

Delaware Supreme Court: Plaintiff Need Not Explain Strategy in Section 220 Document Demand

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On December 10, 2020, the Delaware Supreme Court held that when a Section 220 books and records inspection demand states a proper investigatory purpose it need not identify the particular course of action the stockholder will take if the books and records confirm the stockholder's suspicion of wrongdoing. [AmerisourceBergen v. Leb. Cnty. Emps.' Ret. Fund, 2020 WL 7266362 \(Del. 2020\) \(Traynor, J.\)](#). The court further held that, although the actionability of wrongdoing can be a relevant factor to consider when assessing the legitimacy of a stockholder's stated purpose, an investigating stockholder is not required in all cases to establish that the wrongdoing under investigation is actionable.

Background

Defendant AmerisourceBergen is one of the largest opioid distributors in the United States. Federal regulations require opioid distributors to take steps to maintain effective controls and reporting systems to make certain that drug shipments stay within "legitimate medical, scientific, and industrial channels." Since 2012, AmerisourceBergen has been subject to a number of government investigations and lawsuits relating to its opioid practices. In 2019, plaintiff stockholders served a demand under Section 220 of the Delaware General Corporation Law on AmerisourceBergen that requested inspection of board materials "related to AmerisourceBergen's operations and its potential involvement in the opioid crisis." The demand listed four investigatory purposes: (i) to investigate possible breaches of fiduciary duty, mismanagement, and other violations of law by AmerisourceBergen's directors and its management in connection with its distribution of opioid medications; (ii) to consider any remedies with respect to the aforementioned conduct; (iii) to evaluate director independence and disinterestedness; and (iv) to use the information obtained to evaluate possible litigation or other corrective measures.

AmerisourceBergen rejected the demand, claiming that it "did not state a proper purpose and that, even if [p]laintiffs' purpose were proper, the scope of the inspection was overbroad." Plaintiffs subsequently filed an action in the Court of Chancery, seeking to compel production of the requested documents.

In its memorandum opinion, the Court of Chancery found that plaintiffs had demonstrated a proper purpose sufficient to warrant the

inspection of formal board materials. The Court of Chancery further found that plaintiffs “had established a credible basis, through strong circumstantial evidence, to suspect that AmerisourceBergen’s situation did not result from any ordinary business decision that, in hindsight, simply turned out poorly, but instead may have been the product of [its] violation of positive law.” The Court of Chancery also rejected AmerisourceBergen’s contention that plaintiffs’ sole purpose was to investigate a potential *Caremark* claim, noting that plaintiffs’ demand “reserved the ability to consider all courses of action that their investigation might warrant pursuing.” The Court of Chancery additionally rejected AmerisourceBergen’s contention that plaintiffs were required to show that the wrongdoing they sought to investigate was “actionable” wrongdoing. AmerisourceBergen moved for, and the Court of Chancery granted, certification of an interlocutory appeal.

On appeal, AmerisourceBergen argued that the lower court erroneously found that plaintiffs had stated “a proper purpose and need not identify the objectives of the investigation.” AmerisourceBergen also asserted that the court erroneously determined that plaintiffs “had established a credible basis from which the court could suspect wrongdoing and that such wrongdoing need not be *actionable*.”

Plaintiff Need Not Specify the Ends to Which It Might Use Books and Records

The court began its analysis by noting that Section 220 provides that stockholders who seek to inspect a corporation’s books and records must establish that they have a “proper purpose for the inspection” and that a proper purpose is a “purpose reasonably related to such person’s interest as a stockholder.” The court cautioned that “a stockholder seeking to investigate wrongdoing must show, by a preponderance of the evidence, a credible basis from which the court can infer there is possible mismanagement as would warrant further investigation.” The court further explained that a “stockholder need not show that corporate wrongdoing or mismanagement has occurred in fact, but rather the threshold may be satisfied by a credible showing . . . that there are legitimate issues of wrongdoing.”

Agreeing with the Court of Chancery, the court “reject[ed] AmerisourceBergen’s characterization of [p]laintiffs’ [d]emand as solely limited to pursuing derivative litigation.” The court held that “when the purpose of an inspection of books and records under Section 220 is to investigate corporate wrongdoing, the stockholder seeking inspection is not required to specify the ends to which it might use the books and records.”

AmerisourceBergen contended that unless the objectives of the investigation “are explicitly disclosed in the stockholder’s demand, the corporation will be impaired, if not entirely thwarted in its efforts to evaluate the propriety of the demand’s purpose without resorting to litigation.” The court distinguished AmerisourceBergen’s reliance on *Northwest Industries v. B.F. Goodrich*, 260 A.2d 428 (Del. 1969), which involved a stockholder’s request to inspect the company’s list of stockholders. The court stated that “a request to inspect a list of stockholders is fundamentally different than a request to inspect books and records in furtherance of an investigation of corporate wrongdoing.” The court explained that “[a] corporation cannot discern whether the inspection of its list of stockholders for the purpose of communicating with other stockholders is related to the stockholder’s interest as a stockholder without a disclosure of the substance of the intended communication.” The court stated that “[b]y contrast, corporate wrongdoing is, as the Court of Chancery noted, in and of itself a legitimate matter of concern that is reasonably related to a stockholder’s interest as a stockholder.”

The court further held that when a stockholder can present a credible basis from which a court can infer possible wrongdoing or mismanagement, a stockholder’s purpose will be deemed proper under Delaware law. However, the court cautioned that “a corporation may challenge the *bona fides* of a stockholder’s stated purpose and present evidence from which the court can infer that the stockholder’s stated purpose is not its actual purpose.” Further, the court explained that “when assessing the propriety of a stockholder’s purpose,” the court can imply “what the stockholders’ intended use of the books and records will be.”

Credible Basis Test Reaffirmed, Plaintiff Need Not Show Alleged Wrongdoing Is Actionable

AmerisourceBergen additionally argued that merits-based attacks on the lawsuit that it expected plaintiffs to file someday were justified because plaintiffs “must establish that the wrongdoing they seek to investigate is *actionable* wrongdoing.” AmerisourceBergen asserted that plaintiffs’ claims were not actionable because they were legally barred by a Section 102(b)(7) exculpatory provision and by laches. The court held that it agreed with the Court of Chancery’s grounds for rejecting AmerisourceBergen’s argument.

The court explained that “the Court of Chancery’s determination that [p]laintiffs contemplated purposes *other than* litigation is supported by a fair reading of the [d]emand.” The court then announced that “[w]e need go no further than that to dispose of AmerisourceBergen’s

‘actionability’ argument.” Nevertheless, the court seized the opportunity “to dispel the notion that a stockholder who demonstrates a credible basis from which the court can infer wrongdoing or mismanagement must demonstrate that the wrongdoing or mismanagement is actionable.” The court explained that “[i]f litigation is the stockholder’s sole objective but an insurmountable procedural obstacle unrelated to the suspected corporate wrongdoing bars the stockholder’s path, it cannot be said the stockholder’s stated purpose is its actual purpose.” The court continued that “[g]iven the obvious futility of the litigation the stockholder claims to have in mind, the investigation can only be seen as assuaging the stockholder’s idle curiosity or a fishing expedition.”

The court stated that “[a]s the Court of Chancery has noted, a Section 220 proceeding is not the time for a merits assessment of Plaintiffs’ potential claims against [the corporation’s] fiduciaries.” The court then held that “[w]e therefore reaffirm the ‘credible basis’ test as the standard by which investigative inspections under Section 220 are to be judged.” The court held that “[t]o obtain books and records, a stockholder must show, by a preponderance of the evidence, a credible basis from which the Court of Chancery can infer there is possible mismanagement or wrongdoing warranting further investigation.” The court further held that a “stockholder need not demonstrate that the alleged mismanagement or wrongdoing is actionable.”

The court noted that a 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,” but “in all other cases, the court . . . should defer the consideration of defenses that do not directly bear on the stockholder’s inspection rights, but only on the likelihood that the stockholder might prevail in another action.”

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