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Case Number 106,2019

IN THE SUPREME COURT OF THE STATE OF DELAWARE

LAW OFFICE OF KRUG,	:	
	:	
Defendant Below,	:	
Appellant/Cross-Appellee,	:	
	:	
v.	:	C.A. No. 106,2019
	:	
A&J CAPITAL, INC.	:	**Court Below – Court of Chancery**
	:	**of the State of Delaware,**
Plaintiff Below,	:	**C.A. No. 2018-0240-JRS**
Appellee/Cross-Appellant.	:	

CROSS-APPELLANT'S REPLY BRIEF ON CROSS-APPEAL

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DATED: July 19, 2019

TABLE OF CONTENTS

TABLE OF AUTHORITIES

CASES

ARGUMENT

I. THE COURT OF CHANCERY ERRED BY FAILING TO GRANT SUMMARY JUDGMENT IN A&J'S FAVOR

As set forth in A&J's[1] brief, Krug conceded below that, had the Company been a corporation instead of an LLC, the for-cause removal provision at issue here would have required notice and an opportunity to respond under the over sixty years of corporate law precedent relied upon by A&J. (AJB 14, 42; B167-70).[2] In his six-page argument in opposition to A&J's cross-appeal, Krug fails to respond to this fundamental point, and thus concedes it again by his silence.

As also set forth in A&J's brief, the Court of Chancery erred when it declined to follow the aforementioned corporate law precedent, because the Company's structure is sufficiently similar to a corporation to apply such precedent. (AJB 43-

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[1] Capitalized terms not defined herein have the meanings set forth in Appellee's Answering Brief on Appeal and Cross-Appellant's Opening Brief on Cross-Appeal ("AJB").

[2] While more relevant to Krug's appeal than to A&J's cross-appeal, it is noteworthy that this precedent also supports the proposition that Krug, as the party advocating removal, bore the burden of proving that cause existed. *Campbell v. Loew's, Inc.*, 134 A.2d 852, 860–61 (Del. Ch. 1957) ("The charges in this area made by the Vogel letter are ***legally sufficient to justify*** the stockholders in voting to remove such directors."); *Bossier v. Connell*, 1986 WL 12785, at *5 (Del. Ch. Nov. 12, 1986) ("[I]t is clear that the Administrative Committee ***had adequate grounds*** to direct the trustees to remove Mr. Bossier for cause ….") (emphases added). It should also be recalled that Krug filed a counterclaim seeking a determination that A&J was removed for cause (BR69-71), as to which he plainly bore the burden of proof.

46). As the Court of Chancery recently noted in another case: "If the drafters have opted for a manager managed entity, created a board of directors, and adopted other corporate features, then the parties to the agreement should expect a court to draw on analogies to corporate law." *Freeman Family LLC v. Park Avenue Landing LLC*, 2019 WL 1966808, at *5 (Del. Ch. Apr. 30, 2019) (quoting *Obeid v. Hogan*, 2016 WL 3356851, at *6 (Del. Ch. June 10, 2016)). Krug did not respond to this argument either. Nor did he cite the leading partnership case on which he relied below to argue that corporate law precedent should not apply in this case: *Davenport Group MG, L.P. v. Strategic Inv. Ptnrs., Inc.*, 685 A.2d 715 (Del. Ch. 1996). Additionally, Krug fails to reconcile his rejection of corporate law precedent in this context with his use of such precedent in other contexts. (AJB 26-27).

Rather than addressing these central points, Krug instead focuses on other arguments for why this Court should not follow corporate law precedent in this case. All of these arguments fail.

First, Krug argues that A&J seeks to "rewrite" or "alter or amend" the for-cause removal provision to include the requirements of notice and an opportunity to respond. (KAB 3, 4, 8).[3] If the same provision would require procedural due process if written in a corporate charter, it does not need to be rewritten, altered or amended.

[3] Citations in this format are to Appellant's Reply Brief on Appeal and Cross-Appellee's Answering Brief on Cross-Appeal.

Nor does A&J argue that there is some "gap" that needs to be filled in the language, as Krug suggests. (*Id.* 7-8). The language simply needs to be construed in accordance with corporate law precedent. As a policy matter, failing to apply corporate law precedent in this instance would create confusion among drafters of corporate and alternative entity documents as to whether express language is required in order to invoke procedural protections in a for-cause removal of a director or manager.

Second, and relatedly, Krug relies on the LLC Act's policy of freedom of contract to argue that A&J could have bargained for procedural protections but did not do so. (KAB 4, 8). This again begs the question of how for-cause removal provisions should be construed. The common understanding of such provisions for nearly six decades was that they provided for procedural protections even if they did not say so expressly. Moreover, Krug's argument turns the relationship between common law and the language of LLC agreements on its head: even with the LLC Act's policy of freedom of contract, this Court has repeatedly noted that provisions of a partnership agreement modifying common law fiduciary duty principles must be clear.[4] Thus, the question is not whether the for-cause removal provisions

[4] *See, e.g., Cont'l Ins. Co. v. Rutledge & Co., Inc.*, 1999 WL 66528, *2 n.8 (Del. Ch. Jan. 26, 1999) ("Absent a clear modification of the statutory and common law fiduciary rules, ... it is entirely appropriate for the Court to import rules of law and notions of fairness from outside the limited partnership context.") (citation omitted);

expressly incorporate the protections already provided under common law, but whether they plainly and clearly alter common law protections for for-cause removals. Here, they do not.

Third, Krug now relies (for the first time) on Section 18-405 of the LLC Act for the unremarkable proposition that an operating agreement may provide for the removal of managers. (KAB 5, 7). There is no dispute about this truism. But that statute says nothing about how the for-cause removal provision in this case should be construed and thus adds nothing to the analysis.

Fourth, like the court below, Krug also asserts that express provisions for procedural protections in a for-cause removal are "routinely used in Delaware LLC operating agreements." (*Id.* 8). Also like the court below, however, Krug fails to provide support for this assertion. (AJB 42).

Finally, Krug urges that Delaware common law should not be "grafted" onto or "incorporat[ed]" into LLC agreements. (KAB 4, 8). However, as A&J argued below (BR87 at n.7), such incorporation of Delaware common law occurs as a matter of law application by virtue of the Delaware choice of law provisions in the

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In re Cencom Cable Income Partners, L.P. Litig., 2008 WL 5050624, *4 (Del. Ch. Nov, 26, 2008) ("[F]iduciary principles are a species of common law. Of course, our case law has recognized that parties to a partnership agreement are free to alter by contract common law fiduciary principles. Said another way, 'principles of contract may, in appropriate circumstances, preempt fiduciary principles if the parties to a limited partnership have made their intentions to do so plain.'") (quoting *Sonet v. Timber Co., L.P.*, 722 A.2d 319, 324 (Del. Ch. 1998)).

Operating and Management Agreements. (A113 § 11.8; A79 § 17(a)). *See QTP Fund LP v. Eurohypo Capital Funding LLC I*, 2011 WL 2672092, *8 (Del. Ch. July 8, 2011) (applying Delaware common law to determine interpretation of term "preference shares" as used in LLC and trust agreements with Delaware choice of law provisions); *Greetham v. Sogima L–A Manager, LLC*, 2008 WL 4767722, *14 (Del. Ch. Nov. 3, 2008) (applying Delaware common law to both contract and promissory estoppel claims under LLC operating agreement containing Delaware choice of law provision).

CONCLUSION

For the foregoing reasons, to the extent that this Court reverses the Court of Chancery's decision in A&J's favor after trial, this Court should reverse the Court of Chancery's summary judgment ruling.

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CERTIFICATE OF SERVICE

Kurt M. Heyman, Esquire, hereby certifies that, on July 19, 2019, copies of the foregoing Appellee's Reply Brief on Appeal was served electronically upon the following counsel:

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