or why he was in fact the correct party in interest. The Superior Court's decision on the first issue must be reversed as a matter of law.

II. A COVENANT AND TERM OF GOOD FAITH IS IMPLICIT IN SECTION 8.2 OF THE LLC AGREEMENT

A. Question Presented

Does an implied covenant and term of good faith and fair dealing apply to the indemnity provision of Section 8.2 of the LLC Agreement in this case for purposes of the New Wood's determination that Dr. Baldwin failed to act in good faith and failed to act in a manner that he or she reasonably believed to be in or not opposed to the best interests of the Company? The issue was preserved for appeal. *See* Order ¶¶ 14-19, at 13-18 (**Addendum**), **A124**, **A125-38**, **A192-95**.

B. Scope of Review

The standard of review from the entry of judgment on the pleadings is de novo, as this Court explained as follows:

> Our scope of review of the grant of a motion for judgment on the pleadings, which has not been converted into a summary judgment motion, is limited to a review of the contents of the pleadings. Our standard of review is to determine whether the court committed legal error in formulating or applying legal precepts. Accordingly, our review of the trial court's grant of a motion for judgment on the pleadings presents a question of law, which we review de novo.

Desert Equities, Inc. v. Morgan Stanley Leveraged Equity Fund, 624 A.2d 1199, 1204 (Del. 1993) (citations omitted); *see also W. Coast Opportunity Fund, LLC v. Credit Suisse Sec. (USA), LLC*, 12 A.3d 1128, 1131 (Del. 2010) ("the grant of a motion for judgment on the pleadings presents a question of law, which we review

de novo, to determine whether the court committed legal error in formulating or applying legal precepts." (internal quotations omitted)).

The standard of review for the construction of a contract is likewise de novo. *GMG Cap. Invs., LLC v. Athenian Venture Partners I, LP*, 36 A.3d 776, 779 (Del. 2012) ("We review questions of contract interpretation *de novo*.").

C. Merits of the Argument

1. The Superior Court Held That There Is No Implied Covenant of Good Faith and Fair Dealing

The Superior Court rejected Dr. Baldwin's counterclaim on the grounds that neither an implied covenant of good faith and fair dealing nor a term of good faith by necessary implication could be applied to the requirement in Section 8.2 of the LLC Agreement such that "New Wood [was required] to make an indemnification determination in good faith." Order ¶ 15, at 14 (**Addendum**).

The Court's analytical framework for reaching this conclusion was as follows: (1) an "implied covenant of good faith and fair dealing attaches to all contracts and exists to fill unanticipated contractual gaps," Order ¶ 14, at 13 (**Addendum**); but (2) an "implied covenant 'involves a cautious enterprise' in which a court infers contractual terms to fill gaps or developments that neither party anticipated," *id*.; and (3) "Baldwin's implied covenant claim fails because it would create a free-floating obligation of good faith that is not tethered to any unanticipated gap in the LLC Agreement," *id*. ¶ 15, at 14.

Based on this analysis, the Court held that "the implied covenant Baldwin advances directly would contradict the express language in the LLC Agreement, which conditions indemnification on a determination that a manager acted in good faith and in a manner he believed to be in the company's best interests." Order ¶ 15, at 14-15. As a result, the Superior Court held as a matter of law that all that was required by New Wood was an assertion — not supported by any factual basis and not generated in good faith — that Dr. Baldwin failed to act in good faith and failed to act in a manner he believed to be in New Wood's best interests.

2. Good Faith and Fair Dealing Under the Delaware Limited Liability Company Act

The policy of the Delaware Limited Liability Company Act, 6 *Del. C.* § 18-101 *et seq.,* is "to give the maximum effect to the principle of freedom of contract and to the enforceability of limited liability company agreements." 6 *Del. C.* § 18-1101(b). But such freedom of contract is not boundless and "the limited liability company agreement may not eliminate the implied contractual covenant of good faith and fair dealing." 6 *Del. C.* § 18-1101(c).

Moreover, "a limited liability company 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." 6 *Del. C.* § 18-1101(e). When "[i]nterpreted together, these provisions seem to identify the contractual covenant of good faith as the 'foundational' baseline duty and bad faith as the most restrictive

standard that can be used within the Delaware scheme." Thomas Earl Geu, *A Selective Overview of Agency, Good Faith and Delaware Entity Law*, 10 DEL. L. REV. 17, 37 (2008).

Delaware Courts have recognized that Delaware LLC "agreements will be honored by a reviewing court," but there are "limited exceptions." *Huatuco v. Satellite Healthcare*, C.A. No. 8465-VCG, 2013 Del. Ch. LEXIS 298, at *1 (Del. Ch. Dec. 9, 2013). "One important exception is [the] statutory prohibition on contracting out the covenant of good faith and fair dealing." *Id.* at *1 n.1. In other words, "[a] limited liability company agreement cannot validly eliminate either certain statutory mandates or the implied contractual covenant of good faith and fair dealing." *In re Atlas Energy Res., LLC*, C.A. No. 4589-VCN, 2010 Del. Ch. LEXIS 216, at *53 n.42 (Del. Ch. Oct. 28, 2010).

Furthermore, "[t]he implied covenant is 'best understood as a way of implying terms in the agreement, whether employed to analyze unanticipated developments or to fill gaps in the contract's provisions.'" *Walsh v. White House Post Prods., LLC* , C.A. No. 2019-0419-KSJM, 2020 Del. Ch. LEXIS 105, at *17 (Del. Ch. Mar. 25, 2020) (quoting *Oxbow Carbon & Minerals Hldgs. v. Crestview-Oxbow Acq., LLC*, 202 A.3d 482, 507 (Del. 2010)). It is established that the implied covenant "inheres in every contract and requires a party in a contractual relationship to refrain from arbitrary or unreasonable conduct which has the effect of preventing

the other party to the contract from receiving the fruit' of the bargain." *Kuroda v. SPJS Holdings, L.L.C.*, 971 A.2d 872, 888 (Del. Ch. 2009) (citations omitted).

As a result, good faith and fair dealing are inherent in and a foundational building block of all contracts and business models under Delaware law to fill gaps and to address unanticipated developments. *Walsh*, 2020 Del. Ch. LEXIS 105, at *17. These principles are, or should be, inherent in the judicial system because its mission statement is the administration of justice and inherent in the concept of justice is the concept of good faith and fair dealing.

3. An Implied Covenant of Good Faith Is Tethered to the Indemnity Provision in the LLC Agreement

When parties form a Delaware LLC, and into that LLC Agreement they include a provision whereby a member or manager is entitled to indemnity if sued as a result of their position within the company, and if that entitlement to indemnity is tethered to a requirement that the member or manager acted in good faith and in a way he or she believe was in the company's best interests, inherent in that structure is a requirement that the company exercise good faith and fair dealing when it makes a determination whether the member or manager acted in good faith and in a way that was in the company's best interests.

Such an implied covenant of good faith and fair dealing is inherent in such an indemnification provision; it is inescapable and ineluctable. And the reason why it is necessary to "fill the gap" and to address "unanticipated developments" in the

indemnity paradigm is because if it were not implicit or imposed by necessary implication, it would render nugatory the indemnity provision in Section 8.2 of the LLC Agreement and extricate it out of the LLC Agreement altogether, as described in the next section.

4. Refusing to Recognize an Implied Covenant of Good Faith Negates the Indemnity Provision Altogether

The Superior Court held, as a matter of law, that there is no implied covenant or term of good faith in Section 8.2 of the LLC Agreement when New Wood (or the majority unitholder) makes a finding that someone who received advancement fees failed to act in good faith and failed to act in a manner that he or she reasonably believed to be in or not opposed to the best interests of the Company. Order ¶¶ 14-17, at 13-16 (**Addendum**). As explained below, that construction effectively eliminated the indemnification provision from the LLC Agreement altogether. As a result, the only legally valid way to read Section 8.2 of the LLC Agreement is with an implied covenant of good faith and fair dealing.

This result is driven by the following paradigm, which cannot be contested and the officers and directors of New Wood would be duty-bound to follow it:

1. New Wood *always* has a default financial interest in clawing back whatever fees it has had to pay to a Manager or Member under Section 8.2 of the LLC Agreement;

2. New Wood therefore *always* has an interest in having the majority unitholder (not involved in the underlying litigation) execute a Written Consent finding bad faith and a failure to act in New Wood's best interest, regardless of whether there is a shred of factual support or any good faith basis for it;
3. New Wood will *always* use this claw back procedure, regardless of the truth / good faith basis / validity for the allegation of bad faith against the Manager or Member; and
4. The *only* situation in which this paradigm will not be followed is if the cost of filing suit to claw back the advancement fees would exceed the amount of the fees sought to be clawed back.

This is true regardless of whether the one seeking the advancement fees is the actual majority unitholder because the Written Consent will be generated by the majority unitholder "determined without regard to Members that are party to the Lawsuits." (**A109**.) Which is precisely what Mr. Bursky did in his Written Consent when he defined himself as the holder of "a Majority of the currently outstanding Units (determined without regard to Members that are party to the Lawsuits) . . . ." (**A109**.)

As a result, this Court is faced with two options in terms of the construction of Section 8.2 of the LLC Agreement:

1. Construe Section 8.2 of the LLC Agreement to impose a covenant of good faith and fair dealing on New Wood and the majority unitholder when making a finding that a Manager or Member failed to act in good faith and failed to act in New Wood's best interest; or
2. Construe Section 8.2 not to impose such a covenant of good faith, as the Superior Court did, which effectively eliminates Sections 8.2 and 8.3 from the LLC Agreement altogether.

Dr. Baldwin submits that the only legally permissible construction is to find that there is an implicit covenant and term of good faith and fair dealing embodied in Section 8.2 of the LLC Agreement for purposes of determining whether a Manager or Member is entitled to indemnity. To hold otherwise would be to eliminate the indemnity provision from the LLC Agreement, a result that is wholly contrary to the parties' intent and a result that is judicially proscribed.

5. A Covenant of Good Faith and Fair Dealing Fills a Gap and Addresses Unanticipated Developments

The reasons the Superior Court refused to recognize an implied covenant of good faith and fair dealing was that it would "create a free-floating obligation of good faith that is not tethered to any unanticipated gap in the LLC Agreement." Order ¶ 15, at 14 (**Addendum**). This finding is factually and legally incorrect.

Section 8.2 provides that the right to indemnifications is dependent on a finding that the Manager or Member "acted in good faith and in a manner that he or

she reasonably believed to be in or not opposed to the best interests of the Company . . . ." (**A53**.) That finding is the provision, or gap, to which the covenant of good faith would be tethered and it would not be some "free floating" covenant that could or would be applied randomly to each and every term and condition in the LLC Agreement (not that such a result would necessarily be erroneous).

Rather, it is an inherent requirement, indeed a *sine quo non*, that a finding of bad faith (or at least a failure to act in good faith) *must* be made in good faith. Otherwise, of what possible value is a "finding" made in bad faith that someone else acted in bad faith? That query is obviously rhetorical because such a finding would be of no value whatsoever. This "gap" in Section 8.2 of the LLC Agreement is precisely the type of gap and unanticipated development meant for an implied covenant of good faith.

6. Refusing to Recognize a Term of Good Faith Frustrates the Rights Under the LLC Agreement

The Court also rejected Dr. Baldwin's argument that a term of good faith is implied in Section 8.2 of the LLC Agreement by necessary implication: "Baldwin's argument that this Court should invoke the doctrine of necessary implication to imply a good faith term into the LLC Agreement likewise fails because the implied term would contradict the LLC Agreement's express language." Order ¶ 18, at 16-17 (**Addendum**). This finding is likewise erroneous.

The Court set the correct legal framework for when a term is implied by necessary implication:

> The doctrine of necessary implication permits a court to read an implied promise into a contract in order to carry out the purpose for which the promise was made or prevent one party from frustrating the other's right to receive the fruits of the contract. Terms are implied not because they are reasonable but because they necessarily are involved in the contractual relationship such that the parties only failed to express them because they are too obvious to need expression. In other words, the doctrine appears to be no broader than, and arguably is synonymous with, the implied covenant.

Order ¶ 18, 17 (**Addendum**) (citing *In re IT Grp., Inc.*, 448 F.3d 661, 671 (3d Cir. 2006) (the doctrine of necessary implication is used to "imply an agreement by the parties to a contract to do and perform those things that according to reason and justice they should do *in order to carry out the purpose for which the contract was made and to refrain from doing anything that would destroy or injure the other party's right to receive the fruits of the contract*." (emphasis in original) (quoting *Killian v. McCulloch*, 850 F. Supp. 1239, 1250-51 (E.D. Pa. 1994)).

The Court rejected this argument for the same reason it rejected the argument that there is an implied covenant of good faith — to impose such a term by necessary implication would re-write the terms and conditions of the LLC Agreement, something it refused to do.

But it was the parties' intent in the LLC Agreement to provide indemnity to Managers and Members if they were involved in litigation as a result of that person's position as a Manager or Member. And as explained above, not to impose a term or covenant of good faith on the determination as to entitlement effectively nullifies the right to indemnity altogether. As a result, the only way to "prevent one party from frustrating the other's right to receive the fruits of the contract," Order ¶ 18, at 17 (**Addendum**), is to impose a term of good faith by necessary implication. Any other contractual construction re-writes the LLC Agreement by doing away with the right to indemnity in its entirety.

7. The Paper Record in Terms of "Good Faith"

To determine whether a question of fact is presented in terms of: (1) whether Dr. Baldwin acted in good faith or bad faith; and (2) whether New Wood / Mr. Bursky acted in good faith or bad faith, the parties and this Court are limited to the paper record. On the first question of whether Dr. Baldwin acted in bad faith, as New Wood alleges and as Mr. Bursky supposedly "found," there is no evidence.

Aside from a procedural outline, all that is contained in the Written Consent is Mr. Bursky's bald declaration that Dr. Baldwin failed to act in good faith (i.e., he acted in bad faith) and that he failed to act in a manner that he reasonably believed to be in or not opposed to the best interests of New Wood. (**A108-11**.) There are no factual allegations and there is no outline of acts or omissions; it is simply a recitation

of the words taken from Section 8.2 of the LLC Agreement. (**A110**.) As a result, Mr. Bursky's bald accusation that Dr. Baldwin acted in bad faith, and New Wood's allegations based thereon, were simply accepted as true by the Superior Court.

On the second question — whether New Wood and Mr. Bursky acted in good faith or in bad faith — the paper record demonstrates that New Wood acted in bad faith for a number of reasons:

1. Dr. Baldwin was forced to file the Delaware Advancement Action to compel New Wood to pay the advancement fees that it was contractually obligated to pay because it refused to do so upon demand;
2. Dr. Baldwin was required to file a Motion for Partial Summary judgment in the Delaware Advancement Action to recover the advancement fees that New Wood was contractually obligated to pay because it refused to do so without a court order;
3. Dr. Baldwin was required to file the Rule 88 Motion in the Delaware Advancement Action to recover the advancement fees that New Wood was contractually obligated to pay because it refused to do so without a court order;
4. Dr. Baldwin was required to transfer the judgment in the Delaware Advancement Action against New Wood to Mississippi, have it

domesticated, and serve discovery to ultimately recover the advancement fees that New Wood was contractually obligated to pay;

5. The claims by New Wood and others against Dr. Baldwin in the First Delaware Action — the claims for which Dr. Baldwin was seeking advancement fees to pay — were ultimately dismissed in Dr. Baldwin's favor (i.e., he prevailed in the action for which he sought and recovered indemnification), Order ¶ 2, at 5 (**Addendum**);
6. The "finding" in the Written Consent signed by Mr. Bursky of ACR Winston that Dr. Baldwin (a) failed to act in good faith and that he (b) failed to act in a manner he reasonably believed to be in or not opposed to the best interests of New Wood is without any factual or evidentiary basis whatsoever;
7. The Written Consent was signed by Mr. Bursky, who was: (a) a defendant in the Mississippi Federal Action and was sued by OCI (managed by Dr. Baldwin); (b) a defendant in the Mississippi State Action and was sued by OCI; and (c) a plaintiff in the First Delaware Action and sued Dr. Baldwin and OCI; and
8. Messrs. Bursky and Liebich were the ones who terminated Dr. Baldwin from his position as President and General Manager of WPV, as alleged in the Mississippi Federal Action: "[Through] Defendants Bursky's and

> Liebich's willful and bad-faith conduct, . . . Dr. Baldwin was summarily terminated from his role as President and General Manager of WPV." *Oak Creek Invs., LLC v. Atlas Holdings LLC*, No. 1:18-cv-0023, Plf.'s Compl. ¶ 21 (N.D. Miss. Feb. 9, 2018) (ECF No. 1).

Meaning, neither New Wood nor Mr. Bursky was providing an "objective" assessment of whether Dr. Baldwin was acting in good faith and in the New Wood's best interests in the underlying litigation. To the contrary, New Wood and Dr. Baldwin have been adversaries throughout the entire process and a requirement that New Wood was required to make the indemnity finding in good faith is the only finding in keeping with the administration of justice. Indeed, given their history, a legitimate presumption can be made that the finding that Dr. Baldwin acted in bad faith was itself made in bad faith.

In terms of credibility, this supports Dr. Baldwin's allegation in his Answer that "[T]he Written Consent was entered into in bad faith in an attempt to avoid New Wood's obligation to indemnify Dr. Baldwin." (**A121**.) And in terms of the administration of justice, a question of fact is presented in terms of which party acted in good faith and which acted in bad faith. Judgment on the pleadings was in error.

8. How Courts Have Construed Implied Covenants of Good Faith

Plaintiffs pleaded a successful claim for a breach of an implied covenant of good faith and fair dealing in *Sheehan v. AssuredPartners, Inc.*, C.A. No. 2019-

0333-AML, 2020 Del. Ch. LEXIS 199 (Del. Ch. May 29, 2020). The Sheehans sold their insurance agency to the defendant, AssuredPartners ("AP"). *Id.* at *3. As part of the sale, the Sheehans signed employment agreements with AP and accepted positions. *Id.* at *5-6. The employment agreements provided that the Sheehans' employment could be terminated either with or without cause. *Id.* at *6. The Sheehans were eventually terminated for cause. *Id.* at *16.

Prior to their termination, AP requested certain financial information from the Sheehans, who attempted to provide the information but alleged that they had no access to it. *Id.* Among other things, the reasons AP gave for the Sheehans' termination included purported financial irregularities that demonstrated a violation of fiduciary duties and that the Sheehans "actions appear to have been knowingly done and intentionally concealed from the company." *Id.* at *17. Among other things, the Sheehans alleged that AP breached the implied covenant of good faith and fair dealing because they were not terminated pursuant to their termination agreements. *Id.* at 21.

The Court found that the Sheehans successfully pled a claim for the breach of an implied covenant of good faith. AP argued that "the implied covenant claim fails because the Sheehans do not identify a gap that an implied term might fill." *Id*. at *28. The employment agreements detailed that the Sheehans could be terminated in one of two ways, with or without cause. But the Court held that the "covenant of

good faith and fair dealing 'embodies the law's expectation that 'each party to a contract will act with good faith toward the other with respect to the subject matter of the contract.'" *Id*. at *29 (quoting *Allied Cap. Corp. v. GC-Sun Holdings, LP*, 910 A.2d 1020, 1032 (Del. Ch. 2006)).

The Sheehans' "Amended Complaint identifies a possible gap, specifically that a termination will not be done in bad faith.'" *Id*. at *30. And the Sheehans alleged that "the parties reasonably expected at the time they entered the Employment Agreements that AP Virginia would not terminate the Sheehans in bad faith." *Id*. The Court held that this was a sufficient allegation of a basis for an implied covenant of good faith and fair dealing to fill the possible gap in the employment contract. *Id*. at *31.

The allegations in this case of an implied covenant of good faith and fair dealing are equally applicable to Section 8.2 of the LLC Agreement. It is eminently reasonable for Dr. Baldwin to have assumed that he would not be denied his advancement costs and indemnity based on a bad faith (and wholly illusory) finding that he acted in bad faith. Like the gap in *Sheehan v. AssuredPartners*, this gap must be filled with an implied covenant of good faith and fair dealing. Otherwise, it would allow New Wood to do exactly what it did in this case — make a bald allegation, with no factual support, that Dr. Baldwin acted in bad faith and therefore is not entitled to the contractual indemnity that was one of the bargained for benefits under

the LLC Agreement. And as explained above, such a construction would wholesale extricate the indemnity provision from the LLC Agreement.

9. An Analogy Provides Further Guidance

An analogy provides contextual guidance on whether an implicit covenant of good faith should be imposed on an indemnity assessment under Section 8.2 of the LLC Agreement. New Wood's position was, and the Superior Court held, there is no implicit covenant of good faith and one must simply accept whatever is alleged in a Written Consent in terms of whether the Manager or Member acted in bad faith. Applying that model to an appeal in this Court, it would be the same as requiring an appellant to come forward with nothing more than the following assertion to support a reversal: "The lower court committed reversible error." No appendix, no question presented, no scope of review, no merits of the argument; just a bald attestation that "it is so."[5]

[5] *See, e.g.*, *Minner v. Am. Mortg. & Guar. Co.*, 791 A.2d 826, 851 (Del. Super. 2000) ("An opinion cannot be based simply on the *ipse dixit* of the expert." (citing *General Elec. Co. v. Joiner*, 522 U.S. 136, 146 (1997) ("Nothing in either *Daubert* or the Federal Rules of Evidence requires a district court to admit opinion evidence that is connected to existing data only by the *ipse dixit* of the expert.")); *Manturi v. V.J.V., Inc.*, 431 A.2d 859, 860 (N.J. Super., App. Div., 1981) ("This is an assertion he does not attempt to bolster beyond the bald statement that it is so, and one we find totally lacking in merit."); *Hathaway v. Bazany*, 507 F.3d 312, 318 (5th Cir. 2007) ("Without more than credentials and a subjective opinion, an expert's testimony that 'it is so' is not admissible." (quoting *Viterbo v. Dow Chem. Co.*, 826 F.2d 420, 424 (5th Cir. 1987)).

Fundamental notions of due process, not to mention common sense, demonstrate the absurdity of such a result. Implied covenants of good faith and fair dealing are imposed on contracts for good reason — to avoid absurd, arbitrary, and capricious results. And this will not, as the Superior Court suggested,[6] result in a flood of litigation for New Wood; it will simply limit New Wood to contests when it has a good faith basis for them. Meaning, it will require New Wood to honor its contractual obligation to provide indemnity in good faith.

10. The Superior Court Never Addressed the Allegations in Dr. Baldwin's Answer or Affirmative Defenses

The Superior Court addresses Dr. Baldwin's affirmative defenses and counterclaim on pages 13 to 18 of its August 23, 2021, Order. Although the heading for that section of the Order and Paragraph 13 (finding that Dr. Baldwin should have joined Mr. Bursky as a third-party defendant) contain a reference to Dr. Baldwin's affirmative defenses, the remainder of the Order is focused strictly on the viability of the counterclaim.

Does the Court's legal analysis on Dr. Baldwin's counterclaim apply equally to his affirmative defenses? Perhaps in the Superior Court's view this was just

[6] The Court observed that "[i]mposing an additional free-floating good faith obligation would subject every express and mandatory provision in the LLC Agreement to fact-intensive and unyielding judicial review." Order ¶ 17, at 16 (**Addendum**).

shorthand for its analysis of both the affirmative defenses and the counterclaim (as well as the allegations in the Answer), but they are quite distinct legal vehicles: One is a defense to a claim being asserted, the other a distinct claim being asserted.

Is this a distinction without a difference? Perhaps given that a refusal to construe an implicit covenant or term of good faith into Section 8.2 of the LLC Agreement would undermine both Dr. Baldwin's affirmative defenses and his counterclaim. But it is nonetheless a distinction worth noting given that the Superior Court never actually rendered a decision on whether the lack of an implied covenant or term of good faith in Section 8.2 of the LLC Agreement rendered Dr. Baldwin's affirmative defenses without merit as a matter of law.

CONCLUSION

For the reasons set forth above, this Court should reverse the Superior Court's August 23, 2021, Order and the Final Order and Judgment based thereon dated August 27, 2021.

Respectfully submitted,

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