COURT OF CHANCERY
OF THE
STATE OF DELAWARE

LEO E. STRINE, JR.
CHANCELLOR

New Castle County Courthouse
500 N. King Street, Suite 11400
Wilmington, Delaware 19801-3734

Date Submitted: September 16, 2011
Date Decided: November 10, 2011

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RE: *Robert Y. Garrett IV and Diana B. Garrett v. Zon Capital Partners, L.P., et al.*
Civil Action No. 5607-CS

Dear Counsel:

The named plaintiffs in this purported class action, Robert Garrett and Diana Garrett, are former Limited Partners in defendant Zon Capital Partners, L.P. ("Zon LP"). They filed a four-count class action complaint in this court on June 29, 2010, alleging breach of fiduciary duties (Count I), breach of contract (Count II), negligent misrepresentation (Count III), and unjust enrichment (Count IV) against Zon LP's former "General Partner," Zon Capital Partners, G.P., L.L.C., a Delaware limited liability company, and its three principals, William D. Bridgers, E. Michael Forgash, Jr., and H. Donald Perkins, Jr. The complaint focuses on an allegedly self-interested "Conversion," approved by a majority of the former Limited Partners, through which Zon LP was converted into the defendant Delaware limited liability company, Zon Capital Partners, L.L.C. ("Zon LLC"), thereby supplanting Zon LP's original limited partnership

agreement (the "Partnership Agreement") with a new, and different, limited liability company agreement (the "LLC Agreement"). On February 14, 2011, the court dismissed Counts III and IV, but allowed Counts I and II to proceed.

On April 20, 2011, the named plaintiffs moved under Court of Chancery Rule 23 to have this court certify the class comprised of:

> [a]ll individuals and entities participating as Class B members in [Zon LLC] as of November 23, 2009, excluding, however, the Zon Defendants or the heirs, assigns, or successors-in-interest of any of the Zon Defendants and further excluding any individual or entity participating as a Class D member of Zon LLC.[1]

The court waited to issue a decision on the plaintiffs' motion in deference to the parties' attempt to reach a settlement, but the court was notified on September 16, 2011 that the parties' settlement efforts have failed. The plaintiffs thus requested that the court proceed with the disposition of their motion.[2]

Before the Conversion, and because the General Partner had contributed no capital, the General Partner could not receive any distributions until the former Limited Partners received distributions in an amount equal to their Adjusted Capital Contribution as defined by the Partnership Agreement.[3] As a result of the Conversion, however, the LLC Agreement allegedly altered the distribution hierarchy drastically, enabling the

[1] Pl. Op. Br. at 1. The complaint defines the "Zon Defendants" to mean: the defendants Zon LP, Zon LLC, the General Partner, Bridgers, Forgash, and Perkins. Compl. ¶ 13.
[2] Pl. Letter to the Court (September 16, 2011).
[3] Compl. ¶ 19.

General Partner to receive distributions that it would not have received under the original Partnership Agreement.

Zon LLC has four classes of Members: A, B, C, and D. Class B includes the former Limited Partners of Zon LP (which, according to the plaintiffs' original proposed class definition, would include the 39 former Limited Partners who own approximately 66% of the Class B Member interests), as well as the BlackRock entities (approximately 31%) and affiliates of the defendants Bridgers, Forgash, and Perkins (about 2.55%).[4] In addition to converting their limited partnership interests into Class B Membership interests, the Conversion permitted former Limited Partners of Zon LP to participate alongside the major investor with whom the Conversion was negotiated, Paul Capital, in making additional capital contributions for Class A Membership interests in Zon LLC. Ten of the 39 Limited Partners opted to take advantage of this investment opportunity, so those 10 Limited Partners are both Class A and Class B Members of Zon LLC. Class C is the General Partner's "Carried Interest." Along with their answering brief, the defendants informed the court and the plaintiffs by letter that 6 of the 39 Class B Members are also Class C Members, a fact that was erroneously misstated at the February 2011 oral argument.[5] Since learning of the 6 former Limited Partners who have side agreements to share in the General Partner's Carried Interest (i.e., they have both Class B and Class C Membership interests), the plaintiffs do not object to the exclusion

[4] Pl. Op. Br. at 1; Perkins Aff. ¶¶ 6-11.
[5] Def. Letter to the Court (May 27, 2011).

of those 6 Limited Partners from the proposed class. Indeed, exclusion is "admittedly require[d]"[6] because the Class C Members' interests conflict with the interests of the members of Class B.

I.

Class certification under Rule 23 involves a two-step analysis,[7] and the plaintiff seeking certification bears the burden of establishing that each step is satisfied in accordance with the Rule.[8]

The first step requires satisfaction of Court of Chancery Rule 23(a), which requires the party seeking class certification to demonstrate that: (1) "the class is so numerous that joinder of all members is impracticable;" (2) "there are questions of law or fact common to the class;" (3) "the claims or defenses of the representative parties are typical of the claims or defenses of the class;" and (4) "the representative parties will fairly and adequately protect the interests of the class."[9]

If the proponent of class certification is able to establish the four elements under Rule 23(a), the second step of the class certification analysis requires a demonstration that the class is maintainable as a class action under at least one of the three recognized "prerequisites" contained in Rule 23(b)(1) through (3). The plaintiffs in this case claim

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[6] Pl. Reply Br. at 3.
[7] *Leon N. Weiner & Assocs., Inc. v. Krapf*, 584 A.2d 1220, 1224 (Del. 1991).
[8] *Oliver v. Boston Univ.*, 2002 WL 385553, at *4 (Del. Ch. Feb. 28, 2002) (citing *Dieter v. Prime Computer, Inc.*, 681 A.2d 1068, 1071 (Del. Ch. 1996)).
[9] Ct. Ch. R. 23(a); *see also Barbieri v. Swing-N-Slide Corp.*, 1996 WL 255907, at *3 (Del. Ch. May 7, 1996).

to satisfy Rule 23(b)(1)(B) because "[t]he prosecution of separate actions by or against individual members of the class would create a risk of . . . [a]djudications with respect to individual members of the class which would as a practical matter be dispositive of the interests of the other members not parties to the adjudications or substantially impair or impede their ability to protect their interests,"[10] as well as Rule 23(b)(3) because "questions of law or fact common to the members of the class predominate over any questions affecting only individual members, and . . . a class action is superior to other available methods for the fair and efficient adjudication of the controversy . . . ."[11]

II.

The motion for class certification is in large part uncontested by the defendants. In fact, the defendants go so far in their "response" brief as to say that they "agree that Plaintiffs have satisfied the liberal standard for class certification under [Court of Chancery] Rule 23."[12]

Because the plaintiffs, after being informed about the existence of the 6 Class B Members who, by way of separate agreements with the General Partner, are also Class C Members, agreed to eliminate those 6 former Limited Partners from the proposed class, there is only one point of contention raised by the defendants that I need to address. That

[10] Ct. Ch. R. 23(b)(1)(B).
[11] Ct. Ch. R. 23(b)(3).
[12] Def. Ans. Br. at 1.

is, the defendants object to the inclusion of the 10 Class B Members who also made investments as Class A Members alongside Paul Capital.

The defendants argue, on the basis of the named plaintiffs' deposition transcripts, that the Class B Members who are also Class A Members "potentially have different economic interests than those who are only Class B Members."[13] The defendants do not offer concrete arguments as to why a Class B Member who is also a Class A Member faces a conflict of interest by being a part of the class, but instead posit that "the issue of whether these ten overlapping Class A/B Members should be included in the Class can most prudently be determined after counsel for the parties engage in early settlement negotiations," cautioning that "[i]f the parties cannot reach agreement . . ., it is questionable whether it is appropriate to include the ten combined Class A and B Members in a Class for which Mr. and Mrs. Garrett would serve as the only class representatives."[14]

The defendants' argument is unconvincing. That the parties have failed to reach a settlement in this matter has no bearing on whether it is proper to include the 10 Class A/B Members in the proposed class. An examination of the class action complaint and the remedy it seeks shows that a Class A/B Member will enjoy any recovery along with the Class B-only Members. The complaint alleges that the defendants breached their fiduciary duties by securing the approval of the Conversion, which the plaintiffs allege

[13] *Id.* at 3.
[14] *Id.*

wrongfully has the effect of accelerating distributions to the General Partner at the expense of the former Limited Partners, who are now Class B Members in Zon LLC. In other words, as the plaintiffs argue, "[t]he claims asserted in the Complaint are directed to rectifying the harm caused by Defendants to Class B limited partners *qua* Class B limited partners,"[15] and the class complaint is aimed at making the Class B Members (the former Limited Partners) whole for the defendants' alleged breach of "their fiduciary duties . . . by effectuating a self-dealing [Conversion] that enhanced their own financial positions within the [Zon LP] Partnership at the expense of the financial interests in the Partnership" held by the plaintiffs and the class they seek to represent.[16] Finally, the fact that at some "Tiers," the Class A/B Members receive distributions under the LLC Agreement either as Class A Members or as both Class A and Class B Members does not change the fact that if the class action is successful, the Class A/B Members, like the Class B Members who are only Class B Members, will receive a remedy of repayment to Zon LLC of the amounts the defendants received as a result of the alleged self-dealing Conversion or a reconfiguring of the capital structure to reflect the Class B Members' distribution priority over the General Partner.[17] That the Class A/B Members hold a

[15] Pl. Reply Br. at 3.
[16] Compl. ¶ 72.
[17] The complaint primarily seeks relief in the form of "[r]equiring defendants to compensate Plaintiffs and the Class for all losses and damages Plaintiffs and the Class members have sustained as a result of the wrongs alleged, and establishing a constructive trust for the benefit of Plaintiffs and the Class with respect to all losses and damages caused by defendants' wrongful self-dealing." *Id.* at 26.

Class A Membership interest does not change that reality, and nothing the class action complaint seeks to accomplish would negatively affect Class A Members as Class A Members. That fact is confirmed by looking at the distribution scheme contemplated by the LLC Agreement:[18]

Cash Flow Allocation by Tiers

			Class C — Total "GP Portion"					
	Class A LPs	**Class B LPs**	**Manager**	**To Founding LPs**	**To Class B LPs**	**Total Class B**	**Class D**	**Total**
Tier I	100.0%	0	0	0	0	0	0	100.0%
Tier II	80.0%	7.5%	7.5%	2.5%	0.0%	7.5%	2.5%	100.0%
Tier III	66.0%	17.0%	9.0%	2.5%	3.0%	20.0%	2.5%	100.0%
Tier IV	55.0%	24.0%	10.0%	2.5%	6.0%	30.0%	2.5%	100.0%

As can be seen, although the Class A Members receive distributions before the Class B Members begin to share in the distributions, a successful prosecution of the class action would only have the effect of requiring the General Partner to repay distributions it allegedly wrongfully accelerated to itself (as a Class C Member) or to the BlackRock entities under the terms of the LLC Agreement and distribution scheme above and would not have any adverse effect on the Class A Members. The defendants offer a hypothetical argument that certain Class A/B members might oppose this action because they want to provide the benefits at issue to the General Partner as an instrumental means

[18] *Id.* Ex. 9.

of encouraging the General Partner to continue its service as manager of Zon LLC[19] – benefits that are supposedly vital in their (unidentified) minds.[20] Of course, if this argument is true, these particular class members can renounce their share of any recovery, or transfer some of their own units or their share of any award received to the General Partner in order to convince it to stay.

III.

For the foregoing reasons, subject to the modifications made by the plaintiffs during the course of their briefing, the motion to certify the class is GRANTED. Counsel shall meet and confer and submit within one week an implementing order consistent with my ruling today.

Very truly yours,

/s/ Leo E. Strine, Jr.

Chancellor

LESJr/eb

[19] I note that the objective reality alleged is that, to date, the General Partner's investment performance has resulted in indisputably poor results for the investors. *See id.* ¶¶ 6, 38.
[20] Def. Ans. Br. at 3.