision, in other words, when coupled with § 8.02(a)(ii)'s timing requirements for withdrawals, is to limit the amount of withdrawals from the Hedge Fund to 20% of the total amount in the Fund in any given six-month period. In this case, because the Lerner Fund is the only investor in the Hedge Fund other than

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[99] Partnership Agreement § 8.02(a)(ii).
[100] *Id.* § 8.02(b).

Michele Paige, the Gate Provision would, in essence, only allow the Lerner Fund to withdraw 20% of its capital every six months.

But, § 8.02(d) of the Partnership Agreement provides the process for notifying the Hedge Fund of a withdrawal, and, more importantly, allows the Paiges to waive or modify the withdrawal conditions for certain investors. That section provides in relevant part that:

> [Paige] General Partner, in its sole discretion, may waive or modify the conditions relating to withdrawals for Limited Partners that are employees or affiliates of [Paige] General Partner or the [Paige Capital Management], relatives of such persons, and for *certain large or strategic investors*.[101]

The parties do not dispute that the Lerner Fund was a "large or strategic investor[]" as that term is used in the Partnership Agreement.[102] What the parties do intensely dispute is what effect, if any, the provisions of the Seeder Agreement have on the operation of the Partnership Agreement. Specifically, the parties disagree about whether by executing the Seeder Agreement, the Paiges used the authority granted to them in § 8.02(d) and "waive[d] or modif[ied]" the conditions relating to the withdrawal of the Lerner Fund's capital from the Hedge Fund. In order to analyze that issue, it is first necessary to understand the other contractual provisions of the Partnership and Seeder Agreements that bear on that issue.

Unlike the Partnership Agreement that allows a limited partner to withdraw money subject only to the Gate Provision and the requirement to pay the early withdrawal fees

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[101] Partnership Agreement § 8.02(d) (emphasis added).
[102] Tr. at 250 (Michele Paige) ("Q: Would you consider [the Lerner Fund] a large or strategic investor? A: Yes.").

set forth in § 8.02(a)(ii), the Seeder Agreement contains an explicit prohibition on any withdrawals in the first three years of the investment. Section 6.3 of the Seeder Agreement, entitled "Lock-Up" provides that:

> Notwithstanding anything to the contrary in the Partnership Agreement or the Articles, [the Lerner Fund] may not withdraw all or any portion of the [Lerner Fund's] Initial Capital Contribution and any investment returns thereon prior to the third anniversary of this Agreement, other than as expressly provided in Section 6.4.[103]

Section 6.4 then provides the Lerner Fund with a right of withdrawal (the "§ 6.4 Right of Withdrawal") that is triggered under certain circumstances. Specifically, the Seeder Agreement allows the Lerner Fund to exercise its § 6.4 Right of Withdrawal and withdraw all of its invested capital immediately without penalty if: 1) Michele Paige is no longer able to devote her full time to the operation of the Hedge Fund;[104] 2) the Hedge Fund fails to abide by certain risk covenants;[105] 3) the Paiges engage "in any activity in the course of the [Hedge Fund's] business or investment management which constitutes gross negligence, willful misconduct, a material breach of fiduciary duty, or a knowing violation of any applicable material law, regulation or order. . . .";[106] 4) the Paiges fail to hire a chief operating officer in accordance with the terms of the Agreement;[107] or 5) the Paiges materially breach the Seeder Agreement and such breach is not cured within ten days from the receipt of written notice of the breach.[108]

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[103] Seeder Agreement § 6.3.
[104] *Id.* § 6.4(a).
[105] *Id.* § 6.4(b).
[106] *Id.* § 6.4(c).
[107] *Id.* § 6.4(d).
[108] *Id.* § 6.4(e).

In other words, § 6.3 of the Agreement prohibits the Lerner Fund from withdrawing any of its invested capital for the first three years of the parties' relationship but then § 6.4 provides the Lerner Fund with various protections that gives it a right of withdrawal in the first three years in the enumerated circumstances just described.[109]

There is no reference to the Gate Provision in the Seeder Agreement. At the end of the three-year lock up period, the Seeder Agreement contains no restrictions on withdrawals and permits the Lerner Fund to withdraw all of its invested capital, at which point either party may terminate the Seeder Agreement and end the Lerner Fund's entitlement to a share of the Hedge Fund's profits. To that end, § 6.2 addresses the termination of the Seeder Agreement and provides that:

> Subject to Section 8.10, this Agreement may be terminated by either Party upon the later of (a) three years from the execution of this Agreement and (b) the date of withdrawal of all [the Lerner Fund's] Contributed Capital.[110]

Section 8.10, referenced in § 6.2, provides the remedies available to the Paiges if the Lerner Fund withdraws its funds in violation of the "covenant set forth in Section 6.3."[111]

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[109] Initially, the Lerner Fund asserted, as a basis for its breach of contract counterclaim, that the Paiges breached § 6.4(d) by way of "their [alleged] failure to recruit a replacement COO." Def. Countercl. ¶ 58. But the Lerner Fund did not press this theory of contractual liability at trial, nor did it offer any supporting arguments in its post-trial briefs or at the post-trial argument. In fact, the Lerner Fund acknowledged at the post-trial argument that it decided during the course of the litigation to abandon certain of its initial lines of argument, presumably including its argument about the Paige's failure to recruit a COO. Post-Tr. Tr. at 131-32 (Counsel for the Lerner Fund) (acknowledging that the Lerner Fund decided to abandon certain breach of contract arguments under § 6.4, including one that the Paiges' did not comply with their risk covenants).

[110] Seeder Agreement § 6.2.

[111] *Id.* § 8.10(c). Interestingly, it is not clear how the Lerner Fund could breach § 6.3. The Hedge Fund's accounts are controlled by the Paiges and there is no way that the Lerner Fund could actually effect the withdrawal of its funds without the Paiges' consent. That said, perhaps § 8.10 envisions a scenario in which the Lerner Fund confesses a breach and then is entitled to the return of its capital subject to the penalties in § 8.10.

That is, while purporting to bar all withdrawals, the Seeder Agreement also sets forth a specific remedy for a breach of that prohibition. Specifically § 8.10(c) sets forth the damages to which the Paiges are entitled if the Lerner Fund breaches § 6.3 and withdraws its funds prior to the third anniversary of the Seeder Agreement. That section provides:

> In the event that [the Lerner Fund] breaches the covenant set forth in Section 6.3 above, in addition to any of the remedies provided in Section 8.10(b) above,[112] and subject to the other terms of this Section 8.10, [the Lerner Fund] agrees to pay [Paige Capital Management] an amount equal to (i) in the event of a breach prior to the first anniversary of the date hereof, ten percent (10%) of the [Lerner Fund's] Initial Capital Contribution and any investment returns thereon; (ii) in the event of a breach subsequent to the first but prior to the second anniversary of the date hereof, four and one-half percent (4.5%) of the [Lerner Fund's] Initial Capital Contribution and any investment returns thereon; and (iii) in the event of a breach subsequent to the second but prior to the third anniversary of the date hereof, three percent (3%) of the [Lerner Fund's] Initial Capital Contribution and any investments returns thereon (in each case, without giving effect to the withdrawal resulting in a breach of Section 6.3) (such amount, as applicable, the "Termination Fee"). The Termination Fee will be due and payable without notice of demand on the date such withdrawal occurs. Notwithstanding anything else herein to the contrary, [the Paiges] shall be entitled to set-off the Termination Fee against any [of the Lerner Fund's] Contributed Capital. Each of the Parties acknowledge that the agreements contained in this Section 8.10(c) are an integral part of the transactions contemplated by this Agreement and that the Termination Fee is not a penalty, but rather is liquidated damages in a reasonable amount that will compensate [Paige Capital Management] for the efforts and resources it has expended and opportunities foregone, which amount would otherwise be impossible to calculate with precision. [113]

Section 8.10(e) states that the liquidated damages remedy that the parties fashioned in § 8.10(c), along with the other remedies provided in § 8.10, are the "sole and exclusive

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[112] Section 8.10(b) states that in the event of an uncured material breach of the Seeder Agreement by the Lerner Fund, the Seeder Agreement will immediately terminate and the Lerner Fund will be required to hold the Paiges harmless for any loss resulting from the breach.

[113] *Id.* § 8.10(c).

remedies of the Parties (and all indemnified Parties) for all disputes arising out of or relating to [the Seeder] Agreement . . . ."[114]

Finally, another important provision of the Seeder Agreement must be noted, which the Paiges stress. Section 9.8 of the Seeder Agreement bears directly on the effect of the Seeder Agreement on the Partnership Agreement and therefore is important for purposes of analyzing the relationship between the two Agreements. Section 9.8, entitled, "No Amendment to Partnership Agreement or Articles," provides that:

> This Agreement shall not be deemed to amend in any manner the Partnership Agreement or the Articles. The parties to the Partnership Agreement and the shareholders of the Offshore Master Fund shall continue to have the rights and obligations provided for under the Partnership Agreement and Articles, respectively, as in effect immediately prior hereto.[115]

The Paiges say this makes clear that the Lerner Fund is subject to the Gates. By contrast, the Lerner Fund says that the Seeder Agreement is the sort of specifically negotiated contract with a "large or strategic investor[]" that is permitted under § 8.02(d) of the Partnership Agreement.[116] The Seeder Agreement thus is an exercise of the Paiges' authority under the Partnership Agreement to waive the general withdrawal conditions for the Lerner Fund.

The key question that must be addressed, therefore, is whether by entering into the Seeder Agreement the Paiges contractually waived their ability to apply the Gates to the Lerner Fund after the third anniversary of the Lerner Fund's investment. In other words,

[114] *Id.* § 8.10(e).
[115] *Id.* § 9.8.
[116] *See, e.g.,* Partnership Agreement § 8.02(d).

does the Seeder Agreement set up a comprehensive withdrawal scheme that displaces the withdrawal provisions of the Partnership Agreement, or does the Seeder Agreement provide additional terms, with the Gate Provision of the Partnership Agreement surviving as a background provision that continues to govern the parties' relationship? It is to the resolution of that question to which I will turn shortly, but first I pause briefly to outline the parties' competing arguments with regard to the proper interplay between the two Agreements, particularly when it comes to the related question of whether the Gate Provision of the Partnership Agreement still applies to the Lerner Fund in light of the Seeder Agreement.

2. The Parties' Arguments About The Relationship Of The Seeder Agreement And Partnership Agreement With Regard To Withdrawals

The Paiges argue that the Seeder Agreement did not amend the Partnership Agreement and that therefore the Gate Provision applies to the Lerner Fund. In support of that position, the Paiges advance multiple arguments. First and foremost, the Paiges rely on the fact that § 9.8 of the Seeder Agreement expressly provides that the Seeder Agreement does not amend the Partnership Agreement.[117]

Further, the Paiges argue that the negotiating history of § 9.8 supports their position. First, Michele Paige testified that the Lerner Fund specifically asked for an exemption from the Gate Provision but that she refused. Second, the Paiges contend that the negotiating history of § 9.8 supports their claims that the Seeder Agreement did not change the parties' rights under the Partnership Agreement. Specifically, the Paiges

[117] Seeder Agreement § 9.8.

argue that the Lerner Fund proposed language in §9.8 that stated that the Seeder Agreement did not amend the Partnership Agreement "except as expressly provided for herein."[118] The Paiges then responded with a draft that removed that language and inserted language that stated that the Seeder Agreement did not amend the Partnership Agreement "in any manner."[119] The Paiges also point to an email from their lawyer to the lawyer for the Lerner Fund stating that he was "reluctant to add any language that suggests that the [Seeder Agreement] amends in any way the [Partnership Agreement]."[120]

Next, the Paiges argue that "[t]here is no evidence of any Amendment to the [Partnership Agreement]."[121] In other words, the Paiges claim that the Seeder Agreement and Partnership Agreement are not in conflict with each other and can be read to exist together. For instance, the Paiges suggest that there is no conflict between the withdrawal fees in the Agreements because the early withdrawal fees in the Partnership Agreement are payable to the Hedge Fund itself,[122] but the fees payable under the Seeder Agreement are payable to Paige Capital Management, the Hedge Fund manager.[123]

The Lerner Fund counters that the Seeder Agreement trumps the Partnership Agreement and is the document that governs the relationship between the Lerner Fund and the Paiges in the areas addressed by the Seeder Agreement, with the provisions of the

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[118] JX-24 (Lerner Fund draft of the Seeder Agreement (October 22, 2007)).
[119] JX-26 (Paiges' draft of the Seeder Agreement (October 23, 2007)).
[120] JX-29 (email from Michael Wolf to Daniel Berick and others (October 24, 2007)).
[121] Pl. Rep. Post-Tr. Br. at 6.
[122] Partnership Agreement § 8.02(a)(ii).
[123] Seeder Agreement § 8.10(c).

Partnership Agreement dealing with those areas giving way to the Seeder Agreement. In support of that position the Lerner Fund advances several arguments of its own.

First, the Lerner Fund argues that as a matter of New York contract law, when there are two documents that govern the relationship between parties and one is "specifically prepared for the transaction in question and the other a general form," the more specific document takes precedence as to "all provisions [that] are repugnant in the two documents."[124]

Second, the Lerner Fund contends that the overall structure of the Partnership Agreement and Seeder Agreement supports the Lerner Fund's position because the Partnership Agreement provides for three specific instances in which Paige General Partner can modify the Partnership Agreement for "large or strategic investors": the management fee;[125] the incentive allocation;[126] and withdrawals.[127] And, the parties chose to address each of those three areas in the Seeder Agreement.[128]

Third, the Lerner Fund argues that it is unreasonable to read the two agreements so that, after three years, the Gate Provision is applicable but the protections of the § 6.4 Right of Withdrawal in the Seeder Agreement is inapplicable. In other words, the Lerner Fund argues that under the Paiges' reading, after three years, the Paiges could run the Hedge Fund however they wanted and the Lerner Fund would have no § 6.4 Right of

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[124] Def. Op. Post-Tr. Br. at 47-48 (quoting *Oakgrove Constr., Inc. v. Genesee Valley Nurseries, Inc.,* 834 N.Y.S.2d 822, 823 (N.Y. App. Div. 2007)).
[125] Partnership Agreement § 4.04.
[126] *Id.* § 6.01(b).
[127] *Id.* § 8.02(d).
[128] Seeder Agreement arts. IV, V, VI, §§ 8.2, 8.3, 8.10(c).

Withdrawal under the Seeder Agreement *and* would be trapped by the Gate Provision of the Partnership Agreement.[129]

Finally, the Lerner Fund takes issue with the Paiges' characterization of the negotiation of the Agreements and argues that the negotiation history actually supports its position. Specifically, the Lerner Fund points out that Michele Paige and her lawyer both sent communications stressing that the Seeder Agreement was just the type of separately negotiated deal with a large or strategic investor that the Partnership Agreement contemplated in, for instance, § 8.02(d). The Lerner Fund claims that the possibility of gating the Lerner Fund's investment was never discussed during the negotiations.[130] And, if that is how Michele Paige thought that the Agreements would be read, then the Lerner Fund contends that the forthright negotiator principle requires that the Agreements be construed against her because she should have spoken up, especially in light of her awareness and stated belief that the Seeder Agreement was a side letter contemplated by § 8.02(d) of the Partnership Agreement.[131]

3. <u>The Lerner Fund's Reading Of The Agreements Is The More Reasonable Way To Read The Agreements Together</u>

Before resolving the substantive contract issue, I pause to address a preliminary issue regarding which of the Paige parties can be held liable for breach of the Partnership and Seeder Agreements. The Paiges correctly point out that neither Christopher nor

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[129] Def. Op. Post-Tr. Br at 49-50; Def. Rep. Post-Tr. Br. at 17 (quoting Gould Dep. at 99 ("I never had any discussions with anyone about the gate.")).
[130] Def. Op. Post-Tr. Br. at 50.
[131] *Id.*

Michele Paige[132] are parties to either the Seeder Agreement or the Partnership Agreement. Rather, Paige General Partner, the general partner of the Hedge Fund, and the Lerner Fund are parties to the Partnership Agreement; and Paige General Partner, Paige Capital Management, and the Lerner Fund are parties to the Seeder Agreement. Under New York law, non-parties to a contract generally cannot be held liable for violations of that contract.[133] Therefore, although I will continue to refer to the Paige parties collectively as the Paiges, neither Michele nor Christopher Paige can be held liable for a breach of the Seeder or Partnership Agreement.

I turn now to resolution of the parties' contract claims.

Under New York law, extrinsic evidence may only be considered to aid in the interpretation of an ambiguous contract.[134] In turn, a contract is only ambiguous if it is "reasonably susceptible" to more than one meaning on its face.[135] Therefore, it is only if the Seeder Agreement is reasonably susceptible to more than one meaning that I may consider the evidence of the parties' negotiations.

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[132] Michele Paige is only a party to the Seeder Agreement for the limited purposes of the section requiring her to maintain personal investments in the Hedge Fund. Seeder Agreement at 1. The Lerner Fund does not allege that that provision was violated.

[133] *Walz v. Todd & Honeywell, Inc.,* 599 N.Y.S.2d 638, 639 (N.Y. App. Div. 1993) (holding that a non-party cannot be held liable for a breach of a contract).

[134] *W.W.W. Assocs., Inc. v. Giancontieri*, 566 N.E.2d 639, 642 (N.Y. 1990) ("A familiar and eminently sensible proposition of law is that, when parties set down their agreement in a clear, complete document, their writing should as a rule be enforced according to its terms. Evidence outside the four corners of the document as to what was really intended but unstated or misstated is generally inadmissible to add to or vary the writing.").

[135] *Greenfield v. Philles Records, Inc.*, 780 N.E.2d 166, 171 (N.Y. 2002) ("[I]f the agreement on its face is reasonably susceptible of only one meaning, a court is not free to alter the contract to reflect its personal notions of fairness and equity.").

a. The Agreements Are Ambiguous With Regard To The Applicability Of The Gate Provision To The Lerner Fund, But The Lerner Fund's Reading Is Better Supported By The Text Of The Agreements

Although the reading of the Agreements urged by the Paiges, i.e., that the Gate Provision of the Partnership Agreement applies to the Lerner Fund irrespective of the terms of the Seeder Agreement, is reasonable enough to render the Agreements ambiguous on that point, the Lerner Fund's reading of the Agreements is the most reasonable way to read the Agreements together based on the text of the Agreements. Like Delaware law,[136] New York law is clear that contracts must be read as a whole and in a manner that gives effect to every provision.[137] Where there is more than one agreement that governs a contractual relationship of parties, then a court may look to the agreements to see if they have a "collective design."[138] And, where there is more than one agreement, the more specific agreement is generally given precedence over the more general.[139]

The Paiges place great weight on the fact that the Seeder Agreement does not in any way amend the Partnership Agreement. But that argument misses the point. The Partnership Agreement specifically contemplates that the Paiges may modify that Agreement's terms for "certain large or strategic investors" in three areas: management

[136] *E.g., Kuhn Const., Inc. v. Diamond State Port Corp.*, 990 A.2d 393, 396-97 (Del. 2010) ("We will read a contract as a whole and we will give each provision and term effect . . . .").
[137] *E.g., Beal Savings Bank v. Sommer*, 865 N.E.2d 1210, 1213-14 (N.Y. 2007).
[138] *Id.* at 1215.
[139] *Oakgrove Constr., Inc. v. Genesee Valley Nurseries, Inc.,* 834 N.Y.S.2d 822, 823 (N.Y. App. Div. 2007); *see also* RESTATEMENT (SECOND) OF CONTRACTS § 203(d) (1981) ("Separately negotiated or added terms are given greater weight than standardized or other terms not separately negotiated.").

fees,[140] incentive fees,[141] and withdrawal restrictions.[142] Thus, there was no need to explicitly amend the Partnership Agreement, a generally applicable document, because the Lerner Fund was just the type of "large or strategic investor[]" that the Partnership Agreement allowed the Paiges to make accommodations for without any explicit amendment. It is uncontested that the parties took advantage of those provisions in the Partnership Agreement and that therefore the Seeder Agreement *did* alter the Partnership Agreement in certain important ways with respect to the Lerner Fund. For instance, the Lerner Fund is not required to pay the 15% incentive fee to the Paiges that is specified in the Partnership Agreement.[143] Instead the parties agreed in the Seeder Agreement "to modify the incentive allocation percentage applicable to [the Lerner Fund's] Capital Account(s) to ten percent (10%)."[144] Similarly, the Lerner Fund is not required to pay the 1.5% management fee that is specified in § 4.04 of the Partnership Agreement.[145] Instead the parties again agreed to "modify the management fee percentage applicable to [the Lerner Fund's] Capital Account(s)" and require the Lerner Fund to pay a management fee dependent on the amount of assets the Paiges had under management.[146] The fact that the parties took advantage of the Partnership Agreement's permission to make exceptions for "large or strategic investors" with regard to the incentive and management fees lends weight to the Lerner Fund's argument that the sections of the Seeder Agreement that deal

[140] Partnership Agreement § 4.04.
[141] *Id.* § 6.01(b).
[142] *Id.* § 8.02(d).
[143] *Id.* § 6.01(b).
[144] Seeder Agreement § 4.2.
[145] Partnership Agreement § 4.04.
[146] Seeder Agreement § 4.1.

with withdrawals were also meant to supplant the sections of the Partnership Agreement dealing with withdrawals, including the Gate Provision.

That reading is also bolstered by the fact that § 8.10, the section that spells out the remedy for a breach of the withdrawal restriction in the Seeder Agreement, provides the "sole and exclusive" remedy for such a breach.[147] If the Paiges' reading of the two Agreements was correct, then the damages provided for in the Seeder Agreement would be layered on top of the early withdrawal fees provided for in the Partnership Agreement. But, the terms of § 8.10(e) make clear that the liquidated damages remedy provided in the Seeder Agreement is the sole and exclusive remedy of the parties for an early withdrawal of the Lerner Fund's capital, and by agreeing to the Seeder Agreement, the Paiges agreed that the remedy for such an early withdrawal would be the damages provided in the Seeder Agreement to the exclusion of the early withdrawal fee that other investors in the Hedge Fund would have to pay under the terms of the Partnership Agreement.

The Paiges insist that the damages provision of the Seeder Agreement is not in conflict with the early withdrawal fees in the Partnership Agreement because the fees in the Partnership Agreement are "payable to the Partnership" (i.e., the Hedge Fund),[148] but the fees in the Seeder Agreement are paid to Paige Capital Management,[149] the investment management company that operates the Hedge Fund. That argument fails for two reasons. First, the plain terms of § 8.10(e) dictate that the remedy found in the

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[147] *Id.* § 8.10(e).
[148] Partnership Agreement § 8.02(a)(ii) ("All withdrawal fees are payable to the Partnership.").
[149] Seeder Agreement § 8.10(c) ("[The Lerner Fund] agrees to pay [Paige Capital Management] . . . .").

Seeder Agreement is the "sole and exclusive" remedy and it "replaces all other rights and remedies that any of the Parties may have under any law, rule, regulation *or otherwise*."[150] The "Parties" to the Seeder Agreement were the Lerner Fund, Paige Capital Management, and Paige General Partner. Therefore, by executing the Seeder Agreement, Paige General Partner, the general partner in the Partnership Agreement, had all the other remedies that it might have been entitled to as a result of the Lerner Fund's early withdrawal — i.e., the withdrawal fees found in the Partnership Agreement — replaced by the liquidated damages found in the Seeder Agreement. In that sense, it is immaterial that the fees provided for in the Partnership Agreement were payable to the "Partnership." Second, even if that were not the case, the reality is that the Paiges control the Hedge Fund, Paige Capital Management, and Paige General Partner. Therefore, the fact that in negotiating the Seeder Agreement they chose to have the liquidated damages payable to one of those entities (Paige Capital Management, the one that benefitted the Paiges personally the most), as opposed to another entity, does nothing to persuade me that the liquidated damages provision was somehow meant to protect some distinct interest of Paige Capital Management as opposed to being simply a choice made by the Paiges as to where those funds were to be paid. The Paiges locked the Hedge Fund in to that choice as the general partner by the exclusive remedy provision of the Seeder Agreement.

The Lerner Fund's reading of the Agreements is also more reasonable because reading the Agreements so that Article VI (relating to withdrawals) of the Seeder

[150] Seeder Agreement § 8.10(e) (emphasis added).

Agreement does not amend the Partnership Agreement's Gate Provision leads to unreasonable results. In essence, the relationship between the parties established by the two Agreements can be viewed as having two distinct time periods: the first three years; and everything after the first three years. During both of those time frames, the interpretation of the Agreements urged by the Paiges — i.e., that the Gates in the Partnership Agreement survived the enactment of the Seeder Agreement unscathed — leads to unreasonable results.

During the first three years, the Seeder Agreement prohibits the Lerner Fund from withdrawing its capital from the Hedge Fund but provides certain safety valves that would trigger the § 6.4 Right of Withdrawal. For instance, if the Paiges breached their fiduciary duties or materially violated the terms of the Seeder Agreement, the Lerner Fund would be allowed to withdraw its capital. Under the pure version of the Paiges' position, even such a withdrawal would be subject to the Gates that the Paiges claim remain in full effect despite the Seeder Agreement. At trial, Michele Paige backpedaled from that position and acknowledged that if the § 6.4 Right of Withdrawal was triggered, then the Gates would not apply.[151] In other words, Michele Paige acknowledged that the Gates were in fact altered by the Seeder Agreement during the first three years of the parties' relationship. That acknowledgement was necessary because otherwise the Paiges' position led to the strained proposition that the safety provided to the Lerner Fund

[151] Tr. at 393 (Michele Paige) ("[B]ecause under the § 6.4 [R]ight of [W]ithdrawal, it's irrespective of [the] [G]ates.").

by the § 6.4 Right of Withdrawal in the Seeder Agreement could be undermined by a residual application of the Gates.

Under the pure version of the Paiges' position, another issue arises. If the Lerner Fund could withdraw its capital in the first three years because an event triggered a § 6.4 Right of Withdrawal, the Paiges would claim that even though the Lerner Fund would not be subject to the liquidated damages provision of the Seeder Agreement, it would still have to pay the early withdrawal fee under the Partnership Agreement. This scenario also supports the inference that the withdrawal provisions of the Seeder Agreement displaced the withdrawal provisions of the Partnership Agreement as the Lerner Fund argues.

After the three-year lock up period in the Seeder Agreement, the Paiges' position leads to a different but related problem. On its face, the Seeder Agreement does not restrict the Lerner Fund's ability to withdraw its capital after three years and therefore the protection granted to the Lerner Fund by the § 6.4 Right of Withdrawal in that Agreement does not apply after three years. Therefore, under the Paiges' reading of the Agreements, the Lerner Fund would be subject to the Gates after three years but the protections afforded by the § 6.4 Right of Withdrawal in the Seeder Agreement would not apply. It is not reasonable to read the Seeder Agreement in a way that would deprive the Lerner Fund of those protections but keep it subject to the Gate Provision in the Partnership Agreement so that it would be unable to withdraw all of its money after three years *even if*, for instance, the Paiges breached their fiduciary duties or materially breached the Seeder Agreement.

As a business matter then, the Lerner Fund's reading of the Agreements makes more sense. The Lerner Fund contends that the Seeder Agreement creates a comprehensive withdrawal scheme that displaces the Gates in the Partnership Agreement. In that regard, the Lerner Fund's claim is strengthened by the fact that the Seeder Agreement does create a comprehensive and logically cohesive withdrawal scheme. As the seed investor, the Lerner Fund committed in the Seeder Agreement to stay invested in the Hedge Fund for three years. But, they secured the § 6.4 Right of Withdrawal that would allow them to exit the investment early and without penalty if the Paiges, for instance, violated the Seeder Agreement or breached their fiduciary duties. After the three-year lock up was over, the withdrawal scheme in the Seeder Agreement then allows the Lerner Fund to withdraw all of its capital at any time, rendering the protections of the § 6.4 Right of Withdrawal unnecessary. Similarly, after year three, the Seeder Agreement can be terminated by either party once the Lerner Fund withdraws all of its capital.[152] That means that after three years, the Lerner Fund is free to withdraw all of its funds at which point the Paiges could terminate the Seeder Agreement so that the Lerner Fund no longer shared in the Hedge Fund's profits and management fees. If, on the other hand, the Paiges' reading of the Agreements was correct, a situation could arise after three years where the Lerner Fund wished to withdraw all of its capital, the Paiges used the Gates to keep the Lerner Fund invested, the Lerner Fund would not have any of the protections of the § 6.4 Right of Withdrawal in the event that, for instance, the Paiges

[152] Seeder Agreement § 6.2. After five years, the Seeder Agreement gave the Paiges the right to "buy back" the Lerner Fund's revenue sharing rights for a calculated fee. Seeder Agreement § 5.4.

breached their fiduciary duties[153] or materially breached the Seeder Agreement,[154] and would have its capital tied up by the Gates until it could completely withdraw, a process that could take many years if the Paiges continued to apply the Gates.[155]

In sum, the Lerner Fund's reading of the two Agreements that the Seeder Agreement was the parties' deal about the conditions of withdrawal, with the Partnership Agreement giving way, is better supported by the text of those Agreements. But, because the Paiges' reading is a reasonable, albeit strained, one, it is proper to examine the negotiating history of the Agreements in order to see which meaning was intended by the parties.

b. The Bargaining History Also Supports The Lerner Fund's Position

That the Lerner Fund's reading of the Agreements is the more reasonable reading is confirmed by the bargaining history of the Agreements. As an initial matter, it is important to note that the Seeder Agreement was the document on which the parties focused in the negotiations. The more generally applicable Partnership Agreement was only agreed to in final form after the negotiation of the Seeder Agreement was complete.[156] The parties disagree about two key aspects of the negotiating history of the Agreements. First, they disagree about whether the Lerner Fund specifically sought an exemption from the Gate Provision of the Partnership Agreement during the negotiations.

[153] *Id.* § 6.4(c).
[154] *Id.* § 6.4(e).
[155] For instance, if the Lerner Fund remained the only investor in the Hedge Fund and tried to withdraw all of its capital as quickly as it could but the Paiges used the Gates, the Lerner Fund would still have over $4 million invested in the Fund after five years.
[156] Alimansky Dep. at 158-59.

Second, they disagree about the import of § 9.8, the section that states that the Seeder Agreement does not amend the Partnership Agreement, and how the history of that provision bears on its meaning.

As to the first issue, Michele Paige testified that during the negotiations of the Seeder Agreement, the Lerner Fund specifically asked to be exempted from the Gates and she refused because the Gates were important to her.[157] Her testimony on this was sketchy, but she claims that the Gates were intended to be a contractual tool to protect Paige Capital Management and Paige General Partner's fee stream and business interests.[158] Her testimony is vague, but she says she told the Lerner Fund why the Gates were important to her and refused to remove the Gates.[159] But, the person that Michele Paige says she spoke with at the Lerner Fund about waiving the Gate Provision for the Lerner Fund, Jared Gould, testified that he never had any discussions with anyone about the Gate Provision in the Partnership Agreement.[160] Frankly, this is a case where I do not place great weight on the unsupported testimony of either party. Importantly, however, there is no documentary evidence that the Lerner Fund requested that the Gate Provision specifically be waived during negotiations, no email seeking such a waiver, and no draft of one of the Agreements offered by the Lerner Fund effecting such a waiver. Nor is there any written retort by Michele Paige or her representatives. This is at odds with the bargaining record on other issues, where there was a written give and take. In light of

[157] Tr. at 85 (Michele Paige).
[158] *Id.* at 84-86 (Michele Paige) (stating that Jared Gould of the Lerner Fund called her and requested that the Lerner Fund be exempted from the Gates).
[159] *Id.* at 85-86 (Michele Paige).
[160] *Id.* at 1172 (Gould).

that dearth of supporting evidence, I am not inclined to give credence to Michele Paige's self-interested testimony that the Lerner Fund requested a waiver of the Gate Provision during negotiations and was rebuffed by the Paiges. For reasons I later reiterate, I believe that this case would have never arisen if events were as Michele Paige claims. If Michele Paige, an unproven investment manager, had, as she suggests she did, told a large investor like the Lerner Fund that she wanted the right to gate its capital to protect her fee stream, the Lerner Fund would have refused to invest with her.

What little documentary evidence exists about the history of the negotiation of the Seeder Agreement, and in particular its effect on the Partnership Agreement, supports the Lerner Fund's proposition that the Seeder Agreement was the deal between the parties and contained the terms that would govern their relationship. The record reflects that the Lerner Fund attempted to make clear during the drafting of the Seeder Agreement that the Seeder Agreement would alter its rights under the Partnership Agreement, and proposed language for what would become § 9.8 that stated that the Seeder Agreement was not amending the Partnership Agreement "except as expressly provided for herein."[161]

The Paiges rely on the fact that § 9.8 of the Seeder Agreement was amended during the negotiations to make clear that the Seeder Agreement did not amend the Partnership Agreement. But, critically, Michele Paige told the Lerner Fund that § 9.8 as the Lerner Fund had suggested it was not necessary precisely because the Partnership Agreement allowed for separately negotiated side deals like the Seeder Agreement.[162]

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[161] JX-24 (Lerner Fund draft of the Seeder Agreement (October 22, 2007)).
[162] JX 22 (email from Michele Paige to Ben Alimansky (October 18, 2007)).

For instance, less than two weeks before the parties signed the Agreements, in an October 18, 2007 email to the Lerner Fund, Michele Paige states:

> Also, we're making it clear both here & in Section 9.8 that we're not amending the offering docs [i.e., the Partnership Agreement] because the offering docs expressly permit agreements like ours & thus, *our agreement doesn't conflict with the offering docs*. (Technically, *our agreement is more like a side letter than an amendment*. Frankly, I don't know why this distinction matters, so I'd leave it to the lawyers.)[163]

The Paiges' outside counsel described the relationship between the Seeder Agreement and the Partnership Agreement in similar terms in an October 24, 2007 email to the Lerner Fund's counsel stating that "[t]he reductions in management fee and incentive allocations are permitted by the terms of the [P]artnership [A]greement without requiring an amendment. In some ways, the [Seeder Agreement] is no different than a side letter."[164] The terms of the Partnership Agreement permitting this were what would become §§ 4.04, 6.01(b), and 8.02(d) of the Partnership Agreement which allow the Paiges to "waive or modify" the management fees, incentive fees, and withdrawal conditions for "certain large or strategic investors" like the Lerner Fund.[165]

In other words, during the negotiation of the Agreements, the Lerner Fund sought to insert language that made clear that the Seeder Agreement would be amending the Partnership Agreement, and the Paiges rejected that notion not because the Seeder Agreement would not be altering the Lerner Fund's rights, but because such contractual language was *unnecessary* given the Partnership Agreement's specific contemplation of

[163] *Id.* (emphasis added).
[164] JX-29 (email from the Paiges' counsel to the Lerner Fund's counsel (October 24, 2007)).
[165] Partnership Agreement §§ 4.04, 6.01(b), 8.02(d).

side deals like the one with the Lerner Fund. That history explains the apparent conflict between § 9.8 and the other terms of the Partnership and Seeder Agreements and supports the Lerner Fund's position.

During the parties' attempts to find a mutually agreeable exit plan in early 2010, the Lerner Fund's internal email traffic mentioned application of the Gate Provision.[166] For instance, on February 8, 2010, Randy Lerner emailed Bolandian saying that he should "sit with [Michele Paige] immediately and hear what she has in mind – [G]ates etc."[167] Bolandian responded that "bringing up the Gate[s] will be tricky. I would hate to bring undue attention to it . . . ."[168] The Paiges latch on to those emails as evidence that the Lerner Fund "knew that the [G]ates applied."[169] But, those emails are hardly an admission from the Lerner Fund that the Paiges had a right to apply the Gate Provision to its investment. Rather, they are better understood as a recognition by the Lerner Fund that the Paiges were resistant to allowing the Lerner Fund to withdraw and might well use any means possible to thwart a withdrawal. Notably, during the February 2009 meeting and at earlier times, the Paiges did not refer to the Gates. The first time the Paiges mentioned the Gate Provision was in Christopher Paige's hostile March 2010 Letter.[170]

At bottom, the Seeder Agreement is best viewed exactly as the Paiges described it during negotiations, as a side letter permitted by the Partnership Agreement; a side letter

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[166] *See, e.g.,* JX-160 (email from Bolandian to Lerner (January 15, 2010)) ("There was no discussion of a gate – we obviously did not bring it up.").
[167] JX-166 (email from Lerner to Bolandian (February 8, 2010)).
[168] *Id.*
[169] Pl. Op. Post-Tr. Br. at 18.
[170] Tr. at 384 (Michele Paige).

that contains the specific terms of the deal between the Lerner Fund and the Paiges. It is important to remember the underlying nature of both the Agreements. The Partnership Agreement was meant to serve as the standard agreement for all investors in the Hedge Fund — a large number of investors if the Paiges' expectations were realized. That meant that two years into the parties' relationship there could have been dozens of investors in the Hedge Fund, all of whom, other than the Lerner Fund, would have their rights and obligations governed by the Partnership Agreement. In that sense, it was critical for the Seeder Agreement to make clear in § 9.8 that the lowercase "p" "parties to the Partnership Agreement"[171] would not have their rights or obligations changed by the Seeder Agreement. Rather, the Seeder Agreement changed the rights and obligations of only the capital "P" Parties to the Seeder Agreement, i.e., the Lerner Fund and the Paiges, by taking advantage of the Paiges' ability under the Partnership Agreement to waive or modify provisions for "certain large or strategic investors,"[172] and it changed them in three important ways: the management fee; the incentive fee; and withdrawal rights. Therefore, by executing the Seeder Agreement with the Lerner Fund, the Paiges waived their right under the Partnership Agreement to wield the Gate Provision of that Agreement against the Lerner Fund. Instead, the withdrawal rights of the Lerner Fund are governed by the Seeder Agreement, and after the three-year lock up period expired on October 31, 2010, the Lerner Fund was entitled to an immediate return of *all* of its invested capital. The Paiges' refusal to do so was thus a breach of contract.

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[171] Seeder Agreement § 9.8. Elsewhere in the Seeder Agreement, the Paiges and the Lerner Fund are referred to as the "Parties," with a capital "P." *See*, *e.g*., Seeder Agreement § 8.10(c).
[172] *See, e.g.,* Partnership Agreement § 8.02(d).

4. Even If The Paiges Had Not Contractually Waived The Gate Provision In The Seeder Agreement, Their Fiduciary Duties Would Have Required Them To Waive The Gate Provision For The Lerner Fund

The Lerner Fund argues that, in addition to being a breach of contract, it was also a breach of fiduciary duty for the Paiges not to waive the Gate Provision for the Lerner Fund and return all of its capital after the expiration of the three-year investment term on October 31, 2010.

As the Lerner Fund acknowledges, the Gate Provision in § 8.02(b) states that "if as of any withdrawal date" the Hedge Fund receives withdrawal requests in excess of 20% of the Hedge Fund's net assets, then "[Paige] General Partner *will* reduce on a pro-rata basis the amounts requested to be withdrawn" so that no more than 20% of the Hedge Fund's net assets are withdrawn.[173] But the Lerner Fund then notes that the mandatory language is tempered by the language in § 8.02(d) that says that "[Paige] General Partner, in its sole discretion, may waive or modify the conditions relating to withdrawals . . . for certain large or strategic investors."[174] The Lerner Fund thus argues that even if the Gate Provision had force, Paige General Partner had a fiduciary duty to consider in good faith whether to use the Gates against the Lerner Fund, which was a "large or strategic investor[]" that was clearly requesting that all of its capital be returned. If the use of the Gates by Paige General Partner was not justified by a proper purpose, but only by the self-interest of Paige General Partner and its affiliates (such as Michele Paige and the investment manager, Paige Capital Management), then the Lerner Fund contends that the

[173] *Id.* § 8.02(b) (emphasis added).
[174] *Id.* § 8.02(d).

use of the Gates was a breach of fiduciary duty. As relief for that breach, the Lerner Fund seeks to have all of its capital returned.

The Paiges advance two types of arguments with regard to whether a failure to waive the Gate Provision was a violation of their fiduciary duties. First, the Paiges argue that by naming not only Paige General Partner, but also Paige Capital Management and Michele and Christopher Paige as defendants in its claim for breach of fiduciary duty, the Lerner Fund improperly attempts to impose fiduciary duties on parties that do not owe such duties to the Lerner Fund. Second, the Paiges argue that it was not a violation of Paige General Partner's fiduciary duty to refuse to waive the Gate Provision because the Partnership Agreement provides Paige General Partner with the "sole discretion" to waive or modify the Gates.[175] I will address each type of argument in turn.

I begin with the Paiges' arguments regarding which Paige parties owe fiduciary duties to the Lerner Fund. Before turning to that argument, however, I pause to note a few critical facts regarding the structure of the Paige entities and the authority vested in them by the Partnership Agreement. Although neither party is precise in their briefing when addressing which entity was charged with making the decision whether to waive the Gate Provision,[176] the terms of the Partnership Agreement clearly entrust that decision to the Hedge Fund's general partner, Paige General Partner. Again, § 8.02(d) provides that "[Paige] General Partner, in its sole discretion, may waive or modify the conditions

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[175] *Id.* § 8.02(d).
[176] *E.g.,* Pl. Rep. Post-Tr. Br. at 23 (stating that the Lerner Fund claims that Michele Paige breached a fiduciary duty "when [*Paige Capital Management*] asserted its right to continue managing [the Lerner Fund's] investment"); Def. Op. Post-Tr. Br. at 43 ("Michele's decision to impose the [G]ate[s] breached the fiduciary duties . . . .").

relating to withdrawals . . . for certain large or strategic investors."[177] It is also undisputed that Michele Paige is the managing member of Paige General Partner,[178] and was also the managing member of Paige Capital Management, the entity that serves as the Hedge Fund's investment manager and receives the 1.5% management fee.[179] Although Paige General Partner is undoubtedly an affiliate of Paige Capital Management, the decision to use the Gates was one for Paige General Partner, not Paige Capital Management, to make. Unlike his wife, Christopher Paige was not directly employed by Paige General Partner as an officer or member, but instead served as the general counsel of Paige Capital Management.

With that in mind, I turn to the Paiges' two arguments regarding which entities owe fiduciary duties to the Lerner Fund. First, in a footnote to their opening post-trial brief, the Paiges state that "Mr. and Ms. Paige likewise owe no fiduciary duty to [the Lerner Fund], but rather only to their LLC and its members."[180] In support of that proposition, the Paiges cite to *Bay Center Apartments Owner, LLC v. Emery Bay PKI, LLC,*[181] and apparently suggest that Michele and Christopher Paige do not exert the necessary control over the Hedge Fund (i.e., the partnership) to owe the Hedge Fund and its investors any fiduciary duties. In a footnote of its own in its reply brief, the Lerner Fund disagrees and argues that Michele and Christopher Paige not only exerted control

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[177] Partnership Agreement § 8.02(d).
[178] Pre-Tr. Stip. ¶ 5.
[179] Partnership Agreement § 4.04. But, Paige General Partner receives the incentive fees. Partnership Agreement § 6.01(b).
[180] Pl. Op. Post-Tr. Br. at 34 n.21.
[181] *Bay Center Apartments Owner, LLC v. Emery Bay PKI, LLC*, 2009 WL 1124451, at *8-9 (Del. Ch. Apr. 20, 2009).

over the Hedge Fund, but used that control to embark on an "extortionate scheme" against the Lerner Fund.[182] To the extent that the Paiges suggest that Michele Paige did not "exert control over the assets of [the Hedge Fund]"[183] and therefore does not have a duty "not to use [that] control over the [Hedge Fund's] property to advantage [herself] at the expense of the [Hedge Fund],"[184] that argument is without merit. Michele Paige is the managing member of Paige General Partner, the entity whose decision it was to use the Gate Provision, itself a contractual provision specifically designed to control the property of the Hedge Fund by not allowing an investor, like the Lerner Fund, to withdraw its capital when it would otherwise want to do so.

To the extent that what is necessary to impose fiduciary duties on Michele Paige, the managing member of the Hedge Fund's general partner (i.e., Paige General Partner, a limited liability company), is the control she exerted over the Hedge Fund's assets, i.e., the Lerner Fund's invested capital, Michele Paige would qualify under a line of Delaware precedent that began with *In re USACafes, L.P. Litigation*.[185] That case and its progeny have established that a director, member, or officer of a corporate entity serving as the general partner of a limited partnership, like Michele Paige, who exercises control over the partnership's property owes fiduciary duties directly to the partnership and its limited partners.[186]

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[182] Def. Rep. Post-Tr. Br. at 1 n.2.
[183] *Bay Center Apartment*, 2009 WL 1124451, at *9.
[184] *Id.* at *10.
[185] *In re USACafes, L.P. Litig.*, 600 A.2d 43 (Del. Ch. 1991).
[186] *See id.* at 48 ("I therefore conclude that the amended complaint does allege facts which if true establish that the director defendants have breached fiduciary obligations imposed upon them as

With regard to Christopher Paige and Paige Capital Management, however, the Paiges are correct on this poorly briefed part of the record. It is no doubt correct that Christopher Paige was intimately involved in his wife's decision to cause Paige General Partner to use the Gate Provision against the Lerner Fund. But formalism matters in the area of entity law. Even as to Michele Paige, it is a bit of an oddment that our alternative entity law has treated a director of a corporation that is the general partner of a limited partnership as a fiduciary owing fiduciary duties to the limited partnership and its investors, i.e., limited partners. That step was taken in *USACafes* without much analysis of why the investors in the limited partnership were not required, in the absence of a reason for veil piercing, to look solely to the entity they knew was their fiduciary for relief.[187] With no helpful briefing on this subject from the Lerner Fund, I refuse to go further and hold that someone like Christopher Paige, who is not even an officer, director, or member of the governing fiduciary is a direct fiduciary of the limited partnership and its investors. It may be that he can be held responsible for aiding and abetting or on other

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directors of a Delaware corporation [serving as the general partner] or have participated in a breach of such duties by the General Partner."); *see also Bay Center Apartments*, 2009 WL 1124451, at *9 (holding that a person who was the owner and manager of the LLC that served as the managing member of a second LLC owed fiduciary duties directly to the other members of the second LLC because that person exerted control over the assets owned by the second LLC). I have on previous occasions noted my concerns with the core concept underlying applying fiduciary duties to Michele Paige in a situation such as this. *See, e.g., Gelfman v. Weeden Investors, L.P.*, 792 A.2d 977, 992 (Del. Ch. 2001) ("[The defendants'] argument in this regard raises yet again the awkward position occupied by directors of corporate General Partners . . . . Do they owe fiduciary duties to limited partners akin to those owed by corporate directors to stockholders, even though it is the corporate general partner which is the core fiduciary?"); *Gotham Partners, L.P. v. Hallwood Realty Partners, L.P.*, 2000 WL 1476663, at *20 (Del. Ch. Sept. 27, 2000) (opining that a broad application of a principle that would impose such fiduciary duties on managing members like Michele Paige is difficult to square with traditional understandings of the corporate form and corporate veil piercing).

[187] See the brief discussion of some of the concerns about *USACafes* in note 186, *supra*.

grounds such as unjust enrichment, but none of those grounds has been pled here. The same is also true as to Paige Capital Management. But, because the Paiges raised these issues only in a footnote in their post-trial opening brief, I dismiss the fiduciary duty count against Christopher Paige and Paige Capital Management without prejudice, reserving to the Lerner Fund the right to bring an aiding or abetting or unjust enrichment claim *in the event that* Michele Paige and Paige General Partner do not satisfy the final judgment.

I now turn to the second, more substantive, argument made by the Paiges, which is nothing if not innovative.

As to Michele Paige and Paige General Partner, the Paiges make the argument that those defendants owed no fiduciary duties to the Hedge Fund and its investors in deciding whether to waive the Gates because that decision was one that presented a conflict of interest for Michele Paige and Paige General Partner. Because Paige General Partner and those who controlled it — i.e., Michele Paige — owed fiduciary duties to Paige General Partner and its sole member, i.e., Michele Page herself, and because a decision to waive the Gates would injure Paige General Partner and Michele Paige by depriving them of the financial benefits of continuing to manage the Lerner Fund's capital longer, they were in an impossible position. To waive the Gates in the best interests of the Fund's investors would cause them to breach their obligations to themselves, and thus the answer is that

they owed the Fund and its investors no fiduciary duties in deciding whether to waive the Gates.[188]

The Paiges' novel argument fails to persuade me.

As a matter of default law, Paige General Partner clearly owes fiduciary duties to the limited partners in the Hedge Fund.[189] Although Delaware's Revised Uniform Limited Partnership Act permits the waiver of fiduciary duties,[190] such waivers must be set forth clearly, and as we shall see, there is no provision of the Partnership Agreement that says that Paige General Partner does not owe fiduciary duties to the Fund and its investors. As a result, when Paige General Partner acts as the general partner, it must do so in the good faith belief that it is advancing the best interests of the Fund and its investors, i.e., the limited partners.

As a matter of settled law, it is clear that the existence of a conflict does not absolve a governing fiduciary of responsibility for acting in its own self-interest. To the contrary, when a fiduciary acts in a conflicted situation it is, for that very reason, subjected to a more searching form of judicial review, most commonly one known as the

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[188] Pl. Rep. Br. at 21-22 (citing *Kelly v. Blum*, 2010 WL 629850, at *10 n.67 (Del. Ch. Feb. 24, 2010); *Bay Center Apartments*, 2009 WL 1124451, at *8-9); *see also* Post-Tr. Tr. at 52-53 (Counsel for the Paiges).

[189] *See, e.g.,* MARTIN I. LUBAROFF & PAUL M. ALTMAN, DELAWARE LIMITED PARTNERSHIPS § 11.2.2 (2010) ("Under Delaware law, a general partner of a Delaware limited partnership owes a fiduciary duty to the limited partnership and to the other partners in the limited partnership.").

[190] 6 *Del. C.* § 17-1101(f) ("A partnership agreement may provide for the limitation or elimination of any and all liabilities for breach of contract and breach of duties (including fiduciary duties) of a partner or other person to a limited partnership or to another partner or to another person that is a party to or is otherwise bound by a partnership agreement; provided, that a partnership agreement may not limit or eliminate liability for any act or omission that constitutes a bad faith violation of the implied contractual covenant of good faith and fair dealing."); MARTIN I. LUBAROFF & PAUL M. ALTMAN, DELAWARE LIMITED PARTNERSHIPS § 11.2.6.2 (2010).

entire fairness standard of review. For example, it is common in situations involving squeeze-out mergers by controlling stockholders for both the controlling stockholder and those of its affiliates on the board of the squeezed out subsidiary to face potential liability under the entire fairness standard if the merger is not fair to the subsidiary's minority stockholders. The iconic case of *Weinberger v. UOP, Inc.*,[191] and its progeny stand for that mundane proposition. In the alternative entity context, similar principles apply and controlling fiduciaries and their affiliate directors who are the human instruments through which control of the alternative entity is actually exercised have faced close review when they make decisions where the controller's self-interest conflicts with the best interests of the alternative entity's investors.[192]

I see no sound basis in public policy for our state to turn its back on the use of judicial review to make sure that investors in Delaware entities can hold fiduciaries accountable for compliance with their fiduciary duties. To find that a conflicted fiduciary is by virtue of that status absolved of fiduciary responsibility would be an astounding decision with deleterious consequences for investors, the cost of capital, and the integrity of our law. I refuse the invitation to take such an unwise step. Rather, I proceed from the more traditional premise that Paige General Partner, as the general partner of the Hedge

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[191] *Weinberger v. UOP, Inc.* 457 A.2d 701 (Del. 1983).

[192] *See, e.g., In re Boston Celtics Ltd. P'ship S'holders Litig.*, 1999 WL 641902, at *4 (Del. Ch. Aug. 6, 1999) (noting that where a plaintiff can rebut the presumptions of the business judgment rule by pleading that the corporate general partner and its directors engaged in self-interested conduct, the court will review those actions under the entire fairness standard of review) (citations omitted).

Fund, owed a fiduciary duty to the limited partnership (the Hedge Fund) and its investors (the limited partners).

Even assuming that traditional premise, the Paiges have another argument as to why fiduciary duties do not apply that is less novel.

The Paiges argue that because the Partnership Agreement gave Paige General Partner the "sole discretion" to determine whether to "waive or modify the conditions relating to withdrawal [i.e., the Gate Provision],"[193] the governing contract, which takes precedence over default statutory law when there is a conflict,[194] clearly provides that Paige General Partner may fail to waive the Gates solely for its own self interest, without any consideration of the best interest of the Hedge Fund and its investors. The Lerner Fund disagrees with that assertion and I find that its position is the better one.

Unlike contractual provisions stating that the general partner has "sole discretion" to make a decision for any reason, and then clarify that such "sole discretion" means that the general partner need not consider any other interests, like those of the limited partners,[195] the provision at issue in this case only says that Paige General Partner gets to

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[193] Partnership Agreement § 8.02(d).

[194] *Arvida/JMB Partners, L.P. v. Vanderbilt Income and Growth Assocs., L.L.C.*, 1997 WL 294440, at *2 (Del. Ch. May 23, 1997); *Monterey Investments, Inc. v. HealthCare Investments, Inc.*, 1997 WL 367038, at *1 (Del. Ch. June 26, 1997).

[195] In *Gotham Partners, L.P. v. Hallwood Realty Partners, L.P.*, this court addressed a limited partnership agreement that provided the general partner "sole and complete discretion" to decide issues related to the issuance of partnership units. *Gotham Partners, L.P. v. Hallwood Realty Partners, L.P.*, 2000 WL 1476663, at *5 (Del. Ch. Sept. 27, 2000). But that partnership agreement also went on to state that:

> Whenever in this Agreement . . . the General Partner is permitted or required to make a decision (i) *in its "sole discretion" or "discretion" or under a similar grant of authority or latitude, the General Partner shall be entitled to consider only such interests and factors as it desires and shall have no duty or obligation*

act in its sole discretion and does not further flesh out what that term means. That bare statement does nothing to absolve Paige General Partner of the duty to act for a proper fiduciary purpose; it simply says that Paige General Partner has the singular (i.e., sole) authority (i.e., discretion) to consider and decide this matter. My conclusion that this is so is supported not only by the plain language of the clause, which says only that, but also by prior well-reasoned precedent of this court. In *Cantor Fitzgerald, L.P. v. Cantor*, then-Justice, now Chief Justice, Steele, sitting by designation on the Court of Chancery, similarly found that any "sole and absolute discretion granted by a particular provision is subject to the global requirement that every partner abide by its duty of loyalty . . . and . . . exercise 'good faith' in making all determinations and judgments," and that the "sole discretion" language in the partnership agreement meant only that the party upon whom it was conferred did not need to "seek the guidance or approval of others" in making the decision.[196] The decision in *Gotham Partners, L.P. v. Hallwood Realty Partner, L.P.*

> *to give any consideration to any interest of or factors affecting the Partnership, . . . the Limited Partners or the Assignees.*

Id. at *6 (emphasis in original). Based on that contractual language, this court concluded that the "sole and complete" discretion afforded to the general partner supplanted that partner's traditional duty to consider the interests of the partnership and its limited partners in making a decision. *Id.* at *10. *See also Gelfman v. Weeden Investors, L.P.*, 792 A.2d 977 (Del. Ch. 2001) (holding that where a limited partnership agreement gave the general partner the "*sole [and complete] discretion*," and further clarified that this meant that the general partner "*shall be entitled to consider only such interests and factors as it desires and shall have no duty or obligation to give any consideration to any interest or factors affecting the Partnership . . . , the Limited Partners or the Assignees*," the partnership agreement "clearly preclude[d] the application of *all aspects of* the traditional fiduciary duty of loyalty . . . and the General Partner will not be liable for beach of contract or fiduciary duty simply because the result of its action produces is not 'entirely fair.'") (emphasis in original).

[196] *Cantor Fitzgerald*, *L.P. v. Cantor*, 2001 WL 1456494, at *7 (Del. Ch. Nov. 5, 2001).

and my decision here are also consistent with the basic requirement that any contractual displacement of the fiduciary duties of loyalty and care be made with clarity.[197]

With that underbrush cleared, I turn to the remaining question which is whether the decision not to waive the Gates was a justifiable fiduciary act.

Regrettably, this is too easy a call. The record is uncontroverted that the Paiges' decision to gate the Lerner Fund's capital was entirely self-interested and not justified by the best interests of the Hedge Fund and its investors. Indeed, the record is devoid of any rational reason to gate the capital in order to protect *either* of the investors in the Fund — the Lerner Fund or Michele Paige — *as investors*. As the Paiges' own expert, Christianna Wood, agreed at trial, the purpose of gate provisions generally is to ensure that there is no "run on the bank" and protect investors in a fund from large withdrawals by departing investors that might require the fund manager to sell assets at an inopportune time to be able to satisfy withdrawal requests.[198] In this case, as of October 31, 2010, when the Paiges chose to use the Gate Provision to restrict the Lerner Fund's withdrawal, the Lerner Fund had approximately $39.5 million dollars invested in the

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[197] *See, e.g., Miller v. Am. Real Estate Partners, L.P.*, 2001 WL 1045643, at *8 (Del. Ch. Sept. 6, 2001) (citing *Sonet v. Timber Co., L.P.*, 772 A.2d 319, 322 (Del. Ch. 1998)) ("But just as investors must use due care, so must the drafter of a partnership agreement who wishes to supplant the operation of traditional fiduciary duties. In view of the great freedom afforded to such drafters and the reality that most publicly traded limited partnerships are governed by agreements drafted exclusively by the original general partner, it is fair to expect that restrictions on fiduciary duties be set forth clearly and unambiguously.").

[198] Tr. at 971-72 (Wood) (agreeing with the characterization of gate provisions in Nora Jordan, et al., Advising Private Funds: A Comprehensive Guide to Representing Hedge Funds, *Private Equity Funds and their Advisers* § 20:12 (2010)). The Lerner Fund's expert, John Maltby, also agreed. Tr. at 1203 (Maltby) ("[T]he primary reason for gate or for gating a fund is to protect investors from a run on the bank and to protect investors from a fire sale of their assets.").

Hedge Fund,[199] and Michele Paige, the only other investor in the Hedge Fund, had $39,479 invested.[200] Nothing in the record supports an inference that redeeming the Lerner Fund's entire investment endangered Michele Paige's modest investment in the Hedge Fund. In fact, Wood, the Paiges' own expert, filed reports with the court that do not identify any basis for concluding that Michele Paige's invested capital would have been at any risk because of a full redemption of the Lerner Fund's investment.[201] At trial, she was regrettably dodgy on the question when pressed about this point, but eventually admitted that the investor protection rationale often cited as a reason for application of a gate provision did not apply with any material force in this case with regard to Michele Paige's investment.[202] In other words, a "loyal expert" confessed that Michele Paige's investment would not be materially effected by a withdrawal of all of the Lerner Fund's capital. Most important, Michele Paige never attempted to justify her refusal to waive the Gates on the basis that it was *necessary to protect herself as an investor in the Fund*. Rather, she, as I next discuss, straightforwardly indicated that she advanced her own self-interest as the owner of Paige General Partner and Paige Capital Management in continuing to receive fees by employing the Gates, and was not trying to advance the best

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[199] JX-1044; JX-1045.
[200] *Id.*
[201] JX-318 (Expert Report of Christianna Wood (Feb. 15, 2011)); JX-320 (Expert Rebuttal Report of Christianna Wood (Feb. 25, 2011)). In her initial report, Wood makes the conclusory statement that given Michele Paige's commitment to invest in the Fund, the Gate Provision would "protect [Michele Paige] as the other investor." JX-318 ¶ 53. But, Wood's report contains no discussion of how Michele Paige's investment would be harmed in light of the composition of the Hedge Fund's portfolio and her investment's size. In fact, at trial, Wood admitted that she was never asked to analyze the Hedge Fund's portfolio. Tr. at 953 (Wood).
[202] *Id.* at 890-900 (Wood).

interests of the Fund's investors qua investors. That is, she put her self-interest ahead of her fiduciary duties.

To be concrete about that self-interest, by gating the Lerner Fund's capital and allowing it to withdraw only 20% of its investment on October 31, 2010, Paige General Partner secured for Paige Capital Management the management fees associated with that investment. In the year following the application of the Gate Provision, the 1.5% management fee that the Paiges would collect would result in payments to the Paiges of over $400,000, which would have been lost if the Lerner Fund was allowed to leave the Hedge Fund unimpeded at the end of October 2010. Michele Paige admitted that this amount was material to her.[203]

At trial, Michele Paige was asked by her own counsel to explain her reasons for not waiving the Gate Provision.[204] Her rambling response contained no rational reason relating to the protection of the investors in the fund as investors. Instead, she talked about how she (and her family) had invested in excess of one million dollars *into the* "*operations of the company.*"[205] By that she clearly was not referring to investments made by her and her family as investors in the Hedge Fund, but rather investments as the controllers of the Hedge Fund's controlling entities — Paige General Partner and Paige Capital Management — and her consequent desire to "keep employees" and have "business continuity" going forward.[206] To be sure, if Paige General Partner thought in

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[203] *Id.* at 321 (Michele Paige).
[204] *Id.* at 386-87 (Michele Paige).
[205] *Id.* at 386 (Michele Paige) (emphasis added).
[206] *Id.* at 386-87 (Michele Paige).

good faith that applying the Gate Provision was necessary to protect some interest other than the Paiges' own interest as managers, then applying the Gate Provision might have been proper regardless of how much the Paiges incidentally stood to gain personally from its application. If, for instance, application of the Gate Provision was necessary to protect Michele Paige, in her capacity as an investor, then perhaps Paige General Partner's decision would pass fiduciary muster. But, as shown, that was not the case here. There was no danger to Michele Paige as an investor. Rather, this was a simple decision of a conflicted fiduciary advancing its own self-interest in conflict with the best interests of those it was charged with protecting. The Hedge Fund's best interests are not some ethereal concept for philosophers to debate in this context, they are rather mundane, and consist in what is best for the Fund's investors.

The Paiges argue, however, that even if the decision not to waive the Gate Provision was self-interested, they are statutorily exculpated from liability by 6 *Del. C.* § 17-1101(e). That provision provides that:

> Unless otherwise provided in a partnership agreement, a partner or other person shall not be liable to a limited partnership or to another partner or to another person that is a party to or is otherwise bound by a partnership agreement for breach of fiduciary duty for the partner's or other person's good faith reliance on the provisions of the partnership agreement.[207]

Thus, this court has held that if a provision of a limited partnership agreement is ambiguous, good faith reliance on an incorrect interpretation will not give rise to liability

[207] 6 *Del. C.* §17-1101(e).

for breach of fiduciary duty.[208] But critically, it is the Paiges that must demonstrate that they "acted in good faith reliance on the [P]artnership [A]greement if they are to avoid liability."[209]

Although it is regrettable, I cannot conclude that the Paiges have met their burden of showing that they relied on a good faith reading of the Partnership Agreement. Taken as a whole, Michele Paige's testimony in this case can be fairly read as an assertion that she always believed that the Gate Provision in the Partnership Agreement could be properly used to gate the Lerner Fund's capital after three years and that she always believed that the Gate Provision could be used to ensure the revenue stream to Paige Capital Management, rather than as a way to protect the investors in the Hedge Fund. Michele Paige testified that she viewed the Gates as a tool that the Hedge Fund could use to protect the business interests of the Hedge Fund itself, rather than the best interests of its investors.[210] She also testified that during the negotiations, the Lerner Fund asked to be exempted from the Gate Provision but she refused because that provision was something important to the Paiges.[211] She also said she told the Lerner Fund the reason

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[208] *Cont'l Ins. Co. v. Rutledge & Co., Inc.*, 750 A.2d 1219, 1240 (Del. Ch. 2000) ("If a [general] partner can interpret reasonably a clause in the limited partnership agreement in more than one manner, and that general partner relies in good faith on the incorrect interpretation, then the Court will excuse the general partner's breach of the limited partnership agreement.").
[209] *In re Nantucket Island Assocs. Ltd. P'ship Unitholders Litig.*, 2002 WL 31926614, at *2 (Del. Ch. Dec. 16, 2002).
[210] Tr. at 256 (Michele Paige).
[211] *Id.* at 115 (Michele Paige) ("Well, because we wanted to attract longer-term capital. So we wanted to make sure people understood that there were break fees and there were [G]ates and it was important to us to have those.").

"why" it was "very important" to the Paiges.[212] At trial, the only "why" was that it gave the Paiges a continued fee stream and the chance to keep their hopes alive as investment managers. Taken together, that testimony suggests that Michele Paige claims to have viewed the Gates as a means of protecting the self-interest of the Hedge Fund and its business, even when that conflicted with the best interests of the Fund's investors, and that she told the Lerner Fund as much during the negotiations. But, that Michele held that belief and communicated it to the Lerner Fund is, regrettably, not a scenario I find credible. Had Michele Paige, an unproven investment manager, asserted in her negotiations with the Lerner Fund that the Gate Provision was intended to protect her fee stream and business prospects as an investor in the event she could not raise other capital and thus needed to hold the Lerner Fund's capital to maintain her income, she would have never reached a deal with the Lerner Fund. It is reasonable to conclude that the Lerner Fund would have walked away immediately.

I am left with the firm impression that the Paiges' reading of the Partnership Agreement was not that of a good faith fiduciary grappling with the meaning of an ambiguous partnership agreement, but of self-interested minds bent on protecting their own financial interests. Michele Paige's use of the Gates was not inspired by a good faith attempt to advance the interests of the Hedge Fund and its investors, but as leverage to keep a fee stream going to herself and Christopher Paige. When asked directly at trial, by her own counsel, why she did not waive the Gate Provision, Michele Paige could not

[212] *Id.* at 85 (Michele Paige) ("I had told [Gould] before why I thought the [G]ates were very important to us.").

articulate a non-self interested reason.[213] That raises another core problem for the Paiges. Section 17-1101(e) is not a license to exculpate fiduciaries for self-serving interpretations of governing instruments. It is best read as ensuring that fiduciaries who take action to advance a proper partnership purpose but do so based on a good faith misreading of the agreement are not tagged for liability for a breach of fiduciary duty. To exculpate a fiduciary for breach of fiduciary duty for making a good faith, but erroneous, determination that the partnership agreement allowed the fiduciary to advance its self-interest over the best interests of the investors would seem to extend the statute's reach beyond its sensible borders. Because the Paiges have failed to show that their reading of the Partnership Agreement was a good faith interpretation of that Agreement, but rather as a pretext for self-enrichment, the Paiges are not entitled to the protections of 6 *Del. C.* § 17-1101(e).

For all these reasons, I therefore conclude that it was a violation of Paige General Partner's and Michele Paige's fiduciary duties to fail to waive the Gate Provision for the Lerner Fund.

5. <u>The Conditions Necessary To Permit The Lerner Fund To Withdraw Its Money Before October 2010 Did Not Exist</u>

Having determined that the Seeder Agreement amended the Partnership Agreement and that the Gate Provision does not apply to the Lerner Fund, it is clear that the Lerner Fund is entitled to the return of its capital. But, the Lerner Fund claims that the Paiges' conduct triggered its § 6.4 Right of Withdrawal under the Seeder Agreement

[213] *Id.* at 386-87 (Michele Paige).

in two ways, and thereby entitled the Lerner Fund to withdraw its money before the end of the lock up period. First, the Lerner Fund argues that the Paiges violated its information rights outlined in § 8.2 of the Seeder Agreement. Second, it argues that the Paiges violated their fiduciary duties by engaging in an "extortionate scheme" punctuated by the March 2010 Letter.[214] I deal with each one in turn.

a. The Lerner Fund Has Not Established A Properly Noticed Breach Of The Information Rights In The Seeder Agreement

As discussed, the § 6.4 Right of Withdrawal entitles the Lerner Fund to withdraw the entirety of its investment immediately if the Paiges engage in certain conduct. Section 6.4(e) entitles the Lerner Fund to withdraw its entire investment if the Paiges materially breach the Seeder Agreement and that breach is not cured within ten days of receipt of written notice of the breach.[215]

The Lerner Fund claims that the Paiges have materially breached §§ 8.2(a) and (b) of the Seeder Agreement relating to information rights in two ways:[216] first, by refusing to supply the Lerner Fund with the position level detail that it requested in the wake of Christopher Paige's March 2010 Letter — a violation of § 8.2(b); and second, by thwarting the Lerner Fund's efforts to inspect the books and records of Paige Capital Management — a violation of § 8.2(a). Section 8.2(a) of the Seeder Agreement permits the Lerner Fund "with advance written notice to [Paige Capital Management], and during regular business hours, to review the books and records of [Paige Capital Management],

[214] Def. Op. Post-Tr. Br. at 40.
[215] Seeder Agreement § 6.4(e).
[216] Def. Op. Post-Tr. Br. at 52.

at [the Lerner Fund's] expense, for the purpose of verifying compliance with the terms of this Agreement."[217] Section 8.2(b) states that:

> As soon as reasonably practicable following the close of each calendar month, [Paige Capital Management] will provide [the Lerner Fund] and any of its affiliates, at the expense of [Paige Capital Management], a report reflecting monthly performance estimates and other portfolio information as may reasonably be requested by [the Lerner Fund] in connection with this Agreement, which may include, among other things, portfolio exposures, portfolio positions, performance analysis and risk reports.[218]

After receiving the March 2010 Letter from Christopher Paige, the Lerner Fund requested position level detail because it was worried about the safety of its investment. The Lerner Fund contends that the position level request was reasonable because it is specifically contemplated by § 8.2(b) of the Seeder Agreement, which states that the information the Lerner Fund may request includes "portfolio positions."[219] The reasonableness of such a request, the Lerner Fund points out, was acknowledged at trial by the Paiges' own expert.[220] Relatedly, the Lerner Fund argues that because of § 9.1 of the Seeder Agreement, a no-waiver clause, it is immaterial that the Lerner Fund never requested detailed information from the Paiges or complained about the sufficiency of the information that the Paiges had been providing in the earlier phases of the parties' relationship, and that such a failure did not prevent the Lerner Fund from requesting reasonable information in the wake of the Paiges' March 2010 Letter.

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[217] Seeder Agreement § 8.2(a).
[218] *Id.* § 8.2(b).
[219] *Id.* § 8.2(b).
[220] Def. Op. Post-Tr. Br. at 53 (quoting Tr. at 922 (Wood)).

Next, the Lerner Fund argues that § 8.2(a), which refers only to the Lerner Fund's right to inspect the books and records of Paige Capital Management — the investment manager — must be read to also allow for inspection of the books and records of the affiliated funds that Paige Capital Management manages, i.e., the Hedge Fund, because the Hedge Fund was the entity in which the Lerner Fund was invested, Paige Capital Manager did all the key investing work for the Hedge Fund, and the information rights were granted to the Lerner Fund to allow it to verify compliance with the Seeder Agreement.[221] Finally, the Lerner Fund argues that it provided notice of the breaches in a July 15, 2010 letter from its counsel to the Paiges' counsel, or, in the alternative, when it filed its counterclaims in this action on July 30, 2010.[222]

The Paiges respond with several arguments of their own. Initially, the Paiges say that § 8.2(a) relates only to the books and records of Paige Capital Management and therefore the Lerner Fund has no right to inspect the books and records of the affiliated funds that Paige Capital Management manages, i.e., the Hedge Fund. Conveniently, the Paiges then say that Paige Capital Management has no books and records addressing key issues like the Hedge Fund's investments even though Paige Capital Management, as the investment manager, makes all the investment decisions: a real "gotcha" argument that is never backed up by an explanation of how Paige Capital Management conducts its affairs with no records, when the Hedge Fund itself has no employees. Next, the Paiges contend that the parties' course of dealing under § 8.2(b) establishes that the monthly reports that

[221] Def. Op. Post-Tr. Br. at 54.
[222] JX-1090 (Letter from Christopher Duffy to Steven Molo (July 15, 2010)).

the Paiges had been furnishing to the Lerner Fund since the parties' relationship began were satisfactory. Finally, the Paiges insist that the Lerner Fund never provided the contractually required notice until October 22, 2010, nine days before the § 6.4 Right of Withdrawal terminated and that the notice was therefore untimely.

There is no question that the Paiges violated the information rights of the Lerner Fund by refusing to grant its requests for position level detail after sending the March 2010 Letter. The Lerner Fund might be precluded from arguing that the form of the monthly reporting it had agreed to was all of a sudden no longer proper, but it was not precluded from making additional reasonable information requests. In fact, § 8.2(b) specifically provides that the Lerner Fund may request other information, "which may include, among other things*, portfolio exposures, portfolio positions, performance analysis and risk reports*."[223]

Section 8.2(a) gives the Lerner Fund the right to inspect the books and records of Paige Capital Management, which was the investment manager for the Hedge Fund. The Paiges refused to grant the Lerner Fund access to information that they claimed was possessed by the Hedge Fund because the Hedge Fund is a separate entity from Paige Capital Management. That argument is not persuasive for at least two reasons.

First, there is case law in New York that suggests that provisions such as § 8.2(a) of the Seeder Agreement must be read in light of their purpose and not strictly adhered to in cases where entity structure would thwart the clear purpose of the provision.[224] Here,

[223] Seeder Agreement § 8.2(b) (emphasis added).
[224] *See Nash v. Gay Apparel Corp.*, 193 N.Y.S.2d 246, 249 (N.Y. App. Div. 1959).

the clear purpose of the provision, as the provision itself explicitly states, is to allow the Lerner Fund to "verify[] compliance with the terms of [the Seeder] Agreement."[225] Second, and more practically, if Paige Capital Management's "books and records" did not contain information about the positions of the Hedge Fund, how could Paige Capital Management have managed the Fund? As a matter of reality, Paige Capital Management must have had continuous control of the books and records containing portfolio, trading, and other information regarding the Hedge Fund. Paige Capital Management picked the investments and made the trades; the Hedge Fund itself was inert and had no employees of its own. By the terms of the Seeder Agreement, the parties clearly understood that and made Paige Capital Management responsible for giving the Lerner Fund access to those books and records within its control that were necessary to allow the Lerner Fund to "verify[] compliance with the terms of [the Seeder Agreement]"[226] because it was managing the Fund. The idea that the investment manager who was making the decisions about how to deploy the Hedge Fund's capital does not have books and records about that Fund's activities is, to be understated, not plausible.[227]

For all these reasons, it is plain that the Paiges breached the information rights provisions contained in §§ 8.2(a) and (b) of the Seeder Agreement. But, the Lerner Fund stumbles on another ground, which is whether the Lerner Fund provided the Paiges with adequate notice and an opportunity to cure under § 6.4(e) of the Seeder Agreement so

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[225] Seeder Agreement § 8.2(a).
[226] *Id.*
[227] I also note in that regard that Paige Capital Management, the investment manager, and Paige General Partner, the general partner of the Hedge Fund, were both managed by Michele Paige and it is likely that their books and records were not kept separate and distinct.

that the Paiges' breach of the information rights provisions triggered a § 6.4 Right of Withdrawal. Section 6.4(e) provides that the Lerner Fund may withdraw all its capital if the Paiges materially breach the Seeder Agreement and "such breach is not cured by [the Paiges] to [the Lerner Fund's] reasonable satisfaction within ten (10) calendar days from receipt of written notice thereof."[228] The Lerner Fund contends that a letter it sent to the Paiges on July 15, 2010 acted as notice or, in the alternative, that its counterclaims in this action filed on July 30, 2010 acted as notice.

Under New York notice and cure law, the "notice of default must clearly advise that the cure period has been triggered" and "the notice should apprise the recipient of the drastic legal repercussions that could result from the defaulting party's noncompliance."[229] The party seeking termination has the burden of proving that the notice and cure provision was honored.[230] Given New York law's emphasis on the importance of allowing a period for cure, it is unlikely that New York courts would consider a complaint proper notice, and the letter on July 15 was insufficient in its lack of specificity. Therefore, the Lerner Fund did not provide proper notice of its information rights claims and was unable to use those claims to trigger a § 6.4 Right of Withdrawal.

b. The Lerner Fund Has Not Demonstrated That The Paiges Violated Their Fiduciary Duties Merely By Sending The March 2010 Letter

The Lerner Fund claims that the Paiges violated their fiduciary duties when they sent the March 2010 Letter by trying to extort a settlement payment from the Lerner

[228] *Id.* § 6.4(e).
[229] GLEN BANKS, NEW YORK CONTRACT LAW § 13:11 at 498-99 (Thomson West 2006) (citing *Gil Enters., Inc. v. Delvy*, 29 F.3d 241, 246 (2d Cir. 1996)).
[230] *Id.*

Fund. If that were the case, the Lerner Fund would have been entitled to a return of its capital then because a breach of fiduciary duty by the Paiges would have triggered a § 6.4 Right of Withdrawal under the Seeder Agreement.[231] Importantly, unlike a § 6.4 Right of Withdrawal triggered by a material breach of the Seeder Agreement under § 6.4(e), the § 6.4 Right of Withdrawal triggered by a breach of fiduciary duty under § 6.4(c) does not contain a notice provision.[232]

The Lerner Fund argues that the March 2010 Letter was part of an "extortionate scheme" in which the Paiges attempted to use their role as fiduciaries and their control of the Lerner Fund's invested capital to extract a settlement payment from the Lerner Fund in violation of their fiduciary duties.

The Paiges counter that the March 2010 Letter was merely a heated pronouncement of their contractual rights and as such is not actionable.[233] At most, the Paiges concede, the March 2010 Letter could possibly be construed as a threat to violate their fiduciary duties but not itself a violation of those duties.[234] In support of their position, the Paiges again cite to the provision of the Delaware Revised Uniform Limited Partnership Act that provides a defense for actions taken "in good faith reliance on the provisions of the partnership agreement."[235]

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[231] Seeder Agreement § 6.4(c); Def. Op. Br. at 69-70.
[232] Seeder Agreement § 6.4(c).
[233] Pl. Op. Post-Tr. Br. at 38-40.
[234] *Id.* at 42.
[235] *Id.*. at 37 (citing 6 *Del. C.* § 17-1101(e)).

Although as I noted in my earlier opinion in this case regarding the absolute litigation privilege,[236] it is a colorable reading of the March 2010 Letter that the letter constituted improper threats that could be, by themselves, a violation of fiduciary duty, that color did not blossom into Technicolor at trial. At bottom, the letter is better understood as an inartful, misguided settlement attempt sent in the heat of a personally trying time in which the Paiges use overblown language to convey their mistaken and self-serving beliefs about what the Agreements permitted them to do. Of course, that does not mean that the Paiges' conduct in actually following through on those threats later by gating the Lerner Fund's capital was not a violation of their fiduciary duties. It was, but I am not persuaded on this record to embrace the idea that a heated settlement letter expressing an intent to commit what might be considered a breach of fiduciary duty at a later time itself constituted an immediate, non-curable, breach.[237] Notably, the Lerner Fund itself did not contend so until it filed its counterclaims in July 2010.

B. The Paiges' Claim That The Lerner Fund Violated The Implied Covenant Of Good Faith And Fair Dealing Fails

The Paiges claim that the Lerner Fund violated the implied covenant by engaging in a course of conduct over the course of the parties' relationship that caused the Paiges not to be able to pursue their investment strategy or attract new investors to the Fund. In essence, the Paiges claim that the Lerner Fund strung them along, insisting that they

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[236] *Paige Capital Mgmt., LLC v. Lerner Master Fund, LLC*, 2011 WL 1707346 (Del. Ch. May 5, 2011).

[237] By that, I am not referring to a cure for purposes of any contract but instead reflecting my reluctance to use this case to set a precedent for claims of "threatened" breaches of fiduciary duties lest a useful incentive for cooling heads and warming hearts be closed off.

remain liquid in the event of a redemption that could come at any moment. The Lerner Fund counters that its conduct over that period was in line with industry best practices and that the Paiges' investment and fundraising problems were of their own making. The Lerner Fund portrays its conduct as notifying the Paiges early on that it planned on redeeming its investment *at the end* of the three-year lock up period and that the Paiges should be mindful of that when formulating their investment strategy. The Lerner Fund also contends that by notifying the Paiges early, the Lerner Fund was helping the Paiges because the Paiges could use the remainder of the three-year lock up period to find a new seed investor.

Although the Lerner Fund's conduct in expressing a desire to leave the Hedge Fund after three years may sully its reputation as a potential seed investor in the future, it did not violate the implied covenant of good faith and fair dealing. That is so for a simple reason. It cannot be a violation of the implied covenant of good faith and fair dealing to exercise a contractual right.[238] And, because I have found that the Lerner Fund was contractually permitted to withdraw its entire investment at the end of the three-year term on October 31, 2010, it could not have been a violation of the implied covenant of good faith and fair dealing to have told the Lerner Fund that it planned on exercising that right.

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[238] *See, e.g., Suthers v. Amgen Inc.*, 441 F. Supp. 2d 478, 485 (S.D.N.Y. 2006) ("Indeed, courts have refused attempts to impose liability on a party that engaged in conduct permitted by a contract, even when such conduct is allegedly unreasonable."); *AM Cosmetics, Inc. v. Solomon*, 67 F. Supp. 2d 312, 324 (S.D.N.Y. 1999) ("As a matter of law, enforcing a contract provision agreed to by both parties can not constitute a breach of good faith.").

C. The Paiges' Defamation Claim Fails

The Paiges claim that the Lerner Fund is liable for defamation for two reasons: 1) the Lerner Fund filed a Summons with Notice in New York state court against the Paiges listing "fraud" among its allegations; and 2) the Lerner Fund's counsel, Boies Schiller, made statements to the media that the Lerner Fund did not know where the Hedge Fund was investing its money, and those statements ended up in a story on HedgeFund.net. The parties agree that the Paiges' defamation claims are governed by New York law.

The Lerner Fund offers three arguments as to why its statements do not constitute defamation. First, the Lerner Fund argues that the Summons with Notice it filed in New York state court is protected by a common law litigation privilege recognized by New York.[239] Second, the Lerner Fund argues that the statements by Boies Schiller in response to press inquiries about this case are protected by § 74 of the New York Civil Rights Law.[240] Finally, the Lerner Fund argues that the statements to the press that the Paiges take issue with are "substantially true," which under New York law acts as a complete defense to defamation claims.[241] The Lerner Fund's arguments are persuasive.

The Paiges acknowledge that generally, communications such as the Summons with Notice are covered by a litigation privilege in New York. But, the Paiges contend that the privilege does not apply if the statements are made with malice.[242] The Paiges' argument confuses the "sham" litigation exception to the privilege with the effect that

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[239] Def. Op. Br. at 66.
[240] *Id.* at 66-67.
[241] *Id.* at 67 n. 15 (citing *Dillon v. City of New York*, 261 A.D.2d 34 (N.Y. App. Div 1999); *Love v. William Morrow and Co., Inc.*, 193 A.D.2d 586, 587 (N.Y. App. Div. 1993).)
[242] Pl. Op. Post-Tr. Br. at 69 (citing *Williams v. Williams*, 246 N.E.2d 333 (N.Y. 1969)).

malice has on its application. Setting aside the fact that the Paiges have made no credible showing that the statements in the Summons with Notice were made maliciously,[243] the law in New York is clear that malice alone will not destroy the application of the privilege.[244] Instead, it is only if the lawsuit itself is brought as a sham for the sole purpose of harming or harassing the opponent that the litigation privilege does not apply.[245] Therefore, in order to lose the protections of the privilege, the Summons with Notice would have needed to be a "sham litigation" filed solely for the purpose of harming or harassing the Paiges. Given that the Lerner Fund filed its suit in New York *after* the Paiges filed this suit, there is little basis to infer that the Lerner Fund brought suit solely for the purpose of harming or harassing the Paiges as opposed to getting judicial relief. In this regard, it is notable that when the Lerner Fund brought claims in this court, when the parties' dispute was ultimately centered here, those claims were not frivolous and several of them have been found to have merit. Although the Lerner Fund

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[243] Under New York law, malice has been defined as "personal spite or ill will, or culpable recklessness or negligence." *Herlihy v. Metro. Museum of Art*, 633 N.Y.S.2d 106, 112 (N.Y. App. Div. 1995) (internal quotations omitted). Further, "[i]n order to satisfy the malice requirement, plaintiff must demonstrate that the communication involved is consistent with a desire to injure the targeted individual to justify submitting the question of malice to the jury . . . ." *Id.*

[244] *Rabiea v. Stein*, 69 A.D.3d 700, 700 (N.Y. App. Div. 2010) ("A statement made by counsel during a judicial proceeding, *even if made with malice or bad faith*, is protected by absolute privilege as long as the statement may, in some way, be considered pertinent to the litigation . . . .") (emphasis added).

[245] *See Williams v. Williams*, 246 N.E.2d 333, 343-44 (N.Y. 1969) ("This court — though noting that '(d)amages are rarely recovered * * * for the malicious prosecution of a civil action, unless person or property is interfered with' — made it quite clear that such a suit 'may be founded upon a civil action, when commenced *simply* to harass and oppress the defendant.'") (citations omitted) (emphasis added).

ultimately chose not to press a fraud claim, there is no basis to infer that its earlier New York filing was a mere sham.

Finally, the Paiges have done nothing to show that the mere filing of a Summons with Notice that contains the word "fraud" would work reputational harm by that fact alone. The term "fraud" is a common one, and is used in a very loose way even in the law. Thus, there are variations of fraud that require no showing of culpable scienter.[246] On this record, there would be no way one could say that the Lerner Fund's initial filing in New York was defamatory and caused harm simply because it said that "the nature of the action is fraud and breach of fiduciary duty in connection with [the Paiges'] misrepresentations and omissions in their solicitation of funds from [the Lerner Fund] for investment purposes, and [the Paiges'] subsequent misuse of [the Lerner Fund's] funds."[247] Notably, in this litigation, the Paiges claim that the Gate Provision was intended by them to protect their fee stream. But I have concluded that, to the extent that Michele Paige says she said that during negotiations, her testimony was not credible. If she did not, as I have found, express that belief that the Gate Provision could be used to protect her management fees, her later use of the Gate Provision for that purpose has a

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[246] *Ajettix Inc. v. Raub*, 804 N.Y.S.2d 580, 590 (N.Y. Sup. Ct. 2005) ("Constructive fraud is similar to fraudulent concealment except that the element of scienter need not be proven (*Klembczyk v. DiNardo,* 265 A.D.2d 934, 936, 705 N.Y.S.2d 743). '[T]he element of scienter . . . is dropped and is replaced by a requirement that the plaintiff prove the existence of a fiduciary or confidential relationship' . . . .") (citations omitted); *see also* 26 WILLISTON ON CONTRACTS § 69:3 (4th ed. 2011) ("Constructive fraud has similar elements [as actual fraud], though scienter is not required . . . .") (citations omitted); 37 C.J.S. *Fraud* § 39 (2011) ("There is also authority holding that while scienter must be shown where a claim of legal fraud is asserted, scienter need not be shown where a claim of equitable fraud is asserted.") (citations omitted); 37 AM. JUR. 2D *Fraud and Deceit* § 9 (2011) (same).

[247] JX-208.

colorable relation to the statement in the Summons with Notice that there were material omissions in connection with the Lerner Fund's decision to invest. Furthermore, as was discussed in detail with respect to the Lerner Fund's information rights claims, the Summons with Notice was also filed at a time when the Paiges were adamantly refusing to tell the Lerner Fund where the capital in the Hedge Fund was invested.

With regard to the article published on HedgeFund.net, § 74 of the New York Civil Rights Law prohibits liability arising from the fair and true report of any judicial proceeding.[248] The report must only be substantially accurate in order to be covered by the law.[249] In this case, the report on HedgeFund.net that the Paiges take issue with states that:

> "The reason the withdrawal request was made was because [the Lerner Fund] completely lost confidence in these people," [the attorney] told HedgeFund.net. "They were supposed to get significant investments; they wound up getting zero."
> [The Lerner Fund] also lost confidence in the hedge fund because it wasn't getting the documentation that had been promised [the attorney] said.
> Monthly statements didn't arrive in a timely fashion and, when they did arrive, they included only the amounts supposedly in [the Lerner Fund's] accounts, [the attorney] said, with no additional information about the securities in the [Hedge Fund] or where they were being held.[250]

[248] *See* N.Y. Civ. Rights Law § 74 (McKinney) ("A civil action cannot be maintained against any person, firm or corporation, for the publication of a fair and true report of any judicial proceeding, legislative proceeding or other official proceeding, or for any heading of the report which is a fair and true headnote of the statement published."); *see, e.g.*, *Lacher v. Engel*, 33 A.D.3d 10, 17 (N.Y. App. Div. 2006).
[249] *Fishof v. Abady*, 280 A.D.2d 417, 417 (N.Y. App. Div. 2001) ("The absolute privilege under [§ 74 of the Civil Rights Law] also extends to the release of background material with regard to the case, so long as the statement is a substantially accurate description of the allegation.") (internal citations omitted).
[250] JX-229 (HedgeFund.net Article (October 8, 2010)).

The Paiges claim that the comments by the Boies Schiller attorney, especially in the post-Madoff world we now live in, were defamatory because they suggested that the Paiges were hiding the Lerner Fund's money in order to misappropriate it.[251] Further, the Paiges argue that such an implication "strike[s] at the heart of the Paiges' business,"[252] and their expert stated in her report that being accused of such conduct will "make it virtually impossible for Michele Paige to be employed as an investment manager again."[253]

The problem with the Paiges' argument, however, is that the statements that the Boies Schiller attorney made to HedgeFund.net were "substantially accurate" for purposes of bringing them under the protections of § 74 of the New York Civil Rights Law,[254] and were also "substantially true" so that no recovery could be made for a defamation claim even in the absence of the Civil Rights Law.[255] Although the Paiges were providing the Lerner Fund with some information about the funds, the Lerner Fund was not being told, at the time the statement in the article was made, "where" its money was in the sense that it did not know how the money was invested. The Lerner Fund was refused access to that information after a series of specific demands, and despite a

[251] Pl. Op. Post-Tr. Br. at 66.
[252] *Id.*
[253] JX-318 ¶ 68.
[254] *Holy Spirit Ass'n for Unification of World Christianity v. New York Times Co.*, 399 N.E.2d 1185, 1187 (N.Y. 1979) ("Section 74 of the Civil Rights Law provides, in relevant part, that '(a) civil action cannot be maintained against any person, firm or corporation, for the publication of a fair and true report of any judicial proceeding, legislative proceeding or other official proceeding.' For a report to be characterized as 'fair and true' within the meaning of the statute, thus immunizing its publisher from a civil suit sounding in libel, *it is enough that the substance of the article be substantially accurate*.") (emphasis added).
[255] *Ingber v. Lagarenne*, 299 A.D.2d 608, 609 (N.Y. App. Div. 2002) ("As a defense, truth need not be established to an extreme literal degree. Provided that the defamatory material on which the action is based is *substantially true* (minor inaccuracies are acceptable), the claim to recover damages must fail.") (internal quotations omitted) (emphasis added).

contract, the Seeder Agreement, that gave them the right to receive "portfolio positions."[256] In that sense, the comparison to the Madoff scandal is apropos. The investors in the Madoff scheme were also being shown reports indicating the balances in their accounts, but did not know where that money was in terms of, for instance, which securities it was invested in. In that regard, the attorney's statements to the media, that the Lerner Fund was not being told where its money was invested, were substantially true, and therefore could not serve as the basis for a defamation claim even if they were not covered by the New York Civil Rights Law, which they are.

One final note as to this point. The article on HedgeFund.net was published on October 8, long after the Lerner Fund had filed its first document request in this litigation. In other words, when the HedgeFund.net article was published, not only had the Lerner Fund repeatedly asked the Paiges for more detailed information about its investment in the Hedge Fund, it had done so in the context of this judicial proceeding and was still being rebuffed. In fact, the Lerner Fund only received the portfolio position information that it was seeking about its investment in November 2010, after the Lerner Fund had filed a motion to compel. Even after production, the Lerner Fund had to file a motion to vacate the "highly confidential" designations that the Paiges had improperly placed on those records.[257] On this record, it would be impossible to conclude that any reputational harm suffered by the Paiges did not flow primarily from their own actions in: 1) gating for self-serving reasons the funds of an investor whose capital comprised over

[256] Seeder Agreement § 8.2(b).
[257] *Paige Capital Mgmt, LLC v. Lerner Master Fund, LLC*, C.A. No. 5502-CS, at 5 (Del Ch. Nov. 24, 2010) (TRANSCRIPT).

99.9% of the Hedge Fund's invested capital; and 2) refusing for nearly eight months to give that investor information about the Hedge Fund's investments, despite a contractual provision that gave the investor the right to see the Fund's "portfolio positions" upon reasonable request.[258]

D. The Paiges Are Not Entitled To Indemnity For Their Legal Expenses

The final issue that must be addressed is that of indemnification. Section 3.03(b) of the Partnership Agreement provides that:

> [Paige] General Partner, [Paige Capital Management], each of their respective directors, members, partners, shareholders, officers, employees, agents and affiliates . . . (each an "Indemnitee") *shall be indemnified* and held harmless by the [Hedge Fund] to the fullest extent legally permissible under and by virtue of the laws of the State of Delaware, as amended from time to time, from and against any and all loss, liability and expense (including, without limitation, losses due to trade errors caused by such persons, judgments, fines, amounts paid or to be paid in settlement and reasonable attorney's fees and expenses) *incurred, or suffered by the Indemnitee in connection with the good faith performance by the Indemnitee of his, her or its responsibilities to the [Hedge Fund]* provided, however, that an Indemnitee shall not be indemnified for losses resulting from his, her or its gross negligence, willful misconduct or violation of applicable laws . . . .[259]

In their complaint, the Paiges asserted two counts seeking a declaration under § 3.03(b) of their entitlement to indemnification from the Hedge Fund for: 1) the expenses incurred in this litigation; and 2) the losses suffered by the Paiges as a result of this litigation, including their "loss of reputation, emotional distress, and decreased ability to attract investors . . . ."[260] Of course, because the Lerner Fund's investment comprises

[258] Seeder Agreement § 8.2(b).
[259] Partnership Agreement § 3.03(b) (emphasis added).
[260] Compl. ¶¶ 92-103.

over 99.9% of the Fund's invested capital, the Paiges' request for indemnification is in essence a request to shift the costs and other losses incurred in this litigation to the Lerner Fund.

The Paiges make two main arguments as to why the Hedge Fund should indemnify them for the expenses of conducting this litigation.[261] First, as a practical matter, the Paiges point out that their original complaint only sought a declaratory judgment that the Gate Provision applied to the Lerner Fund and that it was the Lerner Fund that materially expanded the scope of the litigation by filing its counterclaims. The Lerner Fund counters that the Paiges' conduct in bringing this litigation was "partisan" and therefore not "in connection with" the performance of their responsibilities to the Hedge Fund.[262] I agree.

Contrary to what the Paiges argue, the Lerner Fund does not deserve blame for materially expanding the scope of this litigation. The claims the Lerner Fund filed in this

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[261] In the absence of any argument to the contrary, I apply the usual presumption that the Paiges as the plaintiffs bear the burden to prove their claim. That means that they bear the burden to show that their conduct falls within the coverage of § 3.03(b) of the Partnership Agreement. This is the usual allocation in indemnification cases. *See, e.g., Scharf v. Edgecomb Corp.*, 2004 WL 718923, at *3 (Del. Ch. Mar. 24, 2004), *rev'd on other grounds*, 864 A.2d 909 (Del. 2004) (placing the burden of proof on a plaintiff director in an action brought by that director in which he sought indemnification under 8 *Del. C.* § 145 and the corporation's mandatory indemnification bylaw for litigation expenses incurred in an action in which the director was not a named party but was subpoenaed to appear before a grand jury). *But see Stockman v. Heartland Indus. Partners, L.P.*, 2009 WL 2096213, at *13 (Del. Ch. July 14, 2009) (holding that where a party claiming indemnification pleads that it was subject to a proceeding within the scope of a mandatory indemnification provision, and that the proceeding ended favorably for the party seeking indemnity, the party did not have to plead and prove that it was, in essence, not guilty of conduct or scienter that would have taken it outside the provision's reach; but rather, in that limited circumstance, the defendant must, as an affirmative defense, prove that the party's conduct or scienter rendered it ineligible for indemnification).

[262] Def. Rep. Post-Tr. Br. at 34-35 (citing *Active Asset Recovery, Inc. v. Real Estate Asset Recovery Servs.,* 1999 WL 743479 (Del. Ch. Sept. 10, 1999)).

action were compulsory counterclaims that were filed in response to the Paiges' original complaint.[263]

The Paiges' second argument in support of their claim for indemnification is their main one, and is based on the language in § 3.03(b). That is, the Paiges argue that they did not engage in "willful misconduct, gross negligence, or violation of applicable laws," and that in any event, even if the Paiges were incorrect about their reading of the Seeder and Partnership Agreements, such a reading was a good faith and reasonable interpretation of those Agreements such that indemnification is still appropriate.[264] The Lerner Fund counters that the Paiges did not act in good faith, but violated their fiduciary duties by, among other things, sending the March 2010 Letter and applying the Gates against the Lerner Fund.

As an initial matter, I note that the Paiges' second argument in favor of indemnification — that indemnification is proper even if their purported good faith and reasonable reading of the Agreements turned out to be incorrect — is an odd one, and confuses the issue of the Paiges' potential right to indemnification for losses and liabilities under § 3.03(b) of the Partnership Agreement, on the one hand, with the previously discussed issue of statutory exculpation under 6 *Del. C.* § 17-1101(e), on the other. In any event, what seems to be the crux of their argument is that the expenses incurred in this litigation and the losses the Paiges allege to have suffered were incurred

[263] Del. Ch. Ct. R. 13(a).
[264] Pl. Op. Post-Tr. Br. at 61-62 (citing *Delphi Easter Partners Ltd. P'ship v. Spectacular Partners, Inc.*, 1993 WL 328079, at *4 (Del. Ch. Aug. 6, 1993)).

and suffered in connection with the Paiges' good faith performance of their responsibilities to the Hedge Fund.

Putting aside for the moment whether the Paiges have met their burden to show that their losses and expenses in this litigation were incurred as a result of conduct undertaken in good faith as § 3.03(b) requires, I note that their claim for defamation was clearly one designed only to serve the partisan ends of the Paiges and is therefore not "in connection" with the performance of the Paiges' "responsibilities to the [Hedge Fund],"[265] and thus is not indemnifiable.[266]

Having dispensed with that claim, I turn to the question of whether the Paiges' other claims — i.e., those relating to the dispute about the Gate Provision and the Paiges' compliance with their fiduciary duties — are subject to indemnification. Although the litigation of those claims is clearly in connection with the Paiges' performance of their responsibilities to the Hedge Fund, for the reasons I have already discussed at length, the Paiges have not persuaded me that their decision to cause Paige General Partner to impose the Gates was one made in good faith, as opposed to one made to advance their own selfish ends.

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[265] Partnership Agreement § 3.03(b).
[266] *See, e.g.*, *Active Asset Recovery, Inc. v. Real Estate Asset Recovery Servs.*, 1999 WL 743479, at *19 (Del. Ch. Sept. 10, 1999) (quoting *Shah v. Shah*, 1994 WL 586820, at *8 (Del. Ch. Sept. 15, 1994)) (denying indemnification for litigation expenses to a partner where "[m]uch, if not most, of the litigation expense" incurred was of "purely partisan expense, paid to advance [the partner's own] financial position . . . rather than "'for the 'preservation of [the partnership] business or property'").

For the foregoing reasons, the Paiges have not met their burden, and are not entitled to indemnification under § 3.03(b) of the Partnership Agreement.[267]

IV. Conclusion

For the foregoing reasons, the Lerner Fund has proven that it was a breach of contract and of fiduciary duty for the Paiges to apply the Gate Provision to the Lerner Fund.[268] Therefore, the Lerner Fund was entitled to withdraw all of its capital from the Hedge Fund[269] on October 31, 2010.[270] That capital shall be returned with an appropriate award of pre-judgment interest.

Additionally, the Paiges must repay the Hedge Fund any management and incentive fees earned on the Lerner Fund's capital since October 31, 2010. The Paiges' claims against the Lerner Fund for the violation of the implied covenant of good faith and

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[267] To the extent that the Paiges have received throughout the course of this litigation an advance of their legal fees and expenses, and have now been found not to be entitled to indemnification, the Paiges must repay all advanced amounts. *See Majkowski v. Am. Imaging Mgmt. Servs., LLC*, 913 A.2d 572, 587 (Del. 2006) ("A grant of advancement rights is essentially a decision to advance credit to the company's officers and directors because the officer or director must repay all sums advanced to him if it is later determined that he is not entitled to be indemnified.") (citing *Advanced Mining Sys., Inc. v. Frickle*, 623 A.2d 82, 84 (Del. Ch. 1992)); *see also Homestore, Inc. v. Tafeen*, 888 A.2d 204, 214 (Del. 2005) ("If it is subsequently determined that a corporate official is not entitled to indemnification, he or she will have to repay the funds advanced.").

[268] With regard to the Lerner Fund's breach of fiduciary duty claim, as previously discussed, Christopher Paige and Paige Capital Management were not properly subjects of that claim. But, as also noted in that portion of the opinion, I dismiss that claim against them without prejudice.

[269] I note again that although this opinion focuses on the Partnership Agreement for the onshore fund, the relief granted applies with equal force to the Lerner Fund's capital held in the offshore fund, both of which are intended to be captured by the use of the term "Hedge Fund."

[270] The Lerner Fund's claim that the Hedge Fund should be dissolved under 6 *Del C.* § 17-802 is moot because once the Lerner Fund withdraws all of its capital, it will be retired as a limited partner under the terms of the Partnership Agreement and can terminate the Seeder Agreement. *See* Partnership Agreement § 8.02(f); Seeder Agreement § 6.2.

fair dealing; defamation; indemnification; breach of contract;[271] and breach of fiduciary duty all fail. The Paiges are ordered to repay the Hedge Fund any fees and expenses advanced by the Hedge Fund related to this litigation. The parties shall meet and confer and attempt to agree on a form of final judgment and to settle the amount of pre-judgment interest due the Lerner Fund. If they cannot agree, they shall submit competing forms of order with letters justifying their requested order of no more than ten double-spaced pages on or before August 19, 2011. Replies of no more than five double-spaced pages shall be due on or before August 24, 2011. IT IS SO ORDERED.

[271] In addition to their claim that the Lerner Fund breached various written agreements, the Paiges' amended complaint also contains a claim for breach of an oral agreement that the Lerner Fund allegedly made in 2009 to assist the Paiges in their search for a new seed investor. That claim also fails. The Paiges spend no time in their post-trial briefing on this claim and rightly so. The record does not support a fair inference that the Lerner Fund ever made such a binding promise, much less that they received any consideration in exchange for doing so.