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Manufactured Deadlocks? The Problematic “Bad Faith Defense” to Forced-Sales of Delaware Corporations Under Section 226 of the Delaware General Corporation Law

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MANUFACTURED DEADLOCKS? THE PROBLEMATIC “BAD FAITH DEFENSE” TO FORCED SALES OF DELAWARE CORPORATIONS UNDER SECTION 226 OF THE DELAWARE GENERAL CORPORATION LAW

Abstract: Title 8, Section 226 of the Delaware General Corporation Law authorizes courts to force the sale of Delaware corporations when the stockholders or directors are in a state of complete deadlock. Some courts have tentatively acknowledged that a party may successfully oppose the sale by arguing that the stockholder bringing a Section 226 action has done so in bad faith by manufacturing a deadlock in the hopes of obtaining a court-ordered sale (i.e., the “bad faith defense”). This Note explores the idea of the manufactured deadlock in Section 226 actions, through the lens of *Shawe v. Elting*, a recent, highly publicized case where the Delaware Chancery Court ordered the sale of a profitable company against the wishes of a 50% owner. There exist inherent problems in attempting to determine whether an ostensible deadlock between business owners is authentic or manufactured. An examination of cases grappling with deadlock in business dissolution actions, which are analogous to those brought under Section 226, highlights these issues. In light of the fundamental difficulties in determining whether a deadlock is legitimate or fabricated, courts should move towards rejecting the legitimacy of the “bad faith defense” to court-ordered sales entirely.

INTRODUCTION

In 1992, Philip Shawe and Elizabeth Elting co-founded TransPerfect Global, Inc. while attending the New York University Stern School of Business.¹ Notwithstanding the tensions arising out of their personal relationship, the corporation flourished over the subsequent decade from a “dorm room start-up to a major player in the global market for translation ser-

¹ See *Shawe v. Elting*, 157 A.3d 152, 156 (Del. 2017); *In re Shawe & Elting LLC*, C.A. No. 9661-CB, C.A. No. 9686-CB, C.A. No. 9700-CB, C.A. No. 10449-CB, 2015 WL 4874733, at *3 (Del. Ch. Aug. 13, 2015), *aff'd*, *Shawe v. Elting*, 157 A.3d 152 (Del. 2017). This dispute in its entirety (including both the lower court and appellate actions) is referred to throughout the text of this Note as the “TransPerfect case.” See *infra* notes 2–174 and accompanying text. The Chancery Court Order of August 13, 2015, will be cited as “*In re Shaw*” in the footnotes and the Delaware Supreme Court opinion will be cited as “*Shawe v. Elting*.” See *infra* notes 2–174 and accompanying text.

vices.”² In 2007 they incorporated TransPerfect in Delaware as part of a company-wide reorganization.³ In recent years, TransPerfect has achieved staggering profitable growth, recognizing in 2014, for example, revenues exceeding \$470 million and a net income of \$78.9 million.⁴ Despite the corporation’s considerable success, Shawe and Elting’s relationship began to deteriorate in 2011, and eventually became so hostile that in May 2014, Shawe and Elting filed a total of four individual lawsuits against one another.⁵ Of the four separate actions filed, one has since gained national attention: Elting’s petition in the Delaware Chancery Court seeking an appointment of a custodian under Title 8, Section 226(a)(2) of the Delaware General Corporation Law to sell the corporation as a whole.⁶

² See *In re Shawe*, 2015 WL 4874733, at *3. Shawe and Elting were engaged in 1996 but ended their personal relationship in 1997. See *id.* According to Elting, Shawe was thoroughly upset by the breakup and would “say horrendous things” about the man that Elting subsequently married in 1999. See *id.*

³ See *id.* Along with translation services, TransPerfect offers website localization and litigation support services and employs over 3500 people. See *Shawe v. Elting*, 157 A.3d at 156. Shawe and Elting incorporated TransPerfect as a Subchapter S corporation, which allowed for certain income tax benefits—specifically, the ability for income not to be taxed at the corporate level. See 26 U.S.C. § 1361 (2012) (defining Subchapter S corporations); *In re Shawe*, 2015 WL 4874733, at *3. There are 100 shares of common stock of the corporation issued and outstanding. *In re Shawe*, 2015 WL 4874733, at *3. Elting owns (and has owned since the corporation’s founding) fifty shares, and Shawe has owned forty-nine shares, with Shawe’s mother, Shirley Shawe, owning the last remaining share. See *Shawe v. Elting*, 157 A.3d at 156. For all intents and purposes, Shawe and Elting are each viewed (and treated by the Chancery Court) as 50% owners despite the fact that technically speaking, Shawe is only a 49% owner. See *In re Shawe*, 2015 WL 4874733, at *1. This is so because Shawe’s mother has essentially pledged to vote in tandem with Shawe on all issues. *Id.* This point will become relevant in the pages that follow discussing Elting’s petition filed under Title 8, Section 226 of the Delaware General Corporation Law. See DEL. CODE ANN. tit. 8, § 226 (2011) (authorizing the appointment of a custodian or receiver for deadlocked corporations with more than one stockholder). See generally *In re Shawe*, 2015 WL 4874733 (assessing Elting’s petition for the appointment of a custodian). Elting originally filed a petition for dissolution under Title 6, Section 273, a joint venture dissolution statute that governs court-ordered dissolutions of corporations with only two stockholders. See DEL. CODE ANN. tit. 8, § 273 (authorizing the dissolution of corporations with only two 50% stockholders); *In re Shawe*, 2015 WL 4874733 n.7. As noted by the Chancery Court in the TransPerfect case, Elting eventually dropped that action, recognizing that because there are technically three stockholders, Section 273 did not apply, and instead pursued the appointment of a custodian under Section 226. *In re Shawe*, 2015 WL 4874733 n.7.

⁴ See *In re Shawe*, 2015 WL 4874733, at *4.

⁵ *Id.* at *18. At trial, the Chancery Court in *In re Shawe* examined the breakdown of Shawe and Elting’s interpersonal relationship in “painstaking detail” and the Delaware Supreme Court’s opinion reiterated a few examples of the toxic nature of their relationship: Shawe engaged in a “secret campaign to spy on Elting,” seeking to have Elting criminally prosecuted, and disparaged Elting by disseminating a memorandum to company employees and issuing a press release containing “false and misleading information.” See *Shawe v. Elting*, 157 A.3d at 156–57; *In re Shawe*, 2015 WL 4874733, at *2, *27.

⁶ See DEL. CODE ANN. tit. 8, § 226; *In re Shaw*, 2015 WL 4874733, at *18; Fred Lucas, *Judicial Overreach: Small Court, Big Economic Ramifications*, TOWNHALL (May 27, 2016), <https://townhall.com/columnists/fredlucas/2016/05/27/judicial-overreach-small-court-big-economic-ramifications-n2169449> [<https://perma.cc/6VF5-MXC4>] (arguing that Chancellor Bouchard’s decision to appoint

Title 8, Section 226 of the Delaware General Corporation Law (“Section 226”) permits courts, under extreme circumstances, to intervene in the affairs of corporations, with the goal of resolving managerial deadlocks and saving those companies from irreparable harm.⁷ Specifically, Section 226 permits the Chancery Court to appoint a receiver or custodian for a corporation when (1) the “stockholders are so divided” that they cannot elect directors; (2) the directors are in such a state of deadlock that they are unable to make managerial decisions and the corporation is thus faced with “irreparable” harm; or (3) when the corporation has “abandoned its business” purpose and failed to adequately dissolve itself.⁸ The statute also gives the Chancery Court discretion in determining what authority to give the appointed custodian or receiver.⁹ The Chancery Court may use Section 226 to appoint a custodian to act as a “tie breaking” director in order to resolve deadlocks between directors.¹⁰ The Chancery Court has also used Section 226 to give the appointed custodian the power to sell a corporation when it is insolvent in order to protect the business from incurring additional debts and causing further financial damage.¹¹ As such, the Chancery Court surprised the Delaware business community when it used Section 226 to appoint a custodian with the power to sell TransPerfect, Inc., despite the fact that the company was and remains profitable.¹² As discussed in greater de-

a custodian to sell TransPerfect constitutes “judicial overreach,” in light of the corporation’s high profits and thousands of employees). Elting’s petition seeking a court-ordered sale of the corporation, and the Chancery Court’s decision to order the sale, not only solicited attention from reporters, but also drew the ire of business interest groups and politicians. *See infra* notes 14–16 and accompanying text.

⁷ *See* DEL. CODE ANN. tit. 8, § 226(a)(2).

⁸ *See id.* § (a)(1)–(3). The reader should note that the first clause of the statute explains that if any of subsections (a)(1), (a)(2), or (a)(3) are satisfied, then the court may appoint one or more *custodians*, and that if the corporation is insolvent, that the court may appoint one or more *receivers*. *See id.* § 226(a). This differentiation (between the appointment of a custodian and a receiver) signals the legislature’s recognition that in some circumstances, the statute may require the court to intervene in the affairs of solvent companies. *See In re Shaw*, 2015 WL 4874733, at *28 n.293. Because this Note concerns only judicial intervention in the affairs of a solvent, and profitable company, the discussion of Section 226 contained herein will refer only to the statute’s authorization of court-appointed custodians. *See* DEL. CODE ANN. tit. 8, § 226(a).

⁹ *See* DEL. CODE ANN. tit. 8, § 226(b) (stating that the custodian shall have the authority to continue the business of the corporation “except when the Court shall otherwise order”).

¹⁰ *See id.* § 226; *In re Shawe*, 2015 WL 4874733, at *31.

¹¹ *See In re Shawe*, 2015 WL 4874733, at *1, *31 (inferring that in the usual course of events, a custodian is appointed to sell a corporation because the corporation is insolvent or is losing capital).

¹² *See* Lucas, *supra* note 6 (arguing that the decision to appoint a custodian to sell the TransPerfect constitutes “judicial overreach”). Some viewed the decision as one that could set a dangerous precedent for the laws governing corporations in Delaware, especially considering the state’s reputation as a business-friendly locale. *See infra* notes 14–15 and accompanying text; *see also* Karl Baker, *Delaware May Finally Be Done with TransPerfect Feud*, DEL. ONLINE (Nov. 21, 2017), <http://www.delawareonline.com/story/money/business/2017/11/21/delaware-may-finally->

tail below, the public outcry did not deter the Delaware Supreme Court from issuing an unwavering opinion in February 2017 affirming the Chancery Court's order and heavy-handedly rejecting Shawe's argument on appeal that the Chancery Court had exceeded its statutory authority.¹³

The controversial decision in *TransPerfect* placed Section 226 in the national spotlight, soliciting considerable media attention and even served as a debate topic in Delaware's 2016 gubernatorial race.¹⁴ Employees of TransPerfect, calling themselves "Citizens for a Pro Business Delaware", filed a petition with the Delaware Supreme Court arguing that the Chancery Court's contentious decision not only placed their jobs at risk, but also threatened to tarnish the state of Delaware's reputation as the "gold standard" for corporate law.¹⁵ To be sure, much of the media attention surrounding the Chancery Court's decision, and the arguments dealt with by the Supreme Court on appeal, focused on whether the Chancery Court overstepped its bounds in using Section 226 to force the sale of a *profitable* company against the objections of a 50% stockholder.¹⁶ Though the Delaware Supreme Court confidently rejected Shawe's argument that the Chancery Court's decision posed a harrowing threat to Delaware business law, the draconian concerns of judicial overreach, which permeated Shawe's appellate briefs, were echoed in the form of public protest by third parties.¹⁷

done-transperfect-feud/884363001/ [https://perma.cc/S248-DP6T] (noting that "many observers were shocked" by the Chancery Court's decision to force a sale of the company).

¹³ See generally *Shawe v. Elting*, 157 A.3d 152 (affirming the Chancery Court's decision to appoint a custodian with the power to sell the corporation). Indeed, the Delaware Supreme Court explicitly stated that the Chancery Court's decision "was supported by the facts found after trial, was permitted by the statute, and thus was not an abuse of discretion." See *id.* at 160.

¹⁴ Jeff Murdock, *Supreme Court Decision a Loss for TransPerfect Workers*, DEL. ONLINE (Oct. 20, 2016), <http://www.delawareonline.com/story/money/2016/10/18/transperfect-workers-motion-support-appeal-denied/92349636/> [https://perma.cc/KEJ5-SCCF] (discussing the lawsuit filed by TransPerfect employees in response to the Chancery Court's decision to appoint a custodian to sell the company, and noting that the controversial decision earned a seat at the table as a debate topic in the Delaware race for governor).

¹⁵ See *id.* The reader should note that the concern voiced by Citizens for a Pro-Business Delaware that the decision in the TransPerfect case will render them "jobless" may not be valid; indeed, it may well be that following the closing of an impending sale, the majority of the employees will be left in place to continue operating the company. See *id.* Nonetheless, it is not difficult to imagine, given Delaware's reputation as a business-friendly state, why other owners of the countless businesses subject to Delaware law, might share the concerns voiced by the Citizens for a Pro Business Delaware regarding judicial overreach. See *id.* (noting that the heated debate at the heart of the TransPerfect case was "closely watched among businesses incorporated in Delaware").

¹⁶ *Shawe v. Elting*, 157 A.3d at 155 (noting that on appeal, Shawe argued that the Chancery Court "exceeded its statutory authority" by forcing the sale of a "solvent company"); see Lucas, *supra* note 6 (noting the argument that a forced sale of a profitable business constitutes "judicial overreach").

¹⁷ *Shawe v. Elting*, 157 A.3d at 160 (noting that the Chancery Court's decision to use Section 226 to appoint a custodian with the power to sell TransPerfect was not an abuse of the court's

Less attention, however, has been given to the implications of a subsidiary issue raised by the TransPerfect case: the extent to which, in applying Section 226, courts should consider the “bad faith defense” to judicial intervention.¹⁸

On occasion, courts have denied petitions for judicial intervention in cases where the respondent has been able to demonstrate that the director (or stockholder) seeking intervention has done so in bad faith by *manufacturing* a deadlock with the ultimate goal of securing a forced sale of the company.¹⁹ As such, the bad faith defense to a petition for judicial intervention seeks to demonstrate that a director or stockholder has manufactured a “phony” deadlock or has sought to give the appearance of a deadlock by refusing to agree to any business decisions in order to pursue a court-ordered sale.²⁰ In the TransPerfect case, Shawe raised this defense, arguing that Elting actively refused to agree to any business decision so that she could subsequently convince the Chancery Court that she and Shawe were in such a state of deadlock that the appointment of a custodian, with the power to sell under Section 226, was warranted.²¹ Said another way, Shawe alleged that the apparent deadlock between he and Elting was not genuine, but that Elting had manufactured the deadlock in order to pursue her ultimate exit strategy of seeking a forced sale of the corporation under Section 226.²²

discretion); Opening Brief for Appellant at 1, *Shawe v. Elting*, 157 A.3d 152 (Del. 2017) (No. 423, 2016); Murdock, *supra* note 14 (discussing the lawsuit filed by TransPerfect employees).

¹⁸ See Millien v. Popescu, C.A. No. 8670–VCN, 2014 WL 656651, at *2 n.17 (Del. Ch. Feb. 19, 2014) (describing the idea of a manufactured deadlock in the context of a Section 226 action). This Note uses the term “bad faith defense” in relation to Section 226 actions to refer to the same phenomenon articulated by Peter Mahler in his explanation of the “bad faith defense” in relation to business dissolution proceedings in New York: as a defense that a respondent seeks to oppose court-ordered dissolution (or, as in the TransPerfect case, to oppose a court-ordered sale) by arguing that the petitioner has manufactured a deadlock. See Peter Mahler, *Is Bad Faith a Defense in Business Divorce Proceedings?*, FARRELL FRITZ: N.Y. BUS. DIVORCE (Sept. 16, 2013), <https://www.nybusinessdivorce.com/2013/09/articles/deadlock/is-bad-faith-a-defense-to-deadlock-dissolution-petition/> [https://perma.cc/5TKU-XZ9D] (discussing the bad faith defense in relation to New York’s Business Corporation Law, Section 1104-a).

¹⁹ *Millien*, 2014 WL 656651, at *2 n.17 (describing the idea of a manufactured deadlock in the context of a Section 226 action).

²⁰ See *id.*; see also *Vila v. BVWebTies LLC*, C.A. No. 4308-VCS, 2010 WL 3866098, at *7 (Del. Ch. Oct. 1, 2010) (describing the bad faith defense to judicial dissolution in the context of LLCs, though holding that the petitioner had not manufactured a deadlock in bad faith).

²¹ *In re Shaw*, 2015 WL 4874733, at *28.

²² See *id.*; see also Mahler, *supra* note 18 (citing Section 1104-a of New York’s Business Corporation Law in stating that the case law preventing minority shareholders from engaging in acts made in bad faith undertaken with the goal of forcing an involuntary dissolution is clear, but that the New York case law regarding the so-called bad faith defense as it pertains to 50% shareholders is “uncertain” and “sporadic[c]”). The bad faith defense also arises in the context of LLCs. See Peter Mahler, *Bad Faith Defense Gets Boost in LLC Dissolution Case*, FARRELL FRITZ: N.Y. BUS. DIVORCE (Sept. 19, 2016) <https://www.nybusinessdivorce.com/2016/09/articles/dissolution->

This Note explores the phenomenon of the bad faith defense as applied to Section 226 petitions, and the difficulty in determining whether a deadlock between directors is genuine, or whether it has been “manufactured” as a long-term strategy in order to achieve a forced sale.²³ This Note does not endeavor to critique the Chancery Court’s decision nor the Supreme Court’s subsequent affirmation in the TransPerfect case, but rather uses the TransPerfect case to contextualize the thorny issues raised by the bad faith defense (i.e., the difficulty of asking a court to inquire into a director’s subjective and underlying motivations for pursuing a forced sale under Section 226).²⁴ Part I of this Note provides the requisite background information necessary to conceptualize the bad faith defense by detailing the requirements laid out in Section 226 and describes how the Chancery Court applied Section 226 in the TransPerfect case.²⁵ Part II of this Note discusses how courts in both Delaware and foreign jurisdictions have interpreted and applied the bad faith defense in analogous dissolution proceedings and highlights the inherent difficulties in assessing the defense.²⁶ Part III of this Note discusses that although the Delaware Chancery Court has expressly considered the bad faith defense in a number of actions brought under Title 8, Section 273 of the Delaware General Corporation Law (the “joint venture

defenses/bad-faith-defense-gets-boost-llc-dissolution-case/ [https://perma.cc/M27G-EKSW] (discussing the notion that the bad faith defense has “osmosed” into LLC dissolution cases, and discussing *Wilford v. Coltea*, No. 15-856-BC (Tenn. Ch. Ct. 20th Dist. May 16, 2016), a Tennessee business court case where the court applied Delaware LLC law to allegations that a 50% owner of an LLC had manufactured a deadlock in order to seek a forced dissolution).

²³ See Mahler, *supra* note 18 (discussing the bad faith defense to business dissolution actions under New York law); see also Millien, 2014 WL 656651, at *2 n.17 (describing the idea of a manufactured deadlock in the context of a Section 226 action); Vila, 2010 WL 3866098, at *7 (finding that a deadlock in an LLC dissolution case had not been manufactured).

²⁴ See *infra* notes 29–174 and accompanying text.

²⁵ See *infra* notes 29–77 and accompanying text.

²⁶ See *infra* notes 78–123 and accompanying text. The reader should note that the bad faith defense is not tied directly to other notions of good or bad “faith” seen elsewhere in corporate law. See Peter Mahler, *Unraveling the Implied Covenant of Good Faith and Fair Dealing: Guest Post by Professor Daniel Kleinberger*, FARRELL FRITZ: N.Y. BUS. DIVORCE (Nov. 30, 2015), <https://www.nybusinessdivorce.com/2015/11/articles/delaware/unraveling-the-implied-covenant-of-good-faith-and-fair-dealing-guest-post-by-professor-daniel-kleinberger/> [https://perma.cc/RW9H-3Y49] (discussing the differences between the various types of “good faith” claims, and distinguishing, for example, the implied covenant of good faith and fair dealing from the corporate law “Caremark” good faith claims); see also Mohsen Manesh, *Delaware and the Market for LLC Law: A Theory of Contractibility and Legal Indeterminacy*, 52 B.C. L. REV. 189, 244–47 (2011) (noting the often-confused distinction between the implied covenant of good faith and fair dealing and the fiduciary duty of good faith in the LLC context). For the purpose of this Note, the bad faith defense refers only to allegations made by a respondent in a Section 226 or Section 18-802 action governed by Delaware law—that the petitioner has improperly manufactured dissension and deadlock as a long-term litigation strategy in order to convince a court to order the appointment of a custodian (or dissolution, in the case of a Section 273 or Section 18-802 action). See *In re Shaw*, 2015 WL 4874733, at *28; Mahler, *supra* note 18.

dissolution statute”) and Title 6, Section 18-802 (the “LLC dissolution statute”), it has rarely taken an explicit position on the bad faith defense’s viability in Section 226 actions.²⁷ Finally, it argues that because of the inherent difficulty in subscribing to a clear formula to assess the deadlock, coupled with the inexorable reality that, manufactured or not, a deadlock is still a deadlock, the best way for courts to deal with the bad faith defense going forward might be to embrace a wholesale rejection of the defense’s legitimacy.²⁸

I. THE REQUIREMENTS OF SECTION 226 AND ITS APPLICATION IN THE TRANSPERFECT CASE

A. *The Underlying Requirements of Section 226—What Findings Warrant the Appointment of a Custodian?*

Section 226 sets forth three instances in which the Chancery Court has the power to appoint a custodian, two of which are relevant to this Note.²⁹ The first, set out in Section 226(a)(1), permits the court to appoint a custodian for a solvent corporation when the stockholders are “so divided” that they are unable to elect successors to fill director positions.³⁰ The second, laid out in Section 226(a)(2), solicits a markedly more involved analysis.³¹ This subsection requires three conjunctive preconditions for a court appointment of a custodian: (i) the directors of the corporation are deadlocked with respect to managerial decisions such that a vote required for “curative action” by the board of directors cannot be obtained; (ii) the corporation’s

²⁷ See *infra* notes 124–174 and accompanying text.

²⁸ See *infra* notes 124–174 and accompanying text. The reader should note that although this Note specifically argues in favor of rejecting the availability of the bad faith defense in Section 226 actions, the arguments in favor of doing so also apply to the (somewhat) analogous corporate/LLC dissolution provisions found under Sections 273 and 18-802 of the Delaware General Corporation Law, respectively. See *infra* notes 124–174 and accompanying text. As is explained in footnote 174 of this Note, as a practical matter, it might be easier for courts to justify their rejection of the bad faith defense in Section 226 actions despite the reality that the courts have, with some degree of regularity, both implicitly and explicitly accepted and grappled with the defense in Section 273 and Section 18-802 cases, given that there is very little precedent dealing with the bad faith defense in Section 226 cases specifically. See *Millien*, 2014 WL 656651, at *2 n.17. This Note will conclude by arguing that policy arguments in favor of abandoning the bad faith defense in corporate dissolution cases are somewhat analogous to the reasoning that led to the shift away from fault to no-fault divorce statutes. See Ira Mark Ellman & Sharon Lohr, *Marriage as Contract, Opportunistic Violence, and Other Bad Arguments for Fault Divorce*, 1997 U. ILL. L. REV. 719, 719, 721–25 (describing the shift to a no-fault divorce system and rejecting claims that no-fault divorce regimes have contributed to “societal-ills”).

²⁹ DEL. CODE ANN. tit. 8, § 226(a) (2011).

³⁰ *Id.* § 226(a)(1).

³¹ *Id.* § 226(a)(2). Section 226(a)(2) requires a more rigorous analysis given the multipart inquiry that it solicits, as compared to Section 226(a)(1), which asks only one question. See *id.* § 226(a)(1)–(2).

business is suffering or is threatened with irreparable injury; and (iii) the stockholders are unable to terminate the deadlock by way of a stockholder vote.³² The Chancery Court's final order in the TransPerfect case dedicates the bulk of its analysis to reconciling the facts of the case with the three preconditions set forth in Section 226(a)(2).³³ It is worth noting that a court's finding that the requirements of any subsection of Section 226(a) have been satisfied does not trigger a mandatory duty to appoint a custodian.³⁴ The introductory phrase to Section 226(a) states that upon the satisfaction of any of the three following provisions under Section 226(a), a court may appoint a custodian, indicating that such an appointment is "not mandatory."³⁵

The language set forth by subsection (b) of Section 226 is that which ultimately lies at the crux of the ongoing dispute in the TransPerfect case.³⁶ In effect, Section 226(b) is instructive on the powers granted to a custodian, whose appointment the Chancery Court has deemed necessary through application of Section 226(a).³⁷ This subsection states, in pertinent part, that said custodian has the duty to "continue the business" of the company and shall not "liquidate its affairs and distribute its assets" unless the court so orders.³⁸

³² See *id.* § 226(a)(2). See generally *Giuricich v. Emtrol Corp.*, 449 A.2d 232 (Del. 1982) (describing the preconditions that must be met in order for a court to determine that the appointment of a custodian is permitted under Section 226).

³³ *In re Shawe & Elting LLC*, C.A. No. 9661-CB, C.A. No. 9686-CB, C.A. No. 9700-CB, C.A. No. 10449-CB, 2015 WL 4874733, at *26–30 (Del. Ch. Aug. 13, 2015) (citing DEL. CODE ANN. tit. 8, § 226(a)), *aff'd*, *Shawe v. Elting*, 157 A.3d 152 (Del. 2017). The third scenario, laid out in Section 226(a)(3), allows the court to appoint a custodian when the corporation has "abandoned its business" and has subsequently failed to take adequate measures to "dissolve, liquidate, or distribute its assets." See DEL. CODE ANN. tit. 8, § 226(a)(3).

³⁴ See DEL. CODE ANN. tit. 8, §§ 226(a)–(b); *In re Shaw*, 2015 WL 4874733, at *30 n.313 (citing DEL. CODE ANN. tit. 8, § 226(a)).

³⁵ *In re Shaw*, 2015 WL 4874733, at *30. When a court finds that the facts of a case meet any of the three scenarios set out in Section 226(a), and subsequently uses its discretionary authority to appoint a custodian, the analysis then proceeds under Section 226(b) to determine what the custodian has the power to do. See *id.*

³⁶ See DEL. CODE ANN. tit. 8, § 226(b); *In re Shaw*, 2015 WL 4874733, at *30.

³⁷ See DEL. CODE ANN. tit. 8, § 226(a)–(b).

³⁸ See *id.* § 226(b). The factors or circumstances that motivate the court to exercise its discretion to appoint a custodian in the first place will intrinsically be instructive in appropriately determining the role of the custodian. See *In re Shaw*, 2015 WL 4874733, at *30; see also *Miller v. Miller*, C.A. No. 2140–VCN, 2009 WL 554920, at *4 (Del. Ch. Feb. 10, 2009) (detailing the considerations that may inform a court's decision to exercise its discretion to appoint a custodian under Section 226(a), and suggesting that such considerations are intrinsically linked to the limits imposed on the custodian's authority under Sections 226(b)). For example, in the TransPerfect case, the Chancery Court noted that the goal of "remedying an injustice" first bears on the court's decision as to whether or not to exercise its discretion to appoint a custodian, and also informs the court's parameters for the custodian's role or authority. See *In re Shaw*, 2015 WL 4874733, at *30 (citing *Miller*, 2009 WL 554920, at *4). Notably, regarding the question of the custodian's authority, the Chancery

B. Section 226(a) as Applied to the Facts of TransPerfect

The Delaware Chancery Court's analysis in the TransPerfect case illustrates the operation of Section 226 in practice.³⁹ The court's initial task was to shoehorn the nature of the dispute between Elting and Shawe, the co-owners, into one of the scenarios set out in Section 226(a).⁴⁰ First, the court held that the requirements of Section 226(a)(1) were satisfied by pointing to the corporation's bylaws, which provide for a three-member board.⁴¹ The court noted that Shawe and Elting have served as the corporation's only two directors since it was formed in 2007, and that the third director-seat has consistently remained vacant.⁴² In December 2014, the parties eventually stipulated that they were unable to fill the empty seat and also failed to elect successors to Elting and Shawe, whose terms had expired.⁴³ As such, the court summarily held that Section 226(a)(1) was "plainly" satisfied.⁴⁴

Both the Chancery Court and the Delaware Supreme Court dedicated considerable more attention to the analysis of whether or not the requirements of Section 226(a)(2) had been satisfied.⁴⁵ As further examined below,

Court has explicitly stated that upon appointment, the custodian's powers should be "tailored as narrowly as possible." See *Miller*, 2009 WL 554920, at *4.

³⁹ See *In re Shaw*, 2015 WL 4874733, at *26–30.

⁴⁰ See *id.* at *26 (beginning the analysis by detailing the requirements of § 226(a)(1)).

⁴¹ See *id.* (finding § 226(a)(1) satisfied).

⁴² See *id.* In September 2014, Elting brought an action to hold an annual meeting in order to officially elect directors of TransPerfect. See DEL. CODE ANN. tit. 8, § 211 (2011) (vesting shareholders of Delaware corporations with the right to file an action demanding that the corporation hold an annual meeting for the purpose of electing members to the board of directors); *In re Shaw*, 2015 WL 4874733, at *26.

⁴³ *In re Shaw*, 2015 WL 4874733, at *26.

⁴⁴ *Id.* On appeal, the Delaware Supreme Court agreed, noting in particular that Shawe did not specifically object to the Chancery Court's finding that a custodian could be appointed under Section 226(a)(1). See *Shawe v. Elting*, 157 A.3d 152, 161 (Del. 2017). The Delaware Supreme Court reiterated that Shawe acquiesced to the fact that Section 226(a)(1) was satisfied in its subsequent discussion of Section 226(a)(2) by arguing that as a threshold matter, Shawe's argument that Section 226(a)(2) does not apply is "academic," given that he agreed that Section 226(a)(1) was satisfied. See *id.* The reader may, however, consider approaching the Delaware Supreme Court's characterization of this issue with some skepticism, as the counter to that argument would be that Shawe's argument that Section 226(a)(2) does not apply (even though Section 226(a)(1) does) is far from academic and is highly relevant, given that the degree of authority that the court bestows upon a custodian under Section 226(b) is dependent on the court's analysis under Section 226(a). See *Miller*, 2009 WL 554920, at *4 (detailing the considerations that may inform a court's decision to exercise its discretion to appoint a custodian under Section 226(a), and suggesting that such considerations are intrinsically linked to the limits imposed on custodians under Section 226(b)). Indeed, a finding that only Section 226(a)(1) was satisfied and not Section 226(a)(2) as well might lead to the appointment of a custodian with *only* the power to act as a tie-breaking director, and *not* the power to sell the company outright. See *id.*

⁴⁵ See *Shawe v. Elting*, 157 A.3d at 161; *In re Shawe*, 2015 WL 4874733, at *28. In addition to petitioning for the appointment of a custodian with the power to sell the corporation under Section 226, Elting also argued, in the alternative, for the court to exercise its discretion and grant "equitable dissolution" outside the bounds of the statute, but the Chancery Court declined to enter-

a thorough discussion of the applicability of Section 226(a)(2) is necessary in order to ultimately grant the custodian sweeping power to act as an auctioneer.⁴⁶ Section 226(a)(2) sets forth three necessary conditions that must be found in order for a court to implement authority thereunder.⁴⁷

First and foremost, there must be a finding that the directors of the corporation are in a state of deadlock.⁴⁸ The Chancery Court reasoned that this first condition of Section 226(a)(2) was unequivocally satisfied.⁴⁹ In fact, the court stated that Shawe and Elting were in a state of deadlock with respect to “several matters of critical importance to the Company.”⁵⁰ The court identified a number of points of disagreement, each of which lent credence to an overall indicia of deadlock between Shawe and Elting.⁵¹

The court first pointed to the fact that, as evinced by the record, Shawe and Elting had been consistently incapable of reaching an agreement on the issue of “non-tax distributions.”⁵² After noting Shawe’s disagreement with Elting’s distribution strategy, the court forcefully stated that by persistently refusing to agree to a distribution scheme, Shawe had effectively used the fact that Elting needs his consent to implement distributions as “leverage” over Elting.⁵³ This kind of leverage, the court stated, is indicative of the

tain that option, finding that Elting had not successfully demonstrated that Shawe had breached a duty to the corporation or engaged in the kind of self-interested actions necessary to show the kind of aggressive misconduct that equitable dissolution requires. *In re Shaw*, 2015 WL 4874733, at *33–34.

⁴⁶ *In re Shaw*, 2015 WL 4874733, at *26, *31 (stating that such a grant of power should be an act of “last resort”).

⁴⁷ DEL. CODE ANN. tit. 8, § 226(a)(2).

⁴⁸ *See id.*; *Hoban v. Dardanella Elec. Corp.*, No. 7615, 1984 WL 8221, *1 (Del. Ch. June 12, 1984) (explaining that in order for a court to conclude that a deadlock between a corporation’s directors exists, the directors must be “so divided respecting the management of the affairs of the corporation that the required vote for action by the board of directors cannot be obtained”).

⁴⁹ *In re Shaw*, 2015 WL 4874733, at *26 (noting that “the requirements of this statute plainly have been met”).

⁵⁰ *See id.*

⁵¹ *See id.* at *26–27 (listing various disputes between Shawe and Elting regarding the company).

⁵² *See id.* As noted by the court, the corporation had, for the majority of its history, made distributions to the stockholders in order to make up for both Shawe and Elting’s tax liabilities arising out of the income that they each respectively derived from the corporation. *See id.* at *26 n.285. That “seemingly simple” practice became problematic and resulted in considerable controversy between Shawe and Elting in 2013 when Shawe attempted to pay a portion of the \$21 million dollars due in taxes from capital held by the LLC, which Elting absolutely opposed. *See id.* Elting had expressed an interest in having the amount of non-tax distributions paid to her and Shawe increase in conjunction with increases in the corporation’s profits. *See id.* at *26. Elting wanted the corporation to pay regular non-tax distributions to her and Shawe, which could be based on EBITDA or “some other performance based metric.” *See id.*

⁵³ *Id.* at *26 (detailing the areas of disagreement between Shawe and Elting).

“mutual hostaging” that has, over the past two years, come to be the hallmark of Shawe and Elting’s business relationship.⁵⁴

The second point of contention that the court relied on in order to justify its conclusion was Shawe and Elting’s inability to agree on the corporation’s acquisition opportunities and “true ups.”⁵⁵ Elting had consistently opposed Shawe’s desire to pursue acquisitions for the corporation by reasoning that she distrusts Shawe, and that additional acquisitions would increase her investment with Shawe.⁵⁶ With respect to Shawe and Elting’s disagreements over “true-ups,” the court noted that the corporation had historically performed an accounting to square both Elting’s and Shawe’s respective use of the corporation’s funds, and that by preventing the corporation from performing true-ups Shawe had persistently blocked Elting from being able to determine if she was owed extra compensation.⁵⁷

A third area of controversy that the court pointed to evincing a complete deadlock was Shawe and Elting’s fundamental discord in setting hiring and retention policies for employment personnel and advisors.⁵⁸ Elting had expressed a desire to terminate a number of senior executives whom she believed to have sided with Shawe and were “insubordinate” to her despite her role as co-CEO of the corporation.⁵⁹ Having discussed the nature of the contention surrounding distributions, acquisitions, true-ups, and hiring decisions, the Chancery Court had little trouble concluding that Shawe and Elting, the sole directors of the corporation, were in such a state of deadlock regarding management decisions that curative action could not be obtained.⁶⁰ Before moving on to discuss whether the second required condi-

⁵⁴ *See id.*

⁵⁵ *Id.* at *27. Here, the term “true up” is being used as an accounting term referring to a reconciliatory process of squaring projected balance sheet values with real-time reports of the business’s assets, inventory, ecetera. *See True-up*, BUSINESSDICTIONARY, <http://www.businessdictionary.com/definition/true-up.html> [<https://perma.cc/JFP3-Z89G>].

⁵⁶ *In re Shaw*, 2015 WL 4874733 at *27. The court unequivocally sided with Elting on this issue and justified Elting’s distrust of Shawe as entirely reasonable. *See id.* To support its assertion that Elting’s distrust of Shawe was justified, the court pointed to a host of ostensibly hostile endeavors that Shawe undertook including taking part in a “secret campaign to spy on Elting,” seeking to have Elting prosecuted by filing a “Domestic Incident Report” after an apparently benign altercation, and distributing an inter-office memorandum to employees in Elting’s division “accusing her of collusion and financial improprieties.” *See id.*

⁵⁷ *See id.* The court sided with Elting on both of these disagreements, stating that with respect to the disagreement over acquisitions, Elting’s distrust of Shawe was unquestionably justified, and added that, regarding their disagreements over true-ups, it “historically had been the case” that Shawe’s expenses exceeded Elting’s. *See id.*

⁵⁸ *See id.*

⁵⁹ *See id.* Shawe opposed these organizational changes, and the two were also unable to agree on how to replace the head of Human Resources or how to hire a new public relations firm, leaving the corporation without either since 2014. *Id.*

⁶⁰ *See id.* at *28; *Hoban*, 1984 WL 8221, at *1 (describing the degree of director deadlock required in order to justify a finding that Section 226(a)(2) has been satisfied). Accordingly, hav-

tion under Section 226(a)(2) (harm to the business) was satisfied, the court took a quick detour, reviewing a claim that Elting had manufactured a deadlock in order to achieve a court-ordered sale (i.e., Shawe's bad faith defense, which will be addressed in Part II of this Note).⁶¹

Recognizing that the second condition (harm to the business) was a "closer question than the mere existence of deadlocks," the court dedicated a lengthy discussion to this portion of the analysis.⁶² The court was faced with the unavoidable fact that at the time it issued its decision, the corporation was (and still is) highly profitable.⁶³ Shawe continued to argue on appeal that the appointment of a custodian under Section 226(a)(2) was inappropriate in the context of a profitable corporation.⁶⁴ Chancellor Bouchard, however, rejected the idea that the fact that the Corporation was profitable was dispositive, and reasoned that even profitable corporations can be faced with a threat of "irreparable injury."⁶⁵ Accordingly, although recognizing

ing found that the first condition under Section 226(a)(2) (director deadlock) was satisfied, the court proceeded to analyze whether the second and third conditions were satisfied (irreparable harm to the business as a result of the deadlock, and stockholder inability to break the deadlock). *See In re Shaw*, 2015 WL 4874733, at *28–30 (finding Section 226(a)(2) satisfied).

⁶¹ *See In re Shaw*, 2015 WL 4874733, at *28 (refusing to accept Shawe's contention that "Elting had manufactured the deadlocks . . . simply to facilitate a sale of the Company and liquidate her interest in it").

⁶² *Id.*

⁶³ *Id.* at *28 n.292 (citing Post-Trial Brief for Respondent at 71–78, *In re Shawe & Elting* (2015) (C.A. No. 9661-CB, C.A. No. 9686-CB, C.A. No. 9700-CB, C.A. No. 10449-CB)). The question of whether or not the business of the corporation was faced with irreparable injury lies at the heart of much of the public debate and discourse surrounding the *TransPerfect* case. *See, e.g.*, Jeff Mordock, *Delaware Court Orders TransPerfect Sale*, DEL. ONLINE (June 21, 2016), <http://www.delawareonline.com/story/money/2016/06/21/delaware-court-orders-transperfect-sale/86183404/> [<https://perma.cc/N38E-6BF3>] (noting the public condemnation of the decision to auction off a profitable company). That the Chancery Court erred in focusing too much on the personal disputes between Shawe and Elting and ignored the glaring fact that the corporation was (and is) highly profitable also appears to be the crux of Shawe's arguments on appeal. *See* Jeff Mordock, *TransPerfect Case Heads to Delaware Supreme Court*, DEL. ONLINE (Oct. 3, 2016), <http://www.delawareonline.com/story/money/2016/10/03/transperfect-case-heads-delaware-supreme-court/91459168/> [<https://perma.cc/E8TY-3MQ9>] (noting that the appellate briefs filed by Shawe argue that the Chancery Court focused too much on the "dysfunctional working environment" at the corporation, and failed to separate "personal disagreements" from "corporate injury").

⁶⁴ *See* Opening Brief for Appellant at 1, 4, *Shawe v. Elting*, 157 A.3d 152 (Del. 2017) (No. 423, 2016) (arguing that "for the first time in Delaware's modern corporate history" the Chancery Court used Section 226 to force shareholders to sell, and reasoning that the forced sale of such a profitable company is inappropriate given the Chancery Court's inability to point to financial harm).

⁶⁵ *In re Shaw*, 2015 WL 4874733, at *30. Chancellor Bouchard also reasoned that "irreparable injury" to a corporation can involve more than just financial harm, and can include "harm to a corporation's reputation, goodwill, customer relationships, and employee morale." *See id.* at *28 (citing *Kirpat, Inc. v. Del. Alcoholic Beverage Control Comm'n*, 741 A.2d 356, 358 (Del. 1998)); *see also* *Hollinger Int'l Inc. v. Black*, 844 A.2d 1022, 1090 (Del. Ch. 2004) (stating that "irreparable injury" exists whenever a subsequent monetary damages award would require guesswork).

the corporation's high profitability, the court focused on the "dysfunctional" nature of the management and concluded that the "irreparable harm" requirement of Section 226(a)(2) was satisfied.⁶⁶ The court then proceeded to conclude that the third requirement of Section 226(a)(2)—that the shareholders were unable to break the deadlock—was easily satisfied.⁶⁷

C. With Section 226(a) Satisfied, Appointment of a Custodian with the Power to Sell the Corporation Was Next

Having found both Section 226(a)(1) and Section 226(a)(2) satisfied, the Chancery Court concluded that the appointment of a custodian was warranted.⁶⁸ As has already been alluded to, it was not merely Chancellor Bouchard's decision to appoint a custodian that placed this case in the national spotlight, but his decision as to what the appointed custodian would have the authority to do.⁶⁹ Chancellor Bouchard recognized that he had three available options: (i) refrain from appointing a custodian and dismiss the Section 226 petition completely; (ii) appoint a custodian to act as a third director in order to serve as the "tie-breaking" vote; or (iii) appoint a custodian with the power to sell the corporation.⁷⁰ He chose the third option.⁷¹

In August 2016, Shawe appealed the Chancery Court's August 2015 Order, for the appointment of a custodian with the power to sell the corpora-

⁶⁶ *In re Shaw*, 2015 WL 4874733 at *30. In arriving at the conclusion that the corporation was indeed threatened with irreparable harm, the Chancery Court focused on the damage that the feud between Shawe and Elting was doing to "employee morale and retention." *See id.* at *29 (relying on employee statements). The Chancery Court also reasoned that because acquisitions made by the company had historically accounted for a significant portion of its revenue, a continued deadlock resulting in the prevention of further acquisitions could cause harm to the business. *Id.* at *30.

⁶⁷ *Id.* at *30. Because the stockholders (Shawe, Elting, and Shawe's mother (who owns only 1% of the corporation's stock) had indeed been unable to elect directors, the court did not need to dedicate a lengthy analysis to determining whether the "third condition" under Section 226(a)(2) was satisfied. *Id.*

⁶⁸ *Id.* at *30–31.

⁶⁹ *See Lucas, supra* note 6 (arguing that Chancellor Bouchard's decision to appoint a custodian to sell the corporation constitutes "judicial overreach" especially when considering the corporation's high profits and thousands of employees).

⁷⁰ *See In re Shawe & Elting LLC*, C.A. No. 9661-CB, C.A. No. 9686-CB, C.A. No. 9700-CB, C.A. No. 10449-CB, 2015 WL 4874733, at *31 (Del. Ch. Aug. 13, 2015). Chancellor Bouchard rejected the first option by reasoning that it would be unjust to leave Elting to her own devices and force her to sell her 50% interest in the corporation and accepted Elting's argument that doing so would afford Shawe a windfall, because Elting would be able to receive more money were the corporation to be sold wholly and then subsequently divided. *See id.* at *30. Chancellor Bouchard rejected the second alternative by reasoning that simply appointing a third director to act as a tie-breaker would "enmesh" an outsider and the court "into matters of internal corporate governance" for an unnecessarily long period of time. *See id.* Finally, Chancellor Bouchard reasoned that the only viable option was option three: appointing a custodian with the power to sell the corporation. *See id.*

⁷¹ *Id.* at *31.

tion, to the Delaware Supreme Court.⁷² On appeal, Shawe focused less on the underlying factual findings of deadlock and dysfunction and primarily argued that the Chancery Court had acted beyond its power by ordering a custodian to sell a profitable corporation.⁷³ Shawe also argued that in the alternative, the Chancery Court ignored “less drastic measures” that could have been taken to remedy the deadlock.⁷⁴ In a 4–1 decision, the Delaware Supreme Court resolutely affirmed Chancellor Bouchard’s decision to appoint a custodian with the power to sell the corporation and rejected, for a number of reasons, Shawe’s argument that Chancellor Bouchard had gone beyond the bounds of the statute.⁷⁵

⁷² See *Shawe v. Elting*, 157 A.3d 152, 154–55 (Del. 2017). Although this Note will not discuss the details of the auction plan that the Chancery Court eventually approved, the reader should note that the plan allowed for bids from both Elting and Shawe, as well as bids from third parties. See Katia Savchuk, *Delaware Supreme Court Upholds Forced Sale of TransPerfect and Sanctions Against Cofounder*, FORBES (Feb. 13, 2017), <https://www.forbes.com/sites/katiasavchuk/2017/02/13/delaware-supreme-court-upholds-forced-sale-of-transperfect-and-sanctions-against-cofounder/#669430417b5b> [<https://perma.cc/5VYA-THMR>]. This is one of many alternatives to conducting auctions in business divorce cases. See, e.g., Claudia M. Landeo & Kathryn E. Spier, *Irreconcilable Differences: Judicial Resolution of Business Deadlock*, 81 U. CHI. L. REV. 203, 146–47 (2014) (discussing the notion that placing a realistic value on the assets of a closely-held corporation is a difficult task, and suggesting that courts should use the “Shotgun” auction method in business dissolution cases where one owner names a “buy-sell” price, and the other owner must then buy or sell at said price). Landeo and Spier reason that the “Shotgun” method has the beneficial effect of making the owner who names the buy-sell price choose a price that is fair, because, after all, “he or she may end up on either side of the transaction.” See Landeo & Spier, *supra*.

⁷³ See *Shawe v. Elting*, 157 A.3d at 155; see also Opening Brief for Appellant at 18–19, *Shawe v. Elting*, 157 A.3d 152 (Del. 2017) (No. 423, 2016) (arguing that the Chancery Court’s order, which “requires Shawe to sell his own property against his will” is a “radical ruling” and that Section 226 only authorizes a custodian to oversee the liquidation or distribution of the “corporation’s assets, not the sale of a stockholder’s property”).

⁷⁴ *Shawe v. Elting*, 157 A.3d at 155. Shirley Shawe (Shawe’s mother, and 1% stockholder) joined in the appeal to the Delaware Supreme Court, yet took an entirely different approach; represented by Alan Derschowitz, Shirley Shawe argued that the custodian’s sale constitutes an “unconstitutional taking of her one share” of the corporation’s stock. See *id.*

⁷⁵ See generally *Shawe v. Elting*, 157 A.3d 152 (affirming the Chancery Court’s decision to appoint a custodian with the power to sell the corporation). To the extent that the reader is interested in the details and statutory analysis underlying the Delaware Supreme Court’s decision to affirm the Chancery Court, she should turn her attention to the lengthy Delaware Supreme Court opinion. See generally *id.* (affirming the Chancery Court’s decision to appoint a custodian with the power to sell the corporation). This Note, however, will not go into any further detail on the Delaware Supreme Court’s opinion upholding the Chancery Court’s Order, as this Note explores the issue of the bad faith defense to the appointment of a custodian under Section 226 (a defense that Shawe raised in front of the Chancery Court, but that was not explicitly dealt with on appeal). See *In re Shaw*, 2015 WL 4874733, at *28. Because the Delaware Supreme Court did not address Shawe’s bad faith defense, the majority of the citations in the rest of this Note will be to the Chancery Court’s August 2015 Order, which did, albeit briefly, deal with this argument. See *id.*; see also Savchuk, *supra* note 72 (quoting Elting’s reaction to the Supreme Court decision). The reader should also note that in a separate opinion issued on the same day, the Delaware Supreme Court affirmed sanctions ordered by the Chancery Court against Shawe for misconduct during the course of the litigation in the lower court. See *Shawe v. Elting*, 157 A.3d at 145. Shawe petitioned for a writ of certiorari to the U.S. Su-

Along with an appeal to the Delaware Supreme Court, Chancellor Bouchard's decision solicited a palpable outcry in the press, on the Delaware political scene, and even in the form of a lawsuit filed on behalf of TransPerfect employees.⁷⁶ Whether or not the Chancery Court overstepped its bounds is not the purpose of this Note, however; rather, this Note explores the subsidiary issue that the Chancery Court gave relatively short shrift when explaining the second condition of Section 226(a)(2): the idea of a manufactured deadlock (i.e., the bad faith defense).⁷⁷

II. THE BAD FAITH DEFENSE TO JUDICIAL INTERVENTION IN PRACTICE

To say that the Chancery Court's decision to appoint a custodian to sell TransPerfect against the objections of a 50% owner has caused commotion in the Delaware business community would be an understatement.⁷⁸ In the months that followed Chancellor Bouchard's decision, and throughout the appeal in front of the Delaware Supreme Court, even a casual observer would have likely detected the unusual volume of media attention and out-

preme Court on this separate action regarding the imposition of sanctions (which was denied), but has not petitioned for certiorari in the Section 226 action. *See id.* Following the Delaware Supreme Court's decision to affirm the Chancery Court's order to force the sale of the company, Shawe stated that that he planned to appeal that decision to the U.S. Supreme Court. *See Philip Shawe Launches the \$100,000 Law Student Scholarship Competition to Examine TransPerfect Delaware Case at the U.S. Supreme Court Level*, PR NEWSWIRE (Mar. 02, 2017), <https://www.prnewswire.com/news-releases/philip-shawe-launches-the-100000-law-student-scholarship-competition-to-examine-trans-perfect-delaware-case-at-the-us-supreme-court-level-300415171.html> [https://perma.cc/K557-ULH7]. Shawe, however, has since ostensibly backed away from that claim, and in November 2017, the custodian appointed by the Delaware Chancery Court to oversee the sale announced that an agreement had been reached, which would allow Shawe to purchase Elting's shares. *See Baker, supra* note 12. The Delaware Supreme Court also summarily rejected Shirley Shawe's constitutional takings argument as one that was waived for failure to raise it before the Chancery Court. *See Shawe v. Elting*, 157 A.3d at 169.

⁷⁶ *See supra* notes 13–17 and accompanying text.

⁷⁷ *See In re Shaw*, 2015 WL 4874733, at *28; Mahler, *supra* note 18 (describing the bad faith defense in relation to business dissolution actions in New York).

⁷⁸ *See* Jeff Mordock, *Facts, Not Law, to Be in Dispute at TransPerfect Hearing*, DEL. ONLINE (Jan. 17, 2017), <http://www.delawareonline.com/story/money/2017/01/17/facts-not-law-dispute-transperfect-hearing/96659466/> [https://perma.cc/X46R-CWGJ] (predicting that Shawe's attorneys would attempt to argue to the Delaware Supreme Court not that the Chancery Court misapplied Delaware law, but rather that the "factual record [did] not support a need for a sale" and noting that although the Chancery Court's decision was supported by certain "corporate jurists," it had also been criticized by certain "high-profile" names, including Rudy Giuliani); Leslie Pappas, *Did Del. Court Violate Shareholder Rights in TransPerfect Case?* BLOOMBERG LAW: BIG LAW BUS., (Jan. 17, 2017), <https://bol.bna.com/did-del-court-violate-shareholder-rights-in-transperfect-case/> [https://perma.cc/5Z3C-D98A] (suggesting that one of the reasons why this particular case has gained so much attention is that, in addition to the fact that TransPerfect is highly profitable, there are "relatively few instances of 50-50 corporate disputes" in general, quoting an interview with Professor Lawrence Hamermesh from Widener University's Delaware Law School).

rage surrounding the case.⁷⁹ The decision to use Section 226 to force the sale of a profitable Delaware corporation is seen by many as a draconian step backwards for Delaware corporate law.⁸⁰

Pessimistic as the “pro-business” objectors may be, as a practical matter, the Delaware Supreme Court has spoken, and unless and until the U.S. Supreme Court says otherwise, the question of whether courts may use Section 226 to force the sale of a profitable company is no longer up for debate.⁸¹ As such, a more productive mode of discourse might focus on issues that may arise in the developing doctrine surrounding Section 226 itself, rather than one that persists in casting the decision in the TransPerfect case as the catalyst for the crumbling of Delaware’s business-friendly empire.⁸²

⁷⁹ See Randall Chase, *Judge: It’s Time for TransPerfect’s Delaware Court ‘Saga to End,’* WDEL (July 12, 2017), [http://www.wdel.com/news/judge-it-s-time-for-transperfect-s-delaware-court-saga/article_d4c67e34-672a-11e7-a067-4304175186a3.html__\[https://perma.cc/LTM4-7EHF\]](http://www.wdel.com/news/judge-it-s-time-for-transperfect-s-delaware-court-saga/article_d4c67e34-672a-11e7-a067-4304175186a3.html__[https://perma.cc/LTM4-7EHF]) (noting that a New York judge in a related action filed by Shawe referred to the TransPerfect case history as a “saga”); Jeff Mordock, *Alan Dershowitz, Justice Strine Spar Over TransPerfect*, DEL. ONLINE, [http://www.delawareonline.com/story/news/2017/01/18/sparks-fly-heated-transperfect-case/96719902/\[https://perma.cc/PUM9-7N5H\]](http://www.delawareonline.com/story/news/2017/01/18/sparks-fly-heated-transperfect-case/96719902/[https://perma.cc/PUM9-7N5H]) (noting that Attorney Alan Dershowitz had been obtained to represent Shawe’s mother in oral arguments in front of the Delaware Supreme Court and discussing the fact that the Chancery Court’s decision to appoint a custodian to conduct a sale of TransPerfect has “generated a lot of controversy”); Katia Savchuk, *Inside the Nasty Corporate Divorce Between Ex-Lovers Who Built a Company Worth Nearly \$1 Billion*, FORBES (May 25, 2016), [https://www.forbes.com/sites/katiasavchuk/2016/05/25/liz-eling-transperfect-engaged-cofounders-phil-shawe-corporate-divorce/#32e9694a59c6\[https://perma.cc/9MDX-BNMU\]](https://www.forbes.com/sites/katiasavchuk/2016/05/25/liz-eling-transperfect-engaged-cofounders-phil-shawe-corporate-divorce/#32e9694a59c6[https://perma.cc/9MDX-BNMU]) (narrating the background of the feud between Shawe and Elting).

⁸⁰ See Jeff Feeley, *Delaware Judge at Center of Power Controversy Fights Lawsuit*, BLOOMBERG LAW: BIG L. BUS. (Nov. 8, 2016), [https://bol.bna.com/delaware-judge-at-center-of-power-controversy-fights-lawsuit/\[https://perma.cc/VD6M-FU9D\]](https://bol.bna.com/delaware-judge-at-center-of-power-controversy-fights-lawsuit/[https://perma.cc/VD6M-FU9D]) (discussing the lawsuit filed by TransPerfect’s director of corporate strategy, Timothy Holland, against Delaware Chancery Court Judge Andre Bouchard, claiming that Chancellor Bouchard “overstepped his authority” by appointing a custodian to sell a profitable corporation); see also Mordock, *supra* note 78 (noting that high profile individuals, such as the former New York City Mayor, have “blasted” the decision to force the sale of TransPerfect as an instance of inappropriate governmental intrusion into private business affairs); *Pro Business Group Makes Statement in TransPerfect Case*, DEL. ONLINE, <http://www.delawareonline.com/videos/news/local/2017/01/18/pro-business-group-makes-statement-transperfect-case/96735366/> (displaying a video showing Chris Coffey, a spokesperson for Citizens for a Pro-Business Delaware, standing with numerous TransPerfect employees outside of the Delaware Supreme Court courthouse, stating that the Chancery Court’s decision to force the sale of such a successful company has put the jobs of 4,000 employees in ninety-two countries and forty-six states at risk).

⁸¹ See generally *Shawe v. Elting*, 157 A.3d 152 (Del. 2017) (affirming the Delaware Chancery Court’s decision to appoint a custodian with the power to sell the corporation).

⁸² See Tom McParland, *TransPerfect-Linked Group Lobbies to Curb Forced Sales of Corporations*, DEL. L. WKLY. (Jan. 20, 2017), [https://www.law.com/delawerelawweekly/almID/1202777316002/?slreturn=20180017072834\[https://perma.cc/8DMM-Y7GY\]](https://www.law.com/delawerelawweekly/almID/1202777316002/?slreturn=20180017072834[https://perma.cc/8DMM-Y7GY]) (providing an example of a group that has prophesized that the TransPerfect decision is tantamount to a catastrophe that will doom Delaware corporate law if not overturned, Citizens for a Pro-Business Delaware has “waged a sophisticated public relations campaign” and has proposed legislation to the Delaware State Bar Association, which seeks to “curb the Court of Chancery’s power to appoint a corporate custodian”).

Although it seems unlikely that the TransPerfect decision will unleash a sudden outpouring of new Section 226 petitions, it is likely that the Chancery Court will eventually face the same question in a future case and will then be required to square new facts with the precedent laid down in the TransPerfect case.⁸³ Although the Chancery Court's in-depth and deliberate decision in the case indicates that the court is, on the whole, well-equipped to address future Section 226 petitions, there is one aspect of such cases that the TransPerfect case (and previous case law) has left unresolved: how to assess the bad faith defense to an involuntary sale under Section 226.⁸⁴ Section A of this part explains in greater depth what the bad faith defense to judicial intervention is by illuminating how the defense has been applied in other jurisdictions outside of Delaware.⁸⁵ Section B of this part discusses the doctrine's appearance in Delaware case law.⁸⁶

⁸³ See *In re Shawe & Elting LLC*, C.A. No. 9661-CB, C.A. No. 9686-CB, C.A. No. 9700-CB, C.A. No. 10449-CB, 2015 WL 4874733, at *81 (Del. Ch. Aug. 13, 2015) (noting that the legal analysis solicited in the TransPerfect case is "unusual"); Pappas, *supra* note 78 (same).

⁸⁴ See generally *In re Shawe*, 2015 WL 4874733 (carefully analyzing Elting's petition for the appointment of a custodian). As discussed *supra*, although he did briefly consider (before rejecting) Shawe's contention that the deadlock was not one that arose out of bona fide business disagreements but rather was calculatedly manufactured out of Elting's desire to eventually force a sale of TransPerfect, Chancellor Bouchard's decision gave relatively little attention to Shawe's bad faith defense. See *id.* at *28.

⁸⁵ See *infra* notes 87–105 and accompanying text.

⁸⁶ See *infra* notes 106–123 and accompanying text. A brief caveat of the foregoing sections is necessary: the Chancery Court only cited to one case, *Millien v. Popescu*, that had dealt with the bad faith defense in conjunction with Section 226. See *In re Shawe*, 2015 WL 4874733, at *28. This suggests that Delaware courts have rarely expressly considered the bad faith defense with respect to a petition seeking the appointment of a custodian under Section 226. See *id.*; *Millien v. Popescu*, C.A. No. 8670–VCN, 2014 WL 656651, at *2 n.17 (Del. Ch. Feb. 19, 2014). The Chancery Court did consider what could be called a different version of the defense in a 1983 case, *Moore v. C.H.M. Enters., Inc.*, where it denied a Section 226 petition because the petitioner was at fault for failing to service the company's debts, which was the reason for seeking the appointment of a custodian through Section 226. See *Civ. A. No. 7294*, 1983 WL 102620, at *2 (Del. Ch. Nov. 9, 1983). Similarly, the court more recently suggested that a stockholder should not be allowed to use Section 226 to achieve an end that she would not be able to achieve through "proper" conduct. See *Balch Hill Partners, L.P. v. Shocking Techs., Inc.*, C.A. No. 8249–VCN, 2013 WL 588964, at *3 (Del. Ch. Feb. 7, 2013). Although both *Moore* and *Balch Hill* do indeed provide instances where the court has inquired into the conduct/intent of the petitioner in a Section 226 action, they both concern the broader question of whether "unclean hands" should bar a petitioner from seeking Section 226 relief, and do not deal with the specific issue of a petitioner who actively sought to manufacture dissension and deadlock between stockholders or directors for the purpose of convincing the court to appoint a custodian with the power to sell. See *Balch Hill*, 2013 WL 588964, at *3; *Moore*, 1983 WL 102620, at *2.

*A. Opposing Views Regarding the Relevance of Allegations
of a Petitioner's Bad Faith Motives*

“Irreconcilable differences” leading to deadlocks between business owners has been described as a phenomenon somewhat unique to closely-held business entities, including close corporations, limited partnerships, and limited liability companies.⁸⁷ Dissolution proceedings in Delaware for these kinds of entities are governed by Title 8, Section 273 and Title 6, Section 18-802 of the Delaware General Corporation Law.⁸⁸ The TransPerfect case sheds light on another provision of Delaware law that deals with deadlocks in larger corporations with more than two stockholders: Section 226.⁸⁹ Although the statutory hurdles over which a Section 226 petitioner must overcome might serve as a substantial check against frivolous or meritless petitions for judicial intervention, some courts have recognized that the statutory option for a court-ordered sale may nonetheless appear an enticing exit strategy for 50% shareholders looking to “cash out” of the business.⁹⁰

⁸⁷ 6 AM. JUR. PROOF FACTS 2d 387, Westlaw (database updated Feb. 2017) (noting that the phenomenon of director deadlock is one that is “peculiar” and particularly crippling to close corporations in part because of the fact that many persons who choose to incorporate their small businesses using the corporate form do so for tax or limited-liability reasons, and are persons who think of themselves as being partners with their co-founder, but do not necessarily consider certain implications of the corporate form).

⁸⁸ DEL. CODE ANN. tit. 8, § 273 (2011) (governing dissolution petitions for joint ventures with only two stockholders); DEL. CODE ANN. tit. 6, § 18-802 (2013) (governing dissolution proceedings for limited liability companies).

⁸⁹ See DEL. CODE ANN. tit. 8, § 226. Although each of these statutes applies to a different type of entity, all embrace the goal of resolving deadlocks when the court is convinced not only that the company faces irreparable harm but also that there is no possibility of the deadlock being resolved. See 16A FLETCHER CYCLOPEDIA L. CORPS. § 8066.10, Westlaw (database updated Sept. 2016) (suggesting that the dissolution of a deadlocked corporation is seen by the courts as a last resort and detailing alternatives to a forced sale, such as ordering the “buyout of the petitioning shareholder” or appointing a director to serve as a tiebreaker). As discussed in Part I *supra*, Section 226 contains somewhat exacting requirements that must be met in order for a court to decide in favor of a petitioner’s request for judicial dissolution. See *supra* notes 30–77 and accompanying text; see also Kenneth A. Gerasimovich, *Delaware Chancery Court Appoints a Custodian to Sell Deadlocked Company*, GREENBERG TRAURIG: INSIGHTS (Dec. 15, 2015), <https://www.gtlaw.com/en/insights/2015/12/delaware-chancery-court-appoints-a-custodian-to-sell-deadlocked-company> [<https://perma.cc/KE5J-H6UV>] (noting that the TransPerfect case ostensibly posed an “ideal situation” for a Section 273 petition, but that because Shawe’s mother “held a nominal 1 percent” of the Corporation, that statute did not apply).

⁹⁰ See *e.g.*, Millien v. Popescu, C.A. No. 8670–VCN, 2014 WL 656651, at *2 n.17 (Del. Ch. Feb. 19, 2014) (refusing to grant dissolution under Section 226(a)(2) in part because the petitioning stockholder “sought to create a deadlock by refusing to consider any issue” and concluding that the statute was not meant to apply to such circumstances); Feinberg v. Silverberg, Decision and Order, Index No. 3120-11, at *8 (Sup. Ct. Nassau Cty. Sept. 6, 2013) (discussing the phenomenon of the manufactured deadlock created in bad faith by a 50% shareholder in order to obtain a court-ordered dissolution and examining cases that have both accepted and rejected such alleged manufacturing as a defense to dissolution under New York’s dissolution statute (N.Y. BUS. CORP. LAW § 1104), which largely mirrors Section 226).

Said another way, courts have noted the possibility that a savvy individual with a goal of selling a business over the objections of his or her co-owner could act in bad faith with the specific purpose of manufacturing a deadlock as a long-term litigation strategy in the hopes of achieving a court-ordered sale.⁹¹

At first glance, it might seem only fair that the objecting 50% shareholder be able to respond to a petition for judicial intervention by alleging that the deadlock has not arisen out of a bona fide business disagreement but rather out of a premeditated attempt on the part of the petitioner to create the appearance of an irreconcilable situation (i.e., employ the bad faith defense).⁹² That being said, courts have recognized that it is not entirely clear whether such a defense should be accepted.⁹³ Namely, there is a question as to whether a finding of fault on the part of the petitioner is even relevant to dissolution statutes, which ostensibly ask only *whether* there is an irreconcilable deadlock, but do not concern themselves with *why*.⁹⁴ In *Feinberg v. Silverberg*, a 2013 case in New York, the court was faced with this very question and discussed the conundrum that the bad faith defense posed with respect to involuntary dissolution cases brought under Section 1104 of New York's Business Corporation Law (a statute that for the purposes of this Note can be considered analogous to Section 226).⁹⁵

Citing a number of New York appellate cases, the *Feinberg* court asked whether or not the alleged bad faith of a petitioner seeking dissolution is even relevant.⁹⁶ As explained in *Feinberg*, some courts have reasoned that

⁹¹ See *Feinberg*, Index No. 3120-11, at *8.

⁹² See Post-Trial Brief for Respondent at 4–5, 7, *In re Shawe & Elting* (2015) (C.A. No. 9661-CB, C.A. No. 9686-CB, C.A. No. 9700-CB, C.A. No. 10449-CB). In the *TransPerfect* case, Shawe argued at length that long before filing the petition for dissolution under Section 226, Elting set into motion a “calculated plan” to achieve a court-ordered sale of the corporation by “refusing to exercise her business judgment and by manufacturing ‘deadlock’ for purposes of litigation.” See *id.* at 4–5.

⁹³ See, e.g., *Feinberg*, Index No. 3120-11, at *3–6 (illuminating opposing views regarding whether or not bad faith should be considered in dissolution proceedings).

⁹⁴ See *id.* (ultimately finding that a petitioner's bad faith is relevant in deciding whether to order the dissolution of a business, but acknowledging that some courts have ostensibly supported the opposing argument that the petitioner's motives are irrelevant); Mahler, *supra* note 18.

⁹⁵ See *Feinberg*, Index No. 3120-11, at *3–6. In *Feinberg*, the objecting shareholder alleged that the petitioner had intentionally created the “very basis for dissension.” See *id.* The objecting shareholder argued that the petitioner did this with the ultimate goal of convincing a court that the two shareholders were in such a state of deadlock that the business must be sold. See *id.* For a more detailed discussion of the *Feinberg* decision, see Peter Mahler's September 16, 2013, article, *Is Bad Faith a Defense in Deadlock Dissolution Proceedings?* which provides an excellent analysis of the *Feinberg* decision and succinctly summarizes the opposing views in New York case law regarding the viability of the bad faith defense. See Mahler, *supra* note 18.

⁹⁶ *Feinberg*, Index No. 3120-11, at *2, *4–6, *8 (citing *In re Goodman v. Lovett*, 200 A.D.2d 670, 670–71 (N.Y. App. Div. 1994) (holding that the reasons underlying the dissension are irrele-

the corporate dissolution statute does not solicit an investigation into the underlying reason for dissension and that it is entirely irrelevant to “ascribe fault” to either the petitioner or the respondent.⁹⁷ This line of analysis posits that the court’s only concern should be whether or not dissension *exists* and whether it has led to a deadlock between co-owners.⁹⁸ This position appears to suggest that even if a petitioner maliciously instigated quarrels with a co-owner with the specific intent of creating dissension, a resulting deadlock, though manufactured, is still a deadlock.⁹⁹

As noted in *Feinberg*, courts endorsing the opposing approach have explicitly explored the reasons underlying the dissension, inquired into the fault on the part of the petitioner, and held that an allegation of bad faith on the part of a petitioner constitutes a valid defense to dissolution proceedings.¹⁰⁰ The *Feinberg* court recognized that although these two competing strands of cases may appear “contradictory,” they can actually be “harmonized.”¹⁰¹ According to *Feinberg*, an inquiry into fault on the part of a petitioner is *sometimes* relevant.¹⁰² The court explained that in cases where courts have rejected the relevance of the reasons behind the dissension, the “common thread” was that there was “no real dispute” as to whether the deadlock at issue was “bona fide”, thus making an examination of fault unnecessary.¹⁰³ Alternatively, according to *Feinberg*, in cases where the court

vant) and *In re Meyers v. Gold*, 77 A.D.2d 652, 652 (N.Y. App. Div. 1980) (embracing the position that “allegations of a petitioner’s bad faith constitute a defense to a dissolution proceeding”).

⁹⁷ See *In re Goodman*, 200 A.D.2d at 670–71 (noting that it is unnecessary to examine the reasons underlying a deadlock because the law governing court-ordered dissolution only asks if dissension exists and does not solicit an inquiry into the “underlying reasons for the dissension”).

⁹⁸ See *id.* A strict interpretation of a judicial dissolution statute such as Title 8, Section 226 of the Delaware General Corporation Law or Section 1104 of the New York Business Corporation Law appears to support the argument that the underlying reason for the dissension between co-owners is entirely irrelevant to whether a court should grant dissolution based on shareholder/director deadlock. See *id.* A proponent of this view might argue that because the goal supporting such statutes is to act as a remedy of last resort by salvaging for the company’s shareholders whatever value is obtainable, the pivotal inquiry is *whether* a deadlock posing irreparable harm exists, and not *why* that deadlock exists. See *id.* This argument is endorsed in Part III of this Note. See *infra* notes 124–174 and accompanying text.

⁹⁹ See *In re Gordon & Weiss*, 32 A.D.2d 279, 279 (N.Y. App. Div. 1969) (rejecting the notion that the alleged bad faith of a petitioner seeking dissolution under New York’s Business Corporation Law Section 1104 is relevant); see also Mahler, *supra* note 18.

¹⁰⁰ See *Feinberg*, Index No. 3120-11, at *6–7, *8 (citing *In re Meyers*, 77 A.D.2d at 652); see also Mahler, *supra* note 18. Mahler describes the treatment of New York’s judicial dissolution statute (N.Y. BUS. CORP. LAW § 1104) as a “spectrum,” with cases that consider the statute to be a “no-fault statute” and focus solely on whether or not the owners “can no longer get along” on one side; and cases that inquire into the “reasons for, and the bona fides of the alleged dissension” in deciding whether or not to order a dissolution on the other. See Mahler, *supra* note 18.

¹⁰¹ See *Feinberg*, Index No. 3120-11, at *8; see also Mahler, *supra* note 18.

¹⁰² See *Feinberg*, Index No. 3120-11, at *8.

¹⁰³ *Id.*; see, e.g., *In re Goodman*, 200 A.D.2d at 670–71 (rejecting consideration of petitioner’s bad faith by reasoning that “the underlying reason for the dissension is of no moment”); *In re*

has agreed to inquire into the cause of the apparent discord between co-owners, there was a legitimate question as to whether the deadlock was “real” or “feigned”.¹⁰⁴ As such, *Feinberg* concluded that a finding of fault is immaterial when dissension and deadlock “actually exist” but that the “intent” for creating dissension and deadlock is significant in distinguishing between that which is “real” from that which is “feigned.”¹⁰⁵

B. Delaware’s Treatment of the Bad Faith Defense in Section 273 and Section 18-802 Cases

Although discussion of the bad faith defense in Delaware cases involving petitions for judicial intervention under Section 226 is sparse, a number of Delaware cases have explicitly discussed its applicability to Delaware’s dissolution statute for limited liability companies (“LLCs”) (Title 6, Section 18-802) and for joint ventures with only two stockholders (Title 8, Section 273).¹⁰⁶ Although an analysis of such cases does, in the aggregate, lead to the conclusion that Delaware has historically been willing to recognize the bad faith defense, it has not yet offered a concrete approach for assessing the defense.¹⁰⁷ Indeed, the Delaware Chancery Court has provided minimal

Gordon, 32 A.D.2d at 279 (stating that the alleged bad faith of a petitioner seeking dissolution under N.Y. BUS. CORP. LAW § 1104 is irrelevant); *see also* Mahler, *supra* note 18.

¹⁰⁴ *See Feinberg*, Index No. 3120-11, at *8; *see also* Mahler, *supra* note 18. Other jurisdictions have also supported the acceptability of the bad faith defense in deadlock dissolution cases. *See McLaren v. Falk*, No. 88-38-II, 1988 WL 53353, at *4 (Tenn. Ct. App. May 27, 1988). For example, in *McLaren*, the Tennessee Court of Appeals analogized the need for such a defense by stating: “A party should not be allowed to create dissension in the corporation, and then, like the defendant who killed his parents and begged for mercy because he was an orphan, use this grounds for the courts to dissolve the corporation.” *See id.*

¹⁰⁵ *Feinberg*, Index No. 3120-11, at *8. The court referred to “manufactured creation” of dissension as “the *sine qua non*” of bad faith and reasoned that a finding of such manufacturing would “belie a finding that the shareholders’ dissension poses an irreconcilable barrier to the continued functioning and prosperity of the corporation.” *See id.* Peter Mahler notes that the 2013 *Feinberg* decision was important in that it appeared to resolve (to a degree) the confusion over the applicability of the bad faith defense in “deadlock dissolution” cases for businesses with two 50% owners, but that since 1984, the bad faith defense has been used in dissolution cases brought by minority shareholders. *See* Mahler, *supra* note 18.

¹⁰⁶ *See, e.g., Vila v. BVWebTies LLC*, C.A. No. 4308-VCS, 2010 WL 3866098, at *7 (Del. Ch. Oct. 1, 2010) (describing the bad faith defense to judicial dissolution in the context of an LLC and holding that the fact that the owner had attempted to “implement changes” and offer solutions to resolve dissension prior to asserting that an impasse existed suggested that his actions were not in bad faith); *Arthur Treacher’s Fish & Chips, Inc. v. Ft. Lauderdale, Inc.*, 386 A.2d 1162, 1167 (Del. Ch. May 10, 1978) (refusing to strike a bad faith defense to a dissolution petition pursuant to Title 8, Section 273 of the Delaware General Corporation Law); *In re Bermor, Inc.*, No. VC 8401-VCL, 2015 WL 554861, at *3-4 (Del. Ch. Feb. 9, 2016) (reasoning that actions taken by a petitioner in an LLC dissolution case were not bad faith attempts to create dissension, but could be explained by other reasons).

¹⁰⁷ *See Wilford v. Coltea*, No. 15-856-BC, at *11 (Tenn. Ch. 20th Dist. May 16, 2016) (applying Delaware law to a petition for dissolution brought under Tennessee’s dissolution statute and

instruction for how to investigate the reasons underlying apparent dissension, i.e., how to determine whether a deadlock between owners is genuine or phony.¹⁰⁸ For example, in *Arthur Treacher's Fish & Chips, Inc. v. Fort Lauderdale, Inc.*, the court welcomed the respondent's defense to a dissolution petition that alleged that the petitioner sought dissolution "in furtherance of a scheme and conspiracy" to "coerce" petitioner into selling his stake in the company.¹⁰⁹ Although the court accepted the respondent's contention that the court should scrutinize the motives underlying the petition, the court neither discussed a method for how to identify bad faith motives, nor explained how a deadlock caused by bad faith motives differs in practical effect from a deadlock that is bona fide.¹¹⁰

The methodology employed in a more recent case discussing the bad faith defense, *In re McKinney-Ringham*, is similarly unclear.¹¹¹ There, the court provided the opaque explanation that its only grounds for refusing to grant dissolution would be if the petitioner knew that there was "no bona fide disagreement between the parties justifying a basis for disagreement over the dissolution of [the company]."¹¹² The *McKinney-Ringham* court expressed a concern that there may be times when a petition for dissolution

noting the infrequency with which Delaware courts have discussed the bad faith defense). Compare *In re McKinney-Ringham Corp.*, No. Civ. A. 15071, 1998 WL 118035, at *5 (Del. Ch. Feb. 27, 1998) (implicitly endorsing the viability of the bad faith defense by reasoning that dissension between owners must be "bona fide"), with *Fisk Ventures, LLC v. Segal*, No. Civ. A. 3017-CC, 2009 WL 73957, at *6 (Del. Ch. Jan. 13, 2009), *aff'd*, 984 A.2d 14 (Del. 2009) (offering reasoning that could be read to weaken the viability of the bad faith defense). Peter Mahler's September 19, 2016, article *Bad Faith Defense Gets Boost in LLC Dissolution Case* discusses the *Wilford* case and notes that *Wilford* might suggest that the bad faith defense is gaining legitimacy in cases involving the dissolution of Delaware LLCs. See Mahler, *supra* note 22. See generally *Wilford*, Case No. 15-856-BC (assessing the bad faith defense to dissolution of an LLC governed by Delaware law).

¹⁰⁸ See e.g., *Millien v. Popescu*, C.A. No. 8670-VCN, 2014 WL 656651, at *2 n.17 (Del. Ch. Feb. 19, 2014) (implying that allegations that a petitioner had manufactured a deadlock in a Section 226 action would constitute a legitimate defense without explaining how to differentiate a deadlock that a party "sought to create" from a bona fide deadlock); *In re McKinney-Ringham*, 1998 WL 118035, at *5 (stating that a court could deny the appointment of a custodian if there was no "bona fide disagreement between the parties" but omitting a discussion of how to determine whether a disagreement is "bona fide"); *Arthur Treacher's*, 386 A.2d at 1166 (inferring that bad faith could constitute a legitimate defense, but omitting an explanation of a method for examining the motives underlying a dissolution petition).

¹⁰⁹ See 386 A.2d at 1166. The court in *Arthur Treacher's* agreed that it is appropriate to "scrutinize" the "motive and purpose" of a Section 273 petition and underscored that it was "duty-bound" to stand up for the interests of shareholders, but did not explain protocol for determining the difference between a deadlock arising out of improper motives versus a deadlock arising out of genuine disagreements. See *id.*

¹¹⁰ See *id.* at 1167.

¹¹¹ *In re McKinney-Ringham*, 1998 WL 118035, at *5.

¹¹² See *id.* (noting that the court's role is to determine whether the dispute between owners is actually bona fide but omitting an explanation detailing what a non-bona fide or false disagreement would look like).

is based on reasons other than a “genuine impasse” but declined to explain how to differentiate between disputes that are genuine and those that are manufactured.¹¹³

To complicate matters, the Delaware Chancery Court has set forth reasoning that could be read to contradict its ostensible position that an allegation of bad faith motives for seeking dissolution is an acceptable defense at all.¹¹⁴ For example, in *Fisk Ventures, LLC v. Segal*, the Chancery Court explained that a co-owner of the business at issue had the right “to attempt to maximize its position” and the mere fact that he stood to benefit by petitioning for dissolution was not grounds for rejecting the petition.¹¹⁵ Also standing in the face of the argument that the court should examine a petitioner’s underlying motives is dicta set forth in *McKinney-Ringham*, where the court stated that it was a given that any petitioner seeking dissolution does so having come to the conclusion that the benefits of selling the company outweigh the benefits of continuing to carry on business.¹¹⁶ Finally, the Delaware Chancery Court has also suggested that allegations calling into question the integrity of a petitioner are better suited for breach of fiduciary duty actions, not dissolution proceedings.¹¹⁷

¹¹³ See *id.* The *McKinney-Ringham* court ultimately ordered dissolution, stating that it was satisfied that there was a bona fide disagreement about whether or not to continue the business, and also noted that the “potential for an inequitable result” for the opposing shareholders is not a sufficient reason for declining to order dissolution. See *id.* at *6–7.

¹¹⁴ See, e.g., *Fisk Ventures*, 2009 WL 73957, at * 6 (noting that the fact that petitioner stands to secure an advantageous position by seeking a court-ordered dissolution does not mean that the petition has been sought in bad faith and should be rejected).

¹¹⁵ See *id.* The court in *Fisk Ventures* rejected respondent’s argument that petitioner sought dissolution in bad faith and stated that respondent had failed to show that petitioner’s sole motivation for seeking dissolution was “to buy [the company’s] assets at fire sale price” calling such an argument a “conclusory allegation of inequitable action as a last-ditch effort” to deny a motion to dismiss. See *id.*

¹¹⁶ See *In re McKinney-Ringham*, 1998 WL 118035, at *5. The obviousness that anyone seeking a petition for dissolution (or, in the case of the *TransPerfect* case, seeking the appointment of a custodian to sell the corporation) has already concluded that doing so would be more advantageous or financially beneficial for the petitioner than carrying on in the course of business appears to be a somewhat legitimate argument for rejecting the bad faith defense. See *id.* The bad faith defense is premised on the fact that a petitioner who seeks dissolution (or the appointment of a custodian) by manufacturing a deadlock is committing an injustice. See *Feinberg*, Index No. 3120–11, at *8. The fact that the petitioner has decided that dissolution or a forced sale would be financially beneficial and undertakes a long-term strategy to effectuate that goal appears on the one hand, inequitable and malicious. See *id.* On the other hand, whether intentional or not, the court’s dicta in *McKinney-Ringham* suggests that such an inquiry into the petitioner’s motives is equivalent to staring deeply into a shallow pool: *obviously* a petitioner has calculated that seeking a dissolution or forced sale would be in their favor—otherwise, they would not be filing the petition in the first place. See *McKinney-Ringham*, 1998 WL 118035, at *5.

¹¹⁷ See *Wilford*, Case No. 15-856-BC, at *13 (citing *In re Cambridge Fin. Grp., Ltd.*, No. Civ. A. 9279, 1987 WL 19677, at *3 (Del. Ch. Nov. 9, 1987) (noting that there is a “thread running through Delaware law” claims akin to “breach of fiduciary duty claims” that should not be as-

Although the Chancery Court has occasionally appeared to deliver contradictory and ambiguous reasoning with respect to the acceptability of the bad faith defense, it has not left entirely unanswered the question of how to determine whether a deadlock is bona fide or manufactured.¹¹⁸ In 2010, in *Vila v. BVWebTies LLC*, the Chancery Court offered slightly more helpful insight into the manner in which a court can reasonably assess a bad faith defense.¹¹⁹ There, the court appeared to take into consideration factors such as “circumstantial evidence of intent, . . . design and timing, [and the petitioner’s] credibility” to draw inferences as to whether or not a petitioner had manufactured a deadlock in a bad faith attempt to force a sale.¹²⁰ For example, by tracing the timeline leading up to a professed deadlock between the business’s owners, the court found that the petitioner had taken a series of steps that appeared to be “last ditch” efforts to *prevent* an impending deadlock before ultimately filing an action for dissolution.¹²¹ Such attempts at remedial action, the court noted, indicated that the petitioner’s ultimate decision to file a petition for dissolution was not the product of a long-term exit strategy and demonstrated that the deadlock was genuine.¹²² Suffice it to say that although the mode of analysis set forth in *Vila* could be seen as a step in the right direction, it is far from a concrete formulation for determining whether a deadlock is phony or genuine.¹²³

III. DELAWARE COURTS SHOULD REJECT THE AVAILABILITY OF THE BAD FAITH DEFENSE IN SECTION 226 PROCEEDINGS

Although there is at least a traceable body of case law surrounding the Chancery Court’s treatment of the bad faith defense in Section 273 and Section 18-802 cases, the court has rarely given explicit consideration to the

essed in petitions seeking court-ordered dissolutions); *In re S. One-Stop, Inc.*, No. Civ. A. 7500, 1986 WL 628588, at *1 (Del. Ch. Dec. 3, 1986).

¹¹⁸ See *Vila*, 2010 WL 3866098, at *7 (inquiring as to whether or not an alleged deadlock was genuine).

¹¹⁹ See *id.* (ultimately finding that the plaintiff had not “manufactured a phony deadlock”).

¹²⁰ See *Wilford*, Case No. 15-856-BC, at *6 (citing *Vila*, 2010 WL 3866098, at *8). In *Wilford*, the Tennessee Business Court was faced with deciding whether to accept a bad faith defense to judicial dissolution of a Delaware LLC and set forth a detailed analysis of how Delaware cases have dealt with the bad faith defense in relation to the Delaware General Corporation Law Title 8, Section 273 and Title 6, 18-802; see also Mahler, *supra* note 22 (discussing the *Wilford* case).

¹²¹ *Vila*, 2010 WL 3866098, at *4, *7. The *Vila* court underscored the fact that the petitioner had, in what the court considered to be an attempt to prevent a deadlock, “proposed to personally commit an additional \$500,000 of capital and sought to implement managerial changes he hoped would transform [the LLC]” before claiming that the company was deadlocked. See *id.* at *7. Such gestures, the court said, indicated that the petitioner had not “in bad faith manufactured a phony deadlock” in an attempt to achieve a financial gain by securing a court order to dissolve the business. *Id.*

¹²² See *Vila*, 2010 WL 3866098, at *7.

¹²³ See *id.*

merits of the defense in a petition for the appointment of a custodian under Section 226.¹²⁴ Considering the rarity with which courts have used Section 226 to appoint a custodian to sell a company over the objections of a co-owner, the dearth of precedent analyzing the bad faith defense in Section 226 cases is unsurprising.¹²⁵ Although the Chancery Court in the TransPerfect case rejected Shawe's argument that Elting had manufactured the deadlock in bad faith, the court implicitly acknowledged that as a general matter, an allegation that an owner/director acted in bad faith to manufacture a deadlock constitutes a valid defense to a Section 266 action.¹²⁶ Although the Chancery Court did not seize on the opportunity to clarify a clear standard for determining whether a deadlock is manufactured or genuine, courts may be required to do so in the wake of the TransPerfect case.¹²⁷ One way for

¹²⁴ DEL. CODE ANN. tit. 8, §§ 226, 273 (2011) (authorizing court-ordered dissolution upon petition by a co-owner of a deadlocked joint venture with only two stockholders); DEL. CODE ANN. tit. 6, § 18-802 (2013) (authorizing court-ordered dissolution upon petition by an owner of a Delaware limited liability company). Although there are a number of Delaware cases that discuss the bad faith defense in conjunction with Section 273 and Section 18-802 cases, the only "precedent" cited in the TransPerfect decision suggesting that the Chancery Court had previously considered the applicability of allegations of bad faith manufacturing to a Section 226 petition is found in a footnote in a 2014 case that was primarily a contractual dispute between business owners. *See Millien v. Popescu*, C.A. No. 8670-VCN, 2014 WL 656651, at *2 n.17 (Del. Ch. Feb. 19, 2014). There, the court noted that although one party's petition for the appointment of a custodian under Section 226 was moot because of the court's decision on the contract dispute, the petition would nonetheless have been denied because the petitioner had "sought to create a deadlock by refusing to consider any issue." *See id.*; *see also Mahler*, *supra* note 22 (discussing the bad faith defense in relation to a Delaware LLC dissolution proceeding).

¹²⁵ *See In re Shawe & Elting, LLC*, C.A. No. 9661-CB, C.A. No. 9686-CB, C.A. No. 9700-CB, C.A. No. 10449-CB, 2015 WL 4874733, at *4 (Del. Ch. Aug. 13, 2015), *aff'd*, *Shawe v. Elting*, 157 A.3d 152 (Del. 2017). The disagreement over whether the claim that the TransPerfect case is the first time that Section 226 has been used to force a sale over the objections of a 50% owner is indeed accurate. *See id.* Although the Chancery Court took the position that such use is rare but not unprecedented, and Shawe's lawyers repeatedly pointed out that in previous cases where Section 226 had been used to force a sale over the other owner's objections, the owners were nonetheless in agreement that the business needed to be terminated yet simply could not agree as to the proper method of sale. *See Opening Brief for Appellant*, at 20–21, *Shawe v. Elting*, 157 A.3d 152 (Del. 2017) (No. 423, 2016). In his opening appellate brief, Shawe argued that neither of the two cases that the Chancery Court relied on in arguing that appointing a custodian with the power to sell is not unprecedented answers "the critical question of whether a forced sale is permitted because in each the stockholders had agreed that the company should be liquidated or sold." *See id.*

¹²⁶ *See In re Shawe*, 2015 WL 4874733, at *28 (quoting *Millien*, 2014 WL 656651, at *2 n.17) (noting that "this is not a case where a director has 'sought to create a deadlock by refusing to consider any issue'"). The Chancery Court did not reject Shawe's defense that Elting had manufactured the deadlock because such an argument does not constitute a valid defense, but because, according to the Chancery Court, the facts indicated that the deadlock was due to "genuine, good faith divisions." *See id.*

¹²⁷ *See generally In re Shawe*, 2015 WL 4874733 (omitting an in-depth discussion of how to determine if a deadlock is manufactured). Because the Chancery Court in the TransPerfect case tacitly acknowledged that allegations of bad faith deadlock manufacturing could constitute a valid

courts to address allegations of deadlocks manufactured in bad faith in relation to Section 226 actions would be to carry over the (vague) guidelines for determining whether a deadlock is genuine or manufactured from Section 273 and Section 18-802 cases.¹²⁸

A preferable, albeit more radical, approach to dealing with the bad faith defense in Section 226 cases might be to reject the legitimacy of the defense entirely.¹²⁹ The remainder of this Note offers support for this alternative approach.¹³⁰ By drawing on the opaqueness of courts' assessments of allegations of manufactured deadlocks in Section 273 and Section 18-802 cases, and on the difficulties faced by the Chancery Court in weighing the same allegations in the TransPerfect case, Section A of this part argues that abandoning the bad faith defense entirely in Section 226 actions makes sense from a practical standpoint.¹³¹ Section B of this part opines that the bad faith defense also breaks down from a theoretical viewpoint, and concludes by reviewing divorce proceedings, an analogous area of law that could be used to support the prohibition of the bad faith defense.¹³²

A. As a Practical Matter, Rejecting the Applicability of the Bad Faith Defense in Section 226 Actions Will Leave the Courts Better Off

In rejecting Shawe's contention that Elting had manufactured the deadlock leading to her filing of the Section 226 petition in bad faith, the TransPerfect court implicitly acknowledged that such claims, if substantiated by the facts, could constitute a valid defense in future cases.¹³³ Given that the Chancery Court has not explicitly answered whether inquiring into allegations of a manufactured deadlock is relevant to a Section 226 action,

defense, it is likely that respondents in Section 226 actions will continue to attempt to employ the bad faith defense, which might eventually signal to the courts that the development of a workable standard for distinguishing manufactured deadlocks from genuine deadlocks is necessary. *See id.* at *28.

¹²⁸ *See supra* notes 106–123 and accompanying text (noting the lack of tangible explanations in Delaware LLC dissolution cases for how to determine whether a deadlock is phony or genuine).

¹²⁹ *See supra* notes 106–123 and accompanying text; *see also In re Goodman v. Lovett*, 200 A.D.2d 670, 670–71 (N.Y. App. Div. 1994) (stating that the “underlying reason” for deadlock is “of no matter” and that it is also unnecessary to “ascribe fault to either party”). Again, the reader should note that *In re Goodman* and other cases cited by *Feinberg v. Silverberg* assessed the bad faith defense in the context of New York law, but that the reasoning therein is arguably applicable to Delaware law. *See Feinberg v. Silverberg*, Decision and Order, Index No. 3120-11, at *8 (Sup. Ct. Nassau Cty. Sept. 6, 2013); *In re Goodman*, 200 A.D.2d at 670–71.

¹³⁰ *See infra* notes 131–174 and accompanying text.

¹³¹ *See infra* notes 133–147 and accompanying text.

¹³² *See infra* notes 148–174 and accompanying text.

¹³³ *See In re Shawe & Elting, LLC*, C.A. No. 9661-CB, C.A. No. 9686-CB, C.A. No. 9700-CB, C.A. No. 10449-CB, 2015 WL 4874733, at *28 (Del. Ch. Aug. 13, 2015) (acknowledging (implicitly) the viability of the bad faith defense as a general matter by asserting that the facts of the case did not demonstrate that the deadlock had been manufactured).

courts faced with assessing the bad faith defense in future Section 226 actions will have the opportunity to diverge from the Chancery Court's hesitant acceptance of the bad faith defense in Section 273 and Section 18-802 cases.¹³⁴ In this sense, the door for rectifying the maladies of the bad faith defense is wide open in Section 226 actions, and from a practical standpoint, the most rational option might be to reject the relevance of allegations of a petitioner's bad faith in these proceedings entirely.¹³⁵ An inquiry into the motives underlying a Section 226 petition requires extensive fact-finding, and will inexorably hinge on inferences drawn from circumstantial evidence of the petitioner's subjective goals.¹³⁶

The difficulty in assessing the bad faith defense is illuminated by the TransPerfect court's rejection of Shawe's bad faith defense despite its ad-

¹³⁴ See *id.* Cases in both Delaware and foreign jurisdictions have delivered ostensibly contradictory arguments relevant to the question of whether to incorporate the bad faith defense into corporate-dissolution jurisprudence. See *supra* notes 87–123 and accompanying text. In his article detailing the *Feinberg* decision's treatment of the bad faith defense in New York, Peter Mahler describes a "spectrum": on one side rests the position that an inquiry into the reasons underlying apparent deadlock or dissension is both unnecessary and irrelevant. See *Feinberg*, Index No. 3120–11, at *8; *In re Goodman*, 200 A.D.2d at 670–71; Mahler, *supra* note 18. This position embraces the argument that the only relevant question for the court is whether a deadlock exists, and thus a finding of fault on the part of the petitioner is wholly inconsequential. See *Feinberg*, Index No. 3120–11, at *8; *In re Goodman*, 200 A.D.2d at 670–71; Mahler, *supra* note 18. On the opposite side of the "spectrum" rest cases that have taken the opposite approach: that although the existence of a deadlock is a threshold requirement, the court would be remiss not to investigate into the causes motivating the apparent dissension, in order to unearth the possibility that the deadlock has been manufactured in bad faith. See Mahler, *supra* note 18; see, e.g., *In re Meyers*, 77 A.D.2d 652, 652 (N.Y. App. Div. 1980). One might envision the middle ground as being occupied by a number of Delaware Chancery Court cases that accept the legitimacy of the bad faith defense in dissolution proceedings under Title 8, Section 273 and Title 6, Section 18-802 of the Delaware General Corporation Law, but evince slightly differing, even inconsistent, views on its application. See, e.g., *Wilford v. Coltea*, No. 15-856-BC, at *12–13 (Tenn. Ch. Ct. 20th Dist. May 16, 2016) (citing *In re McKinney-Ringham Corp.*, No. Civ. A. 15071, 1998 WL 118035, at *5 (Del. Ch. Ct. Feb. 27, 1998)) (noting that the court could deny a dissolution petition if it found that a deadlock had been manufactured, but also stating that the fact that a party might bring a dissolution action only after concluding that doing so could lead to a beneficial result does not indicate that the dissolution was manufactured); *Fisk Ventures, LLC v. Segal*, No. Civ. A. 3017-CC, 2009 WL 73957, at *6 (Del. Ch. Jan. 13, 2009), *aff'd*, 984 A.2d 14 (Del. 2009) (noting that the fact that petitioner stands to secure an advantageous position by seeking a court-ordered dissolution does not mean that the petition has been sought in bad faith and should be rejected); Mahler, *supra* note 18. That being said, although the Chancery Court has not provided clear guidance on how to determine whether a deadlock is manufactured, and has even appeared to poke holes in the bad faith defense (by noting, for example, that a petitioner's desire to gain an advantage through dissolution is inconsequential), it has generally recognized that the bad faith defense is a legitimate defense to petitions for dissolution. See *McKinney-Ringham*, 1998 WL 1188035, at *5; *Arthur Treacher's Fish & Chips, Inc. v. Ft. Lauderdale, Inc.*, 386 A.2d 1162, 1167 (Del. Ch. May 10, 1978).

¹³⁵ *In re Goodman*, 200 A.D.2d at 670–71 (rejecting consideration of petitioner's bad faith by reasoning that "the underlying reason for the dissension is of no moment").

¹³⁶ See *Wilford*, No. 15-856-BC, at *6; (citing *Vila v. BVWebTies, LLC*, No. Civ. A. 4308-VCS, 2010 WL 3866098, at *8 (Del. Ch. Oct. 1, 2010)).

mission that Elting had at times acted improperly to seek a forced sale.¹³⁷ Further, as discussed *supra*, despite their best efforts to do so, courts faced with interpreting the bad faith defense in Section 273 and Section 18-802 cases have failed to establish a cognizable, portable method for determining whether an apparent deadlock has been manufactured in bad faith and have even appeared to waiver on whether a petitioner's motives are pertinent at all.¹³⁸ If these cases are any indication—and there is no reason to think they are not—the likelihood that courts dealing with the bad faith defense in future Section 226 actions will fare any better appears to be scant.¹³⁹ As it happens, even when a court has expressly considered the bad faith defense and agreed to investigate the motives underlying an apparent deadlock, it has, in most of those cases, provided threadbare guidance for how to determine whether an impasse is genuine or manufactured.¹⁴⁰ Although the type of analysis exemplified in *Vila v. BVWebTies LLC* (which *Wilford v. Coltea* characterized as a consideration of factors such as “circumstantial evidence of intent”) is potentially useful, such modes of inquiry still fall short of providing a workable roadmap for future courts assessing the bad faith defense in Section 226 actions.¹⁴¹

Furthermore, despite the fact that the Chancery Court in the TransPerfect case implied that allegations of bad faith could constitute a legitimate defense in certain circumstances, it simultaneously managed to cast doubt upon whether those circumstances could ever exist and appeared to shy away from wanting to address Shawe's allegations of a manufactured dead-

¹³⁷ See *In re Shaw*, 2015 WL 4874733, at *28; *In re McKinney-Ringham*, 1998 WL 118035, at *5 (evinced seemingly contradictory reasoning in its discussion of the bad faith defense in holding that the court could deny a dissolution petition upon a finding of a manufactured deadlock, but nevertheless stating that for a party to seek a dissolution action only after concluding that such an action could lead to a beneficial result does not indicate that the deadlock was manufactured).

¹³⁸ See *supra* notes 106–123 and accompanying text.

¹³⁹ See *In re Shaw*, 2015 WL 4874733, at *28 (acknowledging that allegations of a manufactured deadlock constitute a valid defense yet omitting an explanation for how to determine whether a deadlock is manufactured or genuine); *In re McKinney-Ringham*, 1998 WL 118035, at *5 (holding that the court could deny a dissolution petition upon a finding of a manufactured deadlock, but nevertheless stating that for a party to seek a dissolution action only after concluding that such an action could lead to a beneficial result does not indicate that the deadlock was manufactured).

¹⁴⁰ See *supra* notes 106–123 and accompanying text. The *Wilford* court did provide some guidance when it cited to *Vila* as an example of a decision that considered “circumstantial evidence of intent” along with “design and timing” and “credibility” of the petitioner in assessing whether a deadlock was manufactured. See *Wilford*, No. 15-856-BC, at *6 (citing *Vila*, 2010 WL 3866098, at *8).

¹⁴¹ See *Wilford*, No. 15-856-BC, at *6 (citing *Vila*, 2010 WL 3866098, at *8) (discussing the factors considered by the *Vila* court in assessing the bad faith defense); *Vila*, 2010 WL 3866098, at *7 (finding that a deadlock had not been manufactured).

lock head-on.¹⁴² Indeed, the court's reasoning for determining that the deadlock was genuine and not manufactured appears somewhat self-contradictory: the court acknowledged that Elting had indeed "acted improperly at times" to "pursue the goal" of being "bought out" yet subsequently concluded that it could not be disputed that the facts demonstrate "genuine, good faith divisions" between Shawe and Elting.¹⁴³ The TransPerfect court's reluctance to acquiesce to Shawe's allegations that Elting had manufactured the deadlock, despite its admission that Elting acted "improperly" in furtherance of her goal of being "bought out," demonstrates the bad faith defense's inherent elusiveness.¹⁴⁴

An explicit statement that allegations of manufactured deadlocks do not constitute valid defenses in Section 226 actions would do away with the need for courts to examine the nebulous question of whether a petitioner conjured a deadlock.¹⁴⁵ It would also save courts from the awkwardness of

¹⁴² See *In re Shawe*, 2015 WL 4874733, at *28. In its 104-page decision, the Chancery Court dedicated only one paragraph to its rejection of Shawe's bad faith defense:

I reject Shawe's defense that Elting has manufactured the deadlocks described above simply to facilitate a sale of the Company and liquidate her interest in it. The record does show that Elting has expressed a desire to be bought out and acted improperly at times to pursue that goal. It also shows that she and Shawe both engaged in "mutual hostageing" over specific [decisions]. That said, this is not a case where a director has "sought to create a deadlock by refusing to consider any issue" until the deadlock is resolved. It cannot be legitimately disputed in my judgment that the matters discussed above reflect genuine, good faith divisions between Shawe and Elting and of a fundamental and systemic nature over how the Company should be managed.

Id.; see also Francis Pileggi, *Chancery Appoints Custodian to Break Deadlock of Profitable Corporation*, DEL. CORP. & COM. LITIG. BLOG (Aug. 28, 2015), <https://www.delawarelitigation.com/2015/08/articles/chancery-court-updates/chancery-appoints-custodian-to-break-deadlock-of-profitable-corporation/> [<https://perma.cc/L25D-7CPN>] (noting the lack of clarity in the Chancery Court's decision as to why the facts of the TransPerfect case differed from those of *Millien*, where the court declined to appoint a custodian in part because the facts indicated that one of the owners had manufactured the deadlock).

¹⁴³ See *In re Shawe*, 2015 WL 4874733, at *28. In fairness, at the time the decision was written, Chancellor Bouchard had been presiding over the TransPerfect drama for over two years, including a full bench trial where the intricacies of the feud between the couple were deeply explored and was thus likely well situated to make a determination as to the root causes of the deadlock. See generally *In re Shawe*, 2015 WL 4874733 (presenting a thorough conceptualization of the nature of the dispute between Shawe and Elting).

¹⁴⁴ See *In re Shawe*, 2015 WL 4874733, at *28. In a sense, the Chancery Court admits that Elting had a hand in manufacturing the deadlock, and the fact that the Chancery Court nonetheless followed that admission with a conclusion that the deadlock was genuine exemplifies the unworkable nature of the bad faith defense in general. See *id.*

¹⁴⁵ See *Wilford*, No. 15-856-BC, at *6 (citing *Vila*, 2010 WL 3866098, at *8). The *Vila* analysis, which, as described by *Wilford* is one that looks to factors such as "circumstantial evidence of intent" along with "design and timing" and "credibility" of the petitioner in order to assess the petitioner's motives, requires an extensive fact-finding mission on the part of the courts—a mission that would be wholly unnecessary if the courts decided to reject the viability of the bad faith

stretching to reject allegations of a manufactured deadlock in the face of facts, like those in the TransPerfect case, which suggest that the deadlock at issue might actually have been manufactured after all.¹⁴⁶ Finally, a wholesale denouncement of the bad faith defense's applicability to Section 226 actions would prevent litigants like Shawe from leading the court down a rabbit hole exploration of personal feuds in a futile attempt to cast doubt upon the petitioner's character.¹⁴⁷

B. Manufactured or Not, a Deadlock Is Still a Deadlock: Theoretical Support for Rejecting the Availability of the Bad Faith Defense

As discussed *supra*, some courts have ostensibly recognized that if the goal of statutes authorizing judicial intervention is to rescue shareholder value from potential irreparable harm caused by a fifty-fifty deadlock, then the reason for the deadlock should not matter.¹⁴⁸ A deadlock—whether arising out of genuine or bona fide disagreements about business decisions, dramatic personal feuds, or calculated, long-term tactics on the part of one owner to effectuate a court-ordered sale—is still a deadlock.¹⁴⁹ This reasoning is sound, and provides further support for future courts to explicitly reject the availability of the bad faith defense in Section 226 petitions.¹⁵⁰ If the court is serious about using Section 226 as a last-resort mechanism to prevent deadlocks from causing irreparable harm, then concerns about petitioners purposefully availing themselves of the statute after having intentionally manufactured the deadlock are irrelevant.¹⁵¹

defense wholesale. *See id.*; *see also In re: McKinney-Ringham*, 1998 WL 118035, at *5 (grappling with an argument that a petitioner had bad faith motives in seeking a court-ordered dissolution).

¹⁴⁶ *See In re Shawe*, 2015 WL 4874733, at *28 (justifying its conclusion that Elting had not manufactured the deadlock by stating that the deadlock was due to genuine disagreements despite admitting that Elting had “acted improperly at times” to “pursue the goal” of being “bought out”); *see also Fisk Ventures*, 2009 WL 73957, at * 6 (noting that the fact that petitioner stands to secure an advantageous position by seeking a court-ordered dissolution does not mean that the petition has been sought in bad faith and should be rejected).

¹⁴⁷ *In re Shawe*, 2015 WL 4874733, at *1 (noting the “painstaking detail” with which the court had to explain the intricacies of the personal feud between Shawe and Elting).

¹⁴⁸ *See Feinberg*, Index No. 3120–11, at *4–5 (Sup. Ct. Nassau Cty. Sept. 6, 2013); Mahler, *supra* note 18 (noting certain New York cases cited in *Feinberg* that have rejected the bad faith defense in connection with Section 1104 of New York's Business Corporation Law).

¹⁴⁹ *See In re Goodman*, 200 A.D.2d at 670–71 (rejecting consideration of petitioner's bad faith by reasoning that “the underlying reason for the dissension is of no moment”).

¹⁵⁰ *See In re Gordon & Weiss*, 32 A.D.2d 279, 279 (N.Y. App. Div. 1969) (rejecting the notion that the alleged bad faith of a petitioner seeking dissolution under Section 1104 of New York's Business Corporation Law is relevant).

¹⁵¹ *See id.* This position does not deny that such strategic manipulation might occur, but rather that such behavior is inevitable and inapposite to the court's determination as to whether a deadlock exists and whether that deadlock poses an irreparable threat to the business. *See id.*; Claudia M. Landeo & Kathryn E. Spier, *Shotguns and Deadlocks*, 31 YALE J. ON REG. 143, 149 (2011)

1. The Theoretical Conundrum that Results When Allegations of Bad Faith Manufacturing Are Considered

The argument for rejecting the availability of the bad faith defense entirely is strengthened when one considers how the situation might devolve after the court, having concluded that a deadlock has been manufactured (i.e., accepting a respondent's bad faith defense), declines to appoint a custodian and dismisses the case.¹⁵² This is a gamble.¹⁵³ On the one hand, the gamble might play out as the court may have hoped, with the petitioner coming back to the "bargaining table" after having his long-term strategy of a court-ordered exit option defeated, ready to continue business in a professional manner.¹⁵⁴ As unrealistic as this sounds, for a court to determine that

(advocating an increased use of negotiated "Shotgun" mechanisms between owners of closely-held corporations and other joint ventures as a way to proactively resolve future deadlock issues, yet recognizing that there will always be a "residual risk" that one owner might "manufacture a deadlock and strategically trigger the Shotgun provision in order to buy out the disadvantaged party at a low price"); see also Landeo & Spier, *supra* note 72 (defining the "Shotgun" mechanism). This theoretical argument that the motives underlying the apparent deadlock are irrelevant to judicial intervention dovetails with the more practical argument already described previously, that inquiries into the petitioner's underlying motives for seeking the petition requires a great deal of fact-sensitive investigation, and a determination that a petitioner did indeed manufacture a deadlock in bad faith requires the court to rely heavily on circumstantial evidence and generous inferences. See *supra* notes 106–123 and accompanying text. Though not specifically addressed in this Part, the argument in favor of abandoning the inquiry into the petitioner's motives (i.e., the argument for abolishing the bad faith defense) appears to be supported by the plain language of Section 226, which only asks whether deadlock exists and, in the case of Section 226(a)(2), whether a deadlock between directors has resulted in the company being faced with an irreparable harm. See DEL. CODE ANN. tit. 8, § 226(a)(2) (2011). There is no statutory requirement that the ultimate deadlock must not have been the goal of the petitioner. See *id.*

¹⁵² See L. CORP. OFFICERS & DIRECTORS: INDEMNIFICATION & INS. § 1:22, Westlaw (database updated Nov. 2016) (pointing out that often, director deadlock "may paralyze the normal and established operations" of the business and concerns relating to "public policy" may guide the court's hand towards dissolution or appointment of a custodian).

¹⁵³ See Post-Trial Brief for Respondent at 70–78, *In re Shawe*, 2015 WL 4874733 (arguing that the court should reject Elting's petition for the appointment of a custodian because of the fact that Elting had intentionally sought to create and exacerbate internal conflict and deadlock by refusing to consider any business decisions pertaining to hiring, acquisitions, true-ups, etc., and implying that were the court to accept his argument and decline to appoint a custodian with the power to sell the corporation, the business would continue to be profitable and that he and Elting would find an alternative way to resolve their feud); see also Mahler, *supra* note 18 (discussing the bad faith defense in relation to New York's Business Corporation Law, Section 1104-a). Interestingly, a comment left by a reader on the webpage containing Peter Mahler's article *Is Bad Faith a Defense in Deadlock Dissolution Proceedings*, poses this same question (asking what would happen if a court were to accept a party's bad faith defense), yet nonetheless states that the reader agrees that bad faith should constitute an acceptable defense. See Mahler, *supra* note 18.

¹⁵⁴ See Mahler, *supra* note 18. This scenario is caveated by the reality that a court could also choose to accept a bad faith defense and at the same time, decline to dismiss the Section 226 action in its entirety. See DEL. CODE ANN. tit. 8, § 226(b). It is entirely possible that the court could find that the petitioner had acted in bad faith to manufacture a deadlock, yet recognize the conundrum that the owners or directors' relationship may, as a result of the petitioner's strategy, none-

an owner has manufactured a deadlock in bad faith is, in a sense, tantamount to concluding that because the petitioner had simply “feigned” dissension and deadlock, the petitioner’s relationship with his or her co-owner is actually not irreconcilable.¹⁵⁵ Is it realistic to assume that just because a deadlock was created with the purpose of achieving a forced sale, the dissension is a sham and the issues between the owners are actually easily resolvable?¹⁵⁶ This theoretical conundrum would be mooted if Delaware courts decided to treat Section 226 as a complete no-fault statute and embraced the position that manufactured or not, a deadlock is a deadlock.¹⁵⁷

2. A Word of Warning: Treating Section 226 as a No-Fault Statute Requires a Full Commitment

Treating Section 226 as a pure no-fault statute would indeed resolve practical and theoretical quandaries that inevitably result when the court is required to determine whether a petitioner has manufactured a deadlock in bad faith.¹⁵⁸ Yet for courts to endorse this approach of concerning themselves only with *whether* a deadlock exists requires a considerable commitment, and in order for this method to function properly, courts must go “all the way” in their treatment of Section 226 as a complete no-fault statute.¹⁵⁹ This requires Delaware courts to go a step beyond *Feinberg v. Sil-*

theless have reached a point of “no return” where they are incapable of simply returning to work together. See *In re Shawe*, 2015 WL 4874733, at *31 (reasoning that leaving Shawe and Elting “to their own devices” was not an option). In that case, the court could take a different approach, such as appointing a third director to act as a tie breaker in the deadlocked business decisions at issue, as opposed to appointing a custodian with the power to sell the business. See *id.*

¹⁵⁵ See *In re Shawe*, 2015 WL 4874733, at *28 (finding that, despite evidence that Elting had pursued a course of action to achieve a court-ordered sale, the deadlock was genuine and not manufactured). For instance, if the Chancery Court in the TransPerfect case decided to accept Shawe’s bad faith defense and concluded that the alleged deadlock had in fact been fabricated, would that have done anything to resolve the dispute at the heart of the litigation, or would the corporation still likely be threatened with irreparable harm? See *id.*

¹⁵⁶ See *supra* notes 153–154 and accompanying text. If the court accepts a bad faith defense and dismisses the Section 226 action wholesale, and the defeated petitioner miraculously returns to his/her position ready to carry on the business, then the court’s gamble pays off. See *supra* notes 153–154 and accompanying text. If, on the other hand, the roulette wheel lands on the alternative, and perhaps more likely scenario, where the petitioner and objector (having just walked out of a lengthy litigation battle) are nevertheless unable to resolve the deadlock that the court has found to be fabricated, then the court loses the bet. See *supra* notes 153–154 and accompanying text.

¹⁵⁷ See *In re Goodman*, 200 A.D.2d at 670–71; Mahler, *supra* note 18 (noting that certain New York cases have treated the dissolution statute as a “no-fault statute”).

¹⁵⁸ See *supra* notes 106–123 and accompanying text (discussing cases evincing the difficulties inherent in determining whether a deadlock is genuine or manufactured).

¹⁵⁹ See *In re Goodman*, 200 A.D.2d at 670–71. The “approach” referred to here is one that embraces the perspective set forth in the New York appellate cases cited in the *Feinberg* decision, which reasoned that the New York business dissolution statute does not solicit an investigation

Feinberg, which could be read to have concluded that the New York corporate dissolution statute could be treated as a *partial* no-fault statute: *Feinberg* tried to “harmonize[]” cases where the court had inquired into the petitioner’s motives (considering fault relevant) with those that had refused to do so (treating it as a no-fault statute).¹⁶⁰ The instability of the *Feinberg* reasoning becomes apparent under close scrutiny: it states that finding of fault is irrelevant where there is “no real dispute” that the deadlock is genuine (“Situation X”) but that an inquiry into the “intent” of a petitioner is warranted in order to determine whether the deadlock is “feigned” (“Situation Y”).¹⁶¹ Although technically sound when viewed in a vacuum, this reasoning becomes circular when applied in practice, when the pivotal question faced by the court is the threshold issue of whether the deadlock is genuine or artificial (i.e., whether to classify a deadlock as Situation X or Situation Y), which requires an inquiry into potential bad faith motives of one of the parties, which is tantamount to a finding of fault.¹⁶² In reality, it is impossible to arrive at the Situation X option of treating the dissolution statute as a no fault statute, without making the threshold determination of whether the deadlock is genuine (which brings the court back to Situation Y).¹⁶³ The circular logic that inevitably results when courts are asked to as-

into the reason underlying an apparent deadlock and thus that “ascribing fault” to either party to the action is irrelevant. *See Feinberg*, Index No. 3120-11, at 2–4. *Feinberg* did not commit to treating N.Y. BUS. CORP. LAW § 1104 as a no fault statute; instead, it tried to split the baby and reconcile cases that had done so with cases that had not. *See Feinberg*, Index No. 3120-11, at 8; Mahler, *supra* note 18.

¹⁶⁰ *See Feinberg*, Index No. 3120-11, at *8; Mahler, *supra* note 18. Although it is admittedly unlikely that Delaware courts adjudicating a Section 226 action would look to New York cases addressing Section 1104 of New York’s Business Corporation Law, the point here is that if Delaware courts do move towards treating Section 226 as a no fault statute, they should be ready to commit fully to that approach (reason being that attempting to reconcile the countervailing approaches of treating Section 226 as a no fault statute on the one hand versus agreeing to accept the bad faith defense and inquire into the motives underlying a Section 226 petition on the other inevitably results in the court needing to adopt a circular, or even contradictory conclusion, as it did in *Feinberg*). *See Feinberg*, Index No. 3120-11, at *8.

¹⁶¹ *See Feinberg*, Index No. 3120-11, at *8. The logic of the court in *Feinberg* is technically sound if indeed it could be ascertained as an inexorable truth that a given deadlock is genuine, but the reasoning becomes problematic when the actual task of the court is characterized as proving that the deadlock is genuine in the first place. *See id.*

¹⁶² *See id.* The *Feinberg* decision, although analytically impressive, is still of little help for cases where the “fault” is the act itself of creating a deadlock. *See id.* Imagine a scenario where party A decided that she wanted to force a sale of the company, but knew that Party B would object: Party A begins to take actions aimed at deteriorating the relationship and creating deadlock and dissension, and as a result, the relationship indeed breaks down and the parties’ working relationship suffers and business decisions are deadlocked. Deadlock actually exists, and thus according to *Feinberg*, a finding of fault is unnecessary, and yet *Feinberg* also states that in this scenario, “the . . . intent for creating the deadlock is nevertheless relevant,” so a finding of fault is actually relevant even in instances where the *Feinberg* analysis would hold that it is not. *See id.*

¹⁶³ *See id.*

sess allegations that a party has manufactured a deadlock would be avoided by an unequivocal commitment to treating Section 226 as a no-fault statute, and declaring outright that when faced with a petitioner seeking judicial intervention, the only question is if the stockholders/directors are in a state of deadlock, ignoring how or why the deadlock arose.¹⁶⁴

3. Looking to No-Fault Divorce Statutes to Support the Proposition That Section 226 Does Not Solicit a Finding of Fault

Those hesitant to adopt the approach of treating Section 226 as a no-fault statute and thereby abolishing the viability of the bad faith defense might consider the analogous field of divorce law, where the trend over the past half-century has been towards treating divorces as no-fault proceedings.¹⁶⁵ Until the mid-twentieth-century, someone seeking to dissolve a marriage would need to prove that the other spouse was guilty of committing certain acts that satisfied the “fault grounds for divorce.”¹⁶⁶ The advent of no-fault divorce regimes has shifted the focus away from seeking to affix

¹⁶⁴ See *In re Goodman*, 200 A.D.2d at 670–71; Mahler, *supra* note 18 (discussing the notion that certain New York cases have treated the New York law governing business dissolution as a “no-fault statute”).

¹⁶⁵ See John H. Matheson & R. Kevin Maler, *A Simple Statutory Solution to Minority Oppression in the Closely Held Business*, 91 MINN. L. REV. 657, 692 (2007) (discussing the fact that state laws governing business dissolutions have not yet recognized the concept of “no-fault divorce” and proposing a “model statute” that would operate as “a kind of no-fault divorce” by giving minority shareholders the option of liquidity in the absence of a pre-negotiated buy-sell agreement); see also CARMODY-WAIT 2D *New York Practice with Forms* § 114:74, Westlaw (database updated Mar. 2017) (detailing the 2010 update to New York divorce law, allowing divorces on no-fault grounds); Ellman & Lohr, *supra* note 28 (describing the shift to a no-fault divorce system and rejecting claims that no-fault divorce regimes have contributed to “societal-ills”); Kristine Cordier Karnezis, Annotation, *Fault as Consideration in Alimony, Spousal Support, or Property Division Awards Pursuant to No-Fault Divorce*, 86 A.L.R.3d 1116, § 2a (1978) (analyzing cases that consider whether fault can still be considered in divorces on “no-fault” grounds for the purpose of property-division). *But see* Peter Nash Swisher, *Reassessing Fault Factors in No-Fault Divorce*, 31 FAM. L.Q. 269, 271 (1997) (questioning the success of the no-fault divorce “regime” in the United States); Lynn D. Wardle, *No-Fault Divorce and the Divorce Conundrum*, 1991 B.Y.U. L. REV. 79, 79–80 (1991) (arguing that despite the hope in the 1970’s that a shift towards a no-fault divorce-law system would extinguish the need for divorce proceedings to ignite interpersonal animosities and would “enhance respect for the law,” no-fault divorce regimes have led to an increase in divorce rates and “inequities in the economic consequences of divorce”).

¹⁶⁶ See Allen M. Parkman, *Reforming Divorce Reform*, 41 SANTA CLARA L. REV. 379, 379, 380–81 (providing an overview of the shift from fault to no-fault divorce statutes). Acknowledging the flaws of this seemingly archaic requirement that a petitioner seeking divorce prove that their spouse was committing a wrong, all states have, since the 1970s, either adopted no-fault grounds for divorce instead of fault grounds, or have added the option of the no-fault divorce in conjunction with their previous fault-ground laws. *Id.* at 380. Common wrongs pointed to under fault regimes were “adultery, desertion, or cruelty.” *Id.*

blame to one of the parties during divorce proceedings.¹⁶⁷ Said another way, no-fault divorce regimes have removed the requirement that the spouse seeking the divorce be “innocent” and that the other spouse is “guilty of marital misconduct.”¹⁶⁸ Similarly, no-fault divorce regimes extinguish the option for the spouse objecting to the divorce to point to the petitioner’s “misconduct” as a defense, because unlike the previous fault regimes, there is no longer a requirement that the petitioner be deemed “innocent.”¹⁶⁹

This shift evinces policy support for extinguishing the defense in Section 226 actions that allege that a petitioner has manufactured a deadlock in order to seek a court-ordered sale (i.e., closing the door on the bad faith defense in Section 226 proceedings).¹⁷⁰ Delaware courts need look no further than the evolution of modern divorce law in their own state.¹⁷¹ Indeed, judges in Delaware divorce proceedings are prohibited from considering evidence of fault or wrongdoing when deciding whether to grant a divorce and whether to order alimony payments.¹⁷² State legislatures and courts alike, in all fifty states, have recognized that if a marriage is damaged beyond repair, legal separation is permitted and an affirmative finding of fault on the part of one spouse is unnecessary.¹⁷³ Similarly, if the relationship

¹⁶⁷ See Karnezis, *supra* note 165 (noting the reasoning that no-fault regimes do away with the need to illuminate “ugly details of conduct” in divorce proceedings).

¹⁶⁸ See Ellman & Lohr, *supra* note 28, at 722.

¹⁶⁹ See *id.* at 730 (noting that under fault regimes, alleging misconduct such as adultery on the part of the petitioner was a valid defense, because such regimes required that the petitioner was “innocent” and that the other spouse was at fault).

¹⁷⁰ See Matheson & Maler, *supra* note 165, at 699 (noting that because state corporate law has not evolved to the point of allowing no-fault business divorces, minority business owners are required to offer proof of “oppressive conduct of the other party”). Although Matheson and Maler’s article supports a type of no-fault divorce relationship in order to do away with the requirement that a *minority owner seeking liquidity* prove fault of the opposing owner, recognizing statutes such as Section 226 as no-fault statutes would also allow courts to refuse to consider allegations made by *the party seeking to prevent judicial intervention* of bad faith on the part of the petitioner seeking the appointment of a custodian (or a court-ordered sale/dissolution). See *id.*; see also Ellman & Lohr, *supra* note 28, at 722–23. Admittedly, the analogy between divorce law and petitions for the appointment of a custodian under Section 226 is far from perfect yet the common ground on which both areas of law are based is easily recognizable. Compare *In re Goodman*, 200 A.D.2d at 670–71 (ascribing fault to one of the parties is unnecessary in corporate dissolution proceeding), with *Schiffer v. Schiffer*, 930 N.Y.S. 2d 827, 829 (2011) (summarizing the New York State no-fault divorce statute, which simply asks whether the relationship between spouses has “broken down irretrievably”).

¹⁷¹ See Amy Castillo, *Adultery in Delaware: Does Cheating Affect Alimony?* DIVORCENET, <https://www.divorcenet.com/resources/divorce/spousal-support/cheating-spouse-alimony-delaware.htm> [<https://perma.cc/K4YA-CMZK>] (noting that although some states still allow fault-based divorces, Delaware is a complete no-fault state, where divorces will be granted on the grounds of an irretrievable breakdown of relations, and that judges are “explicitly forbidden from considering adultery, or any other kind of marital misconduct, when considering whether to award alimony”).

¹⁷² See *id.*

¹⁷³ See Ellman & Lohr, *supra* note 28, at 722–23.

between 50% owners of a corporation has decayed past the point where reconciliation is a viable outcome, there is a cognizable argument that the underlying facts that caused the resulting deadlock—even if those facts indicate that one party consciously aggravated the situation to cause the breakdown—are irrelevant.¹⁷⁴

CONCLUSION

The notion that a 50% business owner might attempt to manufacture a deadlock in order to obtain a court-ordered sale over the objections of their co-owner presents a legitimate concern. As such, it is hardly surprising that respondents to corporate deadlock proceedings, such as Phillip Shawe in the *TransPerfect* case, have raised the specter of the opposing party's bad faith in the hope of preventing a forced sale. With that said, the challenge inherent in assessing allegations that a deadlock between stockholders or directors was manufactured and thus not "genuine" creates a significant burden for the courts. Furthermore, the text of statutes such as Section 226, which allow for court-ordered sales, require only that a deadlock exists and that the company be faced with resultant harm. There is no subsidiary requirement in Section 226 (or Sections 273 or 18-802 for that matter) that says deadlock must not have been the ultimate goal of the petitioner. In fact, the maladies inherent in allowing consideration of the bad faith defense to judicial intervention in such actions outweigh the potential benefits that the

¹⁷⁴ See Castillo, *supra* note 171 (describing divorce law in Delaware). At this point, the reader may have noticed an "elephant in the room" not specifically addressed by the argument section of this Note: if the aforementioned considerations weigh in favor of abandoning recognition of the bad faith defense in Section 226 actions, do not those same considerations point to the conclusion that courts should also close the door on the bad faith defense in Section 273 and Section 18-802 proceedings? See DEL. CODE ANN. tit. 8, §§ 226, 273; DEL. CODE ANN. tit. 6, § 18-802. The simplest answer to that question is a resounding "yes." See *supra* notes 124–174 and accompanying text. That being said, as a practical matter, Delaware courts have rarely explicitly considered the bad faith defense in conjunction with Section 226 actions, whereas the doctrine has received explicit treatment in numerous Section 273 and Section 18-802 cases. See, e.g., *Vila* 2010 WL 3866098, at *7 (discussing the bad faith defense in the context of an LLC); *In re Bermor, Inc.*, No. VC 8401-VCL, 2015 WL 554861, at *3–4 (Del. Ch. Feb. 9, 2016) (same); *Arthur Treacher's Fish & Chips, Inc. v. Ft. Lauderdale, Inc.*, 386 A.2d 1162, 1167 (Del. Ch. May 10, 1978) (allowing a defense for dissolution pursuant to Title 8, Section 273 of the Delaware General Corporation Law). As such, the door is open right now for courts to recognize the doctrine's problematic nature as evinced by its uncertain treatment in Section 273 and Section 18-802 cases and start out on the right foot in its treatment of the bad faith defense in the Section 226 context. See *supra* notes 106–123 and accompanying text. Said another way, the fact that this specific issue has rarely received explicit treatment in Section 226 cases gives the courts an opportunity to take a new position on the bad faith defense in the Section 226 context, after which courts assessing subsequent Section 273 and Section 18-802 cases could follow. See *supra* notes 106–123 and accompanying text (discussing Delaware cases that have grappled with the bad faith defense in Section 273 and Section 18-802 proceedings).

availability of the defense confers on objecting business owners. Although Delaware courts have routinely allowed parties to employ the bad faith defense in Section 273 and Section 18-802 cases, they have rarely addressed the issue directly in actions brought under Section 226. Accordingly, courts should take advantage of the minimal precedent addressing the bad faith defense in Section 226 actions to take an affirmative stance against the defense in Section 226 actions going forward. Such a stance would abolish the need for courts to grapple with identifying the specific reasons underlying corporate deadlocks. Furthermore, this would eradicate the conundrum faced by courts that endeavor to draw an abstract line distinguishing manufactured deadlocks from those that are genuine.

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