IN THE COURT OF CHANCERY OF THE STATE OF DELAWARE

ROSS HOLDING AND MANAGEMENT COMPANY; ELD PARTNERS, L.P.; GREGORY N. SENKEVITCH; NICHOLAS G. STATHAKIS; and GARY J. SOPKO, Plaintiffs, v. ADVANCE REALTY GROUP, LLC; ADVANCE CAPITAL PARTNERS, LLC; ADVANCE REALTY DEVELOPMENT, LLC; PETER COCOZIELLO; ROTHSCHILD REALTY, INC.; ROTHSCHILD REALTY MANAGERS, LLC; FIVE ARROWS REALTY SECURITIES, III, LLC; D. PIKE ALOIAN; JOHN MCGURK; KURT R. PADAVANO; RONALD L. RAYEVICH; and PATRICIA K. SHERIDAN, Defendants.	Civil Action No. 4113-VCN

MEMORANDUM OPINION

Date Submitted: January 24, 2014
Date Decided: September 4, 2014

John V. Fiorella, Esquire and Jennifer L. Dering, Esquire of Archer & Greiner, Wilmington, Delaware, and Joseph A. Martin, Esquire and Darth M. Newman, Esquire of Archer & Greiner, Haddonfield, New Jersey, Attorneys for Plaintiffs.

Christopher Viceconte, Esquire of Gibbons P.C., Wilmington, Delaware, and Brian J. McMahon, Esquire and Christopher Walsh, Esquire of Gibbons P.C., Newark, New Jersey, Attorneys for Defendants.

NOBLE, Vice Chancellor

Plaintiffs are minority unitholders of a real estate investment and development firm. They are also former managers of the company and were terminated from their positions shortly before the company underwent a reorganization. The company's major institutional investor wished to liquidate its holdings and sought to do so by selling the company's revenue-generating, developed assets. The company thus proposed a reorganization to split off capital-intensive, undeveloped properties and to permit the CEO to continue to operate and develop them. The institutional investor and the CEO negotiated with one another to complete the reorganization and little attention was paid to the minority unitholders. The institutional investor also replaced its convertible notes with loans with an outstanding value it fixed itself. To determine the value, it took the number of the common units it would have held had it converted the notes into equity and multiplied it by an internal valuation unsupported by recent market transactions or contemporaneous analysis. The company completed the reorganization in September 2008, on the eve of the recession, and afterwards informed its investors of the terms of the deal.

The minority was given the option of cashing out its holdings at a discounted price or converting them into equity in the newly-split off development company, which was to be run by the CEO who had recently fired plaintiffs and which no longer benefited from the positive cash flows of the stabilized properties. Plaintiffs refused those options and instead retained their holdings in the company. The company has since that time pursued its liquidation strategy. Additionally, the company, like many other real estate companies, suffered during the recession, and the units held by plaintiffs are now without value. Plaintiffs have challenged the reorganization, arguing that the company's board breached its fiduciary duties to the plaintiffs and that the conversion was responsible for the diminution in the value of their units.

This post-trial memorandum opinion contains the Court's findings of fact and conclusions of law. The Court concludes that the company's board owes its unitholders fiduciary duties, which include duties of loyalty and good faith. Plaintiffs presented evidence implicating the board's disloyalty and bad faith which require the board to demonstrate the entire fairness of the self-interested reorganization. No steps were taken by the board which justify a lowered standard of review or which would cause plaintiffs to have to prove the unfairness of the transaction.

The Court finds that defendants did not demonstrate the entire fairness of the reorganization. Although the value of plaintiff's units increased through the Reorganization, the process employed by defendants to structure the conversion was unfair. However, the Court also concludes that plaintiffs were not damaged by the conversion as the value of their units nominally increased. This finding is made, in part, because plaintiffs sponsor the testimony of defendants' expert witness, although they take issue with certain minor aspects of his analysis. Plaintiffs' damages theories were unconvincing, and, although certain reasons exist to question the findings of defendants' expert witness, the failure of plaintiffs to forward a view of their damages that the Court could accept was troubling. Plaintiffs' other claims, many of which were likely abandoned, are also addressed at the end this opinion. Plaintiffs do not prevail on these claims.

I. BACKGROUND

A. *FARS's Loan to ARG*

Peter Cocoziello ("Cocoziello") served as the President and CEO and as a member of the Board of Managers (the "Board") of Advance Realty Group, LLC ("ARG" or the "Company"), a Delaware limited liability company headquartered in New Jersey.[1] ARG is a real estate investment firm, formed in July 2001 by rolling up several limited liability companies and their respective real estate assets, which owns and manages commercial properties in New Jersey, Maryland, and Virginia.[2] ARG's portfolio included certain properties which are subject to more specific claims discussed later: the Gateway property and interests in

[1] Pre-Trial Stip, Ex. A ("Admitted Facts") ¶¶ n-o.
[2] *Id.* ¶ m; Cocoziello Tr. 6.

445 Southgate and the Harrison property.[3] Advance Capital Partners, LLC ("ACP"), a New Jersey limited liability company owned by Cocoziello's family trust, was the majority owner of ARG from its formation in 2001 until 2008.[4] ARG's subsidiary, Advance Realty Development ("ARD"), a Delaware limited liability company based in New Jersey, held the organization's properties which were still being developed.[5]

Also in 2001, during the period of ARG's formation, ARG's management was looking for capital for ARG to grow the business and retained an advisor to locate willing investors.[6] ARG decided to partner with the real estate investment fund Five Arrows Realty Securities, III ("FARS"), a New York limited liability company, which invests funds of the Ohio Public Employees Retirement System ("OPERS").[7] FARS's strategy was to provide growth capital to private and public real estate operating companies in return for a steady return and an opportunity to participate in the increase in the companies' equity value.[8] Rothschild Realty Managers, LLC ("Rothschild") served as an investment consultant to FARS and

[3] The Gateway property was a property in Newark, New Jersey, which had certain associated development rights. Admitted Facts ¶ xxx. 445 Southgate was a vacant office building in Morris Township, New Jersey. *See* Cocoziello Tr. 164-66; Joint Exhibit ("JE")-81. Harrison was an undeveloped property in Harrison, New Jersey in which ARG owned a joint interest. Admitted Facts ¶ vvv.

[4] Admitted Facts ¶ p; Cocoziello Tr. 9-10.

[5] Admitted Facts ¶ r.

[6] Cocoziello Tr. 10-11.

[7] *Id.*; McGurk Tr. 297-98.

[8] McGurk Tr. 296 (FARS typically sought convertible debentures to execute that strategy).

managed its investments.[9] D. Pike Aloian ("Aloian") and John McGurk ("McGurk") were partners at Rothschild.[10]

On August 6, 2001, FARS invested in ARG pursuant to the Credit Agreement; it loaned $60 million with a maturity date of August 6, 2008.[11] The loan required repayment of the principal amount with interest to be paid at a 9% annual rate, which would increase to 15% if the loan was not repaid by August 6, 2008.[12] The promissory note FARS received permitted it to convert all or a portion of its debt into ARG Class A units at a conversion price of $16.65 per unit.[13] FARS could thus convert the debt into approximately 3.6 million common units of ARG, which would make FARS the holder of a majority of ARG's outstanding common units.[14]

McGurk explained that the FARS loan was somewhat atypical because it required certain governance changes, as reflected in an updated operating agreement.[15] Two plaintiffs viewed FARS's investment positively, explaining that they believed the FARS investment validated ARG, that the resulting relationship

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[9] Admitted Facts ¶¶ t-u; McGurk Tr. 212-13. Rothschild Realty, Inc. was the predecessor entity to Rothschild and was in existence from at least 2001 until March 31, 2007.

[10] Admitted Facts ¶¶ w, y. Aloian and McGurk were Managing Directors of Rothschild Realty, Inc., before it converted into Rothschild. *Id.* Rothschild later changed its name to Almanac Realty Investors in December 2012. McGurk Tr. 213-14.

[11] Admitted Facts ¶¶ v, cc-dd; JE-7 (the Credit Agreement).

[12] Admitted Facts ¶ yy; JE-7 § 2.04(a).

[13] Admitted Facts ¶ ww (this $16.65 per unit was consistent with ARG's internal valuation at the time that FARS loaned ARG $60 million); JE-7 at Art. VIII & Ex. A.

[14] JE-7 § 8.01(c).

[15] McGurk Tr. 297.

with FARS would improve ARG's governance, and that Aloian's and McGurk's experience would make the Company stronger.[16]

As a practical matter, through FARS's involvement, ARG amended its operating agreement to establish a four-member Board, which granted Cocoziello two designees and granted FARS two designees.[17] Cocoziello served on the Board and also controlled the vote of his second designee Plaintiff Gregory Senkevitch ("Senkevitch").[18] FARS designated Aloian and McGurk to serve as its representatives on the Board.[19] The terms of ARG's investment provided that if ARG defaulted on FARS's loan, ARG's Board would expand to add a fifth FARS-controlled Board seat, giving FARS majority control of the Board.[20]

In September of 2008, ARG reorganized by splitting off its developmental properties into ARD, turning over control of its revenue-generating properties to FARS, and seeking to cash out the minority at an allegedly discounted price (the "Reorganization"). Sometime before the Reorganization, OPERS's investment strategy had shifted and that prevented FARS from extending or adding to its

[16] Sopko Tr. 409-10; Senkevitch Tr. 736-37.
[17] Admitted Facts ¶ uu; JE-6 § 7.03.
[18] Admitted Facts ¶¶ g, o (Cocoziello continues to serve on ARG's Board).
[19] *Id.* ¶¶ w-y (Aloian and McGurk continue to serve on ARG's Board as well; Aloian replaced Cocoziello as ARG's President and CEO after ARG's conversion.).
[20] JE-6 § 7.03(a)(ii).

investment in ARG.[21] FARS thus had a different investment maturity horizon than ARG's other stakeholders.[22] ARG may have taken on more development commitments than its income from its leasing activities could support and found itself with cash flow problems; in other words, it may have needed more time to address its cash crunch than FARS would tolerate.[23]

ARG explored a variety of possible transactions which might satisfy FARS and permit it to continue its operations. However, ARG was unable to consummate a deal at a valuation it believed reflected its value. The Board thus decided to execute the Reorganization, allowing FARS to exit its investment and providing Cocoziello the opportunity to continue as a real estate developer without suffering adverse tax consequences associated with liquidating ARG's portfolio of

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[21] JE-23 at 1. Rothschild also appeared to become less enamored of FARS's investment in ARG as the vibrant real estate market Rothschild anticipated failed to materialize. A Disposition Report from ARG to OPERS, apparently prepared in conjunction with a 144A offering discussed below, indicates that the ARG investment was recommended because of excitement about ARG's management team, the opportunities within the central New Jersey market, and the possibility of an expected return near 20%. JE-18 at 2. However, the report explains that the "combination of 9/11 and a lengthy recovery in the jobs market caused the return of this investment to fall closer to the worst-case scenario. As of March 31, 2005 the internal rate of return is 8.3%." *Id.* at 3. Various income statements also reveal repeated net losses, operating cash flow deficits, and declining fair value estimates of ARG's equity. *See* JE-109 at Stanger 000334; JE-160 at 4, 6, 13-14; JE-196 at 3, 5; JE-211 at 2, 3, 5.

[22] Aloian explained to a potential investor that "FARS is approaching the end of its investment horizon" and that the objective of the Reorganization was "twofold – first to create a tax-efficient exit for [the principals and senior management team of ARG], who without such an interim step would be subject to substantial gains taxes and, second to provide FARS with a readily marketable cluster of high quality stabilized assets on which it can realize value over the near team." JE-408.

[23] *See* Senkevitch Tr. 750-51.

properties.[24] The events leading up to the conversion are described below, following a brief description of the other parties to the transactions.

B. *ARG's Other Employees*

Plaintiffs are former managers of ARG who were terminated from their positions on August 30, 2007, and are now the minority holders of ARG's Class A units.[25] Senkevitch served both as ARG's Chief Operating Office and as a Board member.[26] ELD Partners, a New Jersey limited partnership affiliated with Senkevitch, owns 60,066 Class A units.[27] Nicholas Stathakis ("Stathakis") served as ARG's Senior Vice President and Controller and owns 9,015 Class A units.[28] Gary Sopko served as ARG's Managing Director of Capital Markets and Acquisitions and also holds 9,015 Class A units.[29]

Senkevitch, Stathakis, and Sopko ran the "day-to-day affairs" of ARG.[30] Senkevitch and Sopko acknowledged that they were very familiar with ARG's real

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[24] *See supra* note 22.
[25] Admitted Facts ¶ l. Senkevitch, Stathakis, and Sopko also all held Class B units as well; however, those units were redeemed when they were terminated.
[26] *Id.* ¶¶ f-g.
[27] *Id.* ¶¶ c-e.
[28] *Id.* ¶¶ h-i.
[29] *Id.* ¶¶ j-k. On a fully-diluted basis Plaintiffs' units represented approximately one percent of ARG's pre-Reorganization value; the total minority interests represented approximately seven percent of ARG's pre-Reorganization value on a fully-diluted basis.
[30] McGurk Tr. 309.

estate assets and their values.[31] Senkevitch, Stathakis, and Sopko are, collectively with ELD Partners, the "Plaintiffs."[32]

Several other ARG employees with long-standing company relationships replaced Senkevitch, Stathakis, and Sopko after their termination. Defendant Patricia Sheridan ("Sheridan"), ACP's Chief Financial Officer since 2005, assumed the responsibilities of Stathakis and Sopko upon their termination.[33] Sheridan was the Treasurer and a Vice President of ARG from September 25, 2007 through September 18, 2008.[34] Defendant Sheridan had functioned in a financial role for a variety of Cocoziello entities over the relevant time period, including ARG, ACP, and ARD.[35] Defendant Kurt Padavano ("Padavano"), ARG's Senior Vice President,[36] assumed the position of COO and Secretary from September 25, 2007 through September 18, 2008.[37] Defendant Ronald Rayevich ("Rayevich") held Senkevitch's seat as ARG's fourth Board member from September 2007 until September 2008.[38] "Defendants" are, collectively, ARG, ACP, ARD, Cocoziello,

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[31] Sopko Tr. 521; Senkevitch Tr. 869-70.

[32] Ross Holding and Management Company, a New Jersey general partnership, was also a Plaintiff, but it settled with Defendants on the eve of trial. It owned 46,000 Class A units which were not redeemed during the Reorganization and thus it remained in ARG. Admitted Facts ¶ b.

[33] Sheridan Tr. 1265.

[34] Admitted Facts ¶ bb.

[35] Sheridan Tr. 1313-18. However, she had no financial interest in any of the entities involved in this dispute. *Id.* at 1268.

[36] Padavano Tr. 1360.

[37] Admitted Facts ¶ z.

[38] *Id.* ¶ aa.

Rothschild, Rothschild Realty, Inc., FARS, Aloian, McGurk, Padavano, Rayevich, and Sheridan.

C. *ARG Explores Financing Opportunities*

By 2005, ARG began exploring options to assist FARS in liquidating its investment in the company. Thus, ARG evaluated the possibility of a Rule 144A private placement and interviewed Citibank and other financial advisors to assist in the transaction. During the interview process, Citibank advised ARG that it could complete the 144A offering at a price of $28 to $30 per unit.[39] As due diligence progressed, Citibank recommended that certain development assets be excluded from the offering.[40] ARG's valuation was lowered to somewhere in the range of $24 to $27 per unit.[41] Aloian, on behalf of Rothschild, wrote to OPERS in June 2005 to explain that the fair market value of the company as of March 31, 2005, was $17.73 per unit and that Rothschild would recommend the offering at a valuation of no less than $25 per unit.[42]

However, the private placement market's interest in such a transaction waned over the summer and ARG was unable to meet certain leasing and cash-flow benchmarks which formed the basis of Citibank's earlier valuation.[43]

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[39] McGurk Tr. 317-18.
[40] Aloian Tr. 703.
[41] JE-15 at 4.
[42] *Id.* at 1.
[43] Aloian Tr. 706-07.

Consequently, the offering price declined to around $17 to $18 per unit and Citibank's prospects of raising the sought after financing became questionable.[44] ARG abandoned the transaction.

ARG later explored the possibility of recapitalizing a majority of its assets in February 2006, still in hopes of cashing FARS out.[45] General Electric Capital Corporation ("GECC") proposed recapitalizing a portion of ARG's portfolio through a $107.5 million mezzanine loan.[46] This amount would allow ARG to pay FARS $90 million, which reflected, according to McGurk, the valuation of FARS's convertible notes at that time.[47] GECC would have provided $95 million upfront and an additional $12.5 million in future funding, which could be drawn down over the five year term of the financing, ending in 2011.[48]

McGurk testified that the GECC transaction would have "left the company under water."[49] He argued that the 9% ARG was paying on the $60 million FARS loan required a payment of only $5.5 million annually to service the debt, which was preferable to paying more than $10 million annually on the GECC debt.[50]

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[44] McGurk Tr. 320.
[45] Senkevitch Tr. 757.
[46] McGurk Tr. 320-21; Senkevitch Tr. 757-64; JE-390.
[47] McGurk Tr. 322.
[48] The contract interest rate of the loan was 7% for years one and two, 7.5% for year three, and 8% for years four and five, and also guaranteed GECC an 11.75% internal rate of return. JE-390.
[49] McGurk Tr. 322.
[50] *Id.* at 322-23. McGurk explained that although ARG paid interest on $60 million, it did not have to pay any interest on the "$30 million of value[.]" *Id.* at 323. However,

McGurk did not waiver from his view that the GECC transaction would leave ARG's unitholders "high and dry," including Cocoziello, the majority holder.

According to Senkevitch, this transaction would have benefited ARG by cashing out FARS and by providing for additional liquidity and capital reserves which did not dilute existing unitholders.[51] Recalling the Board's July 2006 meeting, he claimed that McGurk essentially told Cocoziello that the GECC financing was not good for Cocoziello (or possibly ACP) and thus ARG would not accept the loan.[52] Senkevitch said that no other deliberations occurred at the Board meeting. He testified that he understood McGurk's "under water" comments to mean that McGurk believed ARG would be thrown immediately into a deficient cash flow position.[53] Senkevitch disagreed with that conclusion.

FARS only loaned ARG $60 million dollars and it had no contractual right to be paid 9% on $90 million to FARS. *See infra* notes 89-90 and accompanying text. Moreover, FARS's valuation of its units in ARG appears to reflect what Rothschild believed its investment should be worth, rather than what the market would pay for such units as reflected by the recently tested 144A transaction. McGurk testified that Senkevitch, at some point, asked how much it would cost to cash FARS out and that "we" (presumably Rothschild or FARS) replied that it would cost $90 million. McGurk Tr. 384. This conversation appears to have occurred before or during consideration of the GECC transaction, as a loan amount exceeding $90 million was sought specifically to remove FARS from ARG.

[51] Senkevitch Tr. 767.

[52] As Senkevitch put it, "Mr. McGurk stat[ed] rather emphatically that 'The GE mezzanine loan is not something that's good for you, is it, Peter [Cocoziello].' And Mr. Cocoziello answered no. He said – then Mr. McGurk said, 'So we're not going to do it.'" *Id.* at 768-69.

[53] *Id.* at 767-68.

ARG also lacked cash around this time and, because it was unable to pay certain creditors, needed a cash infusion.[54] To inject additional capital, in August 2006, Cocoziello made a $10 million investment through ACP on the same terms (pari passu) as the FARS loan.[55] Because ACP's investment was on the same terms as FARS's, it also had a strike price of $16.65 per unit, convertible into 600,600 units.[56] The units were valued at approximately $24 per unit around that time and, thus, the pari passu treatment immediately diluted the other unitholders.[57] McGurk testified that the "last money in" would ordinarily receive better terms than the first money in and ACP could have pushed for better terms, but instead generously agreed to be treated equally with FARS.[58]

D. *ARG Explores Sale Opportunities*

After ARG's initial attempts to liquidate FARS's investment failed, ARG sought to sell its operating real estate assets. In September 2006, Cocoziello and Senkevitch met with Aloian and McGurk and were told by Aloian that "[a]

[54] McGurk Tr. 313-14.
[55] Senkevitch Tr. 769.
[56] Stathakis Tr. 618-19.
[57] Senkevitch testified that this was based on the financial statement fair value. Senkevitch Tr. 770. Stathakis, ARG's controller at the time, testified that they had a book value of $24 at the time. Stathakis Tr. 619. Stathakis calculated Cocoziello's loan to have diluted the Class A by 56 cents per share.
[58] McGurk Tr. 314-15.

determination has been made that the best thing for the company and FARS would be to sell all or part of the operating property portfolio."[59]

In December 2006, ARG retained Lehman Brothers to market the assets.[60] Two major bidders emerged during the process: JER Partners Acquisitions IV, LLC ("JER") and Normandy Real Estate Partners, LLC ("Normandy"). They submitted bids in March 2007. Normandy's initial letter of intent ("LOI") offered approximately $730 million for the assets,[61] and JER's LOI offered $705 million.[62] The Board decided that same month that it preferred Normandy's offer over JER's and initiated due diligence with Normandy.[63]

The evidence indicates that Rothschild favored the Normandy bid and that Senkevitch and Sopko favored the JER bid, although the parties dispute the reasons for their differing views. The record demonstrates that Senkevitch and Sopko remained in touch with JER representatives, sought to increase JER's bid price, and hoped to present the feasibility of a JER transaction to the Board in May 2007.[64]

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[59] Senkevitch Tr. 772-73.

[60] Admitted Facts ¶ ggg.

[61] JE-53 at 1. Normandy's LOI also offered $680 million for the assets if the 445 Southgate property was excluded from the portfolio.

[62] JE-50 at 2.

[63] Admitted Facts ¶ jjj.

[64] *See* JE-57; JE-58; JE-61; JE-62; JE-68; JE-73; JE-80. Stathakis's views on the merits of the transactions are less clear and he does not appear to have been copied on the majority of the email communications between Senkevitch, Sopko, and JER.

Defendants contend that Senkevitch, with the assistance of Sopko, sought to sabotage the Normandy transaction because JER offered Plaintiffs an opportunity for employment after the acquisition to manage the assets. Defendants point to emails between JER, Senkevitch, and Sopko contemplating a transaction that would buy out the majority investor (ACP) and FARS and include an investment by Senkevitch and Sopko.[65] However, one of these emails, drafted in advance of a Board meeting, implies that Senkevitch and Sopko intended to present the transaction information to the Board.[66] Senkevitch explained that he was trying to put together a deal which would be acceptable to JER and which would also satisfy the desires of ACP and FARS "to be taken out of the existing core portfolio."[67] Normandy's LOI also acknowledged that there might be a continuing need for management after the transaction.[68]

[65] JE-54; JE-55.

[66] JE-55 ("[O]ur monthly [March] Board meeting start[s] . . . today. Obviously the primary agenda item is the transaction.").

[67] Senkevitch Tr. 934-35. He also explained that the Board knew about his activities because they were discussed at the March Board meeting and the goal of his continued conversations with JER was to have a second option available in case the transaction with Normandy faltered. *Id.* at 790-91.

[68] JE-53 at 1 ("Normandy is prepared to begin discussions with the Company's current management and employees regarding employment possibilities. We believe there will be many opportunities for employment given the lack of overlap between Normandy's and the Company's current management organizations."). Normandy's LOI did, nonetheless, differ from JER's in that an equity participation opportunity for existing management was not articulated.

McGurk thought that Senkevitch created "roadblocks" to delay or undermine the Normandy transaction.[69] Senkevitch apparently sought to have Normandy assume an additional $10 million liability which was not part of the Lehman Brothers book.[70] He and Sopko also appear not to have informed the Board about a December 2006 term sheet[71] from a third party proposing a joint venture through which it would acquire a 75% interest in the 445 Southgate property.[72] Cocoziello, McGurk, and Aloian only became aware of the proposal in May 2007.[73]

Cocoziello claimed that once he became aware of the third party's interest in 445 Southgate, he was able to close the joint venture, on ARG's behalf, in August

[69] McGurk Tr. 331.

[70] Senkevitch testified that the issue was raised at a meeting in which potential "stumbling blocks" were being considered and it was one of several issues he raised to plan the transaction. Senkevitch Tr. 785-89. He states that he was never told this was unproductive until Defendants' counterclaims were asserted in this action.

[71] JE-81.

[72] Senkevitch and Sopko testified that the Board discussed a joint venture proposal for the property at the December 2006 Board meeting. Senkevitch Tr. 797-98; Sopko Tr. 451-52. Senkevitch asserted that a joint venture was discussed generally, while Sopko testified that the third party proposal at issue was specifically discussed at the December Board meeting. In a May 21, 2007 email between McGurk and Aloian, both seem genuinely surprised that they had not heard of the proposal, and Cocoziello apparently learned about it from someone other than Senkevitch or Sopko. Aloian acknowledged in the May 2007 email that joint ventures generally were discussed in December 2006, but believed that the specific proposal nonetheless should have been disclosed before May of the next year. *See* JE-83 (email, dated May 21, 2007, from McGurk to Aloian stating that the joint venture "hadn't been disclosed"). Thus, the Court concludes that the contemporaneous evidence indicates that the proposal was not discussed at the December meeting, although likely the idea of joint venturing the property was discussed and rejected.

[73] JE-83.

2007.[74] Defendants contend that the successful disposition of this property allowed McGurk to complete his negotiations with Normandy and to agree to a memorandum of terms.[75] However, in August 2007, Normandy withdrew its offer and ceased further negotiations, apparently due to a tightening credit market.[76]

On August 30, 2007, Senkevitch, Sopko, and Stathakis were terminated from ARG, in part because of ARG's acknowledgement that it would no longer actively pursue new acquisitions and thus had no need for the management, financial analysis, and accounting processes associated with that strategy.[77] Various departments were downsized while ARG prepared to sell its stabilized portfolio. However, Cocoziello also had stopped trusting Senkevitch, Sopko, and Stathakis and believed that they had manipulated him by withholding the Southgate term sheet and by positioning themselves to profit from that deal.[78]

E. *ARG Plans the Reorganization*

The Board was aware that FARS's convertible notes would mature on August 6, 2008.[79] If the notes were not timely paid, FARS had the right to increase

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[74] Cocoziello Tr. 168.

[75] JE-98 (evidencing a purchase price of $678 million).

[76] Cocoziello Tr. 192. Normandy did, however, purchase two assets in October 2007 and a third in January 2008. Sopko Tr. 498.

[77] JE-144. All three men signed separation agreements with integration clauses and which confirmed that they were "fully vested" in their respective Class A units. The separation agreements did not contain promises to redeem their units. *See* JE-141; JE-146; JE-151.

[78] Cocoziello Tr. 172.

[79] Admitted Facts ¶ dd.

the rate of interest on its loan, put a fifth FARS-controlled director on the Board, and begin the process of recapitalizing or selling assets to recover the amount owed.[80] In response, the Board, newly reconstituted after Senkevitch's termination, decided that the Reorganization could help FARS liquidate its investment and allow Cocoziello to continue to manage ARG's developmental assets. McGurk explained that FARS sought to realize value from ARG and preferred not to impose extreme liquidity pressures on it.[81] Cocoziello acknowledged that McGurk and Aloian were considerate of the minority because FARS had the power to inflict a great deal of damage on the unitholders, for example, by imposing negative tax consequences.[82]

To respond to FARS's desire to exit its investment, the Board sought to create one stabilized, easily-capitalized, and readily-saleable company and a second capital-hungry company which likely would not be profitable for a period of three to six years and would develop those parcels of land that could not immediately be sold.[83] Thus, the Board decided to spin off ARG's development subsidiary, ARD, to ACP, permitting it to own and develop the capital-intensive

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[80] McGurk Tr. 341-42.
[81] *Id.* at 342.
[82] Cocoziello Tr. 183-84. Of course, Cocoziello was among the unitholders and, to the extent McGurk or Aloian intended to convert FARS's notes to units, FARS would have been a unitholder as well.
[83] McGurk Tr. 344-45.

properties. FARS would control ARG, which would keep the revenue-generating properties to sell them to satisfy FARS's investment.[84]

FARS, which valued its convertible debentures at $90 million ($25 per unit), would convert approximately $10 million of its debt at a strike price of $16.65 into approximately 600,000 units of ARG, so that FARS would have a majority equity interest in the reorganized ARG.[85] This amount was calculated to allow FARS to convert the minimum number of units necessary to achieve majority control.[86] After the conversion of $10 million of its debt into Class A units, the remaining balance of FARS's $60 million debt would be converted into $80 million worth of notes in the reorganized ARG. $60 million of these notes would bear interest at 9% and the other approximately $20 million in notes would bear interest at 7.5%.[87] Defendants claim this benefited ARG because the new $80 million in notes would not mature for ten years and would not require any interest payments until that

[84] Plaintiffs generally accept the Defendants' division of, and valuation of, the properties with the exception of certain specific properties discussed herein. Thus, the Court does not emphasize the mechanics of the distribution of properties.

[85] McGurk Tr. 358.

[86] *See* JE-203 ("Based on the data that you provided and assuming that all potential shareholders of ARG become actual shareholders, FARS would need to hold 600,000 shares to be a majority."); JE-200 at 2 ("FARS will convert approximately $[12] million of its existing convertible Note . . . into ARG Class A Common Units which will provide FARS with a greater than 50% equity and voting interest in ARG following the closing under the Redemption Agreement.").

[87] Admitted Facts ¶ vvvv.

time.[88] McGurk acknowledged that FARS's notes only permitted FARS to convert its notes into units, which would have made FARS a common unitholder with the same payment priority as the Plaintiffs.[89] However, the Reorganization allowed FARS to act as though it had converted its notes, but to hold loans which fixed its profits and gave it the right to be paid before the minority unitholders.[90] ARG also entered into an asset management agreement with one of Cocoziello's entities, which is not challenged.

ACP, as the majority equity holder in ARG before the Reorganization, would receive a majority equity interest in ARD and also receive promissory notes from ARG. Between ACP's $10 million pari passu investment in convertible notes, and its other holdings in preferred and common units, it held a total of 3,906,884 units.[91] The Board reasoned that, at a price of $25 per unit, the units were worth $97,672,100. Under the Reorganization, ACP planned to capture $85 million of that value through ARD, which would receive $45 million worth of ARG's developmental real estate assets and a promissory note from ARG for $40 million.[92] ACP would make up the difference in what it believed it was owed

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[88] Nonetheless, ARG paid over $5 million on these loans through quarterly interest payments until the third quarter of 2009. *Id.* ¶ zzzz.
[89] McGurk Tr. 223-24.
[90] *Id.* at 224.
[91] ACP's convertible notes could be converted into 600,600 units at a $16.65 strike price and it otherwise held 108,547 preferred units and 3,197,737 common units.
[92] Defs.' Post-Trial Br. at 31; Admitted Facts ¶ xxxx.

through two promissory notes from ARG in the amount of $12 million.[93] These notes, like FARS's, would not require payments, including interest payments, for ten years.[94] The Reorganization also contemplated cashing out the minority at a price of $21.68, with $5.84 payable in cash and $15.84 through a five-year promissory note accruing interest at 6%.[95]

Defendants rely on Sheridan's testimony that ARG negotiated with John Metzger ("Metzger"), the owner of approximately 75% of the units not owned by ACP, to argue that the Board negotiated with a majority of the minority in anticipation of the Reorganization. She testified that Metzger initially sought $25 per unit, but that by July 2008, Metzger was willing to accept a redemption price of $21.68, with $5.84 paid in cash and the balance paid over five years in the form of a trust preferred security which would earn interest at 7%.[96] The Court was not directed to any documentation supporting Sheridan's claim. Defendants assert that Metzger withdrew the offer because they could not reach an agreement concerning a separate indemnification issue worth approximately $100,000.[97]

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[93] Admitted Facts ¶ wwww.
[94] *See* JE-236; JE-240.
[95] JE-225.
[96] Sheridan Tr. 1283-87. A September 2008 email authored by Metzger stated that he received an offer with terms similar to those offered under the Reorganization, but with a term of four years on the notes. JE-247. It does not evidence his "willingness to accept" those terms.
[97] One may wonder whether the relatively small sum of $100,000 was the stumbling block or whether Metzger wanted to see how good of an offer he could obtain.

In tension with Sheridan's testimony that Metzger was ready to accept ARG's offer, Metzger, on June 30, emailed Sheridan to reject an offer of $21.68 and to inform her that he would confer with counsel.[98] Interestingly, Sheridan wrote back to Metzger and told him that his offer "will probably exceed that which any other unitholder may be receiving."[99] She then forwarded Metzger's email to Cocoziello, McGurk, Aloian, and Padavano and recommended that "we approach the other A unitholders with this offer such that if they accept [Metzger] has less basis for any suit he may contemplate."[100] Metzger eventually accepted the $21.68 offered under the Reorganization.[101] However, despite Defendants' implication that Metzger took the deal he "negotiated" (but later rejected in favor of consulting counsel) with ARG, Metzger received the same deal offered to the minority at the less favorable 6% per annum interest rate.

Sheridan and McGurk explained how they valued ARG's assets to derive the terms of the Reorganization. Sheridan claimed to have started with ARG's December 31, 2007 financial statements, which, coincidentally or not, valued the

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[98] JE-198. Sheridan, in the email, appears to have emphasized how poorly ARG was doing. In response, Metzger questioned whether Sheridan ignored the cash from recent asset sales in setting forth the basis for her offer. In other emails Metzger and Senkevitch questioned whether cash and profits from recent sales were missing from financial data provided to Metzger. JE-206; JE-220.

[99] JE-198.

[100] *Id.*

[101] McGurk Tr. 366-67; JE-225, Ex. B.

Class A units at $21.68.[102] ARG's accounting policies priced the assets using valuation software or, where information was available, by using information from an appraisal or from a sale contract.[103] This method was the same method established by Senkevitch when he was ARG's COO. Sheridan and McGurk then testified that the value of certain development rights of the Gateway property, which were not reflected in the financial statements, were also added to the valuation.[104] ARG also owned an interest in a joint venture with ARD in undeveloped land, the Harrison property. ARG and ARD were both entitled to a return of capital on their investment in the property, after which point ARG, ARD, and ACP were entitled to profit sharing.[105] Harrison was owned by ARG before the Reorganization, but was transferred to ARD during the conversion. Plaintiffs argue that the Defendants undervalued both of these properties when planning the Reorganization.

Curiously, when Defendants explain that the Board calculated the fair value of the Class A units for the purposes of structuring the Reorganization, they cite

[102] Sheridan Tr. 1269; JE-160 at 14.
[103] Sheridan Tr. 1266-67 (preferring to use the contract price, then the appraisal value, and finally the valuation software based on cash flows); JE-256.
[104] McGurk Tr. 351-53 (valuing the Gateway rights at approximately $15 million); Sheridan Tr. 1269 (valuing the Gateway rights at approximately $14.5 million).
[105] JE-361; JE-362. Before the Reorganization, ARG was entitled to 25% of the profits and ACP would receive 75% of the profits (after paying off the debt and returning the invested capital). After the Reorganization, ARG would receive 10% of the profits, ARD would receive 15%, and ACP would receive 75%.

the testimony of their expert witness, Kevin Gannon ("Gannon").[106] Gannon's testimony explains how he calculated fair value in anticipation of trial; this information was not available to the Board as it prepared for the Reorganization. The balance of Defendants' explanation for how they calculated fair value comes from testimony, rather than contemporaneous documents. Furthermore, Defendants assert that the Board arrived at a pre-conversion valuation of $25 per unit; however, the portion of Gannon's testimony to which they direct the Court states that he valued the units at $25.96 per share.[107]

The joint exhibits portray the negotiations between FARS's designees and Cocoziello and demonstrate that they were extremely attentive to the Reorganization's structure.[108] However, in the record before the Court, the minority interests appear to have been an afterthought.[109] The Board meeting

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[106] Defs.' Post-Trial Br. at 31 (citing Gannon Tr. 1156). In Gannon's preamble to this quote, he explains that his team did not rely on valuations given to him by the Defendants. He acknowledges that he received information from them, "but at the end of the day we made independent valuation judgments on every one of the assets ourselves." Gannon Tr. 1148.

[107] Defendants' decision to round the 96 cents down is, in this context, unusual; although the Court recognizes the conversion at a reduced value of $25 per unit would have been favorable to the minority.

[108] Notes, from meetings or otherwise, abound which consider the relative interests of FARS and ACP. *See* JE-162; JE-167; JE-169; JE-170; JE-180; JE-189; JE-200; JE-203; JE-217. These documents occasionally consider how the unitholders might respond to certain aspects of the deal which distribute value between FARS and ACP in non-uniform ways, how to work around the minority interests, and whether the deal accounts for the minority interests. *See* JE-167; JE-203; JE-217.

[109] *See supra* note 108; JE-170 (one sentence preceding a lengthy analysis of the waterfall between FARS and ACP notes that minority unitholders will be redeemed). The Board

minutes are general and state that the Board discussed the Reorganization at each meeting from December 2007 until September 2008; however, the minutes do not indicate that the interests of the unitholders were discussed.[110] Notes and emails reveal that the Reorganization's planners hoped that the minority would be persuaded to redeem their ARG units and instead become unitholders in ARD.[111] ARG also did not seek out a fairness opinion, apparently because of concerns about cost and time.[112]

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already knew that it could not force a minority redemption because it explored that possibility in connection with the Normandy transaction. *See* JE-92; Sheridan Tr. 1309-12.

[110] *See* JE-158; JE-172; JE-177; JE-182; JE-193; JE-195. The most specific considerations concerning the Reorganization which appear in the minutes are the references to obtaining lender consents and the progress reports of the deal's documentation.

[111] JE-174 (Aloian wrote, "This is what we want" next to "Go w/ ARD" from a list of the minority's options); JE-179 (email from Aloian to counsel stating that "[Cocoziello] continues to believe that he can get all of the 3rd party equity (common and preferred) to go with him into ARD, leaving FARS as virtually the only shareholder of ARG. For these reasons our first choice would be not to offer a cash-out option."); JE-203 ("To the extent that there are other shareholders in ARG after all is said and done, this [FARS converted units accruing at a 5% interest/dividend rate] will be a tough trick to pull off. My suggestion in this case would be to simply attach a higher accrual rate to the FARS Junior Note and not accrue anything on the common shares in a way that gets to the same economic result as a 5% accrual on both securities. I'll run some calculations to see what the percentage rate would need to be.").

[112] JE-179 ("[A deeply discounted (40%-50%) cash offer] is not desirable because it might require a fairness opinion (both costly and time-consuming)."). An attorney did advise that a "financial model" be prepared which outlines the "Treatment of ARG units not participating in the exchange offer." His email noted that this would have permitted a synopsis to be attached in the offering memorandum to "demonstrate how it was concluded that everyone was to get $x value, and also to demonstrate that [Cocoziello] is essentially getting the same deal." JE-185.

Furthermore, members of the Board acknowledged that they were acting in their own self-interest throughout the Reorganization. McGurk, in particular, was quite candid throughout his testimony. When asked about FARS's options as its convertible notes became due, he stated that he sought to begin negotiations with Cocoziello, "[a]s the largest shareholder, and as the other board member," asking, "how do we get value out of this, what do we do to essentially try to recover value in the company."[113] McGurk, when describing the events leading up to the Reorganization, first focused on the actions of Cocoziello and FARS, and then on how to deal with the minority.[114] When describing "our" estimation, in one instance, he explained he meant "FARS['s] and the board's" view that ARG should be carved up into two companies, one to further develop the non-cash flow generating assets and the other to be a "more stable, easily capitalized, readily saleable kind of company."[115]

Cocoziello, when recounting the Reorganization's negotiations, asserted that he was negotiating for ARD, ACP, and another related entity and that all of those entities were represented by the same counsel.[116] Cocoziello explained that Aloian and McGurk were negotiating on FARS's behalf. When Cocoziello was asked

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[113] McGurk Tr. 342.
[114] McGurk explained that Cocoziello represented the unitholders in negotiations surrounding the FARS debentures and that McGurk represented FARS. *Id.* at 383.
[115] *Id.* at 344-45. He cautioned, "[i]n addition, . . . we still had minority shareholders," and had to figure out how to deal with them. *Id.*
[116] Cocoziello Tr. 36-39. Sheridan also represented all of those entities.

who was negotiating on behalf of ARG, Cocoziello answered that he "was working and negotiating on behalf of myself and all the other minority shareholders."[117] After additional prompting, Cocoziello stated that the Board (presumably including McGurk and Aloian) represented ARG.[118]

F. *ARG Approves the Reorganization*

On September 5, 2008, ARG approved the Conversion and Exchange Agreement[119] on the terms described above. ARG sent a memorandum to investors, dated September 12, 2008, explaining that ARG and FARS had been working on the transaction for over a year.[120] ARG justified the Reorganization as a response to the fact that FARS's convertible debentures became due on August 6, 2008; thus, ARG asserted that the Reorganization was implemented in order to reach a "mutually agreeable plan for the repayment of the FARS indebtedness."[121]

The memorandum notified ARG's unitholders of the transaction and offered them two options: 1) to exchange their Class A Units for common units in ARD on the same terms as those accepted by ACP, or 2) to receive \$21.68 per unit payable in \$5.84 in cash and a promissory note of \$15.84 with an interest rate of 6%.[122] The memorandum, when explaining how FARS would receive its \$90 million of

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[117] *Id.* at 39.
[118] *Id.* at 39-40.
[119] JE-218.
[120] JE-225.
[121] *Id.*
[122] *Id.*

value from the transaction, contemplated that the Class A unitholders might refuse to redeem their units.[123] ARG's explanation of the Reorganization's impact upon the minority, if holders elected not to redeem their units, was primarily limited to its statement that ARG would liquidate its remaining portfolio of properties which would result in potentially adverse tax consequences for the remaining Class A unitholders.[124]

The September 12 memorandum did not attach the Conversion and Exchange Agreement or contain information detailing how the properties were valued or divided between ARG and ARD.[125] The memorandum notified investors that ARG would hold two conference calls to answer questions on September 15 and 16. Plaintiffs' counsel joined the September 15 call and later met with Sheridan to request $25 per unit, in cash, for Plaintiffs.[126] ARG and the Plaintiffs could not agree and Plaintiffs remained ARG unitholders by refusing to redeem their units.

The Reorganization occurred just before the unprecedented events of September 2008, which signaled that the United States economy was entering (or had entered) a severe recession. Later in September 2008, Lehman Brothers and Countrywide Financial would fail, Bank of America would save Merrill Lynch,

[123] *Id.*, Ex. A.
[124] JE-225.
[125] McGurk Tr. 245-51; Senkevitch Tr. 814-15.
[126] Admitted Facts ¶ qqq; Sheridan Tr. 1295.

and the United States would rescue AIG.[127] ARG suffered during this time, as tenants experienced financial difficulties and vacated leaseholds.[128] ARG made payments on the loans to ARD and FARS before it defaulted on debt owed to one of its major lenders in September 2009 (the "Taberna debt"). ARG's default resulted in its defaulting on the Class A unitholders' notes and in its auditor's questioning whether it could continue as a going concern.[129] Some evidence suggests that ARG hoped the default would force the lender to renegotiate the loan terms.[130] Plaintiffs have not received any value for their units and brought this action alleging breach of fiduciary duty, among other claims.

G. *The Litigation History*

The majority of Plaintiffs' claims survived Defendants' motion for judgment on the pleadings and to dismiss.[131] The Court determined that Defendants were entitled to summary judgment on several other claims made by Plaintiffs.[132] Plaintiffs' remaining claims for breaches of fiduciary duty, breaches of the implied covenant of good faith and fair dealing, fraudulent inducement, civil conspiracy, and aiding and abetting breaches of fiduciary duty, and their request for

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[127] Gannon Tr. 1134-35.
[128] McGurk Tr. 371.
[129] Cocoziello Tr. 147-53; McGurk Tr. 258; Sheridan Tr. 1307.
[130] Cocoziello Tr. 128-34; JE-296.
[131] *Ross Hldg. & Mgmt. Co. v. Advance Realty Gp., LLC*, 2010 WL 1838608, at *16 (Del. Ch. Apr. 28, 2010).
[132] *Ross Hldg. & Mgmt. Co. v. Advance Realty Gp., LLC*, 2013 WL 764688, at *6 (Del. Ch. Feb. 28, 2013, *as revised*, Mar. 7, 2013).

appointment of a receiver are addressed in this post-trial opinion. Defendants' counterclaims against Plaintiffs for breaches of fiduciary duty are also resolved in the reasoning which follows.

II. ANALYSIS

The parties dispute whether the Board owed ARG's members limited fiduciary duties, whether entire fairness review applies, and the merits of the entire fairness analysis. The primary focus of trial and the post-trial briefing was the fairness of, and the proper valuation of, the ARG Class A units at the time of the Reorganization. If the Class A unitholders were not dealt with in an entirely fair manner, the parties dispute whether ARG's operating agreement exculpated the Board's behavior. Finally, they debate whether, and to what extent, Plaintiffs were damaged by the Reorganization. Defendants also argue, in the sole counterclaim they pursue after trial, that Senkevitch and Sopko breached their fiduciary duties to ARG by failing to inform the Board of a corporate opportunity when they did not disclose the joint venture potential for 445 Southgate.

A. *What, If Any, Fiduciary Duties Does ARG's Board Owe to Its Members?*

Plaintiffs and Defendants disagree about whether ARG's Board owed its members those fiduciary duties typically found under the common law, such as the duty of loyalty, or more restricted duties under the terms of the Company's operating agreement. To determine what fiduciary duties are owed in the limited liability company context, the Court must review the company's operating agreement.[133] By default, the traditional fiduciary duties applicable to corporations apply to limited liability companies.[134] Nonetheless, where such default rules have been clearly supplanted or modified, those contractual choices will be respected.[135]

Defendants cite two provisions of ARG's operating agreement to argue that the parties narrowed the Board's fiduciary duties. They claim that Section 7.01 provides the standard of conduct:

> <u>Authority of the Board</u>. The Managing Board shall manage the business and affairs of the Company and shall have the exclusive power and authority . . . to make decisions regarding the management of the Company, and to take any action in connection therewith, which is not inconsistent with the provisions of this Agreement, applicable law or the contractual obligations of the Company. It is understood that the Managing Board shall act reasonably and in good faith in its management of the Company.[136]

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[133] *Zimmerman v. Crothall*, 62 A.3d 676, 702 (Del. Ch. 2013); *Douzinas v. Am. Bureau of Shipping, Inc.*, 888 A.2d 1146, 1149-50 (Del. Ch. 2006).

[134] *Feeley v. NHAOCG, LLC*, 62 A.3d 649, 659-63 (Del. Ch. 2012) (reviewing Court of Chancery decisions recognizing default fiduciary duties, while acknowledging that the Delaware Supreme Court has not made a pronouncement on such duties). Defendants appear to question whether default fiduciary duties apply to a limited liability company if not imposed by its operating agreement. However, *Feeley* is clear that such duties have been held to apply by the Court, subject to a final determination by the Delaware Supreme Court.

[135] *Auriga Capital Corp. v. Gatz Properties*, 40 A.3d 839, 852 (Del. Ch. 2012), *judgment entered sub nom. Auriga Capital Corp. v. Gatz Properties, LLC*, 2012 WL 598121 (Del. Ch. Feb. 23, 2012), *aff'd,* 59 A.3d 1206 (Del. 2012).

[136] JE-6 § 7.01.

Defendants contend the Board's fiduciary duties were structured to require it to act in an objectively reasonable manner and with subjective good faith.[137] They also argue that the operating agreement required that the Board be composed of designees of FARS and Cocoziello. That reality, in conjunction with Section 7.01's grant to the Board to have "exclusive" power and authority, they assert, meant ARG was free to engage in transactions with members of the Board or the interests they represent.

Defendants' arguments are unpersuasive. Drafters of a limited liability company agreement "must make their intent to eliminate fiduciary duties plain and unambiguous."[138] Earlier cases detail a variety of ways by which drafters of operating agreements may eliminate[139] or otherwise modify traditional fiduciary

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[137] Defs.' Post-Trial Br. at 46 (citing *Zimmerman v. Crothall*, 62 A.3d 676, 702 (Del. Ch. 2013)).

[138] *Feeley*, 62 A.3d at 664 (citing *Bay Ctr. Apartments Owner, LLC v. Emery Bay PKI, LLC*, 2009 WL 1124451, at *9 (Del. Ch. Apr. 20, 2009)). The same is true of modifications to default fiduciary duties. *See Kelly v. Blum*, 2010 WL 629850, at *10 n.70 (Del. Ch. Feb. 24, 2010) ("Having been granted great contractual freedom by the LLC Act, drafters of and parties to an LLC agreement should be expected to provide parties and anyone interpreting the agreement with clear and unambiguous provisions when they desire to expand, restrict, or eliminate the operation of traditional fiduciary duties.").

[139] *See, e.g.*, *CNL-AB LLC v. E. Prop. Fund I SPE (MS Ref) LLC*, 2011 WL 353529, at *9 (Del. Ch. Jan. 28, 2011) ("The execution, delivery or performance by the Managing Member . . . of any agreement authorized or permitted under this Agreement shall be in the sole and absolute discretion of the Managing Member without consideration of any other obligation or duty, fiduciary or otherwise, of the Company or the Members and shall not constitute a breach by the Managing Member of any duty that the Managing Member may owe the Company or any Non–Managing Member or any other Persons under this Agreement or of any duty stated or implied by law or equity."); *In re Atlas*

duties.[140] Section 7.01's sentence stating "[i]t is understood that the Managing Board shall act reasonably and in good faith in its management of the Company" does not adopt the lessons of those earlier cases clearly to eliminate or modify the traditional fiduciary duties. An argument exists that the provision could be read to displace the typical fiduciary duties that ARG's Board would otherwise owe its members and that the failure to mention the duty of loyalty indicates that that duty was eliminated. However, this interpretation of the operating agreement overlooks our law's requirement that the drafters' intent to eliminate such duties be plain and unambiguous.

Energy Res., LLC, 2010 WL 4273122, at *7 (Del. Ch. Oct. 28, 2010) ("[W]henever a potential conflict of interest exists or arises between any Affiliate of the Company, on the one hand, and the Company or any Group Member, on the other, any resolution or course of action by the Board of Directors in respect of such conflict of interest shall be permitted and deemed approved by all Members, and shall not constitute a breach of this Agreement . . . or of any duty existing at law, in equity or otherwise, including any fiduciary duty, if the resolution or course of action in respect of such conflict of interest is (i) approved by Special Approval, (ii) approved by the vote of holders of a majority of the Outstanding Common Units (excluding Common Units held by interested parties), (iii) on terms no less favorable to the Company than those being generally available to or available from unrelated third parties or (iv) fair and reasonable to the Company, taking into account the totality of the relationships between the parties involved (including other transactions that may be particularly favorable to the Company)."); *Fisk Ventures, LLC v. Segal*, 2008 WL 1961156, at *11 (Del. Ch. May 7, 2008), *aff'd*, 984 A.2d 124 (Del. 2009) ("[T]he [limited liability company agreement] eliminates fiduciary duties to the maximum extent permitted by law by flatly stating that members have no duties other than those expressly articulated in the Agreement. Because the Agreement does not expressly articulate fiduciary obligations, they are eliminated.").

[140] *See, e.g.*, *Zimmerman v. Crothall*, 62 A.3d 676, 703 (Del. Ch. 2013) (setting standard of conduct concerning duty of care and establishing safe harbor to duty of loyalty); *Flight Options Int'l, Inc. v. Flight Options, LLC*, 2005 WL 6799224, at *7-8 (Del. Ch. July 11, 2005) (applying standard to approve interested party transaction as one on "arms' length terms and conditions").

The first sentence of Section 7.01, titled "Authority of the Board," defines which stakeholders in ARG are responsible for managing the company. Thus, the second sentence, which states that "[i]t is understood" that the Board will act reasonably and in good faith, may have sought to articulate the Board's obligations mirroring the duty of care owed by directors to corporations. By setting forth those conditions, the drafters may not have intended to modify in any way the Board's ability to engage in conflicted transactions.[141] Said another way, an "understanding" that a Board's acts will be in compliance with certain broad standards does not necessarily imply a reciprocal understanding that all other duties, which traditionally apply, are being disclaimed. Moreover, where a line was intended, if one was intended, between loyalty and good faith, is uncertain.

Similarly, Defendants' argument that the operating agreement required that a conflicted Board make decisions because the Board was composed of Cocoziello, his designee, and FARS's designees, does not mean that the agreement's signatories would understand that the Board was released from its usual fiduciary obligations. The fact that the Board was structured in such a way as to be conflicted does not evidence a clear intent to eliminate the duty of loyalty. Delaware law permits conflicted Boards to authorize independent parties to

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[141] Indeed, in *Zimmerman*, a general provision setting forth the board's obligation to act reasonably and in good faith was not determined to have disclaimed the duty of loyalty. *Zimmerman*, 62 A.2d at 702. Drafters of operating agreements may address various duties in a piecemeal fashion throughout the operating agreement.

negotiate transactions with appropriate procedural protections, such as majority of the minority shareholder approval, and thereby potentially receive lessened judicial scrutiny.[142]

Defendants also claim that Section 7.05 creates a safe harbor from judicial review for certain acts which might otherwise violate the traditional duty of loyalty. Section 7.05 provides:

> Action by the Managing Board. The Managing Board shall act by the vote of a majority of the Directors; provided, however, that (a) the FARS Designees shall have the right, on behalf of the Managing Board, to determine whether to approve or disapprove of any proposed transaction or series of related transactions (including, without limitation, the purchase, sale, lease, transfer or exchange of property or assets of any kind or the rendering of services of any kind) involving aggregate value, remuneration or consideration of more than $25,000 between any and all of the Company and its Subsidiaries, on the one hand, and any and all of the Members and other Affiliates of the Company (other than Advance Capital Partners, LLC pursuant to a Co-Investment Agreement) on the other; . . . .[143]

They argue, first, that this provision is the only limit placed on ARG's ability to enter into insider transactions and, second, that because the provision places no limitations on transactions with FARS, the section implicitly authorizes them.[144] Alternatively, they claim that Section 7.05 supplants the traditional duty of loyalty

[142] *See, e.g.*, *Kahn v. M & F Worldwide Corp.*, 88 A.3d 635, 645-46 (Del. 2014).
[143] JE-6 § 7.05 (continuing to define which Board members must agree to approve certain transactions, such as designating employees for the Company's incentive compensation plan; approving additional capital contributions, certain loans, and new classes of units; and approving particular co-investment opportunities).
[144] Defs.' Post-Trial Br. at 44.

and is akin to a provision found in *Zimmerman*, which permitted insider transactions and limited the duty of loyalty in certain circumstances.

The Court disagrees. First, the plain import of the section is to specify certain special circumstances in which the parties agreed that additional approvals would be necessary. Section 7.05 grants FARS a veto in specified circumstances either by giving its designees the right to approve the transaction or by requiring an affirmative vote of at least three out of four directors to approve other actions. Second, this provision differs from that contemplated in *Zimmerman*, in that the *Zimmerman* provision granted a broad right and explained that if certain procedures were complied with the transaction could be immune from challenge.[145] Here, Section 7.05 sets out a default rule (that the Board shall act by majority vote) and then modifies that rule to grant greater protections to certain ARG stakeholders in a limited set of circumstances. There is no language immunizing these acts from challenges as was present in *Zimmerman*.

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[145] *See Zimmerman*, 62 A.3d at 702-03 ("The Members, Directors, and officers and any of their respective Affiliates shall have the right to contract or otherwise deal with the Company or its Subsidiaries in connection therewith as the Board of Directors shall determine . . . . No transaction between the Company or its Subsidiaries and one or more of its Members, Directors or officers . . . shall be void or voidable solely for this reason, or solely because the Director or officer is present at or participates in the meeting of the Directors that authorizes the contract or transaction, or solely because his or their votes are counted for such purpose, if (a) the material facts as to the transaction are disclosed or are known to the disinterested Directors and the contract or transaction is approved in good faith by the vote or written consent of the disinterested Directors; or (b) the transaction is fair to the Company or its Subsidiary as of the time it is authorized, approved or ratified by the Board of Directors or the Members.").

Defendants contend that Section 7.05 does not contemplate a transaction between FARS and the Company and thus does not prohibit such a transaction. Defendants' claim is, again, contrary to Delaware law which requires that fiduciary duties, if they are to be disclaimed, must be disclaimed in the operating agreement. A failure to mention a duty or to contemplate a given conflicted transaction is not an adequate disclaimer of it. Such a rule, which resolves ambiguities in favor of the full panoply of duties, is sensible. Although fiduciary duties may be disclaimed, agreements' drafters must do so clearly, and should not be incentivized to obfuscate or surprise investors by ambiguously stripping away the protections investors would ordinarily receive.[146] In conclusion, Section 7.05 is not a safe harbor which prevents Plaintiffs from challenging the Reorganization.

Defendants also argue that *Zimmerman* compels a conclusion that the Board need only meet a subjective good faith standard. However, the provision evaluated in *Zimmerman* stated that the directors "shall carry out their duties and exercise their powers hereunder in good faith and in a manner reasonably believed by the directors to be in the best interest of the Company and its Members . . . ."[147] The analysis in *Zimmerman* made clear that the drafters articulated their desire to apply a subjective good faith standard through the use of the phrase "reasonably

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[146] *See In re Atlas Energy Res., LLC*, 2010 WL 4273122, at *10 (Del. Ch. Oct. 28, 2010) ("[P]arties to a limited liability company agreement bear the risk that they have drafted it incompletely.").
[147] *Zimmerman*, 62 A.3d at 702.

believed."[148] Section 7.01 contains no similar language contemplating the Board's belief, which permitted the *Zimmerman* court to conclude that a subjective standard applied. Thus, the Court rejects Defendants' view that a subjective good faith standard applies.

B. *What Standard of Review Applies and Who Bears the Burden of Proof?*

Delaware law ordinarily affords directors the benefit of the business judgment rule—the presumption that in making business decisions, they "acted on an informed basis, in good faith and in the honest belief that the action taken was in the best interests of the company."[149] However, a plaintiff may rebut that presumption by providing evidence that the defendant directors, in reaching the challenged decision, breached any of its duties of loyalty or due care.[150] An interested transaction is one in which the directors appear on both sides or expect to derive a financial benefit from it which does not devolve upon the company or its equity holders generally.[151] The personal benefit the directors receive must be so significant that it is "improbable that the director could perform her fiduciary duties . . . without being influenced by her overriding personal interest."[152]

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[148] *Id.* ("They must act with subjective good faith ('in a manner reasonably believed by the Directors to be in the best interests of the Company and its Members') . . . .").

[149] *Aronson v. Lewis*, 473 A.2d 805, 812 (Del. 1984), *overruled on other grounds by Brehm v. Eisner*, 746 A.2d 244 (Del. 2000).

[150] *McMullin v. Beran*, 765 A.2d 910, 917 (Del. 2000).

[151] *See Pfeffer v. Redstone*, 965 A.2d 676, 690 (Del. 2009).

[152] *Id.* (quoting *Hokanson v. Petty*, 2008 WL 5169633, at *7 (Del. Ch. Dec. 10, 2008)).

Defendants appear to argue that because no duty of loyalty was prescribed by ARG's operating agreement, Plaintiffs could only succeed by producing evidence that the Board's duties of good faith or due care have been violated.[153] Because the operating agreement's failure to discuss the duty of loyalty did not disclaim it, the Board must act with loyalty to its unitholders and thus Plaintiffs may provide evidence that that duty was breached to place the burden on Defendants to prove the entire fairness of the transaction.

Here, Plaintiffs have rebutted the presumption of the business judgment rule by demonstrating that ACP and FARS were interested in the Reorganization. Cocoziello and FARS were concerned for the entities they represented, ACP and FARS, throughout the negotiation of the Reorganization. The testimony of Cocoziello and the FARS's representatives revealed that their first impulse was often to think of themselves as representatives of the FARS or ACP, rather than as representatives of all of ARG's unitholders, including the minority. Cocoziello and FARS held three out of the four seats (and Cocoziello controlled the vote of the fourth seat), and thus the majority of the Board was conflicted.

ACP and FARS also received benefits not granted to other unitholders: the opportunity to convert their equity into debt. FARS had secured the right to convert its loan into units of ARG; however, it had no contractual right to treat

[153] Defs.' Post-Trial Br. at 45 (citing *McMullin*, 765 A.2d at 917).

those units as though they had been converted, at a valuation of $25 per unit, and then convert that equity position into a loan senior to the rest of ARG's unitholders. McGurk acknowledged that FARS bargained for this additional result as part of the deal in which FARS agreed not to utilize the full range of contractual provisions to which it was entitled under its convertible notes. Similarly, ACP converted a portion of its Class A units into an approximately $40 million note from ARG to ARD, which, although it was subordinate to some of ARG's debt, was superior to Plaintiffs' units.

Thus, ARG's Board, comprised of representatives of ACP and FARS, granted Cocoziello's entities and FARS these unique benefits not shared by other unitholders during the Reorganization. Because ARG's conflicted Board approved the Reorganization which gave its members (or the entities they represented) benefits not received by the minority, Plaintiffs have provided evidence that ARG's Board acted disloyally.[154] Thus, Defendants must prove that the transaction was entirely fair.[155]

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[154] *Cede & Co. v. Technicolor, Inc.*, 634 A.2d 345, 362 (Del. 1993), *decision modified on reargument*, 636 A.2d 956 (Del. 1994).

[155] Plaintiffs point out that some dissonance exists between *Zimmerman*, in which the parties were found to have altered the burden of proof of entire fairness through the contract such that plaintiff bore it, and other cases such as *Gatz*, where the defendants bore the burden. Pls.' Post-Trial Mem. of Law at 8-9. Defendants do not appear to take a position on the issue and thus the Court determines that Defendants bear the burden as would typically apply under entire fairness. This result appears to be consistent with the Supreme Court's reasoning in *Gatz*, and *Zimmerman* does not seem to be the appropriate

Furthermore, Plaintiffs have provided evidence demonstrating that the Board did not act in good faith. "The good faith required of a corporate fiduciary includes . . . all actions required by a true faithfulness and devotion to the interests of the corporation and its shareholders."[156] A failure to act in good faith may be shown where "the fiduciary intentionally acts with a purpose other than that of advancing the best interests of the corporation."[157] The Board's attempt to cash out the minority at a discount while valuing its members' holdings at $25 per unit,[158] and its willingness to convert its equity into loans with seniority over the other minority equity holders support a theory of the directors acting with a purpose other than that of advancing the best interests of ARG and its residual unitholders. However, the Board's actions also appear to have been taken to assuage a creditor, FARS, to whom payment was owed, thus complicating the analysis of the Board's motive.

Nonetheless, testimony elicited at trial demonstrated the Board's overwhelming concern with the well-being of its members' interests, evidenced by

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precedent to apply to ARG's operating agreement because the *Zimmerman* operating agreement contained a safe harbor not found in ARG's Section 7.05.

[156] *In re Walt Disney Co. Deriv. Litig.*, 906 A.2d 27, 67 (Del. 2006).

[157] *Id.*

[158] The Board's explanation of its financial analysis was unsatisfactory. It appears to have simply used the December 2007 assessment of ARG's fair value as the price it would pay to cash out the minority and never adequately explained, without relying on post hoc rationalizations from its expert witness, why it believed the debentures of FARS and Cocoziello should be valued at $25 per unit. Additionally, the Board never sought a fairness opinion to justify its valuation and the choices it offered the minority.

its desire to benefit ACP and FARS, and its willingness to ensure those entities received favorable terms at the expense of the unitholders. Cocoziello and McGurk testified that they were negotiating on behalf of the entities they represented. Additionally, the record fails to reflect the Board's consideration of ARG's residual claimants, the unitholders. Instead, the vast majority of the Board's efforts, reflected in contemporaneous evidence, were devoted to carving up ARG between Cocoziello's entities and FARS, and structuring the Reorganization to its members' advantage, for example by converting FARS's units into loans senior to the minority's units. This evidence overcomes the presumption of the business judgment rule and thus, under a theory of bad faith as well, Defendants must demonstrate the Reorganization's fairness.

Defendants also argue that entire fairness review is inappropriate because the Reorganization was "entirely voluntary."[159] The Defendants seek a lower standard of review, by citing to cases in which a procedurally fair process was established and thereby obviated the need for more searching judicial inquiry. In these cases, a controller made a non-coercive tender or exchange offer to a fully informed minority of shareholders, who were granted the power to accept or reject the deal. In contrast here, Defendants did not attempt to create a fair process to

[159] Defs.' Post-Trial Answering Br. at 6 (citing *Pfeffer v. Redstone*, 965 A.2d 676, 684 (Del. 2009); *In re CNX Gas Corp. S'holders Litig.*, 2010 WL 2705147, at *5 (Del. Ch. July 5, 2010)).

involve the minority, provide Plaintiffs notice of the deal, or seek their approval. While Plaintiffs were permitted limited choice, after the Reorganization was consummated, to accept the discounted $21.68 per unit for their units or to convert their units into units of ARD (or to refuse both options), they had no opportunity to accept or reject the Board's decision to carve up ARG and sell its stabilized assets. They also were not informed of the transaction until it had been executed and thus had no opportunity to negotiate with the Board or to seek a preliminary injunction of the transaction. A lesser standard of review should not apply to the Reorganization because Defendants failed to create procedural safeguards which justify lesser judicial scrutiny.

Because Plaintiffs have rebutted the presumptions of the business judgment rule with evidence of the Board's failure to act loyally and in good faith, the Court will review the Reorganization under the entire fairness standard. Defendants bear the burden of persuasion as no well-functioning committee of independent directors was organized and no informed minority vote ratified the transaction.[160]

[160] *Kahn v. Lynch Commc'n Sys., Inc.*, 638 A.2d 1110, 1117 (Del. 1994) ("The initial burden of establishing entire fairness rests upon the party who stands on both sides of the transaction.").

C. *Was the Reorganization Fair?*

The fairness of a transaction will be tested by assessing the two prongs of fair dealing and fair price.[161] Fair dealing considers "questions of when the transaction was timed, how it was initiated, structured, negotiated, disclosed to the directors, and how the approvals of the directors and the stockholders were obtained."[162] Fair price "relates to the economic and financial considerations of the proposed [transaction], including all relevant factors: assets, market value, earnings, future prospects, and any other elements that affect the intrinsic or inherent value of a company's stock."[163] However, the fairness inquiry is not bifurcated as between fair dealing and fair price; all aspects of the issue must be examined as a whole, since the question is one of entire fairness.[164] Although the fairness of price has been said to be the preponderant concern,[165] unfair process may also "infect" the fairness of the price granted to the minority.[166]

1. Did the Board Deal Fairly with the Minority?

Defendants argue that the Reorganization was fair because it was not coercive, ACP and FARS engaged in arm's length negotiations, Plaintiffs were

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[161] *Weinberger v. UOP, Inc.*, 457 A.2d 701, 711 (Del. 1983).
[162] *Id.*
[163] *Id.*
[164] *Id.*
[165] *Id.*
[166] *Bomarko, Inc. v. Int'l Telecharge, Inc.*, 794 A.2d 1161, 1183 (Del. Ch. 1999), *aff'd*, 766 A.2d 437 (Del. 2000).

well-informed about ARG, and Plaintiffs' units would have been worthless even if the Reorganization had not occurred. Plaintiffs argue that there was no negotiation by, disclosure to, or approval of any non-interested party and that the timing, initiation, and structure of the Reorganization were also unfair.

The Court agrees with Plaintiffs that the Reorganization was procedurally unfair. Defendants controlled the timing and structure of the transaction. The FARS debentures would mature in August 2008 and were a real, non-manufactured contractual deadline. Thus, the crisis that ARG faced was not a "sham," as Plaintiffs contend.[167] ARG genuinely appears to have faced cash-flow problems and management's estimates of the value of its equity appear to have been steadily declining. Plaintiffs argue that Defendants did not want to consummate the 144A transaction or complete a sale to Normandy or JER because the Board could then respond to the maturing FARS convertible notes to squeeze out the minority on unfavorable terms. The Court is persuaded that both Defendants and Plaintiffs worked diligently in order to consummate a transaction because it was in their interest to do so. All of them hoped for a liquidity event which would allow them to redeem their units for cash. More likely than not,

[167] *See Gatz Properties, LLC v. Auriga Capital Corp.*, 59 A.3d 1206, 1215 (Del. 2012) (recounting evidence supporting finding that fiduciary manufactured a situation of distress culminating in a "sham" auction).

potential transactions were frustrated by the parties' failure to receive the price they believed their units were worth.

Nonetheless, Defendants exercised complete control over the transaction and appeared to have capitulated to FARS's desire to cash out its investment at the $25 per unit price it had demanded throughout the various transactions ARG explored as it tried to pay off FARS's debt. Cocoziello knew FARS would control a fifth Board seat if ARG defaulted and FARS could then have begun liquidating assets to recover what it could from the company. Cocoziello and FARS seem to have agreed that ARG had enough assets to satisfy FARS's liquidation plan while allowing Cocoziello to finish developing ARD's properties and organized the Reorganization to satisfy those goals.

Apparently, the Board considered only this transaction for more than a year and in that time made little effort to consider ARG's minority unitholders or ensure their interests were represented. Defendants' expert, Gannon, argued that "friction" existed between Cocoziello and FARS which adequately represented the minority's interests. However, the evidence does not support his theory.

Defendants appear to have simply used the audited December 2007 financials to value the minority units at $21.68,[168] while valuing their own convertible interests at $25 per unit. The method the Board used to derive this $25

[168] JE-160.

per unit value was never adequately explained. FARS believed, or hoped, its units were worth that amount since at least 2005, when ARG explored the 144A offering. Cocoziello evidently agreed with that valuation; though as a majority unitholder it likely would not have been difficult to persuade him to value his holdings aggressively. Plaintiffs would have been satisfied to receive $25 per unit and appear to have offered to be bought out for that amount in cash.[169] The record does not demonstrate whether any of FARS, Cocoziello, or Plaintiffs truly believed their units were worth that amount or whether it was simply expedient to use that number for the purposes of the Reorganization. Plaintiffs may have reviewed the deal and argued that they deserved the same treatment as FARS and Cocoziello. Whether or not the "valuation" was correct, FARS and Cocoziello locked in the value of their equity by converting many of their units into loans senior to the minority's equity.

Although Defendants reached out to Metzger to buy out his interest, their strategy appeared to be to convince him, as the largest minority unitholder, to agree to terms which devalued his interest and use that as leverage to force others to also accept the same terms. Similarly, Sheridan appears to have recommended attempting to persuade the rest of the minority to accept these terms to pressure Metzger. Gannon's theory that the "friction" between Cocoziello and FARS

[169] JE-247.

benefited the minority is undermined by this evidence concerning the "negotiations."[170] His theory appears to be a thinly-veiled attempt to gloss over what occurred here: two parties agreed to satisfy their interests and left the remaining value to unrepresented third parties.

Defendants also kept Plaintiffs uninformed about the Reorganization. Defendants argue that the Plaintiffs were informed because they ran ARG for seven years and were able to gather some information from other minority unitholders Defendants sought to buy out. However, Defendants executed the Reorganization without notice to the Plaintiffs and thereby denied Plaintiffs the opportunity to attempt to receive better terms or to enjoin the transaction. Defendants also provided minimal information when notifying Plaintiffs of the Reorganization in the September 15 letter and no information which would allow Plaintiffs to value their holdings.[171] Although Plaintiffs were invited to participate

[170] Gannon's explanation for how this "friction" resulted in tangible benefits was unsatisfying. Gannon Tr. 1196-97. He stated that because investors were given choices that FARS and Cocoziello must have believed the alternatives were relatively equal and that FARS and ACP were willing to accept the minority on either side. His statements do not demonstrate that value was created (or maintained) for the minority. The fact that the minority could go with either group does not mean that the investments were equal and the willingness of FARS and ACP to accept them is diminished greatly when considering how they layered debt on top of the equity in order to assure themselves of receiving value for their units.

[171] Aloian wrote to Sheridan to suggest that an exhibit should accompany the conversion agreement which would outline which assets would remain with ARG and which would go to ARD. JE-203. Such an exhibit was not attached to the conversion agreement or provided to ARG's minority unitholders. McGurk Tr. 251. An attorney working for

in two conference calls to discuss the transaction, two limited after-the-fact opportunities to speak openly about the transaction do not convince the Court that the minority was informed. Plaintiffs were not, and Defendants' actions up to that point had failed to create a tone of forthrightness or receptiveness to negotiations or to obtaining unitholder approval.

More specifically, Defendants provided little information about Plaintiffs' ability to remain with ARG. The September 15 letter offering to redeem Plaintiffs' units described two options available to the minority: (1) to exchange their units for ARD units and (2) to be redeemed for cash and a note with a combined value of $21.68.[172] The option to remain with ARG was acknowledged obliquely when the letter informed the unitholders that FARS planned to liquidate ARG's portfolio and that "[t]his liquidation will result in potentially adverse tax consequences for the remaining Class A Unitholders, particularly since the proceeds of such sales will be used to pay outstanding debt and liabilities of the Company."[173] The mention of the adverse consequences ARG's unitholders would suffer reads as an attempt by Defendants to convince Plaintiffs that remaining with ARG would negatively

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Cocoziello's entities also suggested that a financial model be prepared to demonstrate the mechanics of the deal. JE-185. Such information was not conveyed to the minority.

[172] JE-225.

[173] *Id.* Defendants also referenced Plaintiffs' ability to remain with ARG when they listed ARG's remaining post-Reorganization unitholders. Defendants totaled FARS's post-conversion units and the maximum number of units the minority could hold "assuming none of the Class A Unit Holders elect to be redeemed[.]" *Id.*, Ex. A.

impact the value of their units and incentivize them either to become ARD unitholders or to accept the discounted cash out price. Additionally, Defendants did not explain which assets ARD held, stating instead "[i]t is management's belief that the current realizable value of the ARD properties and projects under development is approximately $45MM."[174] Defendants also did not provide any detail on how they came to that conclusion or the valuation data supporting it.

Defendants argue that Plaintiffs were able to choose whether they wished to redeem or remain with ARG and thus the conversion was voluntary. They incorrectly describe the transaction. First, Plaintiffs had no choice as to whether or not the Reorganization occurred; as discussed they had no notice the Reorganization was pending and no opportunity to propose an alternative transaction. Second, a choice among several bad options can be deemed an illusory choice. Plaintiffs were advised that remaining with FARS was likely to result in negative tax consequences which would harm the value of their units. They were also given an option to cash out their units at a discounted price or to join a development company which was left without support of the positive cash flows of the stabilized properties which ARG would retain. Furthermore, Cocoziello would run ARD and he had recently fired Plaintiffs, which may have also made them wary of accepting this option. Thus, although Plaintiffs had a

[174] JE-225, Ex. A.

choice among several options, each option appeared to have a significant downside.

Defendants also contend that, because of the severe economic downturn, ARG's units would have been worthless if the Reorganization had not occurred. They base this conclusion on a model Gannon created which he argues demonstrates that ARG would have been incapable of satisfying the $60 million owed to FARS. Gannon's model begins with ARG's net asset value in 2011 (which was negative) and adds back in payments made to the note holders and to the minority pursuant to the Reorganization to demonstrate that the equity which remained in the combined company could not have paid FARS back.[175] However, this evaluation is speculative when considered at the time of the Reorganization.[176]

Gannon's assessment also obscures the issue, and does not answer the question, of whether ARG had value at the time of the Reorganization, which is the

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[175] Gannon Tr. 1186-90; JE-375; JE-378. Defendants contend that because ARG could have gone bankrupt by 2011, that this case is akin to *Trados*. *In re Trados*, 73 A.3d 17, 76-77 (Del. Ch. 2013) (conflicted merger was fair, despite directors' failure to consider the minority, because the common stockholders "did not have a reasonable prospect of generating value for the common stock"). However, in *Trados* the Court concluded that the common held no economic value at the time of the unfair transaction. Here, it undisputed that the common had value when the Reorganization occurred; Defendants, by projecting a negative asset value for ARG years after the Reorganization, cannot thereby demonstrate that the Class A unitholders lacked a reasonable prospect of generating value.

[176] *Cavalier Oil Corp. v. Harnett*, 1988 WL 15816, at *14 (Del. Ch. Feb. 22, 1988) (explaining that only data "known or susceptible of proof as of the date of the [transaction] and not the product of speculation" can be considered (citation omitted)), *aff'd*, 564 A.2d 1137 (Del. 1989).

primary issue before the Court.[177] Whether ARG could have or would have acted in some manner between September 2008 and the forecasted bankruptcy in 2011 to satisfy FARS and still preserve value for the minority is a hypothetical which cannot be answered with confidence, even if the inquiry were properly before the Court.

Furthermore, the transaction was structured to convert the holdings of FARS and ACP in a manner which granted them a benefit not given to the minority. FARS and ACP valued their convertible notes and their units at $25 per unit for the purposes of conversion. The realities of the arm's-length transactions from a year before, in theory before the markets began "quivering,"[178] did not support a valuation of ARG permitting FARS and Cocoziello to liquidate their units at that price. Neither the 144A transaction nor the sale transactions would have realized the values that FARS and ACP awarded to their holdings.

They then granted themselves a second benefit not offered to the minority: priority over the rest of the equity holders. Instead of simply sitting shoulder-to-shoulder with the rest of the Class A units, they issued themselves interest-bearing

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[177] *Cede & Co. v. Technicolor, Inc.*, 542 A.2d 1182, 1187 (Del. 1988) (explaining, in the context of an appraisal action, that "the only litigable issue is the determination of the value of the appraisal petitioners' shares on the date of the merger"). Entire fairness inquiries often rely on quasi-appraisal remedies, though the measure of damages is not strictly limited to a corporation's fair value as determined by an appraisal. *Ryan v. Tad's Enters., Inc.*, 709 A.2d 682, 698 (Del. Ch. 1996), *aff'd*, 693 A.2d 1082 (Del. 1997).
[178] McGurk Tr. 337.

loans, which would be paid before the minority. Though these loans did not require that ARG aggressively repay them, the fact remains that FARS and ACP permitted themselves to jump the capital stack at a more favorable valuation than they granted the minority. The conversion also had the effect of locking in the Board's $25 per unit valuation.

Certain payments were also made to ARG, ACP, and ARD both at the time of, and after, the Reorganization. As part of the conversion transactions, in late 2008, ARG paid approximately $10 million to ARD.[179] ARG also made quarterly interest payments totaling $5.1 million to ACP and FARS on notes issued pursuant to the self-dealing Reorganization approved by ARG's Board.[180] However, ACP and FARS also had payments due to them from ARG which were senior to the minority's equity from ACP's $12 million of preferred notes and FARS's $60 million convertible note.[181] Thus, the cash transfer from this transaction may not have been cash to which the minority would otherwise have been entitled.

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[179] Admitted Facts ¶ bbbbb. Payments were also made on certain pre-Reorganization obligations at the time of the conversion. *Id.* ¶¶ ccccc, ddddd.
[180] *Id.* ¶ zzzz.
[181] *See* JE-478.

For all of the reasons above,[182] the process employed in structuring this transaction was unfair and McGurk, Aloian, and Cocoziello engaged in self-dealing when consummating the Reorganization at the expense of the minority. The cash transfers from ARG to ACP, ARD, and FARS were part of a procedurally unfair Reorganization, although it is possible that Plaintiffs would nonetheless have no claim to that cash because of additional debt obligations ARG owed to its creditors before the Reorganization.

2. Did the Board Offer the Minority a Fair Price?

Fair value is each unitholder's proportionate interest in a going concern.[183] "The value of a corporation is not a point on a line, but a range of reasonable values . . . ."[184] When evaluating fair price in an entire fairness analysis, the Court answers the question of whether the transaction was one "that a reasonable seller, under all of the circumstances, would regard as within a range of fair value; one that such a seller could reasonably accept."[185] The Court has, after hearing the

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[182] Although the Board's shortcomings, discussed above, do not necessarily lead to a conclusion that the Board's process was unfair, it does bear the burden of proving the fairness of the transaction. It has come forward with little evidence that it sought to serve the minority, and, coupled with its other omissions, discussed above, results in the Court's determination that it dealt unfairly with the minority.

[183] *Cavalier Oil Corp. v. Harnett*, 564 A.2d 1137, 1144 (Del. 1989).

[184] *Cede & Co. v. Technicolor, Inc.*, 2003 WL 23700218, at *2 (Del. Ch. Dec. 31, 2003), *aff'd in part, rev'd in part on other grounds*, 884 A.2d 26 (Del. 2005).

[185] *Reis v. Hazelett Strip-Casting Corp.*, 28 A.3d 442, 466 (Del. Ch. 2011) (quoting *Cinerama, Inc. v. Technicolor, Inc.*, 663 A.2d 1134, 1143 (Del. Ch. 1994), *aff'd*, 663 A.2d 1156 (Del. 1995)).

parties' legal arguments and the expert witnesses' testimony, broad discretion either to adopt one of the experts' models or to fashion its own.[186]

Although the process the Board employed when dealing with the minority left much to be desired, Plaintiffs appear to have been the beneficiaries of FARS's strong bargaining position as a creditor poised to take over ARG and its demand to be redeemed at $25 per unit. FARS held the most leverage in the negotiations and the threat of controlling ARG by controlling the Board's fifth seat apparently motivated Cocoziello to satisfy FARS and then to retain what he could of the development properties in ARD. FARS kept those properties which could be sold, and Cocoziello either sought to cash the minority out or convince them to redeem and join ARD. The post-conversion equity structure of ARG consisted of the small amount of equity which FARS converted in order to retain its majority control of the company and the Plaintiffs. Thus, because FARS retained many of ARG's assets, but the number of ARG's unitholders was drastically reduced, the value per unit of each of those remaining units may have increased significantly. This is true even after ARG's Board added layers of debt on top of Plaintiffs' equity holdings.

[186] *In re Appraisal of Metromedia Int'l Gp., Inc.*, 971 A.2d 893, 899-90 (Del. Ch. 2009).

Interestingly, neither party submitted an expert report demonstrating fair price. However, Defendants submitted the exhibits their expert prepared to support the conclusions in his report, and sought to prove their case from these materials.[187] Plaintiffs also submitted the documents associated with an appendix to their expert's report.[188] The subsections which follow evaluate their arguments: the Court begins with Defendants' expert because Defendants bear the burden of proof.

(a) *Gannon's Testimony*

The exhibits Gannon provided demonstrate his attempt to ascertain the pre- and post-Reorganization value of the various companies involved in the transaction. He did so by trying to value the individual assets held by ARG. If appraisals or contemporaneous sale transactions existed, he used those values to determine an asset's value after checking their reliability. Many properties did not have appraisals or lacked contemporaneous sale transactions and Gannon performed a valuation by sending a team to those properties to evaluate them; to consider their rents, operating statements, tax bills, and discounted cash flows; and to assess the local market.[189] Gannon accepted information from Defendants, but

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[187] Gannon Tr. 1126.
[188] Pietroforte Tr. 992-94.
[189] Gannon Tr. 1138-40.

he made independent valuations of ARG's properties.[190] ARG owned a 25% interest in certain properties and Gannon calculated the value of those properties by backing out the debt owed on them and then applying a minority discount to reflect the remaining equity owned by ARG's joint venturers in these properties.[191]

Gannon took the June 30, 2008 balance sheet and accounted for non-real estate assets and liabilities.[192] He calculated mark to market adjustments to the face amount of ARG's mortgage payables.[193] He then totaled the gross real estate values and other assets and subtracted from that number the total liabilities, debt mark to market adjustment, and minority interest adjustment to determine ARG's net asset value.[194] Gannon concluded the gross real estate values were worth approximately $824 million, the other assets were worth approximately $28 million, the total liabilities were approximately $534 million, and the debt mark to market adjustment and minority interest adjustment were approximately $2 million and $92 million respectively. The net asset value was thus approximately $224 million. He then calculated the number of fully diluted units to be 8,627,515

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[190] *Id.* at 1148.

[191] *Id.* at 1150-51; JE-362; JE-366. Gannon applied a minority discount to ARG's pre-Reorganization value to account for profits from the joint ventures in the Harrison and Southgate properties to which ARG was not entitled. He also added the profits due to ARG to the value of the entity after the Reorganization. *See* JE-362; JE-366; JE-367. Plaintiffs' expert generally appeared to agree with this approach even if he applied different assumptions. *See* JE-479.

[192] JE-363.

[193] JE-364.

[194] JE-366.

units,[195] and divided the net asset value by those units. Gannon thus determined the value of the pre-Reorganization units to be $25.96 per unit.[196]

Gannon also tracked the division of assets and liabilities among ARG, ACP, and ARD.[197] For the joint venture properties, which included the Harrison property, he determined the amount of equity ownership held by each of the post-Reorganization entities in the joint venture when totaling the assets of ARG after the Reorganization. He used these figures to calculate the post-Reorganization net

[195] JE-365. Plaintiffs argue, in a footnote in their post-trial briefing, that Gannon overestimated the amount of outstanding units by several hundred thousand additional units. Pls.' Post-Trial Mem. of Law at 40 n.19. They correctly identify Gannon's failure to explain how he arrived at this figure, which would have been helpful. They rely on a spreadsheet attachment to a November 1, 2007 email between Sheridan and McGurk when arguing that fewer units were in existence. *See* JE-153. Yet, the exhibit upon which Plaintiffs rely is problematic because it may reflect outdated information. Additionally, Gannon's exhibit does not identify the number of units held by individual investors and thus comparing the two figures becomes more complicated. Plaintiffs elsewhere state that they largely agree with Gannon's analysis and they direct the Court to no expert testimony countering Gannon's work. The Court therefore relies on Gannon's work instead of the November 1, 2007 email.

Finally, if 300,000 units are removed from the pre-Reorganization total units outstanding, the Reorganization would nonetheless be accretive to Plaintiffs according to Gannon's models, which Plaintiffs apply to calculate their damages. This is true even assuming the valuations sponsored by Plaintiffs for the Gateway property rights and Harrison are added to the pre- and post-Reorganization net asset values of ARG as described herein.

[196] JE-366. Gannon also argued that untraded securities should reflect a minority illiquidity discount, in this case of 35%. He applied this discount to that portion of the $21.68 offered to the minority which was structured as a loan, and opined that the offer was fair. Gannon Tr. 1165-67. Plaintiffs dispute whether the discount was appropriate, but the issue need not be reached. First, Plaintiffs did not accept $21.68 as consideration for their units. Second, that part of the minority which accepted this consideration did so voluntarily.

[197] Gannon Tr. 1158; JE-367.

asset value of ARG, which was approximately $22 million.[198] The number of units outstanding in the post-Reorganization ARG was greatly diminished because ACP and many of the minority were cashed out or accepted ARD units. Additionally, FARS converted the majority of its convertible debentures into loans, which reduced the number of fully diluted units. Thus, the remaining units in ARG after the Reorganization were those units FARS converted to retain majority ownership in ARG during the conversion and the units of Plaintiffs. Only 724,096 units remained in ARG after the conversion. Gannon again divided the net asset value by the number of outstanding units to determine that ARG's units after the conversion were worth $30.28 per unit.[199] Gannon also compared the amount of value that FARS received before and after the conversion. He used a pre-Reorganization value of $25.96 per unit and a post-Reorganization value of $30.28, added in the value of the FARS loans, and found that FARS received approximately $93.48 million in value for a pre-Reorganization value of $93.55 million.[200]

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[198] Specifically, Gannon calculates the net asset value to be $21,927,377. JE-367.

[199] *Id.*

[200] JE-370. There is reason to be skeptical of Gannon's analysis, but Plaintiffs, as described below, explicitly accept much of it. First, FARS was unable to realize its desired $25 per unit through its 144A transaction in 2005, even before the markets began "quivering" in late 2007. Second, the market values in ARG's audited financials steadily deteriorated up until the end of 2007 and ARG faced ongoing liquidity problems. There is no circumstantial evidence of an upward trajectory in the markets or in ARG's financial performance that explains the turnaround in the Company's value implied by Gannon. Third, only a small reduction in Gannon's valuation of net asset value would

Gannon also determined what the value of ARG's units would have been after the Reorganization if the minority had not been cashed out at $21.68. To do so, he added the value of the payments made to the minority into the net asset value of ARG after the conversion and then divided by the adjusted number of units outstanding. Gannon found the post-Reorganization value of one of ARG's units to be $27.66, assuming the rest of the minority remained with ARG. Gannon thus opined that the consideration received by FARS was fair from a financial point of view.[201]

Finally, Gannon opined, based on similar analysis, that the consideration paid to ACP was fair from a financial point of view.[202] Analyses based upon asset

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demonstrate that the transaction was dilutive of Plaintiffs. As discussed when assessing the Harrison and Gateway properties, the greatly reduced amount of units outstanding as between ARG as a pre- and post-Reorganization entity creates a larger increase in post-Reorganization unit value than in pre-Reorganization unit value, for each dollar of net asset value added to the entity. This effect is what allowed Plaintiffs' expert to opine that the value of Plaintiffs' units after the transaction was $114 per unit. However, the converse is true: for each dollar of net asset value removed from ARG, the value of the post-Reorganization units declines drastically in comparison to the value of the pre-Reorganization units. If the net asset value of ARG in Gannon's models is adjusted so that the pre-Reorganization value of the units equals $25 per unit, and that reduced net asset value is then carried over to ARG after the conversion, then the post-Reorganization value of the units would be $18.94. The transaction would then have been dilutive to Plaintiffs. The net asset value of ARG need only be lowered by $8.21 million to create this result.

Although the fairness of a transaction should be established to the Court's satisfaction and there are reasons for doubt here, Plaintiffs have generally acquiesced in Gannon's work. Thus, the Court accepts the case as it was tried.

[201] Gannon Tr. 1160.

[202] *Id.* at 1163-64; *see also* JE-371.

value have been used to determine a company's value as a going concern and thus Gannon's approach was reasonable.[203] Moreover, Plaintiffs endorse his approach.

(b) *Plaintiffs' Response to Gannon's Testimony*

Somewhat surprisingly, Plaintiffs accept much of Gannon's valuation effort. They assert that "Defendants assigned values for most of [ARG's] properties and property rights and throughout this litigation Plaintiffs have accepted as true almost all of those valuations."[204] Plaintiffs may have been motivated in part, as discussed below, by the aggressive valuation presented by their expert witnesses, Gerald Pietroforte ("Pietroforte"), and thereby felt constrained to adopt Gannon's analysis to assert their case. Thus, after a cursory invocation of Pietroforte's analysis, they otherwise argue only that Gannon's numbers are essentially correct, but that they should be altered to augment the pre-Reorganization value of ARG, which also should increase Plaintiffs' damages award.

Plaintiffs argue that the pre-Reorganization value of ARG should be compared to the $21.68, which they were offered, but did not accept, or to the present value of their units today, which is nothing. The merits of this strategy are discussed later when considering the fairness of the transaction. Plaintiffs make

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[203] *See Kahn v. Household Acq. Corp.*, 591 A.2d 166, 173-75 (Del. 1991).

[204] Pls.' Post-Trial Mem. of Law at 23; *see also* Pls.' Post-Trial Reply Mem. of Law at 21-24. Plaintiffs also explicitly accept Gannon's valuations when they state "Plaintiffs have always been willing to simplify their damages calculations by adopting Defendants' asset values." Pls.' Post-Trial Mem. of Law at 38.

little effort, despite their nearly wholesale adoption of Gannon's figures, to compare the value of the pre-Reorganization value of ARG to its post-Reorganization value when arguing that they were damaged.

When criticizing Gannon's work, Plaintiffs first seek to reduce the number of fully diluted units used to calculate the value per unit of ARG as a pre-Reorganization entity. They therefore argue that Cocoziello's dilutive $10 million pari passu convertible note investment should be backed out and that FARS's notes should only be treated as a $60 million loan, instead of assessed as converted equity. Plaintiffs' second critique of Gannon's work is that Gannon underestimated the value of two properties in his analysis. He failed to include certain development rights when assessing the Gateway property and used an improper appraisal for the Harrison property. Thus, they argue the pre-Reorganization net asset value must be increased by the $16 million value of the Gateway rights and by the approximately $42 million of additional value of the Harrison property. Because Plaintiffs seek to compare the pre-Reorganization value of ARG to either $21.68 or zero, they ignore the post-Reorganization effects of increasing the value of these assets. The Court considers Plaintiffs' arguments.

Pietroforte never opined as to whether it was appropriate to include the number of units into which FARS and Cocoziello could convert their convertible debentures in the count of fully diluted units when assessing the value of ARG's units before the Reorganization.[205] Conversely, Gannon opined that it was customary to use the number of fully diluted units when assessing the value of the units.[206] Plaintiffs seek to reduce the value of the convertible notes by capping the amount due under them to the original loan amounts, when the notes were written to allow FARS and Cocoziello to retain a conversion feature which allowed participation should the value of their units exceed the notes' strike price.

Plaintiffs face two problems in arguing their case. First, they did not come forward with evidence supporting their viewpoint. Second, Gannon's testimony is credible. The conversion feature of the notes should be included when assessing the value of Plaintiffs' units because the inclusion of the converted units more properly reflects the economic value and proportionate interests Plaintiffs hold in ARG. The Court thus rejects Plaintiffs' argument and includes the number of units into which Cocoziello and FARS could convert their notes in the count of fully diluted units for the purposes of evaluating ARG's fair value.

Plaintiffs next argue that Defendants did not include the value of the Gateway rights when estimating the post-conversion value of ARG. However, they depend upon a note, apparently from an auditor, discussing valuation issues,

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[205] Pietroforte's analysis considers the post-Reorganization value of ARG and thus does not include the convertible notes in counting the total number of outstanding units. Pietroforte Tr. 1028-29. This is not equivalent to an opinion by Pietroforte on whether counting such convertible notes as equity is appropriate.

[206] Gannon Tr. 1155-56.

which states that ARG valued the Gateway development rights at $0 on December 31, 2007, but valued them at $16 million by December 31, 2008.[207] Conversely, both Sheridan and McGurk testified that the rights were valued at $14.5 or $15 million for the purpose of the Reorganization.[208] The Court found McGurk to be generally forthright throughout his testimony and thus takes his account to be credible. The Court found that Sheridan exhibited a greater willingness than McGurk to present the facts in a manner favorable to Defendants, although it also concluded she was generally honest in her testimony.

Moreover, Plaintiffs' evidence is not inconsistent with McGurk's testimony explaining how ARG valued the Gateway property. The method of valuing Gateway changed at some point between the end of 2007 and 2008—the only evidence in the record is the testimony of McGurk and Sheridan stating that the development rights were included in their calculations. Plaintiffs have not demonstrated that McGurk or Sheridan testified inaccurately about their valuation efforts, and the auditor's statement does not contradict their version of events. Thus, Defendants have demonstrated that these rights were included and Plaintiffs have not credibly undermined Defendants' testimony.

[207] JE-414 at 2.
[208] McGurk Tr. 351-52; Sheridan Tr. 1269-72.

Perhaps more importantly, even if Plaintiffs were correct that the Board failed to consider the $16 million for the purposes of the Reorganization, it is not apparent how that failure benefits Plaintiffs' damages theory. The $16 million would need to be consistently applied to ARG as both a pre-conversion entity and a post-conversion entity. Thus, an increase in net asset value to ARG as a pre-conversion entity would result in the distribution of the additional $16 million over the eight million fully diluted units outstanding before the conversion. Similarly, the additional $16 million would need to be added to the net asset value of ARG as a post-Reorganization entity, because ARG retained the property,[209] and across the 724,096 units outstanding after the conversion. The value of Plaintiffs' units before the conversion would increase by approximately $1.85 per unit and the value of their units after the conversion would increase by an additional $22.10 per unit. Thus, even if Plaintiffs' arguments are accepted, a consistent application of these units would prove to be accretive to the value of Plaintiffs' units.

Plaintiffs' claims concerning the Harrison property are also unconvincing, both because their arguments are not credible and because if Plaintiffs' arguments are accepted, the increase in value, when applied to the post-Reorganization value of Plaintiffs' units, would be accretive to Plaintiffs. As an initial matter, Plaintiffs appear to abandon the testimony of Pietroforte explaining that Defendants omitted

[209] *See* JE-367.

approximately $43.5 million of value from the post-conversion value of ARG.[210] They instead quote testimony of Senkevitch, who was not offered as an expert witness,[211] when arguing to the Court that Defendants lowered the value of Harrison by $41.9 million for the purposes of the conversion.[212]

Plaintiffs and Defendants both value ARG's joint interest in Harrison by beginning with its asset value, then subtracting its debt and the return of capital owed to investors. They disagree on the appropriate initial valuation of the property and the amount owed to investors. Plaintiffs' estimates of Harrison's asset value were based on an appraisal valuing the Harrison property at $108 million.[213] However, two other appraisals for the same property are also part of, or discussed in, the record. The first asserts that Harrison had a value of approximately $40 million[214] and the second contained two estimates of value at $40 million and $66 million.[215] The Court found Gannon's application of a ten percent discount to the $108 million appraisal to be reasonable in light of the varying appraisals available and his judgment that this single outlier was

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[210] JE-479.

[211] The Court explained at trial that Senkevitch's testimony concerning valuation was permitted for the purpose of explaining what he believed the value of his units was and how the Reorganization impacted them. Senkevitch Tr. 820.

[212] Pls.' Post-Trial Mem. of Law at 24, 27 n.6.

[213] JE-417.

[214] McGurk Tr. 354-55. This appraisal was from approximately a year before the appraisal sponsored by Plaintiffs.

[215] JE-290 (based upon "as is" and "upon completion of improvements" value, respectively). This appraisal was from 2009.

aggressive. Appraisals may be malleable and may be more or less aggressive depending on a company's needs in a given circumstance. Choosing to discount an appraisal to account for such diverse valuations was justified in the circumstances.[216]

Plaintiffs and Defendants also dispute the appropriate return on, or return of, capital owed to investors in the joint venture. Again, Plaintiffs rely solely on Senkevitch's testimony. Pietroforte also based his opinion regarding the Harrison property on Senkevitch's deposition testimony, rather than attempting an independent assessment of the return.[217] Additionally, Senkevitch asserted that ARG was owed a 25% return on invested capital from the Harrison joint venture.[218] However, Senkevitch, in the testimony upon which Defendants and Pietroforte relied, stated that no formalized agreement existed granting such a

[216] The Court's support of Gannon in this context is, to some extent, colored by its assessment of Plaintiffs' strategy as a whole. Plaintiffs first forwarded Pietroforte's theory, but abandoned it and instead relied upon Senkevitch to augment their damages. First, the Court was not convinced of Pietroforte's objectivity in assessing damages. The Court's analysis concerning his theory of damages is discussed below, but stated briefly, his estimate that Plaintiffs' damages should be valued at approximately $114 per unit belied his willingness to improvise with numbers and to advance his clients' case. This assessment was simply not credible given the desire of Plaintiffs, who knew the Company extremely well, to receive $25 per unit in advance of this litigation. *See infra* note 2366 & accompanying text. Second, Senkevitch was not designated as an expert witness and he was not treated as such throughout trial.

[217] *See* JE-479.

[218] JE-394 at 73-76; JE-479.

return.[219] Plaintiffs also do not direct the Court to documentation supporting a 25% return on capital, although Senkevitch claimed that because Aloian expected such a return, it was owed to ARG. In the absence of supporting documentation permitting a 25% return, the Court is reluctant to prefer Plaintiffs' valuation of Harrison over Gannon's and concludes that Gannon's valuation of Harrison was appropriate.

Moreover, adding to the pre-Reorganization value of ARG in the manner Plaintiffs suggest would be accretive to the value of Plaintiffs' post-Reorganization units. Plaintiffs suggest that $41.9 million should be added to the value of pre-Reorganization asset value of ARG to make up for the error in Gannon's analysis. However, they ignore that Gannon valued Harrison's net asset value at $31.4 million before the Reorganization after applying the discount to the $108 million appraisal and a discount to account for ACP's ownership in the joint venture.[220] The difference in Senkevitch's valuation and Gannon's should be the increase in the pre-Reorganization value of Plaintiffs' units.

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[219] Sheridan also testified that no document existed supporting a right to a 25% return on investment. Sheridan Tr. 1273.

[220] Gannon's initial asset value for Harrison was $97.2 million after he applied the ten percent discount to the appraisal value of $108 million. He subtracted the debt load, as did Pietroforte, of $19.1 million. *See* JE-362; JE-479. Gannon then derived the minority interest adjustment to reflect ARG's relative ownership of the remaining equity interest of $46.7 million. Subtracting the debt and minority interest from Harrison's initial asset value meant that Gannon valued ARG's pre-Reorganization interest in the property at $31.4 million.

Senkevitch's argument was based on his view that the total value of ARG's ownership of Harrison before the transaction was $55.2 million.[221] If his argument is accepted, ARG's pre-Reorganization value would increase by $23.9 million.[222] However, that increase in net asset value would also need to be applied to ARG's 10% interest in Harrison after the conversion.[223] This would result in an increase in the value of Plaintiffs' post-Reorganization units and thus would be accretive.[224] Plaintiffs would therefore not have been damaged even if their valuations are accepted.

Thus, the Court rejects Plaintiffs' attempts to augment the value of their units. Their expert's financial analysis was not persuasive and they otherwise rely on the testimony of Senkevitch, who was not presented to the Court as an expert. Gannon has demonstrated that the Reorganization increased the value of Plaintiffs' units and Plaintiffs, after trial, adopt much of his analysis. Finally, even if Plaintiffs' arguments concerning Gateway or Harrison were accepted, ARG's post-conversion interest in those properties would increase the value of Plaintiffs' units.

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[221] JE-235.

[222] The difference between Gannon's pre-Reorganization valuation and Senkevitch's is $23.9 million. The difference in decimal points is based on the rounding of numbers to the nearest hundred thousand in this description, though no such rounding occurred when the calculations were performed.

[223] *See supra* note 105.

[224] The $23.9 million divided by the roughly eight million fully diluted units before the Reorganization results in an increased price of $2.77 per unit. After the conversion, dividing ten percent of $23.9 million by the remaining approximately seven hundred thousand units would result in an increase in value of $3.30 per unit.

The Court proceeds to consider Pietroforte's analysis to complete its assessment of fair price.

(c) *Pietroforte's Testimony*

Pietroforte based his analysis upon affidavits and depositions, letters, emails, memoranda, financial reports, appraisals, and various agreements or other documents regarding the Reorganization.[225] The materials Pietroforte relied upon appeared to have been gathered from discovery and thereby limited Pietroforte from independently attempting to value ARG as a pre- and post-Reorganization entity. He also made no attempt to value individually and independently each discrete asset, although he did offer more specific valuations of the Gateway and Harrison properties. Audited financial statements and pro forma projections appeared to have been the most thorough financial data upon which Pietroforte relied.[226]

Pietroforte offered an exhibit which demonstrates that FARS and ACP were given the opportunity to convert equity into loans, which was an opportunity the minority did not receive.[227] Pietroforte also conducted a 13-week cash flow analysis to evaluate the pre- and post-Reorganization entities.[228] He also opined that two assets, the Gateway air rights and Harrison, were undervalued and thus the

[225] Pietroforte Tr. 994.
[226] *See, e.g.*, JE-388; JE-417; JE-418; JE-427; JE-428; JE-429; JE-430.
[227] JE-478.
[228] Pietroforte Tr. 998-1004.

post-Reorganization value of the units should be increased.[229] Pietroforte then took the post-Reorganization value of Plaintiffs' units based on the December 2008 financials and added in the per unit value of the Gateway rights, the Harrison property, and a $4 million payment to Cocoziello to cover his tax liabilities, to assess Plaintiffs' damages.[230] Pietroforte argued that the sum of those numbers, $114.74 per unit, was the value of Plaintiffs' units following the Reorganization. He then asserted that because the December 2008 financials showed a negative $31 million of net equity, Plaintiffs' units were without value after the Reorganization and their damages are the difference between $114.74 and zero: $114.74 per unit.[231] Yet, Pietroforte conceded that $25 per unit was a "reasonable starting point" for the pre-conversion value of ARG's units.[232] Pietroforte concluded that the Reorganization was not conducted reasonably and in a manner that was in the best interests of ARG or its Class A unitholders.[233] He summarized his comments as (1) the minority received lesser value and (2) Plaintiffs' units were subordinated to Defendants' interests after the Reorganization.[234]

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[229] *Id.* at 1009-10.
[230] *Id.* at 1027-47, 1057; JE-480. Plaintiffs did not pursue Pietroforte's argument based on the $4 million tax payment due to Cocoziello in their post-trial briefing.
[231] Pietroforte Tr. 1057.
[232] *Id.* at 1077, 1091.
[233] *Id.* at 997-98.
[234] *Id.* at 1086-87.

As alluded to above, Plaintiffs appear to distance themselves from Pietroforte's valuation in their post-trial briefing.[235] This may not be surprising, considering that Plaintiffs have asserted that $25 per unit would have been a fair price.[236] Pietroforte's support for damages of more than four times that amount is not credible when Plaintiffs were among those parties who best knew ARG's value before they were fired and would likely have been satisfied with redemptions at a vastly lower price.[237]

From a doctrinal perspective, Pietroforte's analysis is inconsistent with the methods typically applied in determining fair value.[238] Pietroforte encourages the Court to accept damages as the difference between the *post*-Reorganization value and the December 2008 value, which Pietroforte argues is zero.[239] However, our

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[235] Plaintiffs cursorily invoke Pietroforte's analysis when advocating for damages and discussing the Reorganization's fairness. *See* Pls.' Post-Trial Mem. of Law at 38; Pls.' Post-Trial Reply Mem. of Law at 23. Their strategy shifted to trying to sponsor, with modification, Gannon's analysis.

[236] JE-283 at 19; JE-284 at 20; JE-285 at 21; JE-286 at 19.

[237] *See supra* notes 30-31 & accompanying text.

[238] *See In re PNB Hldg. Co. S'holders Litig.*, 2006 WL 2403999, at *22 (Del. Ch. Aug. 18, 2006) ("[T]o measure whether the [transaction] price was unfair, the court must conduct the same essential inquiry as in an appraisal, albeit with more leeway to consider fairness as a range and to consider the remedial objectives of equity.").

[239] Pietroforte Tr. 1057. Pietroforte claims to base his conclusion that the value of the units was zero in December 2008 on ARG's 2008 audited financials, which he acknowledges are estimates of value by management. Pietroforte Tr. 1063-65; *see* JE-427. Pietroforte did not make an effort to understand how management arrived at its valuations or to compare ARG's loss in value with an index measuring New Jersey real estate values to evaluate the role of market forces on these values. Pietroforte Tr. 1064-66. Additionally, he appears to ignore that ARG switched auditors and adopted fair value measurements in between 2007 and 2008. *See* JE-427 at 9. Pietroforte's willingness to

law attempts to value a plaintiff's proportionate interest in a going concern to provide the minority with the "value that was taken from them."[240] The Court, through its broad discretion to tailor a remedy, has in the past found it useful to draw upon the law governing appraisals in fashioning its remedy.[241] In the context of an appraisal, the Court's endeavor is the "determination of value as of the day of merger."[242] Here, it is sensible to determine the initial value of Plaintiffs' units as of the day of the Reorganization. Pietroforte concedes that Plaintiffs' units were worth approximately $25 per unit before the Reorganization, which is largely consistent with Gannon's testimony.

Pietroforte's approach also raises the question of what value should be used for the purposes of valuing Plaintiffs' units after the Reorganization. He argues that the December 2008 value should be used. In an appraisal action, value is fixed by the consideration paid to the shareholders and thus further inquiry is unnecessary. One proper measure of the fairness of the Reorganization would seem to be a comparison of the value of the Plaintiffs' units preceding the

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accept, with minimal independent scrutiny, numbers which favor his clients, again causes the Court to approach his valuations with skepticism.

[240] *Reis v. Hazelett Strip-Casting Corp.*, 28 A.3d 442, 464 (Del. Ch. 2011) (citation omitted).

[241] *See, e.g.*, *Gilliland v. Motorola, Inc.*, 873 A.2d 305, 314 (Del. Ch. 2005) ("Although quasi-appraisal is an equitable remedy and the court is not bound to follow the appraisal statute, the court concludes that it is most appropriate to do so.").

[242] *Universal City Studios, Inc. v. Francis I. duPont & Co.*, 334 A.2d 216, 221 (Del. 1975).

Reorganization and the value immediately following the Reorganization.[243] This approach seeks to emulate the appraisal valuation's comparing the value of a plaintiff's shares immediately preceding a merger, with the price paid to extinguish those shares pursuant to the merger.

Pietroforte also opined that Defendants failed to consider the cash needs of ARG properly after the Reorganization. He stated that he found no evidence of such projections being performed by the Board and that a 13-week prospective cash flow analysis was typical in the restructuring industry.[244] However, Sheridan testified that she prepared, and presented to the Board, 15- to 18-month prospective analyses of ARG to ensure the entity would remain solvent. She stated she began with operating cash, added in projected property budgets and their cash flows, subtracted debt payments, and tried to address contingencies based on possible

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[243] Indeed, Plaintiffs appear to recognize this when they state "[t]he case law, Defendants, and Mr. Gannon all agree that the appropriate time at which to measure the value of Plaintiffs' units is the fall of 2008, at the time of the reorganization, not an arbitrarily selected future date convenient for Defendants. In fact, at trial Mr. Gannon testified that all events that took place after the reorganization were immaterial to, and had no bearing on, his opinions or the proper analysis." Pls.' Post-Trial Reply Mem. of Law at 18. Plaintiffs' quote indicates that they again have strayed from Pietroforte's analysis, which sought to use the value of Plaintiffs' units in December 2008 as the value destroyed by the Reorganization. Though comment may be unnecessary based on Plaintiffs' distance from Pietroforte's opinion, his decision to use the value of ARG's units in December 2008 as the final value of Plaintiffs' units may be criticized as overly broad. It incorporates the effects of the recession upon Plaintiffs' units, which Defendants testify caused additional hardship to ARG. Although a perfect separation of the effects of the Reorganization and macroeconomic events may be impossible, here, because of the severity of those macroeconomic events, Pietroforte's approach is less persuasive.

[244] Pietroforte Tr. 999.

sales and redemption options or dividend payments.[245] She also evaluated and determined that ARG, after the Reorganization, would be in compliance with its lenders' covenants and reported that information to the Board.[246]

Pietroforte argued that the Reorganization evidenced the Board's failure to project its cash flows because ARG defaulted on the Taberna debt and the notes owed to the minority who accepted the $21.68.[247] He also testified that a liquidity facility was put in place in 2010 and further evidenced ARG's cash flow problems.[248] However, these events took place in late 2009 and 2010. Pietroforte's recommended 13-week cash flow analysis would not have been able to project that far into the future and thereby helped ARG to prepare for them. He also does not opine that such an analysis would have been able to account for the effects of the recession upon ARG. Although Defendants' case may have been stronger had they presented contemporaneous evidence of Sheridan's analysis or presentations to the Board, Sheridan's testimony persuades the Court that ARG's Board did not completely fail to project ARG's outstanding cash needs.

Pietroforte's testimony concerning ARG's cash flows raises the question of whether Defendants orchestrated the Reorganization in such a way as to guarantee ARG's equity would later be wiped out. The topic was implicitly raised as a result

[245] Sheridan Tr. 1274.
[246] *Id.* at 1275-76.
[247] Pietroforte Tr. 1004.
[248] *Id.* at 1004-05.

of Plaintiffs' strenuous assertions that the post-Reorganization value of Plaintiffs' units is zero and was not a main focus at trial. Neither party's primary focus was on evaluating ARG's liquidity needs after the Reorganization or sorting out the impact of the recession upon ARG.[249]

Sheridan's projections of ARG's financial viability after the Reorganization and its compliance with its lenders' covenants provides some support for the view that the Reorganization was not set up to render the minority's units valueless. The goals of the Reorganization also support this view; ARG continued to retain the stabilized properties with cash flows and to isolate the riskier properties still undergoing development. As pointed out above, the symptoms of cash flow problems Pietroforte identified did not occur until over a year after the Reorganization and they arose during a time of economic crisis. Although the record contains other evidence that ARG had cash flow problems before the Reorganization, the conversion should have improved these problems by moving the cash-hungry properties to ARD. Finally, it is doubtful that a 13-week cash

[249] Gannon, however, did opine that there was a 25% decline in the value of ARG's assets as a function of the recession. Gannon Tr. 1181. Plaintiffs also raised the issue after trial, although they did so without reference to any expert testimony. *See* Pls.' Post-Trial Mem. of Law at 40-41. They argue that because millions of dollars of debt was layered on top of Plaintiffs' units, Defendants ensured they would be rendered valueless. Their analysis is lacking because it does not acknowledge the reduction in ARG units outstanding after the Reorganization or reference the net asset value of ARG after the Reorganization.

flow projection would have remained an accurate prediction of the financial hardship with which ARG had to contend soon after the Reorganization.[250]

Pietroforte also accurately identified the Board's acts through which they converted their members' equity to loans senior to Plaintiffs' equity. However, Pietroforte's conclusion does not demonstrate that Plaintiffs received an unfair price for their units because even with this additional debt, the distribution of properties (or the discounted payments to the rest of the minority) may have been accretive to Plaintiffs. Pietroforte did not compare the value of Plaintiffs' pre- and post-Reorganization units in a manner which permits the Court to determine whether Plaintiffs received a fair price.[251]

Thus, the Court concludes that Pietroforte's analysis was, on the whole, unconvincing and did not address the question of whether value was taken away from Plaintiffs as a result of the Reorganization. Pietroforte's analysis of the procedural aspects of the Reorganization was accurate, but unhelpful in evaluating fair price. He also properly pointed out the problematic conversion of the

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[250] Perhaps arguments concerning the Company's liquidity situation could have been relevant in causing the Court to consider the value of Plaintiffs' units in December of 2008 or later, had that been the focus of the parties throughout trial.

[251] Indeed, if Pietroforte's analysis were accepted at face value, he demonstrated that Plaintiffs received a fair price because he admitted their units were worth approximately $25 per unit before the Reorganization and argued that they were worth $114 per unit after the Reorganization.

convertible notes of FARS and the units of ACP into loans senior to the Plaintiffs' units, discussed above.

(d) *Plaintiffs' Damages Theory and the Fairness of the Value Received by the Minority*

Plaintiffs offer at least five different values to the Court as a measure of the value of Plaintiffs' units before the Reorganization.[252] They appear to offer two possible valuations for the consideration they received through the Reorganization: either $21.68, the price at which a significant portion of ARG's units were redeemed,[253] or zero, the value of their units today.[254] The Court rejects Plaintiffs' suggestion that they were unfairly redeemed for $21.68, because it is factually inaccurate. Plaintiffs refused to redeem their units at a discounted price and to transfer their equity to ARD.[255] They remained in ARG and thus appear to have benefited from FARS's negotiating leverage over Cocoziello.

Plaintiffs argue that the Court should ignore this because Plaintiffs did not choose to "stay with ARG," but were forced to reject the redemptions in order to preserve their right to sue.[256] However, the Court considered Plaintiffs' lack of choice under its analysis of the fairness of the process employed and the fairness of

[252] *See* Pls.' Post-Trial Mem. of Law at 38-40.
[253] *See id.* at 20, 25, 31-33; Pls.' Post-Trial Reply Mem. of Law at 21-24.
[254] *See* Pls.' Post-Trial Mem. of Law at 38-40.
[255] Plaintiffs assert that the minority who did cash out at $21.68 were required to sign a release and waiver in order to receive their cash and note. *Id.* at 38 n.17.
[256] *Id.*

the process is then a part of the unitary consideration of the transaction's fairness. The Court's inquiry into the fairness of the price evaluates the consequences to the value of Plaintiffs' units as a result of the Reorganization, which was the difference in value of their units in ARG before and after the Reorganization.

The testimony of both Gannon and Pietroforte reveals, in part because of the extreme reduction in the number of outstanding units, that the value of Plaintiffs' units increased through the Reorganization. This appears to have been the case even though the Board layered the notes to FARS and ARD on top of Plaintiffs' equity. The Board, when converting FARS's notes and ACP's units, created an additional approximately $120.8 million of senior debt.[257] Although the parties did not argue this point, a question is raised as to whether the Reorganization still would have been accretive to Plaintiffs if these transactions were unwound. Once again, because Plaintiffs accept Gannon's models, they provide the starting point for this analysis. If FARS had converted its notes to units at the $16.65 strike price, but had not converted those units into loans and the approximately 1.6 million units of ACP were not converted into the $40.7 million note, then the value of Plaintiffs' units after the Reorganization would have been $25.19.[258] This is less

[257] *See* JE-478.

[258] The Court begins with JE-367. The face value of these notes is $120,779,360, and comes from FARS's new $60 million note, its $20,115,375 subordinate note and the approximately $40,663,985 subordinate note from ARG to ARD. However, Gannon performed mark-to-market adjustments to these notes, and thereby derived values of

than Gannon's pre-Reorganization value of $25.96 and therefore appears to be dilutive.

Thus, according to Gannon's assumptions (which include his mark-to-market discounts), Plaintiffs would have lost some value from their units if the layering of debt were completely unwound. This does not, in the Court's opinion, make the transaction's price unfair, because the conclusion is dependent on a series of assumptions, which are readily debatable. Rather, even under a set of assumptions that are the most favorable to Plaintiffs, the value they received appears to be a close approximation of the value they had before the Reorganization. Thus, that value seems to be within a range of reasonable values. Additionally, even under this view, Plaintiffs would have received more value per

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$52,932,922, $22,336,139, and $37,671,080 for the new FARS convertible debentures, FARS subordinate note, and ARD subordinate note, respectively. The sum of that debt, per Gannon's valuation, is $112,940,141. The 600,000 units FARS converted would be subtracted from the 726,096 outstanding units which existed after the conversion and instead the 3,603,603 converted FARS units and the 1,626,559 ACP units, representing the value of the $40,663,985 subordinate note at a conversion value of $25.00 per unit, would be added to the number of units outstanding. The total number of units outstanding after the Reorganization would therefore be 5,354,258. The new outstanding net asset value is $134,867,518, derived by adding back the value of loans at Gannon's discounted value to the net asset value he calculated of $21,927,377. The value per unit is therefore $25.19, taken by dividing $134,867,518 by 5,354,258. If the ARD note is not unwound, then the value per unit becomes $26.07, and the conversion is again accretive to Plaintiffs.

unit than was awarded to FARS and ACP, as the units they converted were valued at $25 per unit.[259]

Plaintiffs also suggest that the Court should assess their damages as the difference between the value of their units at the time of the Reorganization (post-Reorganization or pre-Reorganization) and the value of their units today, which is zero. As discussed above, the Court seeks to determine Plaintiffs' proportionate value in a going concern at the time of Reorganization and assess whether the value received was within a range of reasonableness. At least in this context, the Court is concerned with the disloyalty or bad faith of fiduciaries, with respect to the pertinent transactions, rather than a company's failure due to economic stresses or other factors. To the extent possible, the Court's valuation should focus on the acts of the fiduciaries separately from larger macroeconomic events. The question is whether the Board took value from its unitholders or purposely set up ARG's failure. Thus, the Court's focus is chronologically limited to the period surrounding the Reorganization to reduce the number of factors which may have caused Plaintiffs' units to decline in value.

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[259] Of course, this raises the question of where the excess value went, given that the value of the assets and debts were held constant throughout Gannon's models. Because the minority who accepted a discount could not have captured the excess value, the process of elimination would lead one to conclude that ARD captured the excess value. Another conclusion is that Gannon's figures are within a range of values, but are imperfect and dependent on his valuation of the real estate assets and his mark-to-market assumptions. No real issue was raised relating to either of these sets of assumptions by the parties, except for the disputes concerning the Harrison and Gateway properties discussed above.

When assessing the value of Plaintiffs' units before and immediately following the Reorganization, the testimony of both Gannon and Pietroforte demonstrated that the transaction was accretive to Plaintiffs. Gannon opined that the Class A units were worth $25.96 before the Reorganization and were worth $30.28 afterwards. Pietroforte admitted that the units were worth approximately $25 before the Reorganization and opined that they were worth approximately $114 afterwards. As explained above, Plaintiffs' theories implicate the question of whether ARG might have been set up to fail. However, the symptoms of its failure, cited by Pietroforte, did not occur until 2009 and 2010. Evidence exists that ARG evaluated its liquidity needs following the Reorganization and the Court doubts that such prospective analyses would have predicted the recession which followed and remained accurate, even had a more formal 13-week analysis been produced.[260]

Plaintiffs tried the case to demonstrate that FARS and Cocoziello diluted their units during the Reorganization. Although the process was conflicted and was, from a procedural perspective, unfair, Plaintiffs appeared to have been among

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[260] Pietroforte and Gannon disagreed about the treatment of the rest of the minority who consented to a payment of $21.68, in cash and a note. Gannon opined that the consideration received by the minority was fair because a minority discount was appropriately applied to their holdings. Gannon also opined that the consideration received by ACP and FARS was fair. Pietroforte's analysis was limited to the minority, but he opined that the minority who received $21.68 received an unfair price. However, the Court's inquiry is into the value of Plaintiffs' units. As a factual matter, those units were not liquidated at $21.68 per unit.

the transaction's winners from the perspective of value received through the transaction. Since the Reorganization, the value of ARG's units disappeared. No principled basis has been presented to the Court to decide whether the loss of value of ARG's units between the time of the Reorganization and now was due to the recession, to reasonable managerial decisions which turned out poorly, or even to other unfair acts authorized by ARG's Board. Thus, the Court cannot find that Plaintiffs' damages are measured by the difference in the value of their units at the time of the Reorganization and the value of their units now. Gannon's analysis, which Plaintiffs state they have always been willing to accept, revealed that the transaction was accretive to Plaintiffs. Thus, from a price perspective, they received fair value.

3. Was the Reorganization Entirely Fair to Plaintiffs?

The Court's inquiry into the entire fairness of the transaction is a unitary inquiry. The Delaware Supreme Court has described the "proper test of fairness as whether the minority stockholder shall receive the substantial equivalent in value of what he had before."[261] Under such a view, the fairness of price may be seen as the preponderant concern.[262] However, the Delaware Supreme Court has also recognized that an unfair process may "infect" the fairness of the price granted to

[261] *Sterling v. Mayflower Hotel Corp.*, 93 A.2d 107, 114 (Del. 1952).
[262] *Weinberger v. UOP, Inc.*, 457 A.2d 701, 711 (Del. 1983).

the minority.[263] It has emphasized the "exacting" nature of the entire fairness standard and its requirement that the conflicted fiduciaries "establish to the *court's* satisfaction that the transaction was the product of both fair dealing *and* fair price."[264] Robust procedural protections may support a determination that price was fairly within a range of reasonable values, and a failure of process may prevent a Court from reaching such a conclusion.[265] Additional skepticism may be warranted in certain circumstances, such as when fiduciaries act disloyally or out of self-interest.[266]

The process employed by ARG's Board left much to be desired and was motivated by its members' self-interest. That process did not empower ARG's minority to negotiate with the Board, to seek interim injunctive relief, or to ratify the transaction. The Board failed to provide information to the minority which could help them in evaluating the value of their units and sent inadequate notice

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[263] *Bomarko, Inc. v. Int'l Telecharge, Inc.*, 794 A.2d 1161, 1183 (Del. Ch. 1999), *aff'd*, 766 A.2d 437 (Del. 2000).

[264] *Cinerama, Inc. v. Technicolor, Inc.*, 663 A.2d 1156, 1179 (Del. 1995) (emphasis in original) (citation omitted).

[265] *See Reis v. Hazelett Strip-Casting Corp.*, 28 A.3d 442, 467 (Del. Ch. 2011).

[266] *See William Penn P'ship v. Saliba*, 13 A.3d 749, 758 (Del. 2011) ("Merely showing that the sale price was in the range of fairness, however, does not necessarily satisfy the entire fairness burden when fiduciaries stand on both sides of a transaction and manipulate the sales process."). In similar circumstances, this Court has determined that process has "infected" price and that transactions arguably within a range of fairness were not entirely fair. *See, e.g.*, *Bomarko*, 794 A.2d at 1183; *HMG/Courtland Props., Inc. v. Gray*, 749 A.2d 94, 116 (Del. Ch. 1999). However, it has also determined that an unfair process, ultimately producing a fair price permitted a conclusion that the transaction was entirely fair. *See e.g., In re Trados Inc. S'holder Litig.*, 73 A.3d 17, 76-78 (Del. Ch. 2013).

only after the Reorganization was complete. No fairness opinion guided the Board's valuation efforts. In sum, the Court was not convinced that the Board was adequately representing the minority interests.

The Court is particularly troubled by the process surrounding the conversion of FARS's convertible notes, with a face value of $60 million, into a $60 million note, an approximately $20.1 million subordinate note, and 600,000 Class A units. Similarly, the conversion of 1,626,559 of ACP's units into an approximately $40.7 million note from ARG to ARD is disturbing.[267] Assuming the accuracy of the Board's $25 per unit valuation, the Board nonetheless impermissibly granted itself seniority over the rest of the minority to grant preferential treatment to the entities associated with its members.

However, the Court has found that the price received by Plaintiffs was fair. This is based on the Court's assessment that a comparison of the pre- and post-Reorganization value of Plaintiffs' units is the most appropriate measure of fair price, and the testimony of both expert witnesses, which demonstrated that the

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[267] If a portion of a transaction is not entirely fair, it would not be unreasonable to conclude that the entire transaction, thus, was not entirely fair. The Court distinguishes its inquiry on this unfair aspect of the Reorganization because it consists of a limited and discrete set of events and because the damages suffered by the Plaintiffs, if any, can be more accurately described and calculated. Also, there is no other part of the overall transaction that could somehow "balance out" the effects of the debt exchange.

Reorganization was accretive.[268] Plaintiffs appear to have received the substantial equivalent in value of what they had before, as the value of their units nominally increased through the Reorganization.

In fact, they may have received "the highest value reasonably achievable."[269] The 144A transaction and the Normandy and JER offers demonstrated the lack of interest in different markets for a transaction valuing ARG's units at $25 per unit, even before the markets started "quivering." The record does not suggest that ARG's business or the real estate market had improved. Additionally, FARS and ACP accepted $25 per unit from the pre-Reorganization price of $25.96 per unit, while the value of Plaintiffs' units may have increased from that amount to $30.28 per unit. Thus, according to Gannon's models, Plaintiffs' units fared better than the units held by the Board's entities. Although the minority who accepted the

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[268] The Court has already noted some skepticism about Gannon's testimony, but Plaintiffs' inability to explain convincingly, in the whole of their briefing, how they suffered economically from the Reorganization is equally disconcerting. And, because much of Plaintiffs' analysis relies on Gannon's work, the Court must tentatively accept it. Given the steady deterioration of ARG's assets, it is plausible that Plaintiffs' units were worth less than $21.68 and a buy-out at that price would have been a reasonable liquidation price. Moreover, Plaintiffs may have had the most knowledge of ARG's business and the value of its assets. Their decision to remain in ARG may have been a deliberate application of their knowledge to obtain the best deal available (and a fair one) at the time of the Reorganization. Unfortunately, soon thereafter, the recession diminished the value of ARG's assets. The Court is unable, with any certainty, to resolve these concerns when the parties are in agreement about the appropriateness of Gannon's valuation.

[269] *See Cinerama, Inc. v. Technicolor, Inc.*, 663 A.2d 1156, 1177 (Del. 1995) (citation omitted).

$21.68 per unit received a discounted price for their units, they accepted that price and agreed not to challenge the consideration they received.

After considering the process employed by ARG's Board and the price Plaintiffs received for their units, the Court concludes that ARG's Reorganization was not entirely fair. Although Plaintiffs have received fair value for their units, value exceeding that received by FARS and ACP, the process employed by Defendants was unsatisfactory. In particular, the Board's approval of the conversion of FARS's and ACP's units into loans senior to Plaintiffs' units was inappropriate. Moreover, the Reorganization was a self-interested transaction, and thus any additional leeway which may be permitted to fiduciaries merely acting without care is inappropriate in this context. Thus, the poor process employed by Defendants prevents the Court from finding, to its satisfaction, that price *and* process, assessed as a unitary standard, was fair.

After a fiduciary has been found to have failed to act in an entirely fair manner, the Court considers the appropriate remedy to impose.[270] Such a remedy could be a damages award as would meet an appraisal action's fair value analysis; however, such a determination is not required as the Court's powers are broad in

[270] *Reis v. Hazelett Strip-Casting Corp.*, 28 A.3d 442, 466 (Del. Ch. 2011) (quoting *Cinerama, Inc. v. Technicolor, Inc.*, 663 A.2d 1134, 1143 (Del. Ch. 1994), *aff'd*, 663 A.2d 1156 (Del. 1995)).

fashioning relief under entire fairness.[271] "The law does not require certainty in the award of damages where a wrong has been proven and injury established. Responsible estimates that lack m[a]thematical certainty are permissible so long as the court has a basis to make a responsible estimate of damages."[272]

Plaintiffs have not sought disgorgement or the unwinding of the Reorganization. Their disparate theories of damages were discussed when assessing fair price and the Court's consideration of their theories has not changed.[273] Moreover, Gannon established that Plaintiffs' units increased in value and Plaintiffs affirm the vast majority of his work. Plaintiffs therefore appear to be among the beneficiaries of the Reorganization.[274]

Plaintiffs' units are apparently now worthless, but those events evidencing ARG's stresses, to which Pietroforte directs the Court, manifested themselves in late 2009 and 2010. ARG does not appear to have been set up with the intent to fail and thus the most likely cause for this economic loss is the recession. The value of ARG was directly dependent on the value of its properties and it is unsurprising the ARG's value declined when the real estate market declined.

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[271] *Id.*

[272] *Id.* (quoting *Red Sail Easter Ltd. P'rs v. Radio City Music Hall Prods., Inc.*, 1992 WL 251380, at *7 (Del. Ch. Sept. 29, 1992)).

[273] *See id.* at 468 ("[W]here the fair price analysis and remedial determination coincide, this Court has prudently declined to review fair price twice, first as a range for purposes of the entire fairness standard and later as a point figure for purposes of the remedial calculation.").

[274] The notion of a beneficiary of the Reorganization is illusory in light of the subsequent developments in the economy.

However, the Court cannot say with confidence that the disloyal acts of ARG's Board damaged Plaintiffs. The Court cannot identify a satisfactory method of separating these different harms, and making Plaintiffs whole because of events outside of the control of ARG's fiduciaries would be inequitable. Although the Court's assessment need not be perfect, the inadequacy of Plaintiffs' explanation for how they were harmed reduces the Court's confidence that they were. The Reorganization was accretive to Plaintiffs and the Court has no basis to make a responsible estimate of damages. Thus no damages are justified.[275] Additionally, no principled method of unwinding the Reorganization generally has been presented to the Court.

However, Plaintiffs have complained about the preferential treatment granted to the units of FARS and ACP, and the Court agrees that it was unreasonable. The most sensible remedy may be to unwind those preferential

[275] The exculpation provision in ARG's operating agreement only insulates ARG's Board from liability to its members. *See* JE-06 § 7.10 ("No Member, any agent of any Member, including the Directors and the Executive Officers, or Five Arrows or any of their respective members, partners, officers, directors, employees or Affiliates . . . shall be liable to any other Member, Affiliate of any Member or the Company for mistakes of judgment or for any action or inaction, unless such mistakes, action or inaction arise out of, or are attributable to, willful misconduct or bad faith of the Indemnified Party; . . . ."). Its consideration is unnecessary at this juncture, as Defendants have not been found to be liable to Plaintiffs and the provision does not place ARG outside the reach of the Court's equitable powers. This is consistent with authority requiring that exculpation be considered after finding a fiduciary liable. *See Emerald P'rs v. Berlin*, 787 A.2d 85, 93 (Del. 2001) ("[W]hen entire fairness is the applicable standard of judicial review, this Court has held that injury or damages becomes a proper focus only *after* a transaction is determined *not* to be entirely fair.").

loans and set Plaintiffs, FARS, and ACP shoulder-to-shoulder in ARG. Yet, because the minority's units now are without value, unwinding this transaction also may be meaningless and unnecessary. The parties have not briefed this issue or focused upon it as a remedy and thus they are invited to address the consequences of unwinding these debt reconfigurations. They are also invited to address the topic of attorneys' fees.

Finally, Plaintiffs, in their various damages calculations, encourage the Court to exclude from the count of outstanding units, Cocoziello's $10 million pari passu investment through ACP in 2006 on the same terms as FARS's convertible notes. This issue, like those claims which follow, was not a primary focus of trial, of the expert witnesses, or of the parties' briefing and is less ripe for an entire fairness analysis.[276] McGurk testified, as the last money in, Cocoziello would have

[276] Pietroforte's analysis acknowledged Cocoziello's investment, but he did not consider the fairness of the investment, from a procedural or price perspective, in his testimony. *Compare* Pietroforte Tr. 1026, *with* Pietroforte Tr. 975-1070. Plaintiffs briefly invoke its unfairness, but again rely on Senkevitch's testimony, who is not an expert witness. Pls.' Post-Trial Mem. of Law at 28 (citing Senkevitch Tr. 769-71). The parties' focus at trial was on the Reorganization and no principled manner of assessing Cocoziello's investment was presented. Plaintiffs' goal appears to be excluding Cocoziello's "unfairly obtained" 183,933 preferred units from the count of pre-Reorganization units in order to increase the pre-Reorganization count of units. *See* Pls.' Post-Trial Mem. of Law at 28, 39. Such an analysis is predicated on a demonstration of its unfairness, and moreover, appears only to make the Reorganization relatively less beneficial to Plaintiffs. *See supra* note 195. It does not alter the larger problem facing Plaintiffs: that the most appropriate measure of fairness appears to be a comparison of the pre- and post-Reorganization value of their units, rather than of ARG's pre-Reorganization units and zero or $21.68.

been entitled to better terms than the first money in.[277] More importantly, the transaction replicated the arm's length transaction negotiated by FARS and ARG and thereby satisfies the Court that the transaction was reasonable, particularly given the parties' reduced focus on the issue.

D. *Did Defendants Violate the Implied Duty of Good Faith and Fair Dealing?*

Plaintiffs alleged a broader array of theories than the matters they argued in post-trial briefing. Although arguably such theories were abandoned,[278] the Court briefly addresses them in the balance of the opinion.

Plaintiffs argue that Defendants violated the implied covenant of good faith and fair dealing and appear to suggest that Section 7.01 of ARG's operating agreement was violated. However, for the reasons discussed above, Plaintiffs did not receive an unfair price during the Reorganization and thereby were not harmed by the transaction. In the absence of damages, they cannot prevail on this claim.

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277 McGurk Tr. 313-14. McGurk also is not an expert witness, although his statement provides some marginal support for Cocoziello's investment. Again, the experts' and the parties' lack of focus on the issue prevents the Court from being able to evaluate this claim.

278 Plaintiffs did not respond to Defendants' arguments addressing all but one of Plaintiffs' additional claims throughout post-trial briefing, though they did reserve the right to respond to Defendants' counterclaims and argued that Sheridan aided and abetted ARG's fiduciaries in breaching their duties. Pls.' Post-Trial Mem. of Law at 1 n.1, 37. Defendants argued that Plaintiffs failed to prove a breach of the implied covenant of good faith and fair dealing, any of their three causes of action based upon Padavano's alleged promises to redeem their Class A units, fraudulent inducement, or that they are entitled to a receiver. Defs.' Post-Trial Br. at 67-85.

E. *Did Padavano Breach his Fiduciary Duties to the Plaintiffs, or Fraudulently Induce them to Sign Their Separation Agreements, and Should Defendants Be Estopped from Not Paying Plaintiffs?*

Plaintiffs, in their pre-trial brief, asserted that they would demonstrate at trial that Padavano promised that ARG would redeem Plaintiffs' Class A units at $24.75 per unit upon the sale of two properties, which induced Plaintiffs to sign their separation agreements. To do so, Plaintiffs would need to prove by clear and convincing evidence that

> (i) a promise was made; (ii) it was the reasonable expectation of the promisor to induce action or forbearance on the part of the promisee; (iii) the promisee reasonably relied on the promise and took action to his detriment; and (iv) such promise is binding because injustice can be avoided only by enforcement of the promise.[279]

Plaintiffs have not demonstrated the existence of a promise by Padavano to purchase Plaintiffs' units. Sopko admitted that Padavano did not make a clear and definite promise to redeem Plaintiffs' units upon the sale of the properties.[280] Moreover, the negotiations between Plaintiffs and Padavano when finalizing their separation agreements demonstrated that Plaintiffs were unable to secure the redemption of their units despite their efforts over a period of at least a month.[281] They made multiple efforts to include such language and could only secure

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[279] *Lord v. Souder*, 748 A.2d 393, 399 (Del. 2000) (citation omitted).
[280] Sopko Tr. 510.
[281] Stathakis Tr. 655; Senkevitch Tr. 884. Senkevitch also understood that Padavano was unable to make commitments on behalf of ARG without the Board's approval. Senkevitch Tr. 878, 959. The other Plaintiffs likely also understood this limitation of Padavano's authority.

language indicating that Plaintiffs had an interest in the Class A units; that language is not a promise to redeem.[282]

For the same reasons Plaintiffs' fraudulent inducement claim must fail. They needed to demonstrate by clear and convincing evidence "a material misrepresentation by the defendant of a presently existing fact or past fact; knowledge or belief by the defendant of its falsity; an intent that the plaintiff rely on the statement; reasonable reliance by the plaintiff; and resulting damages to the plaintiff."[283] For the purposes of the fraudulent inducement claim, Padavano's misrepresentations would be his alleged promises; however, they have not been proven by clear and convincing evidence. The testimony from trial instead indicated that Plaintiffs did their utmost to obtain some sort of redemption provision in their separation agreements, that they were unable to do so, and that they therefore accepted a watered-down acknowledgement of their ownership which was not a promise to redeem the units.

Finally, Plaintiffs assert generally that Padavano breached fiduciary duties owed to them by actively misleading them or making false statements. To prove this claim, Plaintiffs must demonstrate that Padavano "knowingly disseminat[ed]

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282 JE-141; JE-146; JE-151.
283 *Liberty Mut. Ins. Co. v. Land*, 892 A.2d 1240, 1247 (N.J. 2006).

materially false information."[284] For the same reasons above, Plaintiffs have not carried their burden of proof. The history of negotiations and Plaintiffs' knowledge of Padavano's ability to make such a commitment in the absence of Board approval made clear that he did not promise to redeem Plaintiffs' units.

F. *Did Defendants Engage in a Civil Conspiracy or Aid and Abet the Alleged Breaches of Fiduciary Duties?*

To prevail on their civil conspiracy claim, Plaintiffs must demonstrate "(1) [a] confederation or combination of two or more persons; (2) [a]n unlawful act done in furtherance of the conspiracy; and (3) [a]ctual damage."[285] Plaintiffs argue that Defendants entered into a conspiratorial agreement when preparing for the Reorganization. The improper means by which Defendants carried out their plan allegedly were their acts of denying Plaintiffs information, fraudulently inducing Plaintiffs to sign separation agreements which would not redeem their units at their fully vested value, and threatening Plaintiffs with negative tax consequences if they did not redeem from ARG. However, Plaintiffs have not demonstrated that they were damaged by the Reorganization, and therefore, they cannot recover.

[284] *Malone v. Brincat*, 722 A.2d 5, 14 (Del. 1998). Arguably (the issue has not been briefed), Plaintiffs may have intended to invoke the higher *Malone* standard, which asks whether "the alleged omission or disclosure is material." *Id.* at 12. First, Plaintiffs failed to make such an argument. Second, even on this standard, Plaintiffs' failure to prove an omission or disclosure by Padavano prevents their recovery.

[285] *Nicolet, Inc. v. Nutt*, 525 A.2d 146, 149-50 (Del. 1987).

A claim of aiding and abetting a breach of fiduciary duty requires Plaintiffs to establish "(1) the existence of a fiduciary relationship, (2) the fiduciary breached its duty, (3) a defendant, who is not a fiduciary, knowingly participated in [the] breach, and (4) damages to the plaintiff resulted from the concerted action of the fiduciary and the non-fiduciary."[286] In the one claim Plaintiffs did forward in post-trial briefing, they argue that Sheridan was the point person for organizing the transaction and assisted in assembling values which resulted in the unfair price of $21.68 offered to Plaintiffs. However, the issue of Sheridan's, or the other Defendants', knowing participation need not be reached, as the Plaintiffs have not demonstrated that they were damaged by the Board's breaching its fiduciary duties. They are therefore not entitled to an award under this theory.

G. *Should a Receiver Be Appointed to Manage ARG?*

Plaintiffs also seek the extraordinary remedy of a receiver for ARG. As the Court explained at an earlier stage of this proceeding "a court may utilize its equitable powers to appoint a receiver only 'when fraud and gross mismanagement by corporate officers, causing real imminent danger of great loss, clearly appears, and cannot be otherwise prevented.'"[287] Plaintiffs have not demonstrated that

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[286] *Feeley v. NHAOCG, LLC*, 62 A.3d 649, 658 (Del. Ch. 2012) (citation omitted).

[287] *Ross Hldg. & Mgmt. Co. v. Advance Realty Gp., LLC*, 2010 WL 3448227, at *6 (Del. Ch. Sept. 2, 2010) (quoting *Drob v. Nat'l Mem'l Park*, 41 A.2d 589, 597 (Del. Ch. 1945)).

fraud occurred. They have demonstrated their unfair treatment as a result of the poor process employed by ARG's Board in preparing for the Reorganization. However, they have not demonstrated that they are in real imminent danger of great loss. Their units are without value and no additional harm has been cited by Plaintiffs. Thus, the Court cannot grant the extraordinary remedy they request.

H. *Did Senkevitch and Sopko Violate the Corporate Opportunity Doctrine?*

Defendants claim that Senkevitch and Sopko, by hiding the term sheet for the 445 Southgate joint venture which they received in December 2006, breached their fiduciary duties to ARG and stole a corporate opportunity. They argue Defendants were motivated by their desire to consummate a deal with JER which would allow them to control ARG. The corporate opportunity doctrine requires that a corporate officer or director "not take a business opportunity for his own if: (1) the corporation is financially able to exploit the opportunity; (2) the opportunity is within the corporation's line of business; (3) the corporation has an interest or expectancy in the opportunity; and (4) by taking the opportunity for his own, the corporate fiduciary will thereby be placed in a position inimicable to his duties to the corporation."[288]

[288] *Broz v. Cellular Info. Sys., Inc.*, 673 A.2d 148, 155 (Del. 1996).

Defendants' theory cannot succeed because Senkevitch and Sopko did not take an opportunity for themselves. Moreover, although they received the term sheet six months before its existence was revealed to the Board, there is evidence in the record that the prospect of entering into a joint venture for 445 Southgate was discussed and rejected at the December Board meeting.[289] Thus, the simple explanation could be that Senkevitch and Sopko concluded that the joint venture need not be discussed when the Board had concluded that month that it did not wish to seek out such an opportunity. Either way, Defendants have not demonstrated that they took an opportunity from ARG which could support the breach of fiduciary duty claim.[290]

III. CONCLUSION

For the reasons set forth above, Plaintiffs appear to have nominally benefited from the Reorganization. However, the process employed by ARG's Board was so deficient that the Defendants could not carry their burden to demonstrate that the Reorganization was entirely fair. At this point, no damages remedy is suitable because of Plaintiffs' nominal benefit from the conversion. The parties are invited to address, first, whether Plaintiffs were harmed by the Board's layering of FARS's and ARD's loans on top of their units and, second, the question of

[289] See supra note 72.

[290] Defendants appear to have abandoned the other arguments in their pre-trial brief; however, to the extent they did not, they have not established damages based on the alleged bad faith actions of Plaintiffs.

attorneys' fees and expenses. Plaintiffs have abandoned many of their other claims and, nonetheless, there is no basis for concluding that they were damaged by the Reorganization. Likewise, Defendants have not shown that Plaintiffs usurped any corporate opportunity.

Counsel are requested to confer and to submit an implementing form of order.