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March 2, 2010

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Re: Cline v. Grelock, et al.
C.A. No. 4046-VCN
Date Submitted: November 4, 2009

Dear Counsel:

This post-trial letter opinion addresses the short life of an ill-fated recovery and towing service, known as American Asset Recovery, LLC ("AAR"), a Delaware limited liability company. The business, which provided services in Pennsylvania, Maryland, and Delaware, began in October 2007.[1] Two life-long friends, Defendant Ryan Grelock and Plaintiff Jeremy Cline, were co-owners but their respective ownership percentages are in dispute. By May 20, 2008, after accumulating debt and with lackluster business prospects, Grelock, without

[1] JX 1.

participation by Cline, had dissolved AAR.[2] Afterwards, Grelock and his wife, Defendant Crystal Grelock ("Crystal"), established Hound Dog Recovery, LLC ("Hound Dog"), which provides similar services. Cline has no interest in Hound Dog.

In January 2008, AAR purchased a motor vehicle with the help of a loan from Sovereign Bank.[3] Both Grelock and Cline guaranteed the obligation;[4] the vehicle is now used by Hound Dog in its business, but Cline remains a guarantor.

AAR had done business as Hound Dog Recovery. Thus, the Grelocks have used the business name, together with a similar logo, of AAR in their new venture; in addition to the vehicle purchased with the Sovereign Bank loan, they have also used the client list of AAR, but only for three customers.

AAR was an unsuccessful venture. Perhaps it simply did not exist long enough to become a thriving business. Its debts were substantial in relation to its income; it did not dependably operate at a profit. By April 2008, the relationship between the Grelocks and Cline had deteriorated to the point where continuing the

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[2] JX 4.
[3] JX 5.
[4] JX 6; JX 7.

business was not likely to be practicable. There were disagreements—some business-related and some personal, especially those between Cline and Crystal.[5]

Other areas of tension were also described at trial. After a few months, Crystal was paid $300 per week to "do the books" and "answer the phone." The office, such as it was, was in the Grelocks' home. Cline objected to the payments to Crystal; the funds paid to her, however, were not unreasonable for the work she performed; the problem was that she started receiving payments without Cline's knowledge. Another example involves the payment of salaries. Grelock and Cline were each to be paid $750 per week. Cline insisted that he be paid every week to meet his personal financial obligations. Grelock, because of the business's cash flow, sometimes delayed his own weekly salary. Thus, Cline observed checks payable to Grelock for $3,000 and complained. It seems, more likely than not, that any payment for $3,000 was simply for four weeks of salary that Grelock had not otherwise received.

[5] Cline concedes that he made some statements to Crystal (or in her presence) that should not have been made. There is no need to reprise them here.

The problems here started where they frequently start in matters such as this one: at the beginning. Grelock enlisted the services of an accountant, Ralph Estep, who met with them, gave them a standard form limited liability company operating agreement,[6] but never saw to the signing of the agreement or the tailoring of it to their specific needs.

There is an agreement drafted by Grelock which sets forth many of the terms that one would expect to see in a document memorializing the status of a new business.[7] Cline, however, denies that he signed it. Moreover, Grelock retained a handwriting expert who could only opine that there is a "strong probability" that the signature on the document purporting to be their agreement was that of Cline. The evidence before the Court simply does not allow a conclusion, found by a preponderance of the evidence, as to whether the agreement bears Cline's signature.[8] The agreement calls for Cline to make a capital contribution of $25,000. Cline never contributed any capital to the business. His only financial

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[6] JX 3.
[7] JX 21.
[8] In light of the Court's conclusions in this matter, whether the agreement is enforceable is of relatively little importance. It is an unfortunate aspect of this case that it is marked by several failures of proof.

material assistance was the signing of the guaranty for the loan used to purchase the vehicle. Yet, without having contributed any capital (despite Grelock's relatively significant contributions), and without conceding any ongoing obligation to "true-up" his capital account, Cline insists that he be treated as the owner of a one-half interest in the venture.

There is evidence supporting the inference that Cline was to be an equal partner. AAR's tax return reflects that ownership arrangement.[9] Nonetheless, it is unreasonable for Cline to claim that he is a fifty percent owner while at the same time denying that he had or has any capital obligation. Even if Cline did not sign the agreement, the Court accepts Grelock's testimony that Cline was expected to contribute $25,000 as part of the price of his entry into the business.

After the business relationship had deteriorated to the point that Cline was effectively excluded, Grelock dissolved AAR and established Hound Dog. He did not have the authority to dissolve AAR unilaterally, without Cline's participation. That conduct constituted a breach of his fiduciary duty because Cline was treated and considered a member of AAR—indeed, the parties dispute only the scope of

[9] JX 8.

Grelock's interest. The harm stemming from Grelock's conduct, however, is entirely speculative.[10] Nothing more of positive value was likely to come from AAR. In short, Cline has neither been able to prove any damages from the ministerial act of dissolving AAR, nor has he demonstrated a reasonable basis for assessing such damages, assuming any were incurred.[11]

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[10] Cline has not sought to share in any profits of AAR from the time he was ousted until the time of its dissolution or, for that matter, until the present.

[11] *See LaPoint v. AmerisourceBergen Corp.*, 2007 WL 2565709, at *9 (Del. Ch. Sept. 4, 2007) ("To be entitled to compensatory damages, plaintiffs must show that the injuries suffered are not speculative or uncertain, and that the Court may make a reasonable estimate as to the amount of damages.") (citing *Cincinnati Bell Cellular Sys. Co. v. Ameritech Mobile Phone Serv. of Cincinnati, Inc.*, 1996 WL 506906, at *20 (Del. Ch. Sept. 3, 1996)). Ordinarily, one would expect that a self-interested breach of fiduciary duty along the lines of Grelock's conduct would have had consequences that should be remedied by damages. In this instance, although Grelock breached his fiduciary duty, the Court has not been provided any basis for a rational award of damages.

Cline offered no fair value of AAR or any reasonable basis for calculating a value of AAR at the time of dissolution. If AAR had a positive fair value at the time of dissolution, then some percentage of that value should accrue to Cline's benefit. Without expert opinion, the Court is reluctant to engage in its own analysis of the financial records of AAR. Without going into any detail, AAR's failure to achieve profitability, the absence of any data showing the growth of the business, and the high debt burden carried by AAR all cut against a finding that AAR at any time in its existence had any positive value.

Of course, as a start-up, it is not unusual that AAR had little, or no, market value at the time of its dissolution. That does not mean that the entity was worthless—and there was at least the possibility of better times which might have benefited both Cline and Grelock. Just because AAR did not achieve profitability does not lead to the conclusion that no compensation would be appropriate. Nonetheless, whatever value that Cline might find in AAR on a going forward basis would be over-ridden by his failure to contribute to the capital of the venture. Had Grelock liquidated AAR to pay creditors after it was dissolved as a matter of public record, there is no reason to believe that anything would have been left over for either Cline or Grelock.

Grelock not only dissolved AAR, but he and Crystal also established a new and similar business, Hound Dog. Some of the assets of AAR have ended up benefiting Hound Dog. Those assets are the vehicle, which was acquired with the Sovereign Bank loan, a similar logo, and a customer list that now provides three customers for Hound Dog. Presumably, the value of these assets should accrue to the benefit of the AAR stakeholders. Cline, again, has offered no proof as to the value of any of these assets. The vehicle is heavily liened and, most likely, has little or no value in excess of the lien. It is not apparent that the logo has any particular value. There is no good evidence to determine how much work (or the income derived from the work) Hound Dog performs for the three former customers of AAR. In short, the Court cannot fairly put a value on those items. At most, it appears that their net value would be nominal.

Perhaps recognizing that his proof of damages is wanting, Cline cites to *Cropper v. Irons*[12] and argues that as a wrongfully-excluded co-owner of the AAR venture, the assets of which are now benefiting Hound Dog, he is entitled to an

[12] 1993 WL 179334 (Del. Ch. May 24, 1993).

equity interest in Hound Dog.[13] Although it may not be accurate to say that Hound Dog has prospered since its inception, it has been able to add both vehicles and employees and is surviving. Cline is correct that a former partner (or member of a limited liability company) may be held accountable for profits earned using partnership assets. He has also correctly noted that Hound Dog has used AAR's assets without an appropriate dissolution process or any payment by Hound Dog for the benefit of AAR or its members. He has not demonstrated, however, what that interest should be or how the Court should calculate it. Moreover, he has not persuaded the Court that someone who fails to make any capital contribution should be able to claim an equity interest in a successor company for which he has still not offered to contribute any capital.

In sum, Cline, who never made any capital contribution to AAR, has shown no basis in law or in equity as to why he is entitled now to an interest in Hound Dog. Either his failure to make a capital contribution precludes him from asserting an equity interest or, as the Court deems the more appropriate analysis, the amount

[13] Pre-Trial Stip. ¶ 4(a). In *Cropper*, the Court recognized "authority for the proposition that a partner is accountable to former partners for profits earned using partnership assets." 1993 WL 179334, at *3.

of capital which he would reasonably have been required to contribute, but did not, far exceeds any value fairly attributed to AAR, including those assets which are now used for Hound Dog's benefit. In short, although Grelock's conduct cannot be condoned, Cline has not proved that he was harmed (or, if harmed, what his compensation should be).[14]

Grelock asserts a counterclaim seeking to have the Court compel Cline to pay his capital contribution for the benefit of AAR, presumably for Grelock's benefit. Grelock's wrongful conduct in dissolving AAR precludes such a claim under these circumstances. Grelock excluded Cline and deprived him of whatever benefit, however marginal, might have resulted from a continuation of the business. In brief, with his improper termination of AAR, he has lost any legitimate basis for insisting that Cline make any contribution after the fact. In a sense, it all nets out.

One final item remains and that is the guaranty to Sovereign Bank as signed by Cline. Cline receives no benefit from that loan; the vehicle now used is entirely

[14] A plaintiff need not prove damages with precision as difficulty of proof does not equate with no relief. *See LaPoint*, 2007 WL 2565709, at *9. Nonetheless, some reasoned approach must be supplied to enable the Court to determine what damages, if any, would be fair and appropriate. *See supra* note 11.

for Hound Dog's benefit and, thus, the benefit of Grelock and Crystal. Accordingly, Grelock and Crystal shall exercise all good faith efforts to obtain Cline's release from the Sovereign Bank guaranty. Failing that, each shall individually indemnify and hold Cline harmless from any claim of whatever nature arising out of the guaranty and the associated vehicle purchase loan, including any attorneys' fees, that he may reasonably incur in enforcing this indemnity obligation.

Because of Grelock's breach of his fiduciary duties, the costs of this action are assessed against him.

IT IS SO ORDERED.

Very truly yours,

/s/ John W. Noble

JWN/cap
cc: Register in Chancery-K