

Court Of Chancery Finds No Section 220 Issue Where Stockholder's And Its Counsels' Purposes For Demand Align

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In *Inter-Local Pension Fund GCC/IBT v. Calgon Carbon Corp.*, C.A. No. 2017-0910-MTZ (Del. Ch. Jan. 25, 2019), the **Delaware Court of Chancery enforced an institutional stockholder's demand for books and records** under Title 8, Section 220 of the Delaware General Corporation Law ("Section 220"). The Court found that the stockholder's affidavit affirming the demand in substantially final form, although not in exact final form, did not violate Section 220's "under oath" requirements where the only change between the versions was the addition of a signature and the date. The Court also found that the stockholder's demand was not lawyer-driven under *Wilkinson v. A. Schulman, Inc.*, C.A. No. 2017-0138-VCL (Del. Ch. Nov. 13, 2017), where the stockholder's goals of the demand and the purposes stated in the lawyer-drafted demand were not fundamentally misaligned, even where the stockholder's representative could not articulate all the legal nuances of such purposes in deposition testimony.

In 2016, Japanese company Kuraray Co., Ltd. ("Kuraray") contacted Defendant Calgon Carbon Corporation, a publicly-traded Delaware corporation ("Calgon" or the "Company"), to express interest in the companies forming a partnership. Although Calgon initially informed Kuraray it was not for sale, on June 14, 2017, Kuraray delivered to Calgon an acquisition proposal with an exclusivity agreement and a promise to retain existing management. Kuraray later delivered a second proposal that increased the purchase price per share. Two months later, upon a favorable recommendation from its financial advisor and senior management, Calgon's board of directors (the "Board") decided to move forward with the second proposal from Kuraray, but refused to extend exclusivity.

On September 5, 2017, a group of Calgon's independent directors prohibited senior management from discussing their post-acquisition job prospects with Kuraray until after all other material terms of the deal were settled. On September 14, the independent directors decided the deal was settled enough to allow Randall S. Dearth, Chairman of the Board and President and CEO ("Dearth"), to discuss his retention with Kuraray. The next day, Dearth met with Kuraray and gave them terms for his and other senior managers' continued employment. The terms included no change in title or base salary, and a one-time post-closing bonus of \$5.5 million for Dearth and \$1.25 million for the others. Dearth reported the contents of the term sheets to the Board on September 16, after which the Board reinstated its prohibition on senior management negotiating their employment with Kuraray until the

deal terms were settled. On September 19, Calgon and Kuraray agreed to the deal terms, and the next day the Board approved the merger with Dearth committed to remain as CEO. On November 28, Calgon issued the proxy statement to its stockholders.

On December 14, 2017, Calgon stockholder Inter-Local Pension Fund GCC/IBT (“Plaintiff”) retained counsel and demanded Calgon’s books and records pursuant to Section 220. Plaintiff sought to investigate potential breaches of the fiduciary duty of loyalty by Calgon directors with respect to the Kuraray transaction, as well as mismanagement and wrongdoing by officers. As evidence of wrongdoing, Plaintiff pointed to the Board’s and senior management’s substantial equity awards received as a result of the transaction. Calgon refused to comply and, the next day, Plaintiff sued to enforce the demand. Kuraray acquired Calgon on March 9, 2018, and the case proceeded to trial in July 2018.

Section 220 grants a stockholder the right to inspect the corporation’s books and records “for any proper purpose.” Investigating wrongdoing and mismanagement of directors is a proper purpose. While the stockholder bears the burden of establishing “credible bases” of director wrongdoing or mismanagement, it need only provide “some evidence” to infer there are legitimate issues that warrant further investigation.

Calgon argued (i) Plaintiff’s demand did not technically conform to Section 220’s form and manner requirements, and (ii) Plaintiff’s purposes for the demand were not its own, but were lawyer-driven and therefore prohibited by *Wilkinson v. A. Schulman, Inc.* Section 220 requires a stockholder to make a demand “under oath.” Stockholders often fulfill this requirement by attaching a notarized affidavit to the demand. Fund plan administrator Lawrence C. Mitchell, a nonparty, signed a notarized affidavit approving the demand “in substantially final form.” Calgon argued that Mitchell’s affidavit violated Section 220’s oath requirement because it approved a version of the demand letter that was not in its final form. The Court found that the demand did comply with Section 220, because there were no substantive differences between the version of the demand Mitchell reviewed and the final form, the only change being that the final demand was signed and dated. However, the Court did recommend that “the best practice is for the stockholder to review the final version of a demand letter, including the effective date.”

A stockholder’s demand under Section 220 can be found to lack a proper purpose “[w]hen counsel for a stockholder presses a purpose that is different from the stockholder’s actual purpose.” The Court upheld this principle in *Schulman*, when it refused to enforce a demand where the stockholder’s counsel initiated the demand, drafted it based on different issues than what motivated the stockholder to seek counsel in the first place, and litigated the demand largely without the stockholder’s involvement. Calgon argued *Schulman* applied because Plaintiff’s demand was lawyer-driven by Plaintiff’s counsel, and therefore Plaintiff lacked a proper purpose under Section 220. The Court held that Calgon failed to prove Plaintiff put forward its demand under false pretenses, a high standard. The Court noted the key issue in *Schulman* was the fundamental “misalignment of goals” between stockholder and counsel, which was not present in this case. Mitchell testified regarding Plaintiff’s purposes for the demand, which aligned with the purposes in the demand drafted by Plaintiff’s counsel. Calgon argued that Mitchell’s inability to articulate the details of the demand showed it was entirely conceived by Plaintiff’s counsel without Plaintiff’s involvement. However, the Court held that a stockholder’s inability to “articulate the legal nuances” of a demand is not enough to establish that the stockholder lacked a purpose. The Court expressed concern that holding otherwise would restrict Section 220 only to “sophisticated stockholders,” and recognized that stockholders are entitled to rely upon counsel to monitor its investments, raise concerns, and pursue appropriate remedies.

Additionally the Court found Plaintiff met its burden of establishing some credible bases to infer possible wrongdoing, mismanagement, and lack of director independence, to justify an investigation. Plaintiff showed Calgon refused Kuraray's overtures until Calgon's management and directors were offered lucrative rewards and personal benefits in the merger, casting doubt on the entire process as artificially restrictive and tainted by the decision-makers' personal interests. Also, Plaintiff sufficiently showed that Calgon employed central projections in the merger with short time-frames; this excluded a potentially lucrative future project that would have increased Calgon's projections substantially. Plaintiff alleged that Calgon's directors purposefully used short projections to facilitate Kuraray's acquisition of the company for their own personal benefit.

Further, the Court found any merit contentions put forward by Calgon would not defeat Plaintiff's credible bases to inspect Calgon's books and records under Section 220 because the Court does not consider the merits beyond the low "credible bases" standard. The Court explained that while Calgon's merit arguments ultimately may be successful in subsequent plenary litigation, they do not defeat Plaintiff's demand to inspect books and records. The Court also found the books and records were "necessary and essential" to that investigation into the credible inferences of wrongdoing and mismanagement because they "address the 'crux of the shareholder's purpose'" and the "information 'is unavailable from another source.'" The Court granted nine of Plaintiff's thirteen documents requests, and narrowed in scope several of the granted requests.

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