

## **Delaware Supreme Court Focuses the Ground Rules for Stockholder Books and Records Inspection Demands**

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Section 220 of the Delaware General Corporation Law affords stockholders a right to inspect a corporation's books and records when the inspection demand comes from an existing stockholder, satisfies the statutory form and manner for presenting a demand, and states a proper purpose reasonably related to the person's interest as a stockholder.

Litigation over Section 220 demands has become more frequent and contentious, with the battle lines often drawn over the propriety of the stated purpose for the demand. In *AmerisourceBergen Corporation v. Lebanon County Employees Retirement Fund*, decided on December 10, 2020, the Delaware Supreme Court focused the ground rules for Section 220 demands by reining in the use of two common proper purpose challenges.

First, the court eliminated as a basis for challenge the requirement that a stockholder must demonstrate that the wrongdoing being investigated by the demand is *actionable*, except in certain limited circumstances. The court indicated that a trial court may be justified in denying inspection in "the rare case in which the stockholder's sole reason for investigating mismanagement or wrongdoing is to pursue litigation and a purely procedural obstacle, such as standing or the statute of limitations, stands in the stockholder's way such that the court can determine, without adjudicating merits-based defenses, that the anticipated litigation will be dead on arrival...."

Second, the court held that a stockholder demanding inspection to investigate potential mismanagement or wrongdoing need not specify the ends to which it might use the requested records. In other words, so long as the stockholder states a credible basis to believe that mismanagement or wrongdoing has occurred, it need not explain every use to which it may put the inspection results should they confirm mismanagement or wrongdoing.

To appreciate this ruling one needs to understand the fundamentals underlying Section 220. An axiomatic principal of Delaware corporate law is that the company's affairs are managed by the board of directors (and the officers elected by the board) and not the stockholders. In this respect, the company and its management enjoy some level of protection from stockholder intrusion into their managerial sphere. On the other hand, stockholders have a right to understand how the enterprise in which they hold an ownership interest is being managed. Section 220 offers a balance of these competing interests by allowing stockholders access to books and records deemed essential to their purported purpose when the statutory elements for doing so are satisfied.

Section 220 lawsuits are summary proceedings, meaning that the allowance of discovery is limited, adjudication is on an expedited schedule and cases are often determined on "paper" trials without live presentation of witnesses or evidence. In recent years, merits-based defenses have crept into Section 220 litigation asking the court to consider the potential

likelihood of success of any stockholder claims of mismanagement and wrongdoing by the officers and directors. The result has been increased complexity, time and expense associated with such litigation, often directing it far from its intended summary nature. This is not to say that merits-based defenses have no place at all in Section 220 litigation. Indeed, as the *AmerisourceBergen* ruling recognizes, there are circumstances where merits-based defenses should be considered, albeit these are the rare case and *AmerisourceBergen* stands for the principle that these are no longer the norm. In this way, the court has focused the ground rules for Section 220 demands in an effort to return to the balance of powers intended by the statute.

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