IN THE SUPERIOR COURT OF THE STATE OF DELAWARE

IN AND FOR NEW CASTLE COUNTY

ANGUILLA RE, LLC, a Delaware limited liability company and successor by assignment from DAVID B. SMALL and DAVID B. SMALL 2004 ANNUITY TRUST U/A/D 7/21/04,	)	
Plaintiff and Counterclaim Defendant,	)	
v.	)	C.A. No. N11C-10-061 MMJ CCLD
LUBERT-ADLER REAL ESTATE FUND IV, L.P., a Delaware limited partnership, LUBERT-ADLER CAPITAL REAL ESTATE FUND IV, L.P., a Delaware limited partnership, and LUBERT-ADLER REAL ESTATE PARALLEL FUND IV., L.P., a Delaware limited partnership,	)	
Defendants, Counterclaim Plaintiffs and Third-Party Plaintiffs,	)	
v.	)	
DAVID B. SMALL, an individual,	)	
Third-Party Defendant.	)	

Submitted: February 27, 2012
Decided: March 28, 2012

On Plaintiff's Motion to Dismiss Defendants' Counterclaims
GRANTED, WITH LEAVE TO RE-PLEAD

On David B. Small's Motion to Dismiss Third Party Complaint
GRANTED, WITH LEAVE TO RE-PLEAD

On Defendants' Motion for the Honorable Mary M. Johnston
To Sit By Designation in the Court of Chancery
DENIED, WITHOUT PREJUDICE

OPINION

Michael R. Lastowski, Esquire (argued), Sommer L. Ross, Esquire, Duane Morris LLP, Wilmington, DE, Attorneys for Plaintiff and Counterclaim Defendant, and Third-Party Defendant

Stuart M. Brown, Esquire, K. Tyler O'Connell, Esquire, Aleine Porterfield, DLA Piper LLP (US), Wilmington, DE; Gregory S. Otsuka, Esquire (argued), DLA Piper LLP (US), Chicago, IL, Attorneys for Defendants, Counterclaim Plaintiffs, and Third-Party Plaintiffs

JOHNSTON, J.

INTRODUCTION

Plaintiff Anguilla RE, LLC ("Plaintiff") filed suit against Defendants Lubert-Adler Real Estate Fund IV, L.P., Lubert-Adler Capital Real Estate Fund IV, L.P., and Lubert-Adler Real Estate Parallel Fund IV, L.P. (collectively referred to as the "Guarantors" or "Defendants"), claiming breach of contract. Defendants counterclaimed against Plaintiff and filed a Third-Party Complaint against David B. Small ("Small").

Pursuant to Superior Court Rule of Civil Procedure 12(b)(6), Plaintiff and Small seek to dismiss the claims brought by Defendants. In addition, Defendants have moved that this Court sit by designation as a member of the Court of Chancery. The Court held oral argument on the motions on February 27, 2012.

FACTUAL BACKGROUND

On May 21, 2005, Small and Barnes Bay Development Ltd. ("Seller") entered into a Purchase and Sale Agreement (the "Original PSA") for the purchase of Unit 6 (the "Villa") of The Villas at Anguilla (the "Resort"), located in the British West Indies. Pursuant to the Original PSA, Small agreed to purchase the Villa for $6,250,000.00, less a 10% incentive subject to additional terms and conditions. The Original PSA provided that this sum

was to be paid in incremental deposits,[1] and that Seller would deliver the Villa in May 2007.

That same day, Small and Seller also executed the following documents: (i) Incentive Addendum to Purchase and Sale Agreement The Villas at Anguilla ("Incentive Addendum"); (ii) Furnishings Addendum to Purchase and Sale Agreement The Villas at Anguilla ("Furnishings Addendum"); (iii) Addendum to Purchase and Sale Agreement The Villas at Anguilla ("Addendum"); and (iv) Non-Deed Use Restricted Addendum to Purchase and Sale Agreement The Villas at Anguilla ("Non-Deed Use Restricted Addendum") (collectively, referred to as "Addenda").

On February 20, 2006, Small, Seller, and the Guarantors executed Rider A which modified the Original PSA. Rider A required Small to make two additional deposits, totaling $1,175,050.00.[2] Rider A also provided, in pertinent part:

> In the event Purchaser has made all Deposits required under this Agreement, such Deposits and all the terms, conditions and obligations of Seller under this Agreement and all ancillary written agreements to the Agreement shall be guaranteed by: 1) Lubert-Adler Real Estate Fund IV, L.P., a Delaware limited

[1] Small was required to pay 20% of the purchase price ($1,125,000.00) upon execution of the Original PSA. Small was required to make an additional 20% deposit ($1,125,000.00) within 15 days of Seller's notice that the Villa's roof had been completed. The balance of the purchase price ($3,375,000.00) was due at closing.

[2] Small was required to pay an additional 20% deposit ($1,125,000.00) and a further deposit ($50,050.00) for the construction of an office within the Villa.

> partnership; 2) Lubert-Adler Real Estate Parallel Fund IV, L.P., a Delaware limited partnership; and 3) Lubert-Adler Capital Real Estate Fund IV, L.P., a Delaware limited partnership as to an undivided one-third obligation each, totaling the entire amount of such Deposits.

Rider A further provided that the Villa would be delivered by December 2008.

In accordance with the Original PSA and Rider A, Small paid all deposits due to the Seller. These deposits totaled $3,425,050.00.

Because of delays in construction of the Villa, Seller offered Small what Small has characterized as "complimentary" stays at the Resort. Defendants claim that Small and his family members stayed at the Resort on eight separate occasions for a total of 68 nights. The value of those stays, Defendants contend, totals $707,500.00.

On August 2, 2008, by assignment, Plaintiff acquired Small's interest and obligations under the Original PSA, Addenda and Rider A.

On May 4, 2009, Small, Seller, and the Guarantors executed a letter agreement, which further modified the Original PSA, Addenda, and Rider A (all executed documents collectively referred to as the "PSA").[3] The letter agreement expressly provided that: "Buyer has the right to terminate the

[3] For reasons not apparent to the Court, Small signed the letter agreement despite having assigned all interest to Plaintiff.

transaction contemplated by the Purchase Agreement at any time and for any reason prior to Closing."

On March 17, 2011, Seller filed for Chapter 11 bankruptcy protection in the United States Bankruptcy Court for the District of Delaware. Thereafter, the Bankruptcy Court entered an order authorizing Seller to take the necessary steps to transfer title to the Resort to SOF-VIII-Hotel II Anguilla Holdings LLC.[4]

By letter dated August 15, 2011, Plaintiff notified the Guarantors that the Seller was in default of its obligations under the PSA: "Defaults and events of defaults have occurred and are continuing under the Purchase and Sale Agreement because, among other things, the transaction contemplated by the agreement has not yet closed." Plaintiff demanded the immediate return of the deposits which totaled $3,425,050.00.

A second demand letter was sent to the Guarantors on October 5, 2011, by which Plaintiff expressly terminated the PSA, effective that date.

The Guarantors did not refund the deposits.

[4] At oral argument, the parties disputed whether title was actually transferred to SOF-VIII-Hotel II Anguilla Holdings LLC.

PROCEDURAL CONTEXT

On October 6, 2011, Plaintiff filed suit in this Court against Defendants, alleging breach of contract against each of the Guarantors.

On November 17, 2011, Defendants filed an Answer to Plaintiff's Complaint and asserted three counterclaims, alleging: (1) breach of contract; (2) breach of the implied covenant of good faith and fair dealing; and (3) entitlement to a declaratory judgment that Defendants are not obligated to make payment.

That same day, Defendants filed a Third-Party Complaint against Small, alleging: (1) breach of contract; (2) breach of the implied covenant of good faith and fair dealing; (3) unjust enrichment; (4) quantum meruit; and (5) entitlement to a declaratory judgment that Defendants are not obligated to make payment.

Plaintiff has moved to dismiss defendants' counterclaims. Small has moved to dismiss the Third-Party Complaint. Defendants have opposed both motions and have moved to have this Court sit by designation in the Court of Chancery for purposes of addressing the equitable relief sought by Defendants.

STANDARD OF REVIEW

When reviewing a motion to dismiss pursuant to Rule 12(b)(6), the Court must determine whether the claimant "may recover under any reasonably conceivable set of circumstances susceptible of proof."[5] When applying this standard, the Court will accept as true all non-conclusory, well-pleaded allegations.[6] In addition, every reasonable factual inference will be drawn in favor of the non-moving party.[7] If the claimant may recover under that standard of review, the Court must deny the motion to dismiss.[8]

Defendants' "Motion for the Honorable Mary M. Johnston to Sit by Designation in the Court of Chancery" is addressed to the sound discretion of the trial court.[9]

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[5] *Spence v. Funk*, 396 A.2d 967, 968 (Del. 1978).

[6] *Id.*

[7] *Wilmington Sav. Fund Soc'y, F.S.B. v. Anderson*, 2009 WL 597268, at *2 (Del. Super.) (citing *Doe v. Cahill*, 884 A.2d 451, 458 (Del. 2005)).

[8] *Spence*, 396 A.2d at 968.

[9] *See Humes v. Charles H. West Farms, Inc.,* 2007 WL 914907 (Del. Super.).

DISCUSSION

Choice of Law

Parties' Contentions

At oral argument, Defendants contended, for the first time, that certain issues raised in the pending motions to dismiss are governed by Anguilla law. Therefore, Defendants urged, any rights belonging to the Guarantors must be decided pursuant to Anguilla law.

In response, Plaintiff and Small argued that Defendants waived any choice of law argument because it was never raised in their briefing. Moreover, Plaintiff and Small claim that Defendants conceded that the application of Delaware law was appropriate because Defendants cited, almost exclusively, Delaware case law in their briefing.

Analysis

It is well-settled Delaware law that a party waives an argument by not including it in its brief.[10] Defendants raised the "Anguilla" choice of law argument for the first time at oral argument. There, Defendants argued:

> [T]here are at least three threshold issues that I think have to be answered before you can even consider the substance of the motions to dismiss. The first is choice of law. The Purchase and Sale Agreement is indisputably governed by Anguilla law.

[10] *Murphy v.* State, 632 A.2d 1150, 1152 (Del. 1993); In *re Asbestos Litigation*, 2007 WL 1651968, at *6 n.82 (Del. Super.).

> Therefore, the interpretation of the PSA and the guaranty, which is part of the PSA, has to be made under Anguilla law.[11]

When questioned by the Court as to whether Anguilla law differs from Delaware law, Defendants' counsel responded as follows:

> I don't know, Your Honor, and I would submit at this stage it's the plaintiff's motion to dismiss. Mr. Lastowski referred again and again to hornbook law. He didn't say what hornbook you should be looking at. They don't say in their motion. They never make any statement that, for example, Delaware law controls their claims, whether Anguilla law.
>
> Certainly, for our counterclaims, for our third-party claims, it will be our burden to prove what law applies. But I think at this stage for the plaintiff's motion to dismiss he has to make some showing of what law applies, and they haven't taken any position on that. I think absent some showing that Delaware law applies, Anguilla law applies, something else applies, I don't know how Your Honor can grant the motion to dismiss.[12]

In stark contrast to this argument, Defendants cited extensively to Delaware case law and statutory law in their pleadings and subsequent briefing. The Court finds that Defendants have conceded that Delaware law governs the matters under consideration, and have waived their right to assert choice of law for purposes of the pending motions.[13]

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[11] Tr. at 28 (Feb. 27, 2012).

[12] Tr. at 28-29.

[13] Moreover, it is not appropriate for counsel to present arguments to the Court that have not been thoroughly researched. *See Roca v. E.I. du Pont de Nemours and Co.*, 842 A.2d 1238, 1243 n.12 (Del. 2004) ("[I]ssues adverted to in a perfunctory manner, unaccompanied by some effort at developed argumentation, are deemed waived .... It is

Rights of the Guarantors

Parties' Contentions

Plaintiff and Small argue that Defendants, as guarantors, may not seek affirmative relief. According to Plaintiff and Small, Defendants may raise any defenses available to the principal obligor but may not assert any independent cause of action belonging to the principal.

In response, Defendants argue that, as guarantors, they assumed the Seller's "terms, condition and obligations" under the PSA. Therefore, they say, the Guarantors are entitled to assert any defenses or counterclaims that were available to the Seller.

Analysis

A contract of guaranty is a promise or undertaking that is collateral to a principal obligation. The guarantor is bound to perform in the event that the principal obligor defaults.[14] In other words, "[t]he guaranty is a separate

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not enough merely to mention a possible argument in the most skeletal way, leaving the court to do counsel's work .... Judges are not expected to be mindreaders. Consequently, a litigant has an obligation to spell out its arguments squarely and distinctly, or else forever hold its peace.").

[14] *Jones Motor Co. v. Teledyne, Inc*., 690 F.Supp. 310, 313 (D. Del. 1988) (citing Black's Law Dictionary (5th Ed. 1979)).

contract involving duties and responsibilities which are different from the basic contract to which it is collateral."[15]

As a general rule, "a guarantor, when sued by the principal's creditor pursuant to a guaranty agreement, cannot rely on an independent cause of action existing in favor of the principal against the creditor as a defense or a counterclaim."[16] Such a rule protects the underlying claims of the principal and minimizes litigation among the parties.[17]

Courts have carved out three exceptions to the general rule. A guarantor may assert the independent claim of the principal where: (1) the guarantor has taken an assignment of the independent claim or the principal has consented to the guarantor's use of the claim; (2) both principal and guarantor are joined as defendants; or (3) the principal is insolvent.[18] In these instances, the guarantor may set off the principal's independent claim

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[15] *FinanceAmerica Private Brands, Inc. v. Harvey E. Hall, Inc*., 380 A.2d 1377, 1379 (Del. Super. 1977).

[16] *Continental Group, Inc. v. Justice*, 536 F.Supp. 658, 661 (D. Del. 1982).

[17] *Id.; see also First Texas Serv. Corp. v. Roulier*, 750 F. Supp. 1056, 1061 (D. Colo. 1990) (noting that the rationale behind the general rule is to protect the claims of the principal, since the guarantor may not be in the best position to assert them).

[18] *Continental Group*, 536 F.Supp. at 661.

against the creditor's claim; however, the guarantor may not recover affirmatively.[19]

The third exception – the principal's insolvency – is relevant to the instant matter. As noted previously, the record establishes that Seller filed for Chapter 11 bankruptcy protection in the United States Bankruptcy Court for the District of Delaware in March 2011. At some point, Seller transferred ownership in the Resort and Villa to another entity.

During oral argument, Plaintiff's counsel stated that Plaintiff does not know the identity of the current owner. Plaintiff argued that it would be inappropriate and impractical for the Court to order Plaintiff to complete the transaction to purchase the Villa when title would be conveyed by an entity that is not a party to this action and is unknown to Plaintiff.

In its Complaint, Plaintiff alleges:

> Upon information and belief, as of the date hereof, title to the Resort has been transferred to SOF-VIII-Hotel II Anguilla Holdings LLC (the "Property Transfer") and, as a result, SOF-VIII-Hotel II Anguilla Holdings LLC is the legal and equitable owner of the Resort and Villa.[20]

[19] *Id.* at 662; *see also First Texas Serv. Corp.,* 750 F. Supp. at 1061 ("[I]f the guarantor's recovery on his counterclaim exceeds his liability under the guaranty, the guarantor may not recover this excess.").

[20] Complaint ¶ 29.

In its answer to the complaint, Defendants averred:

> Upon information and belief, the Lubert Adler Defendants admit that title to the Resort was transferred out of the Barnes Bay Development, Ltd. Bankruptcy estate. The Lubert Adler Defendants lack knowledge or information sufficient to form a belief as to the truth of the remaining allegations...and, therefore, deny them.[21]

During oral argument, the following colloquy occurred:

> DEFENSE COUNSEL: So the question should not be do we know today who the owner is. The question is should we be entitled to seek discovery on that?
>
> As an aside, the answer, as Your Honor knows, is made on behalf of the party. So the answer is made on – that Mr. Lastowski was just reading from is made on behalf of the Lubert-Adler parties. Does counsel know who the owner is? Yes. It's not like we don't know who the owner is, and how are we ever going to find out who the owner of this multimillion dollar property, who bought it, by the way, in a public auction, is. So that really is a red herring that there's no way we can have a trial because the owner is not known. I think that's all I have, Your Honor.
>
> COURT: If you know who they are, why did you say you don't have sufficient information to form a belief as to the truth of the remaining allegations?
>
> DEFENSE COUNSEL: Again, Your Honor, the Lubert-Adler parties do not have knowledge. I'm saying counsel is well aware of who the owner is.[22]

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[21] Defendants' Answer and Counterclaim to Complaint ¶ 29.

[22] Tr. At 57-58. The Court finds this colloquy unsettling. Counsel apparently has concealed knowledge from the clients on an issue directly relevant to these proceedings, *i.e.*, the identity of the current owner of the property subject to Defendants' guaranty. This refusal to reveal the owner's identity is counterproductive and not helpful to the

There appears to be no disagreement that the Resort and Villa are no longer part of Seller's bankruptcy estate. The logical extension of transfer of the Resort and Villa is that the current property owner is not insolvent. Thus, the guarantor Defendants may neither set off nor assert the independent and affirmative claims of the Seller. The burden is on Defendants to demonstrate an exception to the general rule.

No information has been provided to the Court regarding the nature and terms of the transaction transferring ownership of the Resort and Villa to the unknown party. If all rights, obligations and liabilities were transferred to the new owner, it may be that the new owner should be substituted as the principal.[23] If that is the case, and the substitute principal is not insolvent, the Defendant guarantors can neither seek setoff nor assert the affirmative resulting legal claims against Plaintiff and Small. Instead, Defendants would be limited to raising defenses available to the principal obligor.

Court in determining the rights and obligations of the parties. Should there be reasons why counsel must protect the current owner's identity from discovery by Defendants or other parties, such a circumstance may be a conflict of interest requiring counsel to withdraw from all clients' representation. *See* Delaware Lawyers' Rule of Professional Conduct 1.7.

[23] Specific performance is an equitable cause of action, and runs with the land. Obviously, a party cannot be compelled to purchase property from an undisclosed entity. It would follow, therefore, that the present owner is an indispensable party to the specific performance claim under the rules of any Delaware trial court authorized to consider such a claim. *See* Del. Ct. Ch. R. 17(a).

Defendants have the burden of demonstrating the propriety of the insolvency (or any other) exception to the general rule. The exception would permit a guarantor to assert setoff and prosecute claims in the stead of the principal. Because the Seller apparently remains in bankruptcy, Defendants have established a *prima facie* case of insolvency. However, all parties agree that the Resort and Villa are under new ownership. Thus, it is unclear if the insolvency exception applies. Because Defendants are unwilling or unable to provide information regarding the transfer of the Resort and Villa, Defendants have failed, at this juncture, to meet their burden and the counterclaims and third-party claims will be dismissed, with leave to re-plead.

Specific Performance

Parties' Contentions

Small and Plaintiff argue that Defendants are not a party to the PSA, and therefore, cannot enforce the contract. Small and Plaintiff further argue that even assuming, *arguendo*, Defendants were entitled to enforce the contract, this Court does not have subject matter jurisdiction to order specific performance.

In response, Defendants argue that they are entitled to enforce Plaintiff and Small's performance under the PSA. Defendants claim that, as

guarantors, they may assert any defenses or counterclaims that were available to the Seller. According to Defendants, Seller performed its obligations under the contract by creating a "unique" property for Plaintiff and Small. Plaintiff and Small then, according to Defendants, "materially and repudiatorily" breached the PSA by refusing to accept the Seller's tender of the Villa. Therefore, Defendants contend that they are entitled to specific performance.

Analysis

The right to compel the specific performance of a contract is a purely equitable remedy, and will not be given in substitution of a legal remedy when it is adequate.[24] To be "adequate," a remedy at law must afford a party full, fair and complete relief, and be as practical to the ends of justice and to prompt administration as the remedy in equity.[25]

Generally, a party seeking relief based upon a breach of contract claim will have an adequate remedy at law in the form of monetary damages.[26] However, "[a] legal remedy may be inadequate where a party's injury from breach of contract is either noncompensable or cannot be valued with

[24] *Chavin v. H. H. Rosin & Co*., 246 A.2d 921, 922 (Del. 1968).

[25] *Clark v. Teeven Holding Co*., 625 A.2d 869, 881 (Del. Ch. 1992).

[26] *Mills v. Gosling Creek, Inc*., 1993 WL 485901, at *2 (Del. Super.).

reasonable certainty."[27] In such a case, the Court of Chancery may exercise its jurisdiction to compel the opposing party to specifically perform its equitable obligations.

Here, Defendants seek monetary damages as well as specific performance. If a determination is made that monetary relief is inadequate, this Court is vested with authority to sever and transfer the equitable claims to the Court of Chancery.[28] The Superior Court would retain jurisdiction over the claims at law. Subsequent to any transfer, any party could petition for, or either court could *sua sponte* initiate, proceedings to consolidate the cases before one Judge or Chancellor in accordance with Article IV, Section 13(2) of the Delaware Constitution of 1897.

Unless or until a determination is made that remedies at law are inadequate, this Court will not be in a position to consider the propriety of severance and transfer to the Court of Chancery.

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[27] *El Paso Natural Gas Co. v. TransAmerican Natural Gas Corp*., 669 A.2d 36, 40 (Del. 1995); s*ee, e.g.*, *Mills*, 1993 WL 485901, at *2 ("One instance of legal inadequacy occurs where the 'thing' sought by the plaintiff is so unique as to render damages insufficient.")

[28] *See* 10 *Del. C*. § 1902 ("No civil action, suit or other proceeding brought in any court of this State shall be dismissed solely on the ground that such court is without jurisdiction of the subject matter, either in the original proceeding or on appeal. Such proceeding may be transferred to an appropriate court for hearing and determination ....").

CONCLUSION

The Court finds that Defendants have waived their right to assert choice of law by failing to include any choice of law argument in their briefing. Additionally, by citing extensively to Delaware case law and statutory law, Defendants have conceded that Delaware law governs these motions.

The Court finds that denial, with leave to re-plead, is appropriate as to Defendants' counterclaims and third-party complaint. In order to determine whether the insolvency (or another) exception applies, Defendants must allege information regarding the transfer of the Resort, including what interests were transferred to the new owner and the identity of that entity. If Defendants are not able to do so, they will be barred from asserting setoff or prosecuting the principal's affirmative claims, unless an exception to the general rule[29] is applicable.

Finally, unless or until a determination is made regarding the adequacy of the remedies at law, this Court will not be in a position to sever and transfer any equitable claim to the Court of Chancery.

[29] As previously set forth in this opinion, a guarantor cannot prosecute on an independent cause of action that could be asserted by a principal against a creditor. There are three exceptions: (1) the guarantor has taken an assignment of the claim or the principal has consented to the guarantor's use of the claim; (2) both principal and guarantor are joined as defendants; or (3) the principal is insolvent.

THEREFORE, Plaintiff's Motion to Dismiss Defendants' Counterclaims, and David B. Small's Motion to Dismiss are hereby **GRANTED,** with leave to re-plead. Defendants' Motion for the Honorable Mary M. Johnston to Sit by Designation on the Court of Chancery is hereby **DENIED**, without prejudice, pending further determination of the adequacy of remedies at law.

IT IS SO ORDERED.

/s/ *Mary M. Johnston*
The Honorable Mary M. Johnston