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Abstract

After the 2008 recession, it is difficult to imagine that the public is investing billions of dollars in publicly traded entities with little regulation of board conflicts and no fiduciary duty protections. Yet, that is precisely the case for more than $284 billion of investments. Investors have flocked to publicly traded limited partnerships (LPs) and limited liability companies (LLCs), collectively known as master limited partnerships (MLPs), because many are high-performing energy companies with a tax preference. MLP market capitalization, while only $14 billion in 2000, topped $284 billion as of February 2016, and more initial public offerings are on the horizon. Dazzled by the possibility of high yields, individual investors are likely unaware that they do not enjoy the same fiduciary duty protections that apply to stockholders of publicly traded corporations.

Delaware corporate law offers significant investor protections largely flowing from an unwaivable duty of loyalty. In contrast, Delaware's alternative entity scheme permits the waiver of all fiduciary duties in LP and LLC agreements. Publicly traded LPs are also exempt from listing rules that normally require independent board members. Even where special committees vet conflicted transactions, committee members may have affiliations with the MLP's corporate sponsor and owe conflicting duties to the sponsor and the limited partners.

Scholars suggest that "uncorporate" substitutes could theoretically mitigate the absence of fiduciary duties, but empirical research shows that publicly traded MLPs rarely adopt such substitutes. The realities of the MLP marketplace leave investors with only the implied covenant of good faith and fair dealing, which is not a substitute for traditional fiduciary duties.

This Article exposes the many obstacles investors have faced in obtaining remedies under MLP agreements. It argues that contractarian

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theories or legal diversification constructs do not justify the under-regulation of publicly traded MLPs. This Article recommends reinstating the duty of loyalty for MLPs and ending the LP exception from board independence requirements.

INTRODUCTION

"There are many novice investors in MLPs that don't really know what they are, what they do, or what the long-term story is. They're just in it for the yield, or following the 'hot dot' of excellent performance for the past decade."[1]

Many people invest in publicly traded entities thinking that all such entities offer the same board oversight and fiduciary protections to their investment. But, for a growing, multibillion dollar investment area, that is simply not so. These investment vehicles, known as master limited partnerships (MLPs),[2] have grown tremendously: from $14 billion in 2000 to $284 billion as of February 2016.[3] Some estimate that roughly 75% of MLP investors are individuals, the vast majority of whom are over the age of fifty.[4] MLPs attract many of these individuals with their

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1. Tom Laurciella, *MLPs Have Been Getting Crushed. Blame the Newbies?*, WALL ST. J.: MONEY BEAT (Oct. 15, 2014, 7:37 AM), http://blogs.wsj.com/moneybeat/2014/10/15/mlps-have-been-getting-crushed-blame-the-newbies/ (quoting MLP specialist Miller Howard).

2. MLP is the collective term for publicly-traded limited partnerships (LPs) and limited liability companies (LLCs).

3. *MLP Asset Class Overview*, YORKVILLE CAPITAL MGMT., http://www.yorkvillecapital.com/asset-class-overview.aspx (last visited Feb. 8, 2016) ("Since 2000, MLPs have grown in market capitalization from $14 billion to $284 billion today, representing a compounded annual growth rate (CAGR) of 25.9%. Similarly, the number of MLPs has increased from 27 to 127 over the same timeframe, a net increase of 6.6 MLPs per year. In 2014, 18 new MLPs held their initial public offering."). MLP is the collective term used for publicly traded limited partnerships (LPs) and limited liability companies (LLCs). *See id.*

4. *See, e.g.*, NAT'L ASS'N OF PUBLICLY TRADED P'SHIPS, WRITTEN STATEMENT OF THE NATIONAL ASSOCIATION OF PUBLICLY TRADED PARTNERSHIPS SUBMITTED TO THE SENATE COMMITTEE ON FINANCE TAX REFORM WORKING GROUP ON COMMUNITY DEVELOPMENT & INFRASTRUCTURE (2015), http://www.finance.senate.gov/legislation/download/?id=a9191f81-b109-4543-a342-6d0f7ba6f379 [hereinafter NAPTP, WRITTEN STATEMENT]; *Fact Sheet: Publicly Traded Partnerships (PTPs)*, AM. FUEL & PETROCHEMICALS MFRS.,

flashy yields in an otherwise low-yield market.[5] While these investors can easily compare returns and understand MLPs energy-based lines of businesses, many investors are unaware of the actual nature of their investments.[6] They do not appreciate that an investment in a publicly traded energy corporation is very different from an investment in a publicly traded energy MLP. When these investors do consider risk, they may not comprehend that conflicted transactions and inadequate managerial oversight may permissibly occur in an MLP.[7] Dazzled by the promise of high yields, direct or indirect investors in MLPs may also discount regulatory risks clearly disclosed in a prospectus.[8]

As with much of corporate law, Delaware is a key regulator of MLPs,[9] and so this Article compares Delaware's treatment of MLPs to its treatment of other publicly traded entities. In short, Delaware MLPs, which include limited partnerships (LPs) and limited liability companies (LLCs), have comparatively few mandatory provisions to protect

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http://www.afpm.org/WorkArea/DownloadAsset.aspx?id=3877 (last visited Feb. 8, 2016) (login required) ("Recent surveys show that up to 80% of MLP investors are individuals, with roughly 75% over the age of 50.").

5. Murray Coleman, *How Much Longer Can MLPs Remain Attractive?*, WALL ST. J.: MONEY BEAT (Jan. 14, 2014, 5:05 PM), http://blogs.wsj.com/moneybeat/2014/01/14/how-much-longer-can-mlps-remain-attractive/ ("The widely followed Alerian MLP Index has produced an average annual return of about 15% in the past 10 years, through last week. At the same time, the benchmark has generated distribution growth of almost 8% a year.").

6. *See* Telis Demos, *Mom and Pop Want Yield from Their IPOs, Too*, WALL ST. J.: MONEY BEAT (July 22, 2014, 2:11 PM), http://blogs.wsj.com/moneybeat/2014/07/22/mom-and-pop-want-yield-from-their-ipos-too/ ("But bankers and brokers say that more often, what retail investors really want are dividend-payers. Those include real-estate investment trusts, master limited partnerships and business development corporations. Mom and pop may not always understand what 'REIT' means, but they know they want to get better than the zero-point-nothing that they are getting from a savings account.").

7. *See infra* Part II.

8. *See, e.g.*, *ClearBridge Energy MLP Total Return Fund Inc.*, SEC. EXCH. COMM'N, http://www.sec.gov/Archives/edgar/data/1547341/000119312512285786/d334622d497.htm (last visited Feb. 8, 2016) ("Certain environmental statutes . . . and analogous state laws and regulations, impose strict, joint and several liability for costs required to clean up and restore sites where hazardous substances have been disposed of or otherwise released. . . . There is an inherent risk that MLPs may incur environmental costs and liabilities due to the nature of their businesses and the substances they handle. For example, an accidental release from wells or gathering pipelines could subject them to substantial liabilities for environmental cleanup and restoration costs, claims made by neighboring landowners and other third parties for personal injury and property damage, and fines or penalties for related violations of environmental laws or regulations.").

9. *See* Mohsen Manesh, *Contractual Freedom Under Delaware Alternative Entity Law: Evidence from Publicly Traded LPs and LLCs*, 37 IOWA J. CORP. L. 555, 567, 575 (2012) (identifying "85 publicly traded Delaware LLCs and LPs in existence as of June 2011").

investors under Delaware alternative business entity law.[10] Delaware law provides corporate investors considerable protections, many of which flow from an unwaivable duty of loyalty.[11] In recent years, board independence requirements, constraints on independent conflicts committee members, and duty of loyalty jurisprudence and literature that provides important socializing cues have strengthened corporate stockholder protections.[12] In contrast, investor protections for publicly traded LPs and LLCs have abated, primarily because Delaware permits the waiver of all fiduciary duties in LP and LLC agreements.[13] Exemptions from independence requirements under SEC listing rules, compromised membership on conflicts committees, express contractual standards that tend to be highly protective of management, and a covenant of good faith and fair dealing that is an inappropriate substitute for fiduciary duties further diminish MLP investor protection.[14]

Alternative entity literature has justified fiduciary duty waivers under contractarian and other theories.[15] Contractarians such as Professor Larry E. Ribstein have theorized that the market will provide substitute "uncorporate" mechanisms to discipline management in lieu of fiduciary duties.[16] Empirical research has shown, however, that publicly traded MLPs have, by and large, not adopted substitute mechanisms.[17] This Article argues that contractarian or legal diversification theories do not justify the under-regulation of publicly traded alternative business entities.[18] Furthermore, although subject to some dispute, some finance

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10. *See Facts & Answers About Publicly Traded Partnerships*, NAT'L ASS'N OF PUBLICLY TRADED P'SHIPS, https://web.archive.org/web/20150711081207/http://www.naptp.org/PTP101/FAQs.htm (last visited Feb. 8, 2016) [hereinafter *Facts About PTPs*] (contrasting MLPs and PTPs). Publicly traded LLCs are often categorized as either MLPs or PTPs because of their similar pass-through tax treatment. *See id.*

11. *See infra* Subsection II.A.3.

12. *See infra* Section II.A.

13. *See* DEL. CODE ANN. tit. 6 § 17-1101(d) (2015) ("[T]he partner's or other person's duties may be expanded or restricted or eliminated by provisions in the partnership agreement; provided that the partnership agreement may not eliminate the implied contractual covenant of good faith and fair dealing."); *id.* § 18-1101(c) ("[T]he member's or manager's or other person's duties may be expanded or restricted or eliminated by provisions in the limited liability company agreement; provided, that the limited liability company agreement may not eliminate the implied contractual covenant of good faith and fair dealing.").

14. *See infra* Part II.

15. *See infra* Section III.B.

16. *See, e.g.*, Larry E. Ribstein, *The Uncorporation and Corporate Indeterminacy*, 2009 U. ILL. L. REV. 131, 142–43.

17. *See, e.g.*, Manesh*, supra* note 9, at 567–80 (studying numerous publicly traded LPs and LLCs, and noting that "[o]nly 10 of the 85 firms . . . d[id] not fully waive or exculpate liability arising from the breach of fiduciary duties").

18. *See infra* Section III.B.

literature shows a positive relationship between independent monitoring and various measures of firm performance.[19] Extension of this literature supports the inclusion of fiduciary duties rather than their waiver.

The rest of this Article proceeds as follows: Part I focuses on the growth of MLPs in the energy industry, the structure of these entities, and their important role in the economy. Part II turns to Delaware law governing corporations and compares it to Delaware alternative entity law, to which MLPs are subject. Part II also discusses the obstacles preventing MLP investors from obtaining judicial remedies for inadequate oversight and conflicted transactions. Finally, Part III examines policy reasons for requiring fiduciary duties for publicly traded MLPs.

I. MLPS AND THE OIL AND GAS INDUSTRY

An MLP is a type of publicly traded entity that is taxed as a partnership.[20] It may be structured as an LP or as an LLC, but the term MLP refers to either form.[21] Much of the interest and investment in these entities can be attributed to their tax-preferred treatment and governance attributes.[22] The oil industry has long sought to reduce tax and regulatory costs, and has been highly successful in the alternative business entity arena.[23] MLPs have become an attractive investment due to the combined characteristics of favorable taxation and liquidity offered by a publicly traded market.[24]

A. *MLP Structure*

An MLP is most often structured as an LP under Delaware law.[25] The

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19. *See infra* Section III.D.

20. *Facts About PTPs*, *supra* note 10.

21. Manesh, *supra* note 9, at 557.

22. *See Facts About PTPs*, *supra* note 10.

23. *See, e.g.*, Sandra K. Miller, *What Standards of Conduct Should Apply to Members and Managers of Limited Liability Companies?*, 68 ST. JOHN'S L. REV. 21, 23 n.3 (1994) (observing that the movement toward LLCs began in Alaska when a Texas oil company sought to obtain favorable tax status for its Alaskan operations); Joseph A. Rodriguez, Comment, *Wyoming Limited Liability Companies: Limited Liability and Taxation Concerns in Other Jurisdictions*, 27 LAND & WATER L. REV. 539, 544–45 (1992).

24. JOSH FREED & MAE STEVENS, THIRD WAY: THE CLEAN ENERGY PROGRAM, A SMALL TAX CHANGE, BIG CLEAN ENERGY RESULTS 4 (2011), http://content.thirdway.org/publications/475/Third_Way_Idea_Brief__A_Small_Tax_Change_Big_Clean_Energy_Results.pdf (noting the liquidity, low cost capital, performance, and investment suitability of MLPs).

25. TIM FENN, MASTER LIMITED PARTNERSHIPS (MLPS): A GENERAL PRIMER 1 (2012), https://www.lw.com/admin/Upload/Documents/MLP/Resources/Latham%20Master%20Limited%20Partnerships%20Primer.pdf; *see also* ANDREW BRETT & TIM BRUCE, NEPC, INVESTING IN MASTER LIMITED PARTNERSHIPS: RISKS AND OPPORTUNITIES 1 (2012), http://www.nepc.com/writa

ownership is in the form of a general partner (GP) interest and limited partner interests, referred to as units.[26] The units are publicly traded.[27] In many MLPs, the GP's interest is a small equity stake, usually two percent or less.[28] An MLP GP's small equity stake masks significant, if not total, governance control of the MLP.[29] Thus, in an MLP, equity interest and control are wholly divorced: the limited partners hold the vast majority of the equity, but the GP typically holds control.[30]

MLP structure has become more sophisticated over the last decade,[31] but the primary MLP model continues to use a controlled (or sponsored) GP.[32] Under the sponsored model, the sponsor is commonly, although not exclusively, a publicly traded corporation subject to U.S. Securities and Exchange Commission (SEC) requirements.[33] The sponsor corporation creates an affiliate with few substantial assets, which in turn owns the entity that will serve as the MLP's GP.[34] Issuing limited partner "units" on an exchange raises the vast majority of the MLP's equity.[35] In practice, the corporate sponsor, as an indirect owner of the GP, is the ruler behind the throne. Under the sponsored model, the GP often has a board of directors.[36] The GP's directors may have management positions with the

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ble/research_articles/file/2012_09_nepc_investing_in_mlps_-_risks_and_opportunities.pdf (noting that MLPs operate under a partnership structure as opposed to a subchapter C-Corporation).

26. JEFFREY BENNER, CORPORATE GOVERNANCE STRUCTURE OF MASTER LIMITED PARTNERSHIPS CARRIES CREDIT RISK 2 (2007), https://www.moodys.com/sites/products/AboutMoodysRatingsAttachments/2006600000441511.pdf ("MLPs are publicly traded entities with equity divided into a general partnership interest and publicly traded common units.").

27. BRETT & BRUCE, *supra* note 25, at 1 ("Equity shares of these partnerships are called units which are publicly traded on exchanges, just like C-Corp securities.").

28. *See* BENNER, *supra* note 26, at 2 (commenting that the general partnership interest is "typically 2%"); *see also* John Goodgame, *New Developments in Master Limited Partnership Governance*, 68 BUS. LAW. 81, 83 (2012) (noting that GP ownership is between 0.1% and 2.0%).

29. *See* BENNER, *supra* note 26, at 2 ("[B]ut the GP has broad contractual authority under a partnership agreement to control and manage the MLP and its assets. This structure separates economic ownership, of which the common unitholders hold 98%, and control of the assets, which lies with the GP.").

30. *See id.*; *see also* Thomas E. Rutledge & Steven G. Frost, *RULLCA Section 301—The Fortunate Consequences (and Continuing Questions) of Distinguishing Apparent Agency and Decisional Authority*, 64 BUS. LAW. 37, 41–42 (2008) (discussing the management of LLCs and the role of agency in both LLC statutes and the Revised Uniform Limited Liability Company Act).

31. *See* Goodgame, *supra* note 28.

32. *See id.* at 86 (discussing the popularity of the sponsorship model). For an overview of the sponsored MLP model, see Appendix A of this Article.

33. *Id*. at 83–84.

34. *See id.* at 86 (discussing the degree of control exercised by the GP within the sponsored MLP model).

35. *See id.* at 82 (stating that limited partner interests are typically called "common units" and are analogous to common stock issued by a corporation to raise capital).

36. *Id.* at 84.

sponsor.[37]

The business structures employed are diverse and complex, and profoundly impact both the governance rights and the financial risks and rewards. For example, under the sponsored model, the corporate sponsor may elect the GP's board.[38] However, contractual features may exist to mitigate the impact of the corporate sponsor's domination. For instance, the MLP agreement may require minimum distributions and may offer incentive distribution rights to the GP.[39] Distributions may provide the GP with substantial incentives to distribute available cash to the limited partners by increasing the GP's distribution in step with larger distributions to the limited partners.[40]

Under the publicly traded LLC model, an LLC replaces the LP.[41] Under the LLC model, the investors rather than the corporate sponsor may elect the board of directors, whose members may be contractually subject to corporate-like fiduciary duties.[42] Another model, the so-called "GP tuck-in transaction," falls between the sponsored and LLC models.[43] The GP tuck-in uses an LP, but the MLP owns the GP, and a corporate sponsor and public investors own the MLP.[44] In some deals, although the public unit holders may elect the GP's board of directors, there may be no mandatory distributions to the unit holders and no incentive distribution rights.[45] Also, the MLP partnership agreement may eliminate all fiduciary duties.[46] Under some of these arrangements, the corporate sponsor may own a substantial percentage of the outstanding units and thus may have financial interests aligned with other unitholders.[47] Nevertheless, if there is a downturn in the industry, or if the corporate sponsor wants to divest, then the interests of the corporate sponsor and those of the public unitholders may diverge.

B. *MLP Governance*

Partnerships are creatures of their governing contract, and MLPs, as

37. *See, e.g.*, *In re* El Paso Pipeline Partners, L.P. Derivative Litig., C.A. No. 7141-VCL, 2015 WL 1815846, at *2–*3 (Del. Ch. Apr. 20, 2015) (involving seven individual defendants of a GP, many of whom also held management positions with El Paso's parent company).

38. Goodgame, *supra* note 28, at 84.

39. *See* BENNER, *supra* note 26, at 3 (discussing mandatory quarterly distributions of the majority of cash flow to limited partners).

40. *See id.*

41. *See, e.g.*, Goodgame, *supra* note 28, at 87–88.

42. *See id.* at 87, 90.

43. *See id*. at 91.

44. *See id.* at 92.

45. *See id.* at 92–93.

46. *See id.* at 93.

47. *See, e.g.*, *id.* at 94.

LPs, are no different. Partnership agreement provisions may solidify the GP's control of the entity.[48] MLP agreements are often drafted to maximize the GP's control and to minimize the limited partners' remedies.[49] MLP agreements typically grant the GP the rights to make daily, management-like decisions as well as strategic, board-like decisions.[50] MLP agreements may also grant the GP the right to amend the partnership agreement itself, tantamount to total control of the entity.[51] Some MLP agreements do not permit limited partners to elect the GP, attend annual meetings, or put forth stockholder-type resolutions.[52] MLP agreements may also limit the GP's access to partnership proceeds until limited partners have been paid in full.[53]

MLP agreements often include limitations to the GP's authority, such as limitations for permissible operations or investments.[54] In addition, agreements typically contain provisions that, on their face, appear to grant substantial rights to the limited partners, such as management removal rights.[55] These provisions are often toothless when the agreement is read as a whole. For example, MLP agreements may provide for ouster of the GP by a two-thirds vote of the limited partners.[56] Nonetheless, agreements may also contain a clause that strips voting rights from any limited partner owning more than twenty percent.[57] Accordingly, while

48. Conrad S. Ciccotelloa & Chris J. Muscarella, *Contracts Between Managers and Investors: A Study of Master Limited Partnership Agreements*, 7 J. CORP. FIN. 1, 2 (2001) ("The obligations and rights of managers and shareholders are vague in corporate charters whereas MLP partnership agreements (PAs) often specify the relationship between management (the general partner) and investors (the limited partners).").

49. *See* Goodgame, *supra* note 28, at 84 ("The most salient governance difference is the difference between limited partnerships and corporations: a corporation is governed by its board of directors, which is elected by its shareholders and owes the corporation and its shareholders fiduciary duties; a limited partnership, on the other hand, is governed by its general partner." (footnotes omitted)).

50. *See id.* at 84–85.

51. *See, e.g.*, *id.* at 100 (discussing a partnership agreement provision permitting a GP to amend the partnership agreement).

52. *See id.* at 86.

53. BENNER, *supra* note 26, at 3 ("[A partnership agreement] does not typically allow distribution of proceeds to the GP from 'capital transactions,' such as an asset sale, or proceeds from borrowing until common unitholders have received distributions over the life of the MLP equal to the initial sale price of all common units at IPO or in subsequent offerings.").

54. *See id.* (noting various MLP agreement provisions that afford rights and duties to GPs).

55. *Id.*

56. *See id.* ("A ubiquitous, if not universal, PA term stipulates that any person or group that acquires more than 20% of common units loses voting rights on all of its common units. Combined, as is typical, with a requirement of approval of two-thirds of common units for removal of the GP, this term creates a formidable defense for the GP from a challenge to its control.").

57. *See id.*

ouster of the GP is possible in theory, the addition of the vote-stripping clause ensures that ouster is unlikely to occur. MLP agreements often take advantage of Delaware legal provisions that allow the GP to waive duties of care and loyalty to copartners in a partnership agreement.[58] Part II discusses the extent and ramifications of these provisions.

Despite the tighter stock exchange listing requirements spawned by the Sarbanes–Oxley Act,[59] New York Stock Exchange (NYSE) and NASDAQ rules treat MLPs similarly to controlled companies.[60] Under NYSE rules, MLPs are exempt from the requirements for a majority of independent directors, a nominating committee, or a compensation committee.[61] Similarly, the NASDAQ rules for MLPs do not require a majority of independent directors;[62] the rules require only a sufficient number of independent directors to possess an audit committee.[63] Thus, an MLP's GP only needs three independent directors as required under

58. Goodgame, *supra* note 28, at 85 ("[I]n practice the MLP board rarely owes corporate-style fiduciary duties to the MLP and its common unitholders because MLP partnership agreements explicitly modify or eliminate any such duties."); *see also* BENNER, *supra* note 26, at 2 (discussing the waiver of fiduciary duties under Delaware law).

59. Sarbanes–Oxley Act of 2002, Pub. L. No. 107-204, 116 Stat. 745 (codified as amended in scattered sections of 11, 15, 18, 28, and 29 U.S.C.); *see also* John C. Coffee, Jr., *The Political Economy of Dodd-Frank: Why Financial Reform Tends to Be Frustrated and Systemic Risk Perpetuated*, 97 CORNELL L. REV. 1019, 1027 (2012) (noting that there were those opposed to Sarbanes–Oxley because of the tighter controls it imposed).

60. Goodgame, *supra* note 28, at 98; *see also, e.g.*, NASDAQ STOCK MKT. R. IM-5615-5 (2015), http://nasdaq.cchwallstreet.com/nasdaq/main/nasdaq-equityrules/chp_1_1/chp_1_1_4/chp_1_1_4_3/chp_1_1_4_3_8/default.asp (noting requirements for controlled companies); N.Y. STOCK EXCH. LISTED CO. MANUAL § 303A.00 (2009), http://nysemanual.nyse.com/lcm/ [hereinafter NYSE MANUAL] (same); *FAQ: What Types of Companies Do Not Have to Have an Independent Board of Directors?*, NASDAQ OMX, https://listingcenter.nasdaqomx.com/Material_Search.aspx?cid=108&mcd=LQ (last visited Feb. 8, 2016) (same).

61. NYSE MANUAL, *supra* note 60, § 303A.00 ("A listed company of which more than 50% of the voting power for the election of directors is held by an individual, a group or another company is not required to comply with the requirements of Sections 303A.01, 303A.04 or 303A.05. Controlled companies must comply with the remaining provisions of Section 303A."); *see also* BENNER, *supra* note 26, at 2 ("MLPs . . . are considered 'controlled entities' under NYSE rules, and subsequently are exempt from NYSE rules requiring listed companies to have a majority of independent directors, and compensation and nominating committees composed entirely of independent directors. As a result of the exemption, most GP boards have only a minority of independent directors, and their role is often limited to reviewing related party transactions.").

62. NASDAQ STOCK MKT. R. 5615(a)(4) ("A limited partnership is not subject to the [corporate governance] requirements of the Rule 5600 Series, except as provided in this Rule 5615(a)(4).").

63. *See* NASDAQ STOCK MKT. R. 5605(c)(2)(A), 5615(a)(4)(C) (requiring the GP to satisfy the rules for an audit committee, including that the committee have at least three independent directors).

the rules applicable to audit committees.[64] Notwithstanding audit committee independence rules, some MLPs voluntarily have a majority of independent directors.[65] Even if there is an independent board of directors, an independent audit committee, or both, conflicts committee members appointed to review a conflicted transaction may themselves have previous ties to the corporate sponsor.[66]

C. *MLP Taxation*

The tax code permits pass-through partnership tax treatment for MLPs.[67] Consequently, the MLP's income is allocated to its owners in proportion to their ownership interests and taxed to the owner at the owner's respective tax rate.[68] The upshot is that the MLP avoids entity-level taxation,[69] which allows richer cash distributions of earnings to owners.[70] In addition, pass-through tax treatment allows owners to share in some of the MLP's deductions.[71]

The MLP's tax advantages have prerequisites. Ninety percent of the MLP's income is limited to "qualifying income" from limited sources.[72] These sources include interest, dividends, real property rents or gains

64. *See* NASDAQ STOCK MKT. R. 5605(c)(2)(A), IM-5615-5.

65. *See* Goodgame, *supra* note 28, at 99.

66. *See, e.g.*, *In re* El Paso Pipeline Partners, L.P. Derivative Litig., C.A. No. 7141-VCL, 2015 WL 1815846, at *15 (Del. Ch. Apr. 20, 2015).

67. *See* 26 U.S.C. § 7704(c)–(d) (2012); STAFF OF JOINT COMM. ON TAXATION, 108TH CONG., DESCRIPTION OF H.R. 4520, THE "AMERICAN JOBS CREATION ACT OF 2004," at 43 (Comm. Print 2004) ("In general, a publicly traded partnership is treated as a corporation . . . , but an exception to corporate treatment is provided if 90 percent or more of its gross income is interest, dividends, real property rents, or certain other types of qualifying income."); PAUL COMSTOCK PARTNERS, MASTER LIMITED PARTNERSHIP PRIMER "MLP 101," at 3 (2009), http://paulcomstockpartners.com/quarterly-webinars/master-limited-partnership-primer-mlp-101/.

68. BRETT & BRUCE, *supra* note 25, at 1 (noting that MLPs are pass-through entities in which tax is assessed on the limited partners); *see also* PAUL COMSTOCK PARTNERS, *supra* note 67, at 3–4 (noting the tax structure and consequences of MLP ownership).

69. PAUL COMSTOCK PARTNERS, *supra* note 67, at 3 ("This eliminates the double taxation found within the traditional corporate structure, giving MLPs a cost-of-capital advantage as they are able to distribute more of their earnings to their limited partners in the form of quarterly cash distributions."); FREED & STEVENS, *supra* note 24 (reporting that MLPs' income is taxed once).

70. *See* PAUL COMSTOCK PARTNERS, *supra* note 67, at 3.

71. *See* STAFF OF JOINT COMM. ON TAXATION, DESCRIPTION OF H.R. 4520, *supra* note 67, at 43 ("The special rule for publicly traded partnerships provides that the passive loss rules are applied separately with respect to items attributable to each publicly traded partnership (sec. 469(k)). Thus, income or loss from the publicly traded partnership is treated as separate from income or loss from other passive activities."); FREED & STEVENS, *supra* note 24, at 3–4 ("In addition, investors in MLP's are able to reduce their tax liability because they receive their share of the partnership's depreciation.").

72. 26 U.S.C. § 7704(c)(2); *see also* PAUL COMSTOCK PARTNERS, *supra* note 67, at 3 (discussing the limitations on MLP income).

from real property disposition, and income or gain from commodities.[73] While these are primarily passive income sources, qualifying income also includes income or gain from mineral or natural resources.[74]

D. *MLP Performance*

The provision for mineral and natural resource income qualifies the entity for partnership taxation and provides an obvious subsidy to that industry.[75] Consequently, most MLPs are midstream energy producers.[76] On the whole, current MLPs have produced attractive returns. Some of these returns can be attributed to the performance of the energy industry, which has grown at over ten percent annually.[77] Returns can also be attributed specifically to energy infrastructure investment that nearly tripled in two years.[78] Midstream MLPs have outperformed the S&P 500 and Dow Industrials,[79] and this track record has been established for more than a decade.[80] Market capitalization has grown dramatically, doubling in only a few years.[81] Trading in MLP units has nearly quadrupled over

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73. 26 U.S.C. § 7704(d)(1).

74. *See id.* § 7704(d)(1)(E).

75. *See* Felix Mormann, Dan Reicher & Mark Muro, Opinion, *Clean Energy Scores Success with the Master Limited Partnership Parity Act*, BROOKINGS INST. (Dec. 19, 2013), http://www.brookings.edu/research/opinions/2013/12/19-clean-energy-mormann-reicher-muro (discussing the lower costs of capital for oil, gas, and other fossil energy infrastructure versus clean energy capital); *Master Limited Partnership Parity Act to Expand Investment Opportunities for Clean Energy Projects*, PEW CHARITABLE TRUSTS (Apr. 24, 2013), http://www.pewtrusts.org/en/about/news-room/news/2013/04/24/master-limited-partnership-parity-act-to-expand-investment-opportunities-for-clean-energy-projects (noting the liquidity, low-cost capital, and high rate of return for energy projects that qualify as MLPs).

76. *See* STEELPATH, MASTER LIMITED PARTNERSHIP PRIMER: UNDERSTANDING AN EMERGING ASSET CLASS 4, https://mlpprotocol.files.wordpress.com/2013/03/steelpath-mlp-primer.pdf (discussing the reasons for MLP concentration in energy).

77. Chris Eades, *Energy MLPs: A Suitable and Sustainable Asset Class*, CLEARBRIDGE INVS. (July 9, 2013), http://www.advisorperspectives.com/articles/2013/07/09/energy-mlps-a-suitable-and-sustainable-asset-class (discussing energy production).

78. *Id.* at 4 (noting energy infrastructure growth from $11 billion to $35 billion over two years).

79. *See* Andrew Bary, *Pipelines to Profits*, BARRON'S (June 2, 2012), http://online.barrons.com/news/articles/SB50001424053111904081004577434252994880844 (noting MLP annualized returns of 16% compared to about 5% for the Dow Industrials and the S&P 500).

80. *See* STEELPATH, *supra* note 76, at 4 ("Over the past 15 years, MLPs have outperformed the S&P 500 with a cumulative gain of over 938%, a compound annual return of 17%, versus 157% for the broader market, a compound annual return of less than 7%."); *see also* Eades, *supra* note 77, at 2 (discussing the past returns and attractive factors for MLP investment).

81. *See* Eades, *supra* note 77, at 1 ("[In 2011,] there was between $250 billion and $300 billion in combined market capitalization for the space, and today we are rapidly approaching $450 billion in total market capitalization."); BRETT & BRUCE, *supra* note 25, at 4 ("Since 1996 [through 2012], the market cap of MLPs has increased from $8 billion to more than $240 billion.").

the same time period.[82] Given that the national need for energy is unlikely to abate[83] and that energy is a national policy imperative,[84] the future for midstream energy MLP performance is quite bright.[85] Indeed, analysts generally predict MLP growth.[86]

While attractive MLP returns can be attributed to their primary industry, some returns can also be attributed to their tax-preferred treatment.[87] The lower effective tax rate achieved through the avoidance of corporate taxation can lower the cost of capital[88] and increase net income.[89] MLPs are designed to regularly distribute cash to limited partners as a form of management discipline[90] and as a result of their business model.[91]

E. *Who May Invest in an MLP?*

Given the dramatic increases in market capitalization and trading volumes, investors appear quite interested in MLPs. Only ten years ago, mutual funds could not invest in MLPs. When Congress wrote the rules

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82. *See* Eades, *supra* note 77, at 1 ("Five or six years ago, daily trading in MLPs was about $200 million. Last year, that figure had increased to $550 million per day and today it's in excess of $800 million per day.").

83. *See id.* at 4 (discussing energy industry and MLP exposure to economic cycles); BRETT & BRUCE, *supra* note 25, at 12 (noting that there is a "need for increased investment in energy infrastructure in North America").

84. *See id.* at 4 (discussing the relationship between MLPs and national energy policy).

85. *See* COHEN & STEERS, COHEN & STEERS MLP STRATEGY 2 (2013), http://www.cohenandsteers.com/assets/content/resources/insight/MLP_Commnetary.pdf (noting increased shale basin production and the need for a redesigned energy grid with pipelines, processing plants, and storage facilities as support for likely growth); LEGG MASON, MASTER LIMITED PARTNERSHIPS: AN INTRODUCTION 3 (2013), http://www.leggmason.com/individualinvestors/documents/brochure/D9241-Understanding_MLPs.pdf (predicting increased growth in energy infrastructure, processing, and distribution for MLPs).

86. *See* W. BRUCE BULLOCK, BERNARD L. WEINSTEIN & BEN JOHNSON, LEVELING THE PLAYING FIELD: A CASE FOR MASTER LIMITED PARTNERSHIPS FOR RENEWABLES 2 (2012), http://www.awea.org/Advocacy/Content.aspx?ItemNumber=4612 (reporting financial modeling for MLPs).

87. *See* Tom Lydon, *Master Limited Partnership ETF: Attractive Yields with Risks*, ETF TRENDS (Mar. 10, 2013, 6:51 AM), http://www.etftrends.com/2013/03/master-limited-partnership-etf-attractive-yields-with-risks (noting that a structure and tax treatment that permits "more money to distribute to stockholders").

88. *See* COHEN & STEERS, *supra* note 85, at 3.

89. *See* Phyllis Cuttino, *Master Limited Partnerships and Clean Energy Investment*, PEW CHARITABLE TRUSTS (Aug. 7, 2013) ("MLPs could retain almost 40% more net income by investing in an MLP vs a Corporation.").

90. *See* BRETT & BRUCE, *supra* note 25, at 3 (noting that MLPs pay around 90% of income as quarterly distributions).

91. *See id.* at 2 ("Midstream businesses provide relatively stable revenues from toll-like fee arrangements, which minimize the impact of commodity price volatility on revenues.").

surrounding permissible investments for mutual funds, MLPs did not exist.[92] This likely slowed early investment in MLPs.[93] In 2004, however, Congress changed the rules to permit mutual funds to invest in MLPs.[94] There are, of course, some limitations on how much they may invest in MLPs generally and in any single MLP.[95] These limitations have not significantly abated investment flow into MLPs.

II. CONTEXTUALIZING MLP FIDUCIARY DUTIES

Evaluating MLP governance requires an understanding of the overall landscape of investor protections, including corporate investor protections. The Delaware corporate framework supports management yet offers significant investor protections.[96] These investor protections include a duty of loyalty to the corporation and stockholders as well as a duty of care.[97] Under Delaware's LP and LLC statutes, investors have protections similar to those extended to corporate stockholders, but only if fiduciary duties are left intact. However, this is not often the case because Delaware law permits the waiver of all fiduciary duties in both LP and LLC agreements.[98] Delaware MLPs, therefore, may waive all fiduciary duties regardless of whether the entity uses an LP or LLC model. MLP agreements often use narrow definitions of good faith,

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92. *See* STEELPATH, *supra* note 76, at 2–3.

93. *See id.* at 3.

94. *Id.* ("On October 22, 2004, the American Jobs Creation Act was enacted effective January 1, 2005. A section of this law allows regulated investment companies (RICs), such as mutual funds, to invest in MLPs by amending the definition of what was considered to be qualifying income for a RIC in the tax code.").

95. *See id*. ("RICs may now invest freely in MLPs as long as such investments do not constitute more than 25% of their assets, and as long as they do not own more than 10% of any one MLP.").

96. *See infra* Section II.A.

97. *See* DEL. CODE ANN. tit. 8, § 102(b)(7) (2015) (permitting a corporation to "eliminat[e] or limit[] the personal liability of a director to the corporation or its stockholders for monetary damages" but not to "eliminate or limit the liability of a director . . . [f]or any breach of the director's duty of loyalty . . .[,] acts or omissions not in good faith or which involve intentional misconduct or a knowing violation of law," or certain violations regarding distributions or "transaction[s] from which the director derived an improper personal benefit"); 1 R. FRANKLIN BALOTTI & JESSE A. FINKELSTEIN, THE DELAWARE LAW OF CORPORATIONS & BUSINESS ORGANIZATIONS § 4.16 (3d ed. Supp. 2015).

98. DEL. CODE ANN. tit. 6, § 17-1101(d) ("[T]he partner's or other person's duties may be expanded or restricted or eliminated by provisions in the partnership agreement; provided that the partnership agreement may not eliminate the implied contractual covenant of good faith and fair dealing."); *id.* § 18-1101(c) ("[T]he member's or manager's or other person's duties may be expanded or restricted or eliminated by provisions in the limited liability company agreement; provided, that the limited liability company agreement may not eliminate the implied contractual covenant of good faith and fair dealing.").

expansive discretion clauses, and consents to conflicts of interest.[99] These agreements often eliminate the duty of loyalty and the affirmative disclosure obligations that accompany fiduciary duties.[100] Thus, publicly traded corporations and alternative business entities may engage in the same business and trade on the same exchange but offer wildly different investor protection, and consequently present significantly different risks to investors.

A. *Comparing Corporate and MLP Fiduciary Duties*

Although one scholar contends that corporate fiduciary duties are largely irrelevant due in part to deference shown to business judgment,[101] the corporate business model is undoubtedly committed to the concept of operating the corporation in good faith.[102] The requirement to act in good faith appears in the monitoring function,[103] corporate opportunity doctrine,[104] conflicted transactions,[105] and use of expert reports.[106] Furthermore, the law does not permit exculpation of breaches of the duty of loyalty.[107]

The internal governance rules for publicly traded corporations offer three major investor protections that are largely lacking under the publicly traded MLP paradigm. First, corporations have extensive board

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99. *See infra* Section II.B.

100. *See infra* Subsection II.B.4.

101. *See* J. Robert Brown, Jr., *The Irrelevance of State Corporate Law in the Governance of Public Companies*, 38 U. RICH. L. REV. 317, 318–19 (2004) (arguing that the laxity of fiduciary duties makes them largely irrelevant).

102. *See* Leo E. Strine, Jr. et al., *Loyalty's Core Demand: The Defining Role of Good Faith in Corporation Law*, 98 GEO. L.J. 629, 642–43 (2010) (discussing how the creators of Delaware's statutory and common law have put the Berle–Means policy of "powers in trust" for fiduciaries into action).

103. *E.g.*, *In re* Caremark Int'l Inc. Derivative Litig., 698 A.2d 959, 971 (Del. Ch. 1996) (observing that directors could be liable for failing to establish a proper monitoring system if they acted in bad faith where "a sustained or systematic failure . . . to attempt to assure a reasonable information and reporting system exists—will establish the lack of good faith that is a necessary condition to liability"); *see also* Stone v. Ritter, 911 A.2d 362, 364 (Del. 2006) (holding that there are some necessary conditions for director oversight liability that corporate directors must install).

104. *See* DEL. CODE ANN. tit. 8, § 144 (2015) (providing that an interested transaction is not voidable if approved in good faith by a majority of disinterested directors, if material facts are disclosed to stockholders who vote to approve the transaction, or if the transaction is fair); Strine, *supra* note 102, at 658, 670 ("Section 144 therefore makes plain the definitional relationship between good faith and the duty of loyalty, with the term good faith identifying the loyal state of mind required for an approving vote to be given immunizing effect. The use of good faith in this manner does not establish a new duty; it gives life and meaning to the central duty of loyalty.").

105. *See, e.g.*, Guth v. Loft, Inc., 5 A.2d 503, 510 (Del. 1939).

106. *See, e.g.*, DEL. CODE ANN. tit. 8, § 172 (involving good faith reliance on expert report as to whether a dividend can be lawfully distributed); Strine, *supra* note 102, at 656.

107. *See* DEL. CODE ANN. tit. 8, § 102(b)(7).

independence requirements under stock exchange listing rules from which LPs, but not LLCs, are exempt.[108] Second, corporations have conflicts committees that are typically composed of independent third parties—a characteristic lacking in some MLPs.[109] Third, the corporate fiduciary duties of loyalty and care constrain management and offer a socializing message that is rendered largely irrelevant to publicly traded LPs and LLCs with expansive waivers in their governing documents.[110]

1. Board Independence Under Listing Standards

An explosion of accounting and financial scandals in late 2001 and 2002 led to federal intervention in the form of the Sarbanes–Oxley Act.[111] Following the Enron, Worldcom, and Tyco debacles,[112] Congress enacted the Sarbanes–Oxley Act in an effort "to improve the audit process and internal controls, increase board independence from management, and improve disclosure and transparency."[113] Although Sarbanes–Oxley itself contained numerous rules regarding board independence and introduced independence requirements with regard to the audit committee,[114] the Act also ushered in NYSE and NASDAQ listing requirements that require independence of a majority of a listed company's directors.[115] The listing rules require a fully independent audit committee.[116] Although publicly traded LPs must have three independent members on the audit committee, they do not need a majority of independent directors.[117]

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108. *See infra* Subsection II.A.1.

109. *See* Leo E. Strine, Jr. & J. Travis Laster, *The Siren Song of Unlimited Contractual Freedom*, at 21–22 (forthcoming in ELGAR HANDBOOK ON ALTERNATIVE ENTITIES (Mark Lowenstein & Robert Hillman eds., Edward Elgar Publ'g 2014)), http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2481039; *infra* Subsection II.A.2.

110. *See infra* Subsection II.A.3.

111. John C. Coffee, Jr., *Gatekeeper Failure and Reform: The Challenge of Fashioning Relevant Reforms*, 84 B.U. L. REV. 301, 305 (2004).

112. *Id.* at 303.

113. Spencer Stuart, *Ten Years Later: Sarbanes–Oxley Act Continues to Shape Board Governance Landmark Governance*, PR NEWSWIRE (July 30, 2012), http://www.prnewswire.com/news-releases/10-years-later-sarbanes-oxley-act-continues-to-shape-board-governance-164296516.html.

114. *See* Sarbanes–Oxley Act of 2002, Pub. L. No. 107-204, 116 Stat. 745 (codified as amended in scattered sections of 11, 15, 18, 28, and 29 U.S.C.).

115. NASDAQ STOCK MKT. R. IM-5605(a)(2), (b)(1) (2015) (defining independence and requiring a majority of the board of directors to be independent); NYSE MANUAL, *supra* note 60, §§ 303A.00–.01 (requiring a majority of a board of directors to be independent).

116. *See* NYSE MANUAL, *supra* note 60, § 303A.07 (requiring a fully independent audit committee).

117. *See id.* § 303.A.00.

This exception to the board independence requirements arguably places limited partners at a disadvantage vis-à-vis comparable corporate investors because board independence is integral to effective internal governance.[118] Independence arguably curbs excessive conflicts of interest in corporate board decision-making.[119] As noted in the Commentary to the NYSE Listing Requirements, "[e]ffective boards of directors exercise independent judgment in carrying out their responsibilities. Requiring a majority of independent directors will increase the quality of board oversight and lessen the possibility of damaging conflicts of interest."[120] Just as increased independence strengthens governance, it follows that eliminating or diminishing independence weakens the position of investors in an enterprise.

Some have argued that there is no positive relationship between independence and positive firm outcomes.[121] More recently, however, it has been persuasively argued that board independence facilitates wealth-maximizing strategies for the benefit of stockholders.[122] As one commentator observed:

> [I]ndependent directors are more valuable than insiders. They are less committed to management and its vision. Instead, they look to outside performance signals and are less captured by the internal perspective, which, as stock prices become more informative, becomes less valuable. They can be more readily mobilized by legal standards to help provide the public goods of more accurate disclosure and better compliance with law. In this way, independent directors are an essential part of a new corporate governance paradigm.[123]

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118. *See* Stuart, *supra* note 113; *infra* Section III.D.

119. *See* CHARLES A. BOWSHER, CONTROLLER GEN. OF THE UNITED STATES, CORPORATE ACCOUNTABILITY: A TIME FOR REFORM ADDRESS BEFORE THE SECURITIES REGULATION INSTITUTE 8 (Jan. 23, 1992), http://www.gao.gov/assets/200/195714.pdf ("Real corporate accountability is not possible without a board of directors that is independent of management and willing to act on its own authority.").

120. NYSE MANUAL, *supra* note 60, § 303A.01 cmt.

121. *See, e.g.*, Roberta Romano, *The Sarbanes–Oxley Act and the Making of Quack Corporate Governance*, 114 YALE L.J. 1521, 1530–31, 1604 (2005) (providing an appendix of empirical studies showing no correlation between audit committee independence and positive outcomes).

122. Jeffery N. Gordon, *The Rise of Independent Directors in the United States, 1950–2005: Of Shareholder Value and Stock Market Prices*, 59 STAN. L. REV. 1465, 1563 (2007); *see also* Sanjai Bhagat & Brian Bolton, *Director Ownership, Governance, and Performance*, 48 J. FIN. & QUANTITATIVE ANALYSIS 105, 105 (2013) (finding a positive relationship between corporate governance and firm performance from 2002 to 2007).

123. Gordon, *supra* note 122, at 1563.

Board independence requirements have not cured all abusive practices, and scholars hotly debate the extent to which independence is helpful.[124] Nevertheless, board independence requirements may improve the odds that board decisions will reflect the best interests of the firm rather than the best interests of the managers or managing companies. Professor Richard Clark has noted that post-Sarbanes–Oxley empirical studies have found positive effects of increased requirements for internal controls and board independence.[125] Additionally, in a widely recognized, comprehensive pre-Sarbanes–Oxley empirical study, Professors Bernie Black and Sanjai Bhagat initially did not find a meaningful positive effect of director independence upon shareholder value.[126] However, in a recent post-Sarbanes–Oxley study, Professors Bhagat and Brian Bolton considered five measures of corporate governance during the period of 1998 to 2007 and reported a positive, significant relationship between board independence and operating performance.[127] Thus, post-Sarbanes–Oxley independence requirements likely offer corporate investors a helpful safeguard that investors in publicly traded LPs may unwittingly relinquish.

2. Corporate Board Structure and Conflicts Committee Membership

As indicated above, listing standards have been important in achieving board independence in publicly traded corporations. In addition, corporate board structure and the use of conflicts committees to approve conflicted transactions promote managerial independence. Where a decision presents a conflict of interest, an independent conflicts committee can step in to assess conflicted transactions.

Delaware's corporate paradigm encompasses standards of conduct and standards of judicial review,[128] and also provides a "safe-harbor" statute that offers a pathway for handling interested director transactions.[129] The law is well-suited for handling conflicted director decision-making. As succinctly explained in *Chen v. Howard-Anderson*:

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124. *Compare* Romano, *supra* note 121, at 1530–31 (concluding that independent boards do not improve, and may negatively affect, performance), *with* PAUL W. MACAVOY & IRA M. MILLSTEIN, THE RECURRENT CRISIS IN CORPORATE GOVERNANCE 42 (2003) ("[E]mpirical evidence seems to suggest . . . that reform efforts are having some impact on current governance practice."), *and* Bhagat & Bolton, *supra* note 122, at 105 (finding a negative relationship between board independence and performance before 2002 but a positive correlation after 2002).

125. *See* Richard C. Clark, *Harmony or Dissonance? The Good Governance Ideas of Academics and Worldly Players*, 70 BUS. LAW. 321, 326 (2015).

126. *See* Sanjai Bhagat & Bernard S. Black, *The Non-Correlation Between Board Independence and Long-Term Performance*, 27 J. CORP. L. 231, 233 (2002).

127. Bhagat & Bolton, *supra* note 122.

128. Chen v. Howard–Anderson, 87 A.3d 648, 666–67 (Del. Ch. 2014).

129. BALOTTI & FINKELSTEIN, *supra* note 97, § 4.16[A].

> "Delaware has three tiers of review for evaluating director decision-making: the business judgment rule, enhanced scrutiny, and entire fairness." Which standard of review applies will depend initially on whether the board members (i) were disinterested and independent (the business judgment rule), (ii) faced potential conflicts of interest because of the decisional dynamics present in particular recurring and recognizable situations (enhanced scrutiny), or (iii) confronted actual conflicts of interest such that the directors making the decision did not comprise a disinterested and independent board majority (entire fairness). The standard of review may change further depending on whether the directors took steps to address the potential or actual conflict, such as by creating an independent committee, conditioning the transaction on approval by disinterested stockholders, or both.[130]

Further, Delaware corporate law provides a safe harbor for dealing with interested director transactions.[131] An interested director transaction will not be void or voidable merely because it is conflicted; if a fully informed majority of disinterested directors or shareholders approves the conflicted transaction or if it is fair to the corporation, then the conflicted transaction will not be void or voidable.[132]

As discussed below, MLP agreements typically eliminate fiduciary duties. Moreover, in the MLP context, the listing requirement exceptions and the composition of conflicts committees may compromise managerial independence. Even if some or all of the directors of the MLP's GP are independent, the directors may be in an inherently conflicted position.[133] Under the sponsored model, the MLP includes a GP that manages the MLP.[134] The GP owes fiduciary duties to the GP's owners, which are likely affiliates of the corporate sponsor.[135] Thus, the directors of the MLP's GP potentially serve two conflicting constituencies—the corporate sponsor via fiduciary duties and the limited partners via contractual duties and the implied covenant of good faith and fair dealing. This potentially troublesome conflict was first noted in *Gotham Partners, LP v. Hallwood Realty Partners, LP*[136] and is one of

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130. 87 A.3d at 666–67 (citation omitted).

131. *See* DEL. CODE ANN. tit. 8, § 144 (2015).

132. *Id.*

133. *See* Strine & Laster, *supra* note 109, at 22.

134. Goodgame, *supra* note 28, at 83.

135. *Id.* at 85–86.

136. No. CIV.A.15754, 2000 WL 1476663, at *19–20 (Del. Ch. Sept. 27, 2000). *See generally* Sandra K. Miller, *The Role of the Court in Balancing Contractual Freedom with the*

the many reasons that Delaware Supreme Court Chief Justice Leo E. Strine and Delaware Court of Chancery Vice Chancellor J. Travis Laster have called for a change in the rules concerning the elimination of fiduciary duties in diversely held Delaware LPs and LLCs.[137]

Managerial independence is further compromised when the GP's directors serve on a conflicts committee to review business transactions that present a conflict of interest between the limited partners and the corporate sponsor or affiliates.[138] A review of recent litigation reveals that parties with ties to the MLP's sponsor or its affiliates may heavily populate GP boards.[139] As Chief Justice Strine and Vice Chancellor Laster pointed out:

> [A] corporate managing members' independent directors are often called on to approve conflict transactions between the managing member and the alternative entity, and that approval is given liability-limiting effect. But, of course, there is a fundamental difference that is elided. An independent director of a corporation is accorded that status precisely because she has no conflict of interest and is not subject to any material influence that would prevent her from acting solely in the best interests of the corporation and its stockholders *qua* stockholders and thus is well positioned to act to protect against any unfair proposals from managers who do suffer from conflicts of interests. But an independent director of a corporation that is a managing member . . . owes a fiduciary duty to act in that corporation's best interest, and is not in a direct fiduciary position as to the alternative entity and its investors.[140]

Thus, it appears that the corporate paradigm provides greater investor protection than the contractual MLP framework when it comes to interested director decision-making.

Need for Mandatory Constraints on Opportunistic and Abusive Conduct in the LLC, 152 U. PA. L. REV. 1609, 1638–40 (2004) (discussing the implications of *Gotham*).

137. *See* Strine & Laster, *supra* note 109, at 22.

138. *See id.*

139. *See, e.g.*, Allen v. Encore Energy Partners, L.P., 72 A.3d 93, 98 (Del. 2013) ("[A] majority of the Encore Board members were Vanguard employees and Vanguard owned Encore GP."); Allen v. El Paso Pipeline GP Co., 113 A.3d 167, 174–75 (Del. Ch. 2014) (involving multiple BP board directors who had ties with the El Paso parent company), *aff'd*, No. 399, 2014, 2015 WL 803053 (Del. Feb. 26, 2015); Brinckerhoff v. Enbridge Energy Co., C.A. No. 5526-VCN, 2011 WL 4599654, at *7 (Del. Ch. Sept. 30, 2011) ("EEP GP's Board is made up of seven members, and . . . four of them were beholden to Enbridge."), *aff'd*, 67 A.3d 369 (Del. 2013).

140. Strine & Laster, *supra* note 109, at 21–22.

3. Fiduciary Duty Constraints and the Socializing Role of Duty of Loyalty Literature and Jurisprudence

In addition to board independence protections, corporate stockholders enjoy fiduciary duty protection, including the duty of loyalty and the duty of care.[141] Both fiduciary duties, the duty of loyalty in particular, play an important socializing role in the business community.[142] However, as more fully discussed below, the duty of loyalty is frequently eliminated in MLP agreements.[143]

Delaware corporate directors are subject to a mandatory duty of loyalty to act in the best interests of the corporation and a duty to refrain from grossly negligent conduct.[144] The corporate business model is committed to the concept of operating the corporation in good faith.[145] In the words of former Delaware Court of Chancery Chancellor William B. Chandler III and Chief Justice Strine (then-Vice Chancellor), "[t]he statutory constraints on unilateral action that exist in the Delaware General Corporation Law have been chosen with some care."[146] For

141. *See* BALOTTI & FINKELSTEIN, *supra* note 97, § 4.16.

142. *See generally* Margaret M. Blair & Lynn A. Stout, *Trust, Trustworthiness, and the Behavioral Foundations of Corporate Law*, 149 U. PA. L. REV. 1735 (2001) [hereinafter Blair & Stout, *Behavioral Foundations*] (proposing that "the behavioral phenomena of internalized trust and trustworthiness play important roles in encouraging cooperation within firms").

143. *See* Manesh, *supra* note 9, at 567–80 (studying eighty-five publicly traded LPs and LLCs and noting that ten of the eighty-five firms studied did not fully waive or exculpate liability arising from breach of fiduciary duties).

144. *See* Usha Rodrigues, *From Loyalty to Conflict: Addressing Fiduciary Duty at the Officer Level*, 61 FLA. L. REV. 1, 6 & n.8 (2009) ("The directors of Delaware corporations have a triad of primary fiduciary duties: due care, loyalty, and good faith" (quoting Emerald Partners v. Berlin, 787 A.2d 85, 90 (Del. 2001))). In the landmark case of *Smith v. Van Gorkom*, the Delaware Supreme Court held that the business judgment rule was inapplicable where the directors made an uninformed decision approving a merger that Van Gorkom wanted so that he could sell his interest before retiring. 488 A.2d 858, 864 (Del. 1985), *overruled on other grounds by* Gantler v. Stephens, 965 A. 2d 695, 713 n.54 (Del. 2009). Directors cannot waive or be exculpated for violations of the duty of loyalty. Lyondell Chem. Co. v. Ryan, 970 A.2d 235, 239 (Del. 2009). They do, however, have the benefit of the business judgment rule, which grants a presumption that they make business decisions on an informed basis, in good faith, and in the honest belief that the conduct is in the best interests of the company. *See id.* at 242–44. *See generally* Lyman Johnson, *Unsettledness in Delaware Corporate Law: Business Judgment Rule, Corporate Purposes*, 38 DEL. J. CORP. L. 405, 410–11 (2013) (noting the history of the business judgment rule in Delaware case law).

145. *See* Strine et al., *supra* note 102, at 640–41 ("[T]he concept of loyalty pervades all of Delaware corporate law.").

146. William B. Chandler III & Leo E. Strine, Jr., Symposium, *The New Federalism of the American Corporate Governance System: Preliminary Reflections of Two Residents of One Small State*, 152 U. PA. L. REV. 953, 976 (2003).

example, the requirement of stockholder approval for important transactions, including certain types of mergers, sales of substantially all corporate assets, and increases in authorized shares, plays an important role in constraining director discretion.[147] Fiduciary duties provide a key mechanism for enforcing the corporate stockholder safeguards.[148] Further, the fiduciary duty review includes the entire fairness standard in conflicted transactions and heightened judicial review in connection with mergers and acquisitions.[149]

Although the director's fiduciary duty of care may be exculpated, the duty of loyalty may not.[150] Section 102(b)(7) of the Delaware statutes permits a corporation to eliminate or limit the personal liability of a director, except for a breach of the duty of loyalty, for acts or omissions not in good faith or which involve intentional misconduct or a knowing violation of law, and liability for other misconduct (i.e., unlawful dividends or improper personal benefits).[151] A corporation may exculpate the director for violations of the duty of care but not for violations of the duty of loyalty or conduct not in good faith.[152] While the duty of care has been defined in different ways, one decision noted that "[w]ords must be taken seriously and gross negligence has a stringent meaning under our law of entities, to wit, one 'which involves a devil-may-care attitude or indifference to duty amounting to recklessness.'"[153]

Arguably, lack of good faith is a formidable obstacle to prove,[154] and only inexcusable inattentiveness or a complete abdication of duties to

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147. *Id.* at 977.

148. *Id.* ("The Delaware courts have deployed a variety of tools . . . including the entire fairness standard of review for conflict transactions and the heightened *Revlon* and *Unocal* standards that are applied to certain director actions in the mergers and acquisitions context." (footnotes omitted)).

149. *See id.*

150. *See* DEL. CODE ANN. tit. 8, § 102(b)(7) (2015).

151. *Id.*

152. *See In re* Walt Disney Co. Derivative Litig., 906 A.2d 27, 66–67 (Del. 2006). Delaware's LLC indemnification provision permits the LLC to indemnify any member or manager from "*all* claims and demands whatsoever." DEL. CODE ANN. tit. 6, § 18-108 (2015) (emphasis added). Other states' LLC indemnification provisions tend to be more restrictive than Delaware's. *Compare id.*, *with* FLA. STAT. § 607.0850(7) (2015) (prohibiting indemnification for violations of criminal law, transactions generating improper personal benefits, certain improper distributions, and willful misconduct or a conscious disregard for the best interests of the LLC). Although a statute does not specifically prohibit indemnification for acts of bad faith, it would arguably violate public policy to exculpate an LLC manager for acts of bad faith. *See* Miller v. Am. Real Estate Partners, L.P., No. CIV.A.16788, 2001 WL 1045643, at *11 (Del. Ch. 2001). *But see* Lyman Johnson, *Delaware's Non-Waivable Duties*, 91 B.U. L. REV. 701, 706 (2011) (noting that Delaware LLC and GP statutes express a "contractarian policy preference").

153. Gelfman v. Weeden Inv'rs, L.P., 859 A.2d 89, 114 (Del. Ch. 2004).

154. *See* Lyondell Chem. Co. v. Ryan, 970 A.2d 235, 239 (Del. 2009) (interpreting the so-called "*Revlon* duties" as not requiring any specific steps to take in evaluating an offer); *In re*

oversee the business have resulted in legal liability.[155] The Delaware Chancery Court recently indicated that conduct not in good faith includes "situations where the fiduciary intentionally breaks the law, where the fiduciary intentionally acts with a purpose other than of advancing the best interests of the corporation, or where the fiduciary intentionally fails to act in the face of a known duty to act."[156]

Notwithstanding the prospect of duty of care exculpation,[157] Delaware's corporate fiduciary duty regime offers significant protections in connection with interested director transactions,[158] oversight duties,[159] corporate opportunities,[160] and duties of disclosure.[161] In fact, one of the most significant effects of waiving fiduciary duties is the loss of protection afforded by the director's duty to disclose all relevant facts. As noted recently by Vice Chancellor Laster, Delaware's fiduciary duty law requires affirmative disclosure of material information in connection with self-interested transactions.[162] In connection with self-interested

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Caremark Int'l Inc. Derivative Litig., 698 A.2d 959, 971 (Del. Ch. 1996) ("Such a test of liability—lack of good faith . . . —is quite high."); Daniel S. Kleinberger, *Delaware Dissolves the Glue of Capitalism: Exonerating from Claims of Incompetence Those Who Manage Other People's Money*, 38 WM. MITCHELL L. REV. 737, 758 (2012).

155. *E.g.*, ATR-Kim Eng Fin. Corp. v. Araneta, No. CIV.A. 489-N, 2006 WL 3783520, at *1 (Del. Ch. Dec. 21, 2006) (involving two directors who were jointly liable with the ninety percent owner of a corporation because they failed to implement a reporting or monitoring system to prevent the transfer of the company's assets to the majority owner's children), *aff'd*, 930 A.2d 928 (Del. 2007) (unpublished table decision); *see also In re Disney*, 906 A.2d at 66–67 (holding that where the behavior is qualitatively more culpable than gross negligence, liability will be imposed such as where there has been an intentional dereliction of duty or conscious disregard for one's responsibilities); SANDRA K. MILLER, LIMITED LIABILITY COMPANIES: A COMMON CORE MODEL OF FIDUCIARY DUTIES § 6.15 (2014); Bernard Black, Brian Cheffins & Michael Klausner, *Outside Director Liability*, 58 STAN. L. REV. 1055, 1057–58, 1062 (2006) (observing that although twelve outside directors personally paid $24.5 million in the WorldCom securities class action settlement and ten outside directors paid $13 million out of their own pockets in the Enron settlements, out-of-pocket settlements by outside directors are rare).

156. *In re* BioClinica, Inc. S'holder Litig., Civil Action No. 8272-VCG, 2013 WL 5631233, at *5 (Del. Ch. Oct. 16, 2013) (quoting *In re* Goldman Sachs Grp., Inc. S'holder Litig., Civil Action No. 5215-VCG, 2011 WL 4826104, at *13 (Del. Ch. Oct. 12, 2011)).

157. Some have argued that judicial interpretations following the enactment of Delaware's statutory exculpation rules as well as a rather expansive application of the business judgment rule have substantially reduced the stringency of corporate fiduciary duties. *See, e.g.*, Kleinberger, *supra* note 154, at 739–40.

158. *See* BALOTTI & FINKELSTEIN, *supra* note 97, § 4.16[A].

159. *See id.* § 4.16[B].

160. *See id.* § 4.16[C].

161. *See id.* § 17.3.

162. *See In re* El Paso Pipeline Partners, L.P., C.A. No. 7141-VCL, 2014 WL 2768782, at *19 (Del. Ch. June 12, 2014); *In re* Wayport, Inc. Litig., 76 A.3d 296, 314–15 (Del. Ch. 2013); Latesco, L.P. v. Wayport, Inc., C.A. No. 4167-VCL, 2009 WL 2246793, at *6 (Del. Ch. July 24, 2009).

transactions, directors have a fiduciary duty to disclose all material facts to stockholders.[163] This duty requires a director to fully and fairly reveal all material facts that would have a significant effect upon a stockholder vote.[164] This disclosure duty plays an important role in creating a foundation for fair play.[165] Notwithstanding business judgment deference and liberal statutory exculpation rules, corporate case law and literature on fiduciary duties have played a critically important role in promoting expectations of honesty, forthrightness, and fairness in business entity governance.[166]

With regard to business culture, fiduciary duties have an important, positive *ex ante* role to play in ensuring managerial faithfulness to investor interests.[167] As noted by Professor Lyman Johnson, "[l]oyalty and fairness, moreover, are more than legal duties. They are important personal virtues and social norms in the wider culture, and historically and behaviorally, might well be pre-supposed to exist within a particular business arrangement as well, LLC or otherwise."[168]

The socializing message of the duty of loyalty is unmistakable.[169] *Guth v. Loft*,[170] a corporate opportunity case, reflects this message. In *Guth*, the Delaware Supreme Court noted that "[t]he rule that requires an undivided and unselfish loyalty to the corporation demands that there shall be no conflict between duty and self-interest. The occasions for the determination of honesty, good faith and loyal conduct are many and varied, and no hard and fast rule can be formulated."[171]

Delaware's rich case law, including dicta, articulates the notions of fairness and responsibility underlying Delaware's corporate internal

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163. Stroud v. Grace, 606 A.2d 75, 85 (Del. 1992); *see also* BALOTTI & FINKELSTEIN, *supra* note 97, § 17.3 (remarking that a director's duty of disclosure runs to the stockholders and other directors of the same corporation).

164. S*ee* BALOTTI & FINKELSTEIN, *supra* note 97, § 17.3.

165. *See, e.g.*, VGS, Inc. v. Castiel, No. C.A. 17995, 2000 WL 1277372, at *2–*3 (Del. Ch. Aug. 31, 2000) (enjoining an underhanded squeeze-out in which the defendant directors breached the duty of loyalty by secretively consenting to a merger without informing the plaintiff of a merger that had the effect of divesting the plaintiff of majority control), *aff'd*, 781 A.2d 696 (Del. 2001).

166. *See, e.g.*, MILLER, *supra* note 155, at 143–44.

167. *See id.* (discussing the socializing message of *Jones v. H.F. Ahmason*, 460 P.2d 464 (Cal. 1969)).

168. Lyman Johnson, *Dynamic, Virtuous Fiduciary Regulation* 13 (Wash. & Lee Pub. Legal Studies Research Paper Series, Paper No. 2013–14, 2013), http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2273869 (footnote omitted).

169. *See* Blair & Stout, *Behavioral Foundations*, *supra* note 142, at 1752–53.

170. 5 A.2d 503 (Del. 1939).

171. *Id.* at 510.

governance framework.[172] Further, as Professor Mohsen Manesh observed, several major fiduciary duty cases articulate, through dicta, expectations of directors and best practices.[173] Even in a case such as *In re Disney*, in which the court ruled in favor of the defendants, the court used fiduciary duties to outline best practices in connection with executive compensation determinations.[174]

MLPs' unique features should be changed if there are overriding legal and ethical concerns—particularly where management accountability is at stake and especially in industries that profoundly affect U.S. infrastructure, the environment, and the economy. The legal framework should promote, rather than undermine, doctrines designed to further fundamental notions of trustworthiness, loyalty, and transparency. The Delaware MLP model, coupled with reduced stock exchange oversight,[175] frustrates rather than promotes the socializing functions of the law. Professors Margaret Blair and Linda Stout have long argued that economic interests are best served when the board maximizes the interests of all groups, not just management's own interests.[176] Managers can be expected to do the best job when the regulatory environment demands trustworthy and loyal conduct.[177] In summary, publicly traded corporations offer three major investor protections that are largely lacking in the publicly traded MLP paradigm. These include the benefits of board independence requirements under stock exchange listing rules,[178] the constraints of independent conflicts committee members,[179]

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172. *See* Mohsen Manesh, *Damning Dictum: The Default Duty Debate in Delaware*, 39 J. CORP. L. 35, 55–62 (2013) (discussing Delaware Chancery Court and Delaware Supreme Court dicta and indicating that dicta provides important guidance in the case of ambiguous legal areas, supplies guidelines for best practices, and helps address contemporary concerns).

173. *See id.* at 55 (observing that in several cases, the Delaware Supreme Court's dicta laid the groundwork for the best practice of using an independent committee of the board to negotiate and establish arms-length terms).

174. *Id.* at 55–56.

175. *See* Goodgame, *supra* note 28, at 98; *supra* notes 59–64 and accompanying text.

176. Margaret M. Blair & Lynn A. Stout, *Director Accountability and the Mediating Role of the Corporate Board*, 79 WASH. U. L.Q. 403, 404 (2001) [hereinafter Blair & Stout, *Director Accountability*]; *see also* Steve Lydenberg, *Reason, Rationality, and Fiduciary Duty*, 119 J. BUS. ETHICS 365, 379 (2013) ("Finance as it has evolved under the tutelage of those advocating self-interested rationality has sharpened its laser-like focus on 'beating the markets' and in doing so has become disconnected from the world. This connection needs to be restored through an affirmative conviction that, through the objective principles of reasonable behavior, one's investments can, and indeed should, contribute not only to one's own limited good but to the broader public good as well.").

177. *See* Blair & Stout, *Director Accountability*, *supra* note 176, at 404–05.

178. *See* NASDAQ STOCK MKT. R. IM-5605(b)(1) (2015); NYSE MANUAL, *supra* note 60, § 303A.01.

179. *See* Strine & Laster, *supra* note 109.

and jurisprudence that contains a mandatory duty of loyalty with socializing cues regarding loyal conduct and fair disclosure.[180] The next Section examines the MLP realities that create fertile grounds for overreaching.

B. *Obstacles to Fiduciary Duties and Accountability in MLPs*

Delaware's alternative business entity scheme offers immense advantages for managers and those owning a majority interest in an enterprise.[181] From a limited partner's perspective, however, MLP legal framework carries with it distinct disadvantages. Several major obstacles prevent judicial remedies for inadequate managerial oversight and conflicted transactions. At present, MLPs exist in a regulatory environment that permits management abuse. The discussion that follows exposes (1) the one-sided nature of many MLP agreements, (2) the difficulties in challenging fairness opinions, (3) the problems proving bad faith, (4) the reduced or eliminated duties of disclosure, (5) the difficulties imposing secondary liability, and (6) the limited nature of the implied covenant of good faith and fair dealing.

1. The One-Sided Nature of MLP Agreements

In the sponsored MLP model, the GP may have near-complete governance control, and the investors have few ways of influencing business entity governance.[182] As one expert noted, "[t]he only rational action that a dissatisfied unitholder can take with regard to a sponsored MLP is to vote with her wallet and sell her common units."[183]

A litany of risks may even appear at the beginning of an MLP agreement.[184] For example, the risks in an MLP agreement utilized by El Paso Pipeline are far-reaching.[185] The agreement lists risks associated

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180. *See* DEL. CODE ANN. tit. 8, § 102(b)(7) (2015) (providing that a certificate of incorporation may include a provision "eliminating or limiting the personal liability of a director to the corporation or its stockholders for monetary damages for breach of fiduciary duty as a director, provided that such provision shall not eliminate or limit the liability of a director: (i) For any breach of the director's duty of loyalty to the corporation or its stockholders; (ii) for acts or omissions not in good faith or which involve intentional misconduct or a knowing violation of law; (iii) under § 174 of this title; or (iv) for any transaction from which the director derived an improper personal benefit").

181. *See* Franklin A. Gevurtz, *Why Delaware LLCs?*, 91 OR. L. REV. 57, 104–05 (2012).

182. Goodgame, *supra* note 28, at 86.

183. *Id.*

184. *See, e.g.*, EL PASO PIPELINE PARTNERS, PROSPECTUS, http://www.nasdaq.com/markets/ipos/filing.ashx?filingid=5269554#H48563B4E424B4_HTM_188 (discussing a litany of risks on the first page of the El Paso Pipeline Partners' prospectus).

185. *See id.* ("We may not have sufficient cash from operations following the establishment of cash reserves and payment of fees and expenses . . . to enable us to make cash

with the uncertainty of distributions, the conflict of interest between the GP and the GP's affiliates and parent, the GP's right to compete, and the GP's lack of a duty to present business opportunities.[186]

MLP agreement provisions may also make an investor vulnerable to managerial misconduct. For example, in one agreement, the GP's consent is required to amend the agreement, and there is no fiduciary duty that might otherwise compel the partner's consent;[187] only limited partners holding at least twenty percent of the outstanding units may nominate directors or call meetings;[188] and the GP's consent is required for a merger.[189]

Even more concerning, fiduciary duties are often waived to the fullest extent possible.[190] Two empirical studies demonstrate that firms often waive fiduciary duties without substituting other compensating contractual protections[191]—the protections that Professor Ribstein described as "uncorporate" substitutes.[192] Professor Manesh studied eighty-five publicly traded LPs and LLCs.[193] Only ten of the eighty-five firms did not fully waive or exculpate liability arising from a breach of fiduciary duties.[194] In other words, seventy-five of the eighty-five firms, or 88.24%, had waived or exculpated liability.[195] Also, only twenty-two of the eighty-five companies, or 26%, permitted the right to elect all or a majority of the governing body (i.e., board managers or board of directors).[196] Professors Michelle Harner and Jamie Marincic also analyzed 129 operating agreements of publicly available LLCs.[197] Of the

distributions. . . . We own 10% minority interests in two of our three primary assets, . . . [and a]s a result, we will be unable to control the amount of cash we will receive from those operations. . . . Our natural gas transportation and storage systems are subject to regulation by agencies, . . . which could have an adverse impact on our ability to establish transportation and storage rates. . . . Our general partner and its affiliates, including El Paso Corporation, have conflicts of interest with us and limited fiduciary duties, and they may favor their own interests to the detriment of our unitholders.").

186. *Id.*

187. *See, e.g.*, *id.* at 35.

188. *E.g.*, *id.* at 38.

189. *E.g.*, *id.* at 35.

190. *See, e.g.*, *id.* at app. A-19.

191. *See* Michelle M. Harner & Jamie Marincic, *The Naked Fiduciary*, 54 ARIZ. L. REV. 879 (2012); Manesh, *supra* note 9, at 567.

192. *See* Larry E. Ribstein, *Partnership Governance of Large Firms*, 76 U. CHI. L. REV. 289, 289–90 (2009); Ribstein, *supra* note 16, at 136.

193. Manesh, *supra* note 9, at 567.

194. *Id.* at 575.

195. *See id.* (75/85 ≈ 88.24%).

196. *Id.* at 580–89 (the data was drawn from operating agreements that were available through the Edgar Pro On-Line service).

197. Harner & Marincic, *supra* note 191, at 902.

129 agreements sampled, approximately 73% modified or eliminated fiduciary duties, and 68% authorized members to compete in some manner.[198]

Professor Manesh's research shows that these firms have not adopted alternative investor protections to the degree Professor Ribstein suggested.[199] A total of fifty-nine firms relinquished both fiduciary duties and the right to elect managers.[200] Of these fifty-nine firms, six failed to have either mandatory distribution rights or mandatory liquidation rights, forty used either mandatory distribution rights or mandatory liquidation rights, and only thirteen used both mandatory distribution rights and mandatory liquidation rights.[201] Even if firms made mandatory distributions, their constraining impact is questionable because most of the managers had discretion to make determinations about what constituted "available cash."[202]

MLP contractual practices have left investors with few contractual protections and fewer rights than their corporate counterparts. Corporate stockholders have the protection from the duty of loyalty, voting rights, and dissenters' rights.[203] Stockholders may also seek injunctive relief for violations of the duty of loyalty or violations of the duty of care.[204] Many MLP unitholders have none of these protections. Contemporary contractual practices in MLPs arguably create fertile grounds for opportunistic conduct.

Limited partners are also not in a position to exert market pressure to curb abuses.[205] They often will be subject to a poison pill barring voting for those with at least twenty percent of outstanding units.[206] Further, as noted above, the GP's consent may be necessary for any amendment of the partnership agreement.[207] The GP may be entitled to withhold consent to a merger free of fiduciary obligations.[208] Moreover, limited partners must exercise care to refrain from engaging in management activities,

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198. *Id.* at 906.

199. Manesh, *supra* note 9, at 589.

200. *Id.* at 583.

201. *Id.*

202. *Id.* at 590.

203. *Compare* DEL. CODE ANN. tit. 6, §§ 17-101 to -111 (2015), *with* CAL. CORP. CODE §§ 15911.20–.32 (2014). *But cf.* UNIF. LTD. P'SHIP ACT § 305(a) (NAT'L CONFERENCE OF COMM'RS ON UNIF. STATE LAWS 2001) (stating that a limited partner does not owe fiduciary duties to the limited partnership).

204. *See, e.g.*, *In re* BioClinica, Inc. S'holder Litig., Civil Action No. 8272-VCG, 2013 WL 5631233, at *1 (Del. Ch. Oct. 6, 2013).

205. *See* Goodgame, *supra* note 28, at 98–99.

206. BENNER, *supra* note 26, at 3.

207. *See supra* note 187 and accompanying text.

208. Goodgame, *supra* note 28, at 101.

given that limited liability protection rests on the fact that limited partners are passive.[209]

While it is not impossible to remove an errant GP, the experience of several Chicago pension funds demonstrates that it may be difficult and time-consuming to do so given the partnership agreement's contractual terms. In *DV Realty Advisors LLC v. Policemen's Annuity and Benefit Fund of Chicago*,[210] the limited partners were ultimately successful in removing the GP, but it took years of protracted litigation.[211] Approximately $65.5 million in pension funds had been invested in DV Realty Advisors LLC on behalf of City of Chicago policemen, teachers, and other municipal employees.[212] A consultant issued a report recommending a change in management, observing that there had been chronic financial statement delays, significant management resignation had occurred, and the GP had taken out recourse debt in violation of the LP agreement.[213] Further, there were serious pending lawsuits, and the limited partners' advisory committee had stopped meeting and was described as dysfunctional.[214] The limited partners had a right to remove the managing GP if 75% of the limited partners consented and in good faith determined that the removal was necessary for the best interests of the partnership.[215] The GP challenged the removal, and it took the limited partners from 2009, when the financial statement delays began, until 2013 to successfully remove the GP.[216] The limited partners in *DV Realty* were lucky insofar as the contract permitted them to remove the GP, even if the partnership agreement required a 75% vote.[217]

In other instances, however, MLP agreements may impose even more obstacles for GP removal. For example, agreements may contain clauses that permit the GP to have unilateral authority over agreement amendments, to divest voting rights from limited partners gaining ownership over thresholds, or to prohibit limited partners from proposing stockholder-type resolutions.[218] Given fiduciary duty waivers and other contractual provisions favoring management, it is likely that some limited partners would find GP removal more difficult than it was in *DV Realty*.

209. *Id.* at 100.

210. 75 A.3d 101 (Del. 2013).

211. *See id.* at 111–12.

212. Policemen's Annuity & Benefit Fund of Chi. v. DV Realty Advisors LLC, C.A. No. 7204-VCN, 2012 WL 3548206, at *1 (Del. Ch. Aug. 16, 2012), *aff'd.* 75 A.3d 101 (Del. 2013).

213. *Id.* at 8.

214. *See id.*

215. *See id.* at 10.

216. *See DV Realty*, 75 A.3d at 111.

217. *Id.* at 107.

218. *See* BENNER, *supra* note 26, at 3; Goodgame, *supra* note 28, at 100–01.

2. Difficulty in Challenging Unfair Fairness Opinions

Fairness opinions are increasingly common in MLPs.[219] The use of conflicts committees and third-party opinions bears more than a passing resemblance to the use of typical business judgment rule protections within the corporate context. Delaware corporate law allows both conflicts committees and third-party opinions to shield officers and directors. In particular, Delaware General Corporate Law Section 144(a) contemplates the use of conflicts committees to authorize conflicted transactions,[220] and Section 141(e) shields directors when they rely in good faith on external opinions.[221]

While scholars have described fairness opinions as a best practice, their use can unfairly insulate the GP in self-interested transactions.[222] Many MLP agreements bar inquiry into the GP's conduct if the GP obtains "special approval" from a designated committee to approve the transaction in question.[223] With a corporation, special committee members are typically independent; however, as previously explained, MLP committee members likely have an allegiance to the GP or the MLP's sponsor.[224] Consequently, the presumed lack of bias from a special approval may never materialize.

Unfair fairness opinions have been difficult to challenge.[225] Four 2013

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219. *See, e.g.*, Allen v. Encore Energy Partners, L.P., 72 A.3d 93, 99 (Del. 2013); Gerber v. Enter. Prods. Holdings, LLC, 67 A.3d 400, 406 (Del. 2013), *overruled on other grounds by* Winshall v. Viacom Int'l Inc., 76 A.3d 808 (Del. 2013); Brinckerhoff v. Enbridge Energy Co., 67 A.3d 369, 371 (Del. 2013); Norton v. K-Sea Transp. Partners L.P., 67 A.3d 354, 356 (Del. 2013); Allen v. El Paso Pipeline Partners, L.P., 113 A.3d 167 (Del. Ch. 2014).

220. DEL. CODE ANN. tit. 8, § 1-144(a) (2015) ("No contract or transaction between a corporation and 1 or more of its directors or officers, or between a corporation and any other corporation, partnership, association, or other organization in which 1 or more of its directors or officers, are directors or officers, or have a financial interest, shall be void or voidable . . . if: (1) . . . the board or committee in good faith authorizes the contract or transaction by the affirmative votes of a majority of the disinterested directors.").

221. *Id.* § 1-141(e) ("A member of the board of directors . . . shall . . . be fully protected in relying in good faith upon . . . opinions, reports or statements presented . . . by any other person as to matters the member reasonably believes are within such other person's professional or expert competence and who has been selected with reasonable care by or on behalf of the corporation.").

222. *See* Strine & Laster, *supra* note 109, at 16–17.

223. *Id.* at 16–17 & n.23.

224. *See supra* note 66 and accompanying text.

225. *Compare* Allen v. Encore Energy Partners, L.P., 72 A.3d 93, 110 (Del. 2013) (demonstrating an unsuccessful challenge to fairness opinion), Brinckerhoff v. Enbridge Energy Co., 67 A.3d 369, 373 (Del. 2013) (same), *and* Norton v. K-Sea Transp. Partners L.P., 67 A.3d 354, 369 (Del. 2013) (same), *with* Gerber v. Enter. Prods. Holdings, LLC, 67 A.3d 400, 426 (Del. 2013) (demonstrating a remand by the court on a variety of issues, including those related to the fairness opinion), *overruled on other grounds by* Winshall v. Viacom Int'l Inc., 76 A.3d 808 (Del. 2013). For more information on these unfairness opinions, see Thomas A. Mullen & Janine M. Salomore, *MLPs Take Center Stage in the Delaware Supreme Court*, BUS. L. TODAY (Aug. 2013),

Delaware Supreme Court LP cases involved an independent special committee or conflicts committee that vetted transactions.[226] Each of the committees engaged advisors to render opinions on the value or fairness of the questionable transactions.[227] Despite the special procedures, the limited partners in each case alleged unfairness or deficiency with respect to the transactions.[228] In several of these cases, the MLP contractual standards for fairness opinions were tied to good faith.[229] It may be even harder to establish bad faith in alternative entities, particularly where courts presume compliance with contractual standards if a fairness opinion has been obtained.

In *Brinckerhoff v. Enbridge Energy Co.*, the Court considered, among other things, whether limited partners had adequately pled bad faith in their challenge to a flawed fairness opinion concerning the MLP's equity stake in a joint venture.[230] Here, the court imported the standard for bad faith from prior corporate case law.[231] Consistent with the approach to good faith taken in Delaware's corporate fiduciary duty law, "good faith" is defined by reference to bad faith.[232] As noted in *DV Realty*, in connection with the determination of whether limited partners acted in good faith by removing the GP, the criteria used to define the good faith requirement in an LP agreement focuses on bad faith and whether the conduct falls "so far beyond the bounds of reasonable judgment that it seems essentially inexplicable on any ground other than bad faith."[233]

Delaware courts follow a subjective approach to good faith when an agreement uses it as an express contractual standard of conduct and where the contract does not provide guidance to the contrary.[234] The Delaware Supreme Court has refused to adopt the UCC's definition of good faith that contains not just a subjective dimension but an objective component

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http://www.americanbar.org/publications/blt/2013/08/delaware_insider.html ("Indeed, the safe harbors in MLP agreements are generally designed to encourage and reward good behavior—by putting the decision in the hand of independent directors and encouraging reliance on expert advice. . . . not unlike . . . Sections 141(e) and 144 of the Delaware General Corporation Law, which similarly encourages reliance on experts and independent decision makers in conflict situations.").

226. *Encore*, 72 A.3d at 95–96; *Gerber*, 67 A.3d at 405; *Brinckerhoff*, 67 A.3d at 371; *Norton*, 67 A.3d at 357.

227. *See Encore*, 72 A.3d at 99; *Gerber*, 67 A.3d at 406; *Brinckerhoff*, 67 A.3d at 371; *Norton*, 67 A.3d at 356.

228. *See Encore*, 72 A.3d at 99; *Gerber*, 67 A.3d at 406; *Brinckerhoff*, 67 A.3d at 371; *Norton*, 67 A.3d at 356.

229. *See, e.g.*, *Encore*, 72 A.3d at 101.

230. 67 A.3d at 370.

231. *See id.* at 373 (quoting Parnes v. Bally Entm't Corp., 722 A.2d 1243, 1246 (Del. 1999)).

232. *See id.*

233. 75 A.3d at 110 (quoting *Brinckerhoff*, 67 A.3d at 373).

234. *See id.* at 107.

as well.[235] As noted by Chief Justice Strine, "the term good faith has long been used as the key element in defining the state of mind that must motivate a loyal fiduciary."[236]

Bad faith is a difficult standard to meet for corporate stockholders and limited partners alike, but limited partners face additional complexities due to elaborate partnership agreements. Instead of a single statutory criterion under Section 102(b)(7), limited partners must navigate the specific language contained in the agreement. For example, in *Norton v. K-Sea Transportation Partners, LP*,[237] the GP obtained a fairness opinion, and the transaction was approved pursuant to an elective special approval process contained in the agreement.[238] The Delaware Supreme Court analyzed the interactions between a broad discretion clause, an over-arching clause that authorized decisions reasonably believed to be in the partnership's best interests, a clause exculpating conduct in good faith, an elective provision for obtaining special approval, and an additional clause providing that nothing in the contract required the GP to consider the interests of any person other than the partnership.[239] Ultimately, the Delaware Supreme Court affirmed the Chancery Court's dismissal.[240]

Unique contractual language makes it more difficult to predict outcomes. Some agreements might require GPs to "reasonably believe" that a transaction is in the partnership's best interests; others may have entirely different formulations.[241] While the definition of good faith in a corporate setting has always been murky at best, there is the potential for even greater uncertainty in the MLP context given the variety of contractual terms employed and the nuances between one contract and the next.

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235. *See id.* at 111.

236. *See* Strine et al., *supra* note 102, at 633.

237. 67 A.3d 354 (Del. 2013).

238. *Id.* at 356, 358.

239. *See id.* at 361–63, 368.

240. *See id*. at 369.

241. *See* Strine & Laster, *supra* note 102, at 5, 12. Under the special approval process, obtaining a fairness opinion creates the presumption of good faith. *See Norton*, 67 A.3d at 366. Further, the court concluded that the GP was conclusively presumed to have exercised good faith by choosing to invoke the special approval process. *Id.* at 367–68. There was a provision that did not require a consideration of interests other than those of the partnership. *Id.* at 363. The court determined that the opinion properly addressed the fairness as a whole, and the fairness opinion was not required to have addressed the fairness of certain Incentive Distribution Rights (IDR) that were payable to the GP. *Id.* at 368. *Cf.* Gerber v. Enter. Prods. Holdings, LLC, 67 A.3d 93 (2013).

3. Difficulty in Proving Bad Faith

In addition to added burdens due to complexity, MLP unitholders may face a slightly different burden than corporate stockholders in asserting "bad faith" using a conscious disregard theory. In *Allen v. Encore Energy Partners, L.P.*,[242] the contract required the GP to consent to a merger in accordance with the contract's good faith standard.[243] The contract defined good faith as a "belie[f] that the determination or other action is in the best interests of the Partnership."[244] Thus, the key requirement was subjective good faith.

A conflicts committee approved the merger in *Encore*, and the court determined that the conflicts committee's approval satisfied the defendants' contractual duties so long as the independent directors acted with subjective good faith.[245] The court recognized two ways of proving lack of subjective good faith. First, the plaintiffs could introduce evidence of a bad motive—the committee approved the merger knowing that it was against the partnership's interests.[246] Second, the plaintiffs could introduce evidence that the defendants consciously disregarded their duty to form a subjective belief that the merger was in the partnership's best interests.[247] The court observed that this type of dereliction is different from the conscious disregard of duties in the case of corporations.[248] In the corporate arena, the court explained that an intentional dereliction of one's duties is conduct falling between gross negligence and bad faith, and that such an intentional dereliction of duty is conduct in bad faith—therefore non-exculpable under Delaware's corporate law.[249]

In *Encore*'s contractual setting, however, there were no fiduciary duties because they had been contractually eliminated.[250] The court believed that absent a showing that the defendants believed that the merger was against the partnership's interests, the plaintiffs did not have

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242. 72 A.3d 93 (Del. 2013).

243. *Id.* at 101. Encore Energy Partners, LP (Encore) was a publicly traded Delaware LP engaged in the acquisition and development of oil and natural gas in the United States. *Id.* at 96. Vanguard initially acquired Encore's GP, a Delaware LLC, as well as forty-six percent of Encore from a third party. *Id.* Thereafter, Allen, representing the limited partners as plaintiffs, contended that the GP had intentionally made inaccurate negative public disclosures that depressed Encore's price and had violated its contractual duty of good faith in its approval of a subsequent merger of Encore with Vanguard. *Id.* at 97.

244. *Id.* at 101 (alteration in original); *see also Norton*, 67 A.3d at 362 (involving a standard tied to "reasonable" belief).

245. *Encore*, 72 A.3d at 99, 102.

246. *Id.* at 104.

247. *See id.* at 105–06.

248. *See id.* at 106.

249. *Id.* at 105.

250. *See id.* at 100.

to show that the conflicts committee consciously disregarded its duties.[251] Instead, the plaintiffs merely had to show that the committee *consciously disregarded their duty to form a subjective belief* that the merger was in the partnership's best interests.[252] The court itself admitted the difficulty in presenting such proof, saying that "it would take an extraordinary set of facts to do that."[253]

Proof of bad faith is both similar and different in corporate and alternative entity settings. Proving a bad motive (i.e., purposeful action to approve a transaction against the entity's interests) appears to be roughly the same in corporate and non-corporate contexts. The conscious disregard theory for showing bad faith, however, likely differs between a corporate setting and an alternative entity setting where fiduciary duties have been contractually replaced with a subjective good faith standard such as the one employed in *Encore.* In such an event, there would be no need to show that one was derelict in discharging one's fiduciary duties. There would be no duties. Instead, there would merely be a need to show that one has been derelict in complying with the contractual duty to form a subjective belief as to whether a transaction was in the best interests of the entity.

Is there a meaningful difference between a conscious disregard of the fiduciary duty to further a corporation's best interests and a dereliction of the duty to form a subjective belief that a transaction is in an alternative business entity's best interests? What "extraordinary set of facts" would show a dereliction in the duty to form a subjective belief? Would it take a total failure to appoint a conflicts committee altogether to establish dereliction to form the required subjective belief? What if a committee was appointed and convened for one hour? At the borders, dereliction to form a subjective intent to determine whether a transaction is in the best interests of the MLP may blend into purposeful bad faith conduct.

Thus far, it appears that only extreme misconduct will be sufficient to establish a failure to form a subjective belief that a contractual standard of good faith was met. The court in *Encore* observed:

> Plaintiffs could have argued that the price is unfair and Jefferies was incompetent and that there was *no* basis for relying on the Jefferies analysis. That's not at all what [p]laintiffs argue. . . . [T]he fact that where they ended up was within a range of fair value doesn't answer the proposition that they were ineffective and not-in-good-faith

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251. *See id.* at 105–06.

252. *Id.*

253. *Id.* at 106.

bargaining agents.[254]

Merely shoddy negotiations by a conflicts committee or submission of a counteroffer showing only a meager exchange ratio improvement was not enough to conclude that the conflicts committee members subjectively believed they were acting against the LP's interests.[255]

The starting point for ascertaining whether a contractual standard of a subjective good faith belief exists must be the contract itself and any relevant guidance from the agreement. Beyond that, *Encore* clarifies that objective facts do have a role to play even where a contract calls for only a "subjective belief" rather than "a reasonable belief." The court observed that "objective factors may inform an analysis of a defendant's subjective belief to the extent they bear on the defendant's credibility when asserting that belief."[256] Facts demonstrating that directors *knew* that a transaction was not in the partnership's best interests and took the action *nonetheless*, *or* circumstances showing that a committee disregarded key information[257] or blindly rubber-stamped a proposed sales value might be indicative of a failure to form a subjective belief that a transaction was in the MLP's best interests.[258]

For example, in *In re El Paso Pipeline Partners*, the El Paso parent corporation sold a 51% interest in its subsidiary to the El Paso MLP in a March transaction in which the parent "dropped down" the 51% interest in the subsidiary to the MLP.[259] Thereafter, in a November transaction, the parent "dropped down" the remaining 49% interest in the subsidiary.[260] A conflicts committee approved both drop-downs pursuant to the MLP agreement, permitting the committee to approve conflicted transactions if it determined that the transaction would be in the best interests of the MLP.[261]

The Chancery Court's different reactions to the March and November transactions provide insight into the sort of conduct that may be indicative of a conscious disregard of the duty to form a subjective belief that a conflicted transaction is in an MLP's best interest. With regard to the earlier March drop-down, the conflicts committee had not discounted the value of certain service agreements, even though only seventeen percent

254. *Id*. at 108 n.56 (alterations in original) (emphasis added).

255. *See id.* at 108.

256. *Id.* at 107.

257. *In re* El Paso Pipeline Partners, L.P Derivative Litig., C.A. No. 7141-VCL, 2015 WL 1815846, at *15 (Del. Ch. Apr. 20, 2015).

258. *Id.* at *16.

259. *Id.* at *1.

260. *Id*.

261. *Id.*

of the revenue stream was guaranteed.[262] However, the court observed that the conflicts committee's judgment to ignore discounting was not so extreme as to support an inference of bad faith.[263] Reasonable minds could differ as to the assessment of risk and hence the value of service agreements.[264] Thus, the court granted summary judgment in favor of the GP with regard to the March drop-down.[265]

The Chancery Court's view of the November drop-down was quite another matter. The court refused to grant summary judgment as to the November drop-down and wanted to more fully develop the facts of the case.[266] When it did, the court concluded that the committee members had failed to provide a credible account of their evaluation of the November drop-down.[267] The court noted that the conflicts committee did more than negotiate poorly.[268] By November, the committee had received market evidence that the MLP had overpaid for the subsidiary.[269] The committee knew and ignored the fact that recent transactions had used materially lower multiples than those used in the estimation of the proposed price.[270] One committee member shared his opinion via email with two other members that it was not in the MLP's best interest "to have too much of its assets tied up in the [liquidated natural gas] trade."[271] Although the committee members believed that the November drop-down would result in increased revenue flow to the MLP, they failed to consider whether the MLP was paying a fair price or to assess the deal's long-term potential to add value.[272] Moreover, the court was highly critical of the financial analyst's work product, observing that the analyst did not use appropriate numbers in the analysis[273] and had merely sought to justify the parent company's asking price.[274] Ultimately, the committee had allowed the price of the March drop-down to set the bar for the November drop-down.[275] This was highly inappropriate because the November drop-

262. *In re* El Paso Pipeline Partners L.P. Derivative Litig., C.A. No. 7141-VCL, 2014 WL 2768782, at *13 (Del Ch. June 12, 2014).

263. *Id.* at *14.

264. *Id.*

265. *Id*. at *16.

266. *Id.* at *2.

267. *In re* El Paso Pipeline Partners, L.P. Derivative Litig., C.A. No. 7141-VCL, 2015 WL 1815846, at *1 (Del. Ch. Apr. 20, 2015).

268. *Id.* at *19.

269. *Id.*

270. *Id.*

271. *Id.* at *17.

272. *See id.* at *18.

273. *Id.* at *24.

274. *Id.* at *21.

275. *Id.* at *20.

down involved a minority interest and not a majority interest.[276] Additionally, the market for liquidated natural gas had deteriorated in the interim.[277]

Clearly, the *El Paso* litigation illustrates that courts may scrutinize the committees' processes (including emails),[278] challenge assumptions made by financial analysts,[279] and make credibility judgments with regard to testimony.[280] Nevertheless, proof of subjective bad faith continues to be difficult for limited partners to establish. As previously stated, the Delaware Supreme Court has noted the difficulty of demonstrating a dereliction of a contractual duty to form a subjective belief that a transaction is in an MLP's best interests.[281] Further, the court has cautioned against superimposing common law fiduciary duties onto a contractual relationship where contractual standards have replaced fiduciary duties.[282] What courts find problematic in one set of contractual circumstances may not necessarily create difficulties in another contractual context.[283] Thus, it may be difficult for an MLP unitholder to evaluate the strength of her case against a conflicts committee in all but the most egregious of circumstances. By the same token, it may be difficult to distill a universal composite of best practices given variations among contractual settings.

4. No Affirmative Duty of Disclosure

In addition to providing insight into the determination of whether a conflicts committee had a subjective belief that a transaction was in an MLP's best interests, the first *El Paso* decision highlights the difference

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276. *Id.*

277. *Id.*

278. *Id.* at *17.

279. *Id.* at *24.

280. *Id.* at *16.

281. Allen v. Encore Energy Partners, L.P., 72 A.3d 93, 105–06 (Del. 2013).

282. *Id.* ("Furthermore, Section 7.9(b) and (e) [of the contract] together replace any common law fiduciary duties with a contractual duty of subjective good faith. Given this explicit language, it is clear that only the contractual duty, not contract or tort law standards, would govern the Conflicts Committee's action."). The court has used corporate precedents to interpret an MLP contractual standard requiring that special committee members believe in good faith that the transaction was in the best interests of the MLP. The court used the corporate precedents to describe the necessary showing of committee members' subjective beliefs. *See In re El Paso Litig.*, 2015 WL 1815846, at *15 (quoting *In re* Walt Disney Co. Deriv. Litig., 906 A. 2d 27, 64 (Del. 2006)).

283. *See, e.g.*, *In re El Paso Litig.*, 2015 WL 1815846 at *16 ("In this case, the trial record revealed numerous problems with the [November] Dropdown. None of these problems, standing alone, would have supported a finding that the Committee members did not act in subjective good faith. Even a combination of problems would not have been sufficient to overcome the presumption of good faith and the testimony of the Committee members.").

between disclosure obligations under the duty of loyalty and the narrow implied contractual covenant of good faith and fair dealing.[284] In *El Paso*, the plaintiffs alleged that the parent company had not informed the conflicts committee that the parent company had failed to exercise its right of first refusal to buy into another liquid natural gas terminal at a substantially lower price.[285] The plaintiffs argued that this failure to inform the conflicts committee was evidence of a violation of subjective good faith.[286] The court refused to accept the argument.[287] The court indicated that because the parties waived their fiduciary duties and had a contractual relationship, the general rules regarding disclosure in contractual relationships applied.[288] In a contractual relationship, "similarly situated counterparties have no duty to . . . disclose private information to the other."[289]

The plaintiffs argued that the parent company violated the implied covenant of good faith and fair dealing because the parent company intentionally concealed material information from the conflicts committee regarding the parent's own failure to purchase another liquid gas terminal. The court observed that, "[a]bsent contractual modification, a general partner owes fiduciary duties that include a 'duty of full disclosure.'"[290] The court believed that had the parties intended such affirmative disclosure obligations, they should have expressly stated them in the contract.[291]

As more fully discussed below in Part III, it is particularly troubling that managers of publicly traded alternative business entities may shield themselves from liability even where they have failed to affirmatively disclose all material information. Investors' only recourse would be an action for common law fraud.[292] Investors who have waived all fiduciary duties may not realize that if they want the benefits of full disclosure, they must ensure that the governing agreement expressly contains contractual duties to disclose.[293] Because GPs normally have a duty of full disclosure, MLP unitholders may simply assume that the GP would disclose all

284. *See In re* El Paso Pipeline Partners, L.P. Derivative Litig., C.A. No. 7141-VCL, 2014 WL 2768782, at *7, *9–*10, *14–16 (Del. Ch. June 12, 2014).

285. *See id.* at *7.

286. *See id.*

287. *See id.*

288. *See id.* at *21.

289. *See id.*

290. *Id.* (quoting Sussex Life Care Assocs. v. Strickler, CIV. A. No. 911, 1988 WL 156833, *4 (Del. Ch. June 13, 1989)).

291. *Id.*

292. *Id.*

293. *See id.*

relevant information.[294] However, the Delaware Chancery Court has made it clear that the implied covenant of good faith and fair dealing does not support a generalized duty to disclose all material information reasonably available.[295] It is doubtful that investors in publicly traded alternative business entities fully appreciate the legal rights they have relinquished.

5. Problems with Primary and Secondary Liability

With little protection from opportunistic conduct, some limited partners have sought to hold the GP's or sponsor's directors liable.[296] Critics have called the emergence of secondary liability claims in alternative business entities against directors of the governing entity "a particularly odd pattern of routine veil piercing."[297] They observed that under principles of corporate governance, a governing fiduciary's directors would not be directly liable to plaintiffs unless there were reasons for piercing the corporate veil of limited liability.[298]

Plaintiffs have sought to impose direct liability upon MLP GPs and secondary liability upon the directors of the GP by arguing that the directors aided and abetted a breach of a contractual fiduciary duty or tortuously interfered with the MLP contract.[299] Direct and secondary liability claims have been difficult to support where investors waived fiduciary duties.[300] Nevertheless, plaintiffs continue to allege that defendants have violated the implied covenant of good faith and fair dealing, and to assert secondary claims against individual defendants.[301]

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294. *See id.*

295. *See id.* at *21–*22 ("[T]he plaintiffs cannot rely on the implied covenant to fill the gap in the LP Agreement with a mandatory disclosure requirement. The gap exists by design to replicate an arm's-length, non-fiduciary negotiation.").

296. *See generally* Collin P. Marks, *Piercing the Fiduciary Veil*, 19 LEWIS & CLARK L. REV. 74 (2015) (discussing when "second-tier managers" of alternate entities should have fiduciary duties imposed).

297. Strine & Laster, *supra* note 109, at 19.

298. *Id.* at 19–20.

299. *See, e.g.*, Allen v. El Paso Pipeline, GP Co., 113 A.3d 167, 182 (Del. Ch. 2014) (involving an agreement that presumed that the conflicts committee was acting in good faith unless the plaintiffs rebutted the presumption). The court concluded that there was no evidence that the conflicts committee did not believe that the transaction was in the MLP's best interest and that the implied covenant of good faith was not violated because the fairness opinion that had been obtained did not address the dilution that the limited partners would suffer. *Id.* at 182, 192–93.

300. *E.g.*, *id.* at 174.

301. *See, e.g.*, Gerber v. Enter. Prod. Holdings, LLC, 67 A.3d 400 (Del. 2013), *overruled on other grounds by* Winshall v. Viacom Int'l Inc., 76 A.3d 808 (Del. 2013). The *Gerber* court concluded that a contractual presumption of "good faith" does not bar a claim for a breach of the implied covenant of good faith and fair dealing. *Id.* at 418. The court used a different temporal

Moreover, some of the governing instruments can be interpreted as permitting liability for gross negligence.[302] Thus, in some measure, the ability to eliminate fiduciary duties has introduced considerable uncertainty in the law—the very result that contractual freedom was intended to rectify.[303]

Secondary liability claims against directors of a GP or special committee members have raised particular concern because they may be asserted against individual defendants.[304] Secondary liability claims originate in the case of *In re USACafes, L.P. Litigation*.[305] *In re USACafes* involved limited partners suing a corporate GP and the individual directors of the corporate GP on the grounds that they had received certain side payments that should have been paid to the partnership.[306] The Chancery Court upheld a claim for a breach of a fiduciary duty against the director of the corporate GP, relying heavily on precedents involving trust law.[307] After *In re USACafes*, the court held a director of a GP liable in connection with a hedge fund in *Paige Capital Management, LLC v. Lerner Master Fund, LLC*.[308] In *Paige*, Michelle Paige and her husband controlled a series of LLCs to manage a hedge fund.[309] A conflict arose when the plaintiff investor wanted to withdraw funds after three years.[310] The court applied the principle that a director, manager, or officer of a GP who exercises control over an LLC's property owes fiduciary duties directly to the LLC and its owners.[311]

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focus when evaluating violations of good faith in connection with the implied covenant, since good faith in the implied covenant sense looks back to the time of original negotiations. *Id.* In contrast, good faith as an express contractual standard looks ahead to the time that the violation or wrong occurred. *See id.* at 418–19.

302. *See* Strine & Laster, *supra* note 109, at 18–19.

303. *Id.* at 22; *see also* Mullen & Salomore, *supra* note 225 (observing that the remanding of *Gerber* was "particularly troubling, given that MLP general partners are typically judgment-proof shell entities and the directors and controlling parents are the principal actors on behalf of the MLP").

304. *See, e.g.*, *In re* El Paso Pipeline Partners, L.P. Derivative Litig., C.A. No. 7141-VCL, 2014 WL 2768782, at *3–*4, *13 (Del. Ch. June 12, 2014).

305. 600 A.2d 43, 47–48 (Del. Ch. 1991).

306. *Id.* at 46.

307. *Id.* at 48–49.

308. Civil Action No. 5502-CS, 2011 WL 3505355, at *2 (Del. Ch. 2011).

309. *Id.* at *3.

310. *Id.* at *8. The plaintiff had signed a separate "Seeder Agreement" that permitted such withdrawal. *Id.* at *1. However, the LP agreement contained a Gate provision that prohibited withdrawal if more than twenty percent of funds were withdrawn within a six-month period. *Id.* Michelle Paige and her husband were not parties to the Seeder Agreement or to the LP agreement. *Id.* However, Michelle Paige was the managing partner of the entity that invoked the Gate provision that barred the plaintiff's withdrawal of funds. *See id.* at *13.

311. *Id*. at *29–*30.

In *Gotham Partners v. Hallwood Realty Partners*, the Delaware Supreme Court concluded that "where a corporate General Partner fails to comply with a contractual standard [of fiduciary duty] that supplants traditional fiduciary duties and the General Partner's failure is caused by its directors and controlling stockholder, the directors and controlling stockholders remain liable."[312] Support for the position rested on a prior Delaware Chancery Court decision that clearly stated that a claim for aiding and abetting a breach of a fiduciary duty is not dependent on the origin of the underlying fiduciary duty.[313] However, *Gotham Partners* and the precedents on which it rested arose before the Delaware legislature amended the statute to permit the elimination of fiduciary duties.[314]

Since *Gotham Partners,* the Court of Chancery has not recognized claims for aiding and abetting breaches of contract. Indeed, in both *Zimmerman v. Crothall*[315] and *Allen v. El Paso Pipeline GP Co.*,[316] the Court of Chancery, citing *Gotham Partners,* definitively stated that Delaware does not recognize claims for aiding and abetting a breach of contract.[317] In reaching this conclusion, Vice Chancellor Laster has distinguished hybrid situations involving cases where an agreement may substitute a duty or may present its own metric for fiduciary duty compliance from cases in which the agreement expressly waives all traditional duties.[318] Where the agreement establishes a purely contractual relationship and thus includes a contractual elimination of fiduciary duties, the Chancery Court's position is that "a claim for aiding and abetting cannot be used to expand the possible range of defendants."[319]

The Court of Chancery currently has another opportunity to revisit the question of whether a claim for aiding and abetting the breach of a contractual fiduciary duty can be sustained where the relevant agreement purports to contractually eliminate fiduciary duties. In *Gerber v.*

312. Gotham Partners, L.P. v. Hallwood Realty Partners, L.P., 817 A.2d 160, 173 (Del. 2002) (alteration in original) (quoting Gotham Partners, L.P. v. Hallwood Realty Partners, L.P., 795 A.2d 1, 34 (Del. Ch. July 18, 2001)).

313. *See id.* at 172 (citing Fitzgerald v. Cantor, No. CIV. A. 16297-NC, 1999 WL 182573, at *1 (Del. Ch. Mar. 25, 1999)).

314. *See* MILLER, *supra* note 155, at § 1.3.

315. C.A. No. 6001-VCP, 2012 WL 707238 (Del. Ch. Mar. 27, 2012).

316. 113 A.3d 167 (Del. Ch. 2014).

317. *Zimmerman*, 2012 WL 707238, at *19 (citing *Gotham Partners*, 817 A.2d at 172); *Allen*, 113 A.3d at 193 (citing *Gotham Partners*, 817 A.2d at 172).

318. *See, e.g.*, *Allen*, 113 A.3d at 193–94.

319. *Id.* at 194.

Enterprise Products Holdings, LLC,[320] the Delaware Supreme Court remanded the question of whether non-GP defendants might be liable for aiding and abetting a breach of contract or for tortious interference due to a breach of the implied covenant of good faith and fair dealing.[321] The court did so, notwithstanding the fact that the Delaware Chancery Court had previously found that the applicable LP agreement had supplanted fiduciary duties with a contractual criterion resting on a belief in the best interests of the partnership.[322] It remains unclear how the Delaware Chancery Court and the Delaware Supreme Court will reconcile their views regarding the development of the aiding and abetting cause of action.

Even where an agreement does not eliminate fiduciary duties, an aiding and abetting theory for contractual fiduciary duties creates uncertainty for both limited partners and for management. It may be difficult to distinguish an agreement's purely contractual language from language that amounts to a contractual fiduciary duty. Assuming the contract has not eliminated fiduciary duties, an aiding and abetting claim may still be difficult to support given that plaintiffs must prove: "'(1) the existence of a fiduciary relationship, (2) a breach of the fiduciary's duty, . . . (3) knowing participation in that breach by the [non-fiduciary] defendants,' and (4) damages proximately caused by the breach."[323] An alternative theory of secondary liability lies in a claim for tortious interference with a contract; however, tortious interference is equally difficult to establish.[324]

Ironically, contractual freedom has generated a great deal of uncertainty and presents significant legal risks to investors of publicly traded MLPs. As a result, some have suggested reinstating a corporate-like duty of loyalty subject to the business judgment rule and a default standard of no liability in the case of a breach of the duty of care in diversely-held alternative entities.[325]

320. 67 A.3d 400 (Del. 2013), *overruled on other grounds by* Winshall v. Viacom Int'l Inc., 76 A.3d 808 (Del. 2013).

321. *Id.* at 425–26.

322. *Id.*

323. Malpiede v. Townson, 780 A.2d 1075, 1096 (Del. 2001) (omission in original) (quoting Penn Mart Realty Co. v. Becker, 298 A.2d 349, 351 (Del. Ch. 1972)).

324. Tortious interference with contracts requires proof of (1) a valid contract, (2) knowledge of the contract, (3) intentional conduct that is a significant factor in causing the breach, (4) a lack of justification, and (5) resulting injury. Beard Research Inc. v. Kates, 8 A.3d 573, 605 (Del. Ch. 2010).

325. *See, e.g.*, Strine & Laster, *supra* note 109, at 30.

6. The Judicial Role and the Implied Covenant of Good Faith

MLP agreements that use the good faith standard have required differentiating the definition of "good faith" as an express contractual term from "good faith" as used in the implied contractual covenant of good faith and fair dealing. In *Gerber*, the Delaware Supreme Court distinguished an express contractual standard of good faith from the good faith reflected in the implied contractual covenant.[326] The case preserves the role of the judiciary by preventing a contractual presumption in a partnership agreement from barring judicial inquiry into whether there has been a violation of the implied covenant of good faith and fair dealing.[327] However, *Gerber* also reinforces the notion that the implied covenant of good faith and fair dealing is not an equitable doctrine to recalibrate the parties' duties in the interest of fairness.[328]

In *Gerber*, the LP agreement contained a contractual presumption that if the GP obtained a fairness opinion with respect to the transaction, it would satisfy the contractual fiduciary duty of care.[329] The GP obtained a fairness opinion, but the opinion addressed only the overall fairness from a financial standpoint and not the fairness of the distinct components of the transaction, such as the fairness of prior transactions from the standpoint of the limited partners.[330] The Delaware Supreme Court reversed the Chancery Court's dismissal of the case and established that an important temporal difference exists between the judicial inquiry of whether a party has breached an express contractual standard of good faith and whether a party has breached good faith as an implied term in the contractual covenant of good faith and fair dealing.[331] Like a common law fiduciary duty, an express contractual duty of good faith looks to the conduct at the time of the alleged wrong.[332] However, the breach of the implied covenant of good faith and fair dealing looks backward to the initial time of contracting, asking what the parties would have agreed to during initial negotiations had they thought to address the issue or

326. *Gerber*, 67 A.3d at 417–18.

327. *See id.*

328. *See id.* at 421–22.

329. *Id.* at 419–20.

330. *Id.* at 406–08. Beginning in 2007, Enterprise GP Holdings, L.P. (EPE) acquired a Texas LLC, Teppco, for $1.1 billion worth of EPE limited partnerships units. In 2009, EPE L.P. sold Teppco to Enterprise Products, L.P. for only $100 million dollars, a mere nine percent of the original purchase price. *Id.* at 406. Thereafter in 2010, EPE's merger into Enterprise Products, L.P. used an exchange ratio that did not recognize any value to the claims held by EPE unitholders. *Id.* at 407–08. A fairness opinion was obtained from Morgan Stanley that stated that the 2009 sale was fair from a financial standpoint but expressed *no opinion* with respect to the *fairness to EPE or its limited partners of any particular component* of the consideration. *Id.*

331. *Id.* at 418.

332. *Id.*

issues.[333] The court concluded that, at the time of contracting, the parties would have reasonably expected that the fairness opinion would have addressed the fairness of the consideration paid to the limited partners in the sale that preceded the merger.[334]

Although *Gerber* leaves open the judicial inquiry into the implied covenant of good faith and fair dealing, the doctrine does not carry with it the affirmative duty of disclosure provided by the traditional duty of loyalty.[335] Moreover, it does not appear that MLP investors can expect much protection from the "fair dealing" component of the implied covenant. Little attention has been placed upon the requirement of fair dealing.[336] It is open to question whether this omission is because (1) good faith subsumes fair dealing; (2) courts intentionally eschew fair dealing, perhaps because the term arguably introduces morality and uncertainty; or (3) courts inadvertently—and perhaps conveniently—disregard fair dealing.

Under the *Restatement (Second) of Contracts*, there is no separate definition provided for fair dealing. Good faith appears to subsume fair dealing and includes reasonable expectations and community standards.[337] The comment to Section 205 provides:

> Good faith is defined in Uniform Commercial Code § 1-201(19) as "honesty in fact in the conduct or transaction concerned." . . . Uniform Commercial Code §2-103(1)(b) provides that good faith means "honesty in fact and the observance of reasonable commercial standards of fair dealing in the trade." The phrase "good faith" is used in a variety of contexts, and its meaning varies somewhat with the context. Good faith performance or enforcement of a contract emphasizes faithfulness to an agreed common purpose and consistency with the justified expectations of the other party; it excludes a variety of types of conduct characterized as involving "bad faith" because they violate community standards of decency, fairness or reasonableness. The appropriate remedy for a breach of the duty of good faith also varies with the circumstances.[338]

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333. *Id.*

334. *Id.* at 422.

335. *See* Mohsen Manesh, *Express Contract Terms and the Implied Contractual Covenant of Delaware Law*, 38 DEL. J. CORP. L. 1, 4–6 (2013) (noting that the doctrine of implied covenants is largely defined and that under Delaware law, "the express terms of every contract must be judicially construed").

336. *See infra* Part III.

337. RESTATEMENT (SECOND) OF CONTRACTS § 205 cmt. a (AM. LAW. INST. 1981).

338. *Id.*

At least in the early years of discussion, fairness or reasonableness played a viable role in defining good faith and fair dealing.[339] This, however, has fostered concerns that courts will use concepts such as reasonable expectations to redesign the parties' contracts.[340]

The Delaware Supreme Court has already rejected the UCC's definition of good faith and fair dealing in connection with the interpretation of an LP's express requirement of good faith when used as a contractual standard.[341] It is quite likely that the Delaware Supreme Court will similarly eschew the UCC's definition of good faith and fair dealing in connection with alternative entity internal governance.

Care should be taken to resist the judicial temptation to use good faith to create a fair and equitable result. Judge Frank Easterbrook has argued for restraint in interpreting good faith to preserve the parties' rights to structure their own affairs and to preserve the advantages flowing from freedom of individual action.[342] In fact, in addition to flow-through taxation, the desire for contractual certainty has been one of the central goals of the alternative business entity revolution.[343] Therefore, an overly expansive judicial definition of the implied covenant of good faith is likely to undermine the policy interests served by most alternative business entity statutes. Nevertheless, overly formalistic interpretations can betray the very purposes of a contract and can lead to the denial of the benefits of the bargain. A focused judicial inquiry into the parties' reasonable expectations at the time of contracting is important in preserving the judicial role, and such inquiry does not threaten the policy interest in respecting contractual freedom.

The role of equitable powers of the court should not be overlooked in alternative business entity jurisprudence. For example, the Chancery Court has recognized that an assignee who had lacked standing under Delaware's LLC statute nevertheless had standing to seek a judicial

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339. *See, e.g.*, Melvin A. Eisenberg, *The Duty of Good Faith in Corporate Law*, 31 DEL. J. CORP. L. 1, 25 (2006); Robert M. Phillips, Comment, *Good Faith and Fair Dealing Under the Revised Uniform Partnership Act*, 64 U. COLO. L. REV. 1179, 1216 (1993); Robert S. Summers, *The General Duty of Good Faith—Its Recognition and Conceptualization*, 67 CORNELL L. REV. 810, 826 (1981) ("[T]he good-faith requirement serves: 1) 'faithfulness to an agreed common purpose and consistency with the justified expectations of the other party,' and 2) 'community standards of decency, fairness or reasonableness.'" (quoting RESTATEMENT (SECOND) OF CONTRACTS § 205 cmt. a)).

340. *See, e.g.*, Carolyn Edwards, *Freedom of Contract and Fundamental Fairness for Individual Parties: The Tug of War Continues*, 77 UMKC L. REV. 647, 689 (2009).

341. DV Realty Advisors LLC v. Policemen's Annuity & Benefit Fund, 75 A.3d 101, 109 (Del. 2013) (involving the interpretation of good faith as an express contractual standard).

342. Edwards, *supra* note 340, at 688–89 (citing Kham & Nate's Shoes No. 2, Inc. v. First Bank of Whiting, 908 F.2d 1351, 1357 (7th Cir. 1990)).

343. *See* MILLER, *supra* note 155, at § 1.1.

dissolution in equity.[344] However, the express terms of an operating agreement are of extreme importance to business planners who seek certainty in business relationships.[345] Undoubtedly there would be an uproar if courts turned the implied covenant of good faith and fair dealing into a broad-based equitable remedy where the business community desires certainty in the law. Even if courts eschew the UCC definition of the implied covenant, there may nevertheless be a role for reasonable commercial standards to play in the inquiry of whether a party has breached the implied covenant or has breached an express contractual standard tied to subjective good faith. In *Encore,* the court went out of its way to state that objective facts can inform the analysis of whether a party's actions satisfy the express contractual standard of subjective good faith.[346] Additionally, objective facts may inform the analysis of whether, at the time of contracting, the parties would have agreed to proscribe the conduct that subsequently formed the basis of the plaintiff's complaint.[347] In determining the parties' reasonable expectations, reasonable commercial standards may provide a useful point of reference. As discussed below, restoring the duty of loyalty, at least in publicly traded alternative business entities, may be an important next step in eliminating courts' temptations to turn to the implied covenant of good faith to protect the spirit of the contract. Chief Justice Strine and Vice Chancellor Laster made this very point based on their extensive experience presiding over alternative business entity legislation.[348]

III. PUBLICLY TRADED MLPS NECESSITATE FIDUCIARY DUTIES

Publicly traded corporations offer three major investor protections: board independence requirements under stock exchange listing rules,[349] constraints on independent conflicts committee members,[350] and duty of

344. *See In re* Carlisle Etcetera, LLC, 114 A.3d 592, 607 (Del. Ch. 2015).

345. *See* Elf Atochem North America, Inc. v. Jaffari, 727 A.2d 286, 291 (Del. 1999); *see also* Anne Tucker, *Micro-symposium: Contract is King, But Can it Govern its Realm*? BUS. L. PROFESSOR'S BLOG (Nov. 12, 2015), http://lawprofessors.typepad.com/business_law/2015/11/micro-symposium-contract-is-king-but-can-it-govern-its-realm.html.

346. Allen v. Encore Energy Partners, L.P., 72 A.3d 93, 108 (Del. 2013).

347. *See* Gerber v. Enter. Prods. Holdings, LLC, 67 A.3d 400, 418 (Del. 2013), *overruled on other grounds by* Winshall v. Viacom Int'l Inc., 76 A.3d 808 (Del. 2013).

348. Strine & Laster, *supra* note 109, at 5; *see also* Daniel Kleinberger, *Careful What You Wish for—Freedom of Contract and the Necessity of Careful Scrivening* (Wm. Mitchell Legal Stud. Research Paper Series, Paper No. 52, 2006), http://papers.ssrn.com/sol3/papers.cfm?abstract_id=93009 (discussing the case law of states that have inserted "Contract is God" provisions into their corporate statutes).

349. *See supra* Subsection II.A.1.

350. *See supra* Subsection II.A.2.

loyalty jurisprudence with important socializing cues.[351] In contrast, publicly traded alternative business entities and their owners experience one-sided MLP agreements,[352] difficulties in challenging fairness opinions,[353] problems proving bad faith,[354] reduced or eliminated duties of disclosure,[355] difficulties in imposing secondary liability,[356] and limited protection from the implied covenant of good faith and fair dealing.[357]

This Part argues that there is a need for traditional fiduciary duties in publicly traded alternative business entities. While the rise of institutional investors and stockholder activism challenge the Berle–Means corporate model, neither of these trends obviate the need for effective firm monitoring or constraint of opportunistic behavior.[358] Disciplining mechanisms predicted to substitute for fiduciary duties in alternative entities rarely occur in MLPs.[359] Similarly, the arguments for legal diversification ring hollow for MLPs, where fiduciary duties assume increased importance in the absence of arms-length bargaining.[360] Research shows a positive relationship between independent monitoring for compliance with fiduciary duties and performance further strengthens the case for fiduciary duties.[361]

A. *Continuing Relevance of Fiduciary Duties Despite Challenges to Berle–Means Model*

The question of whether the law should permit the elimination of fiduciary duties for publicly traded LPs and LLCs belongs within a broader discussion of the future of the Berle–Means corporate model and its support of fiduciary duties.[362] As far back as 1776, Adam Smith observed that those who manage other people's money would never use

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351. *See supra* Subsection II.A.3.
352. *See supra* Subsection II.B.1.
353. *See supra* Subsection II.B.2.
354. *See supra* Subsection II.B.3.
355. *See supra* Subsection II.B.4.
356. *See supra* Subsection II.B.5.
357. *See supra* Subsection II.B.6.
358. *See infra* Section III.A.
359. *See infra* Section III.B.
360. *See infra* Section III.C.
361. *See infra* Section IV.D.
362. *See generally* Harwell Wells, *A Long View of Shareholder Power: From the Antebellum Corporation to the Twenty-First Century*, 67 FLA. L. REV. 1033 (2015) [hereinafter Wells, *Shareholder Power*].

the same "anxious vigilance" as employed over their own.[363] Thus, the fundamental problem caused by the separation of ownership and control was identified well before 1932 when Adolf A. Berle Jr. and Gardiner Means published their seminal work on the subject in *The Modern Corporation*.[364] Berle and Means presented empirical research that demonstrated that stock ownership in the United States was dispersed, leaving stockholders vulnerable to agency costs.[365] This separation of ownership from management led Berle to recommend increasing fiduciary duties to protect stockholders.[366] Berle, Professor Michael C. Jensen, and Dean William H. Meckling recognized the problem of managerial discretion and regarded managers as agents of stockholders.[367] Berle and Means argued that managers' powers are "powers in trust."[368] In accordance with this view, Chief Justice Strine has described the duty of loyalty as one that "most fundamentally requires that a corporate fiduciary's actions be undertaken in the good faith belief that they are in the best interests of the corporation and its stockholders."[369]

Two major factors have prompted questions as to the continuing relevance of the Berle–Means corporate model and its reliance on fiduciary duties to accomplish the purposes of the corporation. First, there has been a dramatic shift from individual to institutional ownership in the United States.[370] Second, the ownership change has spawned stockholder activism.[371] Given such marketplace changes, one must ask whether the increased concentration of ownership and sophistication of investors substantially eliminates informational asymmetries and thus reduces the

363. Harwell Wells, *The Birth of Corporate Governance*, 33 SEATTLE U. L. REV. 1247, 1251 (2010) [hereinafter Wells, *Corporate Governance*] (quoting ADAM SMITH, AN INQUIRY INTO THE NATURE AND CAUSES OF WEALTH OF NATIONS 606–07 (1776) (Penn State Press ed. 2005)).

364. ADOLF A. BERLE & GARDINER C. MEANS, THE MODERN CORPORATION AND PRIVATE PROPERTY (1932); *see* Wells, *Corporate Governance*, *supra* note 363, at 1286.

365. John Armour & Jeffrey N. Gordon, *The Berle-Means Corporation in the 21st Century* 6 (2008), http://www.law.yale.edu/documents/pdf/Intellectual_Life/Armour_BerleMeansCorp091021.pdf (2008) (unpublished manuscript) (on file with author).

366. Wells, *Shareholder Power*, *supra* note 362, at 1072.

367. *Id*. at 1087–88. *See generally* Frank H. Easterbrook & Daniel R. Fischel, *Close Corporations and Agency Costs*, 38 STAN. L. REV 271 (1986) (discussing agency costs in the context of closely held corporations).

368. Wells, *Corporate Governance*, *supra* note 363, at 1290.

369. Strine et al., *supra* note 102, at 633.

370. *See* Ronald J. Gilson & Jeffrey N. Gordon, *The Agency Costs of Agency Capitalism: Activist Investors and the Revaluation of Governance Rights*, 11 COLUM. L. REV. 863, 865 (2013) (discussing the ownership change from dispersed share ownership to institutional ownership).

371. Wells, *Shareholder Power*, *supra* note 362, at 1077–93.

need for mandatory fiduciary duties.[372] As discussed below, despite the changing face of U.S. stock ownership and the emergence of stockholder activism, agency costs still exist, and a mandatory duty of loyalty is vitally important in the case of publicly traded LPs and LLCs.[373]

Institutional investors now own over 70% of the outstanding stock of the thousand largest U.S. public corporations.[374] At the same time, there has been a rise in activist stockholders.[375] These developments have not eliminated agency costs, risks, or problems; nor have these developments obviated the need to provide effective internal governance mechanisms. Rather, the shift to concentrated ownership arguably adds a second layer of agency costs.[376]

The market will require regulatory adjustments as scholars in the fields of law, economics, and finance sort out the long-term impact of concentrated stock ownership and stockholder activism.[377] Some academics predict that the optimal governance approach for the United States and United Kingdom will be to provide a mix of mechanisms to control agency costs including a hybrid of legal duties, robust mandatory disclosure, strong stockholder rights, checks against stockholder opportunism, and reasonably intense enforcement.[378]

The shift to concentrated stock ownership and the emergence of stockholder activism has not eliminated the need for fiduciary duty constraints upon the management of publicly traded LPs or LLCs. Thus far, institutional investors have not offered socializing messages or managerial constraints, which are the heart and soul of fiduciary duties.[379] In fact, commentators have expressed concern that institutional investors are too passive.[380] Further, the empirical evidence "on whether

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372. *See* Kelli A. Alces, *Legal Diversification*, 113 COLUM. L. REV. SIDEBAR 1977, 1996 (2013).

373. *See* Strine et al., *supra* note 369, at 633 ("Because the discretion that the DGCL affords directors is so wide, it is vitally important that directors exercise this discretion to advance the corporation's best interests and not for improper purposes.").

374. Gilson & Gordon, *supra* note 370, at 865, 867 (discussing the governance implications of a shift to institutional equity ownership, the rise of stockholder activism, and the impact on agency costs).

375. Wells, *Shareholder Power*, *supra* note 362, at 1077–93.

376. *Id.*

377. *See* Lucian A. Bebchuk et al., *The Long-Term Effects of Hedge Fund Activism*, 115 COLUM. L. REV. 1085, 1087, 1089 (2015) (refuting the so-called "myopic activists" claim, which asserts that actions of stockholder activists may be favorable in the short term but have a value-decreasing effect in the long term).

378. *See, e.g.*, Armour & Gordon, *supra* note 365, at 44.

379. *See* Edward B. Rock, *Institutional Investors in Corporate Governance* (Univ. of Pa. Law Sch. Faculty Scholarship, Paper No. 1458, 2015), http://scholarship.law.upenn.edu/cgi/viewcontent.cgi?article=2459&context=faculty_scholarship.

380. *See id.*

institutional investors do . . . provide effective monitoring is somewhat mixed."[381] While institutional investors and activist stockholders present pressures with which management must contend, institutional ownership and stockholder activism is not a substitute for traditional legal monitoring.[382]

B. *The Contractarian Argument Overlooks Efficiencies of Standard Corporate Terms and Presupposes Perfect Market Conditions*

Contractarian theory overlooks the efficiencies provided by standard corporate terms.[383] Moreover, it presupposes perfect market conditions and fails to fully appreciate the impact of inequality in the contractual playing field. As pointed out by Professor Michael Klausner, the contractarian failure to study the actual facts is not surprising given that the theory emerged in the late 1970s and 1980s before empirical research began to play an important role in legal scholarship.[384]

Professor Ribstein initially provided a comprehensive analysis of the contractarian approach to internal governance of alternative business entities.[385] Under the contractarian view, mandatory corporate fiduciary duties impose unnecessary transaction costs due to increased costs of

381. *See* Stuart L. Gillan & Laura T. Starks, *Corporate Governance, Corporate Ownership, and the Role of Institutional Investors: A Global Perspective* 8 (John L. Weinberg Ctr. for Corp. Governance, Univ. of Del. Working Paper Series, WP No. 2003-01), http://papers.ssrn.com/sol3/papers.cfm?abstract_id=439500.

382. *See* Stephen M. Gill & Kai Haakon E. Liekefett, *Spotlight on Shareholder Activism in the Energy Industry*, LAW360 (Jan. 10, 2014, 7:28 PM), http://www.velaw.com/uploadedFiles/VEsite/Resources/SpotlightShareholderActivismEnergyIndustry.pdf (observing a surge of stockholder activism during 2012 and 2013 in the North American energy sector and that activists have pushed companies to drop assets into tax-efficient MLP structures, but for the most part MLPs have sponsors who select all board members and, consequently, are unlikely to be a target for many MLPs except those who lack a sponsor); Holly J. Gregory, *Corporate Governance Issues for 2015*, HARVARD LAW SCH. FORUM ON CORP. GOVERNANCE & FIN. REGULATION (Dec. 12, 2014), http://blogs.law.harvard.edu/corpgov/2014/12/12/corporate-governance-issues-for-2015/ (indicating that it is unclear whether institutional ownership and stockholder activism will be beneficial in the long run).

383. *See* Michael Klausner, *Fact and Fiction in Corporate Law and Governance*, 65 STAN. L. REV.1325, 1330 (2013).

384. *Id.* at 1329–30.

385. *See* Larry E. Ribstein, *Accountability and Responsibility in Corporate Governance*, 81 NOTRE DAME L. REV. 1431, 1432–33 (2006); Larry E. Ribstein, *Why Corporations?*, 1 U.C. BERKELEY BUS. L.J. 183, 185–86 (2004). *See generally* LARRY E. RIBSTEIN, THE RISE OF THE UNCORPORATION (2009) (discussing how "uncorporations" heavily rely on contractual relationships). Professors Michael C. Jensen and William H. Meckling, who regarded the firm as a nexus of contracts, first articulated the contractarian approach in the 1970s. *See* Michael C. Jensen & William H. Meckling, *Theory of the Firm: Managerial Behavior, Agency Costs, and Ownership Structure*, 3 J. FIN. ECON. 305, 310 (1976).

contracting and unexpected litigation.[386] Contractarians criticize corporate law and traditional corporate fiduciary duties in part on the grounds that the law is indeterminate.[387] Professor Ribstein maintained that the costs of indeterminate fiduciary duties are unnecessary in alternative business entities because there are powerful noncorporate factors that incentivize and discipline managers of alternative business entities.[388] Such disciplining forces include mandatory liquidations, mandatory distributions, and managerial equity stakes.[389]

One might expect that highly efficient agreements would govern alternative business entities and that market forces would lead to optimal and efficient internal governance provisions. However, as it turns out—and as discussed above in Part II—one-sided agreements have governed MLPs, leading to extensive litigation. Corporate standard default terms may in the end provide greater efficiencies than custom-tailored agreements.[390]

Although contractarians presupposed perfect market conditions, empirical evidence reveals something very different. As discussed in Section I.B, Professor Manesh examined eighty-five publicly traded Delaware LPs and LLCs, and concluded that these entities had either *not* adopted uncorporate substitutes or had adopted substitutes that only *trivially* constrain management.[391] Professor Manesh observed:

> [A]s a descriptive matter, publicly traded alternative entities are not the kind of uncorporations that Professor Ribstein has envisioned. Rather than trading corporate accountability mechanisms for high-powered contractual devices to discipline and incentivize managers, publicly traded alternative entities appear to utilize freedom of contact as a one-way ratchet: to reduce managerial accountability without committing to meaningful contractual constraints on managerial discretion.[392]

386. Myron T. Steele, *Freedom of Contract and Default Contractual Duties in Delaware Limited Partnerships and Limited Liability Companies*, 46 AM. BUS. L.J. 221, 239–40 (2009).

387. *See, e.g.*, Ribstein, *supra* note 16, at 142–43.

388. *See id.*

389. Mohsen Manesh, *Legal Asymmetry and the End of Corporate Law*, 34 DEL. J. CORP. L. 465, 494 (2009); *see also* RIBSTEIN, *supra* note 385, at 1–10.

390. *See* Klausner, *supra* note 383, at 1330; *see also* Strine & Laster, *supra* note 109, at 14.

391. Manesh, *supra* note 9, at 583, 589 ("A second conclusion to draw from this study is that despite the widespread use of operating agreement provisions eliminating or exculpating for the breach of fiduciary duties, publicly traded alternative entities have either not adopted uncorporate substitutes or, more commonly, adopted uncorporate substitutes that only trivially constrain managerial discretion.").

392. *Id.*

As noted above, MLP agreements appear to be highly protective of management—a symptom of market failures. Ideally, under contractarian theory, it is most efficient for parties to price and select constraints themselves.[393] So-called market failures may defeat these efficiencies.[394] Inequalities in the playing field, information asymmetries, and the effect of repeat transactions challenge contractarian assumptions.[395] As discussed in Section II.B, the problems investors have holding managers accountable in publicly traded entities in which the duty of loyalty has been waived illustrate such inequalities.

In recognition of market failures and the potential for unfairness, Professors Michelle M. Harner and Jamie Marincic have argued that LLC governance requires a nuanced approach to internal governance.[396] They argue in favor of mandatory fiduciary duties except in cases involving "co-active" LLCs—LLCs in which the parties are fully informed, have actively participated in negotiation, and have control or a meaningful role in material transactions.[397] Thus, they would recommend mandatory fiduciary duties in passive investments, which would include publicly traded LPs and LLCs. For similar reasons, discussed more fully below, this Article recommends ending contractual waivers for publicly traded LPs and LLCs.

C. *Appropriate Legal Diversification as Between Public and Private Companies*

Some argue that the diversification of business entities encourages investors to develop portfolios of investments that include a variety of legal regimes.[398] Such legal diversification disperses the risk that particular legal rules will fail to successfully constrain management.[399] As pointed out by Professor Kelli A. Alces, states can serve as legal laboratories to the extent that they employ different laws.[400] The diversification that Professor Alces contemplates between publicly traded alternative business entities and traditional corporations rests upon assumptions about uncorporations that do not hold true for publicly

393. *See* MILLER, *supra* note 155, at 109–10 (citing Larry E. Ribstein, *Fiduciary Duty Contracts in Unincorporated Firms*, 54 WASH. & LEE L. REV. 537 (1997)).

394. *See* JOHN ROBERTS, THE MODERN FIRM: ORGANIZATIONAL DESIGN FOR PERFORMANCE AND GROWTH 78–79 (2004) (discussing market failures).

395. Harner & Marincic, *supra* note 191, at 937–38 ("The potential for information asymmetry and unequal bargaining power exists and may expose parties—particularly minority or passive investors—to increased risk of loss."); MILLER, *supra* note 155, at 110–11.

396. *See* Harner & Marincic, *supra* note 191, at 932–33.

397. *Id.* at 933–34.

398. *See, e.g.*, Alces, *supra* note 372, at 1980.

399. *Id.*

400. *Id*. at 2023.

traded alternative business entities.

Professor Alces argued that traditional corporations rely upon fiduciary duties to control agency costs, but that uncorporations rely on other managerial incentives to constrain management.[401] She argued that such legal diversity is a benefit because the structures offer different degrees of freedom to management and different types of managerial constraints.[402] Mandatory fiduciary duties are thought unnecessary in uncorporations because they are assumed to rely upon contracts, owner control, incentive compensation, and direct monitoring by owners to control agency costs.[403] As previously noted, Professor Manesh's empirical research found these substitutes absent in MLPs.[404] Moreover, some MLP structures may not provide other constraints, such as mandatory distributions or incentive distribution rights.[405] In an economic downturn, financial incentives tied to profits will not provide constraints on management. Also, the alignment of incentives may not extend to extraordinary transactions. The status quo may make sense for private LPs or LLCs or a public corporation where factors are present to control agency costs;[406] however, many MLP investors may lack financially based incentives and strong contractual protections to guard against managerial abuse.

D. *Positive Relationship Between Independent Monitoring and Performance*

Those with financial interests in the legal status quo of fiduciary duty waivers—MLP sponsors, their executives, employees, outside financial experts, lawyers, accountants, investment bankers, and lobbyists—may argue that the business model requires a waiver of fiduciary duties and the suspension of Sarbanes–Oxley and Dodd–Frank rules.[407] They may contend that fiduciary duty rules must give way because managers must juggle multiple projects for which there is inherent competition.[408] Further, they may argue that reduced regulation and the elimination of burdensome fiduciary duty rules are important to reduce transaction costs and to promote economic prosperity.[409]

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401. *See id.* at 2005–07.

402. *Id.* at 2006–07.

403. *See id.*

404. Manesh, *supra* note 9, at 589.

405. *See* Goodgame, *supra* note 28, at 91–93.

406. Examples of such factors include actively negotiated governing documents, buy-out provisions, and feasible direct monitoring.

407. *See supra* Sections I.A–B.

408. *See* Paul M. Altman et al., *Eliminating Fiduciary Duty Uncertainty: The Benefits of Effectively Modifying Fiduciary Duties in Delaware LLCs*, 2013 BUS. L. TODAY 1, 3 (2013).

409. *See* Manesh, *supra* note 9, at 563–64.

Business models subject to appropriate regulation, however, arguably produce the best financial results for the economy at large.[410] Although the independence issue is still hotly debated,[411] the finance literature is ripe with research correlating greater board independence with positive business outcomes.[412] For instance, greater board independence is linked to increased firm performance.[413] Greater independence is also correlated with a decreased likelihood of fraudulent financial reporting,[414] smaller probability of the firm's financial distress,[415] and a lower incidence of firm bankruptcy.[416] Given the link between board independence and firm performance and other positive outcomes, it is unsurprising that greater board independence also correlates with positive stock market reaction.[417] Scholars have opined that the enhanced firm performance may be due to more effective monitoring by independent directors.[418] An

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410. *Compare* Bhagat & Bolton, *supra* note 122 (finding a positive relationship between corporate governance and firm performance post-2002), *with* Sanjai Bhagat & Bernard S. Black, *The Uncertain Relationship Between Board Composition and Firm Performance*, 54 BUS. LAW. 921, 931 (1999) (finding a negative relationship between corporate governance and firm performance prior to 2002 and the passage of the Sarbanes–Oxley Act), *and* Bhagat & Black, *supra* note 126, at 233–34 (finding no consistent correlation between board independence and firm performance).

411. *See, e.g.*, Romano, *supra* note 121, at 1526.

412. *See* Bhagat & Bolton, *supra* note 122, at 105; Romilda Mazzotta & Stefania Veltri, *The Relationship Between Corporate Governance and the Cost of Equity Capital: Evidence from the Italian Stock Exchange*, 18 J. MGMT. GOVERNANCE 419, 427–28 (2014).

413. *See* Bhagat & Bolton, *supra* note 122, at 105; Sharon K. Lee & R. Loring Carlson, *The Changing Board of Directors: Board Independence in S&P 500 Firms*, 11 J. ORG. CULTURE, COMMC'N & CONFLICT 31, 31 (2007).

414. Mark S. Beasley, *An Empirical Analysis of the Relation Between the Board of Director Composition and Financial Statement Fraud*, 71 ACCT. REV. 443 (1996) ("[N]o fraud firms have boards with significantly higher percentages of outside members than fraud firms."); *see also* Patricia M. Dechow et al., *Causes and Consequences of Earnings Manipulation: An Analysis of Firms Subject to Enforcement Actions by the SEC*, 13 CONTEMP. ACCT. RES. 1 (1996) (finding that firms are more likely to manipulate earnings when they have a board dominated by management); Paul Dunn, *The Impact of Insider Power on Fraudulent Financial Reporting*, 30 J. MGMT. 397 (2003) (noting that fraud is more likely when there is not an independent board).

415. *See* Fathi Elloumi & Jean-Pierre Gueyié, *Financial Distress and Corporate Governance: An Empirical Analysis*, 1 CORP. GOVERNANCE INT'L J. BUS. SOC. 15, 18–19, 21 (2001).

416. Catherine M. Daily et al., *Corporate Governance: Decades of Dialogue and Data*, 28 ACAD. MGMT. REV. 371, 377 (2003).

417. *See* Stuart Rosenstein & Jeffrey G. Wyatt, *Outside Directors, Board Independence, and Shareholder Wealth*, 26 J. FIN. ECON. 175, 178, 184 (1990).

418. *See, e.g.*, Renée Adams & Hamid Mehran, *Is Corporate Governance Different for Bank Holding Companies?*, 9 ECON. POL'Y R. 123, 124 (2003); James A. Brickley, Jeffrey L. Coles & Rory L. Terry, *Outside Directors and the Adoptions of Poison Pills*, 35 J. OF FIN. ECON. 371, 383 (1994); Eugene F. Fama & Michael C. Jensen, *Separation of Ownership and Control*, 26 J.L. & ECON. 301, 308 (1983); Lee & Carlson, *supra* note 413, at 31; M. D. Saibaba, *Do Board*

independent director's lower reputational concerns and her greater willingness to challenge and remove poor performing management may drive this monitoring efficiency.[419] The same traits that lead to monitoring efficacy help independent directors control opportunistic behavior within the firm and mitigate conflicts among majority and minority owners.[420] In conclusion, the empirical research linking board independence with positive economic outcomes suggests skepticism for arguments predicting negative economic consequences for the imposition of fiduciary duties in MLPs.

E. *The MLP Investor Profile: Who Are the Investors and What Do They Know About MLP Governance?*

As far back as 1988, Professor Deborah DeMott questioned whether investors would agree to waive fiduciary duties if they truly understood the legal impact of the rights they would relinquish.[421] Given the extent to which MLP partnership agreements protect management, one wonders whether MLP investors understand the governance risks they assume when they invest in an MLP. Who are these investors and what are they told about MLPs? Are disclosures of governance risks made to investors? If so, are the disclosures adequate? A comprehensive exploration of these questions goes far beyond the scope of this Article. However, research should be undertaken to develop both a reliable MLP investor profile and a detailed compilation of disclosures typically made to investors by advisors, brokers, other organizations, and MLPs.

Details on the MLP investor profile have been difficult to obtain; however, the National Association of Publicly Traded Partnerships (NAPTP) has been helpful in responding to inquiries regarding MLP investor demographics.[422] In testimony before the Senate Finance Committee Business Income Tax Reform Working Group, NAPTP concluded that most MLP investors are individuals, the vast majority of whom are over age fifty.[423] As noted in the testimony:

Independence and CEO Duality Matter in Firm Valuation?—An Empirical Study of Indian Companies, 12.1 IUP J. CORP. GOVERNANCE 50, 51 (2013).

419. *See* Mustafa A. Dah et al., *Board Changes and CEO Turnover: The Unanticipated Effects of the Sarbanes–Oxley Act*, 41 J. BANKING & FIN. 97, 99 (2014); Fama & Jensen, *supra* note 418, at 315; Michael S. Weisbach, *Outside Directors and CEO Turnover*, 20 J. FIN. ECON. 431, 432–33 (1988).

420. *See* Ronald C. Anderson & David M. Reeb, *Board Composition: Balancing Family Influence in S&P 500 Firms*, 49 ADMIN. SCI. Q. 209, 209, 222 (2004).

421. *See* Deborah A. DeMott, *Beyond Metaphor: An Analysis of Fiduciary Obligation*, 1988 DUKE L.J. 879, 880, 902, 920–21 (1988).

422. NAPTP is now called the Master Limited Partnership Association. *See* MASTER LIMITED PARTNERSHIP ASS'N, http://www.mlpassociation.org/ (last visited Feb. 8, 2016).

423. NAPTP, WRITTEN STATEMENT, *supra* note 4, at 3.

> According to surveys done by . . . members, the vast majority of the investors providing this capital are individual investors. Many of the investors are seniors—roughly 75 percent are over the age of 50. For the most part, they are individuals seeking a relatively secure income-oriented investment providing a reasonable return, something that is hard to come by in today's market.[424]

PriceWaterhouseCoopers (PWC), which provides K-1 services for the vast majority of MLPs and their investors, has compiled the most current and detailed information on MLP investors.[425] In 2011, for example, PWC prepared more than eight million MLP K-1s.[426] Based on discussions with industry experts and unpublished data gathered from industry sources, individuals, estates IRA/SEP/Keoghs, or Roth/Education IRAs comprise over 75% of investor accounts.[427]

Further empirical research is necessary to determine how well-informed individual MLP investors are regarding fiduciary duties and contractual waivers in MLPs. It is likely that investors may have some knowledge regarding MLP taxation but may be much less informed regarding the significance of waiving fiduciary duties. At least one scholar has stressed that legal regulations should not be premised upon the existence of a unitary, "reasonable investor" because investors are diverse.[428] Empirical data would be of enormous value to clarify the identity of MLP investors, including investors' ages and educational backgrounds. Also, it would be helpful to perform a systematic review of the information that investment brokers and advisors, accounting firms, industry associations, and the MLPs themselves provide to MLP investors. Such an analysis would not assume a reasonable investor model; rather, it would be grounded in facts surrounding MLP investors and communications they receive.

F. *Approaches to Restoring the Duty of Loyalty for MLPs: The Path Forward*

One approach to solving the MLP problem is to prohibit the ability to eliminate the duty of loyalty in all business entities. However, advocates for legal diversification might argue that a diversity of legal regimes is

424. *Id.*

425. *Proven Experience You Can Trust*, PWC MLP INV'R PRACTICE, https://www.pwcmlp.com/practice_experience.aspx (last visited Feb. 8, 2016).

426. *Id.*

427. Unpublished documents on file with authors. For details, the authors suggest contacting the National Association of Publicly Traded Partnerships. NAT'L ASS'N OF PUBLICLY TRADED P'SHIPS, http://www.naptp.org.

428. *See* Tom C.W. Lin, *Reasonable Investor(s)*, 95 B.U. L. REV. 461, 461–63 (2015).

beneficial in the long run. Moreover, practitioners have long argued that managers who manage multiple investments with different investors need contractual flexibility.[429] Practitioners who represent real estate managers, fund managers, or managers of multiple lines of business are likely to take the position that the contractual elimination of fiduciary duties is necessary to prevent investors from suing for improper competition or improper conflicts of interests.[430] Nevertheless, there is already a corporate opportunity doctrine that could address competition issues.[431] Chief Justice Strine and Vice Chancellor Laster have pointed out that Delaware corporate law now has a safe harbor provision that permits a certificate of incorporation to renounce any interests of the corporation in business opportunities presented to the officers or directors.[432]

A narrower approach to the MLP problem is to restore a mandatory duty of loyalty for publicly traded alternative business entities.[433] One possibility is to retain the ability to eliminate fiduciary duties for the privately owned entity and to provide for mandatory duties for publicly traded companies. This approach would make sense if one concludes that contractual waivers remain desirable for private firms. Professors Harner and Marincic suggest that there may be a place for contractual waivers in actively negotiated business contexts.[434] Further, there are precedents for using special close business entity statutes. For example, Maine and Wyoming offer close LLC provisions containing several separate rules.[435] It may be difficult, however, to develop a workable definition of "close LLC." Further, because business entities grow and change, care must be taken to ensure that dual statutes would not be an impediment to growth or reorganization.

Chief Justice Strine and Vice Chancellor Laster propose restoring the duty of loyalty in a targeted manner.[436] They would prohibit publicly traded entities from waiving the duty of loyalty.[437] They observed that:

> [T]he experience with litigated cases suggests that alternative entity governing instruments are not the products

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429. *See* Altman et. al., *supra* note 408, at 3.

430. *See id.*; Sandra K. Miller, *The Best of Both Worlds: Default Fiduciary Duties and Contractual Freedom in Alternative Business Entities*, 39 J. CORP. L. 295, 306 (2014).

431. *See* Strine & Laster, *supra* note 109, at 9.

432. *Id.* at 9 (citing DEL. CODE ANN. tit. 6, § 122(17) (2015)).

433. *Id.* at 9–10.

434. *See* Harner & Marincic, *supra* note 191, at 933–37.

435. *See* ME. REV. STAT. tit. 31, § 1637 (2015); WYO. STAT. ANN. §§ 17-25-101 to -111 (2015).

436. *See* Strine & Laster, *supra* note 109, at 5.

437. *Id.*

> of negotiation, but are drafted solely by entity managers. Those governing instruments seem to achieve little in terms of wealth-creating efficiency beyond what can be achieved under current "broadly enabling" corporate statutes, which already provide for the ability to avoid liability under the corporate opportunity doctrine.[438]

Under their nuanced approach, Chief Justice Strine and Vice Chancellor Laster would make the duty of loyalty mandatory for private entities where the entities have diverse investors.[439] One possibility is to use an SEC-style threshold for determining whether an LP or LLC should be classified as a large or diverse entity that is ineligible for waivers of the duty of loyalty (i.e., assets exceeding $10,000,000 and equity held by either 500 persons who are not accredited investors or 2000 persons).[440] A nuanced approach would be an improvement. A broader prohibition on fiduciary duty waivers does a better job of accomplishing the socializing goals of the law. Nonetheless, the achievement would come at the cost of some degree of contractual freedom.

CONCLUSION

Fiduciary duty waivers for publicly traded LPs and LLCs should end. Recent Delaware case law reveals that MLP investors may be significantly disadvantaged by one-sided contracts and face difficulties in challenging deficient fairness opinions and proving bad faith. Fiduciary duty waiver, and by extension the elimination of the affirmative duty of disclosure, has invited sharp dealing and unfair conduct. MLP investors are left with only the protection of the implied covenant of good faith and fair dealing, which is not an adequate substitute for the protective effects of fiduciary duties. The implied covenant of good faith and fair dealing also fails to offer the socializing value of traditional fiduciary duties. Prior contractarian literature theorized the inclusion of substitute mechanisms to discipline management in lieu of fiduciary duties, but these mechanisms are rare in publicly traded MLPs. Moreover, market failures demonstrate the need for minimum investor protections in MLPs. Although still debated, a link between director independence and positive firm performance lends further credence to the argument that publicly traded alternative business entities should be subject to the same independence listing requirements as public corporations.

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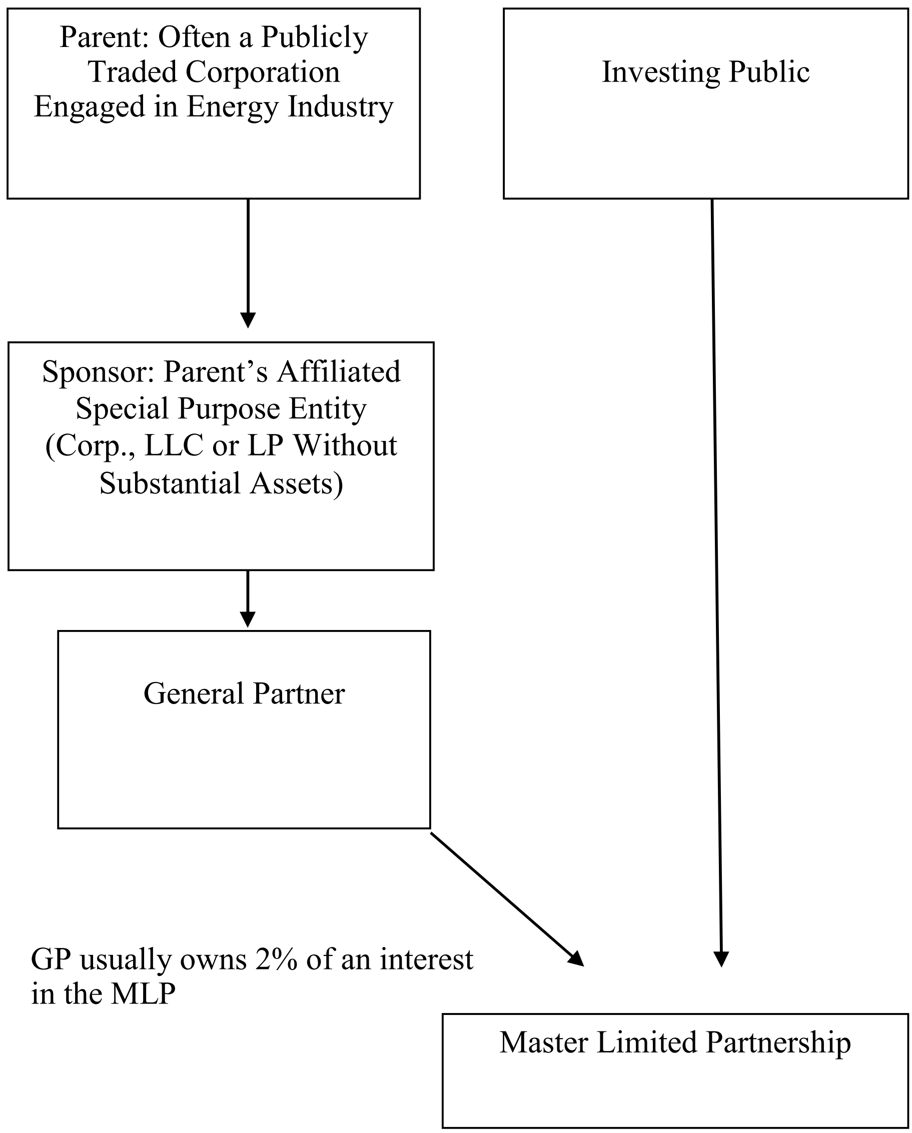
438. *Id.* at 30.
439. *See id.*
440. *Id.* at 5 & n.5.

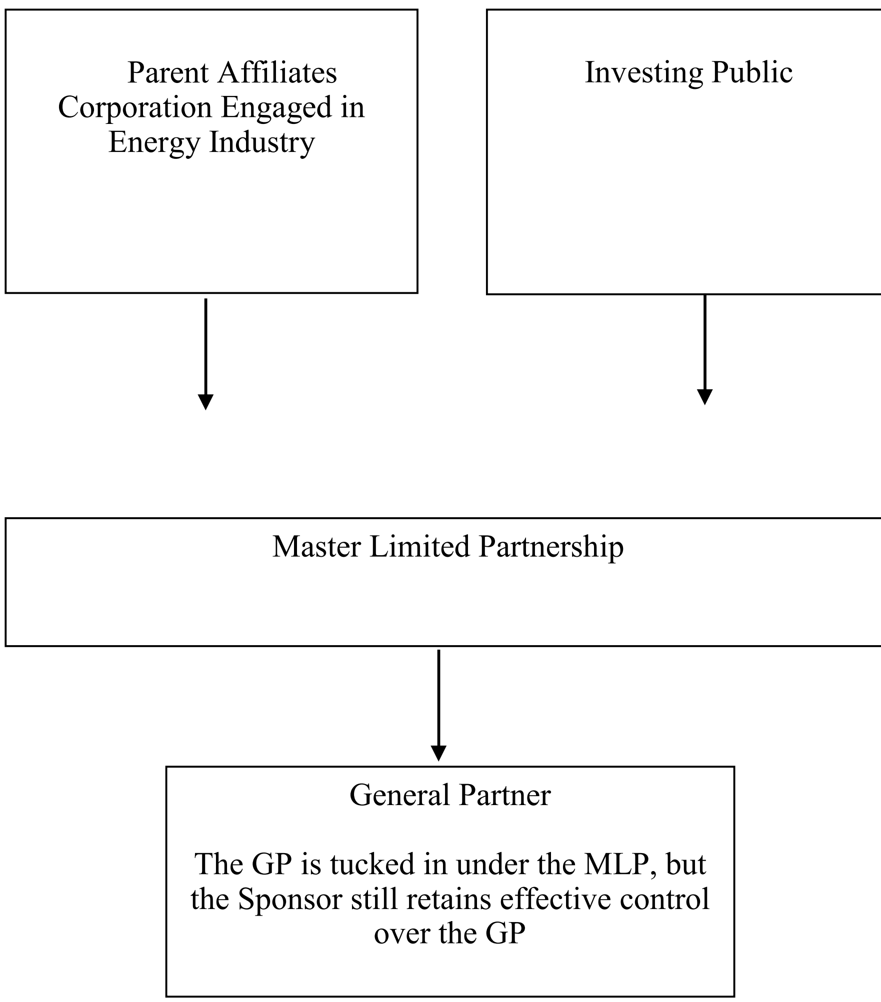
Appendix A

SIMPLIFIED STRUCTURE OF SPONSORED MLP MODEL[441]



441. *See supra* Section I.

EXAMPLE OF A GP TUCK-IN[442]



442. *See* Goodgame, *supra* note 28, at 91–92 (describing the structure of Markwest Energy Partners, L.P. as a GP tuck-in where investors annually elect directors as in the public LLC model, but the agreement does not have minimum distribution requirements and contractually eliminates fiduciary duties, replacing them with a contractual good faith standard).