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Delaware Chancery Court Dismisses Challenge to Merger of MLPs

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Reaffirms Ability of Limited Partnerships to Modify Fiduciary Duties by Contract, Including Disclosure Obligations in Mergers

In an opinion issued on March 29, 2016, the Delaware Chancery Court dismissed a challenge to the 2015 acquisition of Regency Energy Partners LP (“Regency”) by Energy Transfer Partners L.P. (“ETP”), holding that Regency’s limited partnership agreement precluded judicial review of the transaction. Although the plaintiff asserted that unitholders were not fully informed about the transaction and therefore the unitholder vote was not effective, the court found that the vote was effective because Regency’s limited partnership agreement (the “LP Agreement”) extinguished the common law duty of disclosure that exists under Delaware law and replaced it with only one disclosure requirement when seeking unitholder approval of a merger, which was satisfied by Regency delivering a copy or summary of the merger agreement to unitholders with the notice of special meeting.

The case, *Dieckman v. Regency GP LP*, arose from the merger of Regency and ETP, both Delaware master limited partnerships, pursuant to which ETP acquired Regency in a transaction valued at approximately \$11 billion. The transaction was approved by Regency’s unitholders—including approximately 60% of the total unaffiliated units—at a special meeting held in April 2015.

Soon after the completion of the merger, the plaintiff filed suit on behalf of the Regency unitholders alleging that Regency’s general partner had breached provisions in the LP Agreement requiring it to act in good faith. Regency, in turn, asserted that two safe harbors in the LP Agreement shielded the transaction from judicial review. The first safe harbor, which the court did not consider, applies if the transaction is approved by a conflicts committee consisting of at least two unaffiliated directors. The second applies if the transaction is approved by a majority of the units not held by the general partner or by any entity controlling, controlled by, or under common control with it. The plaintiff, however, contended that the unitholder approval safe harbor could not be asserted because the unitholders were not fully informed about the transaction and therefore the unitholder vote was not effective.

In finding for the Regency defendants, the court emphasized the primacy of contractual arrangements in the limited partnership context. Although fiduciary duties owed in the corporate context cannot be waived, the court explained that a limited partnership may eliminate fiduciary duties, including the duty of disclosure, if its partnership agreement so

provides. In this case, the court found that Regency's LP Agreement had clearly extinguished the duty of disclosure and replaced it with only one disclosure requirement pertaining to the approval of a merger. The court found that, under the LP Agreement, Regency was required only to provide unitholders with a copy or a summary of the merger agreement together with the notice of special meeting.

The court further held that the implied covenant of good faith and fair dealing—which is contractual in nature where alternative entities are concerned—did not create any additional disclosure obligations. As the LP Agreement expressly waives fiduciary duties and clearly defines Regency's disclosure obligations, the court held that the implied covenant could not be invoked to add further disclosure requirements to the agreement, as it would contradict the explicit arrangements to which the partners had agreed. Having determined that Regency had satisfied its disclosure obligations and that a majority of the unaffiliated units had voted to approve the merger, the court found that the unitholder approval safe harbor applied and the transaction therefore could not be challenged for a contractual breach.

Acknowledging that its conclusion might be viewed as harsh, the court offered a reminder to investors in alternative entity structures that “the express policy of this State is to give maximum effect to the principle of freedom of contract.” This policy provides commercial parties with considerable freedom in structuring their arrangements, but also requires investors to take care in reading agreements and to understand the corresponding limitations on their rights. For MLPs, *Dieckman* reinforces the ability to structure their partnership agreements to permit a flexibility not afforded to corporate entities where potentially conflicted transactions arise.