



## Analysis of Section 220 Demand Request

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**Editor's note:** [David Berger](#), [Brad Sorrels](#), and [Katherine Henderson](#) are partners at Wilson Sonsini Goodrich & Rosati. This post is based on a WSGR publication by Mr. Berger, Mr. Sorrels, and Ms. Henderson, and is part of the [Delaware law series](#); links to other posts in the series are available [here](#).

On November 13, 2017, the Delaware Court of Chancery issued a short but potentially important opinion in *Jack Wilkinson v. A. Schulman, Inc.*,<sup>1</sup> an action to inspect books and records brought under Section 220 of the Delaware General Corporation Law. Section 220 gives stockholders of Delaware corporations the ability to inspect certain corporate books and records provided they have a “proper purpose” for seeking such materials. This statute can provide an important tool for stockholders seeking to investigate allegations of corporate wrongdoing, but also can cause significant burdens on companies with little benefit to stockholders. The court’s decision in *Schulman* represents an important effort to try to balance these considerations.

Counsel for stockholder plaintiff Jack Wilkinson first sent the company a demand letter on his behalf seeking specified categories of books and records ostensibly to investigate possible breaches of fiduciary duty in connection with the decision by the company’s board of directors to accelerate the vesting of shares of restricted stock worth more than \$3.9 million to the company’s president and CEO upon his retirement. The letter alleged that the board’s decision harmed the company by causing it to lose favorable tax treatment under Section 162(m) of the Internal Revenue Code and amounted to corporate waste. After the company refused to produce documents in response to the demand, the plaintiff filed an action in the Court of Chancery. The parties engaged in discovery, during which the stockholder plaintiff was deposed.

After a trial (on a paper record), Vice Chancellor J. Travis Laster entered judgment for the company, finding that the stockholder plaintiff failed to state a proper purpose for his demand after concluding that counsel for the stockholder (rather than the stockholder himself) had come up with the issues identified in the demand. Specifically, the stockholder testified at his deposition that the event that prompted him to pursue the demand was his unhappiness with the company’s financial results—an event wholly unrelated to the compensation issues identified in the demand letter and lawsuit. Indeed, the stockholder testified that “he [wa]s not aware of any facts suggesting wrongdoing, mismanagement, or waste relating to the compensation decision....”<sup>2</sup> The court also noted that the stockholder plaintiff had served as what Vice

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<sup>1</sup> C.A. No. 2017-0138-VCL.

<sup>2</sup> Mem. Op. at 5.

Chancellor Laster described as the “nominal plaintiff” in at least seven other lawsuits prosecuted by the same law firm in which he had had minimal involvement.

According to the court, these facts and circumstances reflected that the stockholder plaintiff had simply “lent his name to a lawyer-driven effort by entrepreneurial plaintiffs’ counsel.”<sup>3</sup> While noting that there is nothing wrong with employing counsel to prosecute a Section 220 action (indeed, it is advisable to do so), the court observed that “a stockholder seeking an inspection and retaining counsel to carry out the stockholder’s wishes is fundamentally different than having an entrepreneurial law firm initiate the process, draft a demand to investigate different issues than what motivated the stockholder to respond to the law firm’s solicitation, and then pursue the inspection and litigate with only minor and non-substantive involvement from the ostensible stockholder principal.”<sup>4</sup> Although the demand at issue in this case may be distinguishable from many proper demands that stockholders might advance under Section 220, it is nevertheless representative of a class of similarly styled Section 220 demands brought by “entrepreneurial” lawyers. The court’s opinion and commentary on such efforts by plaintiffs’ counsel may be useful to practitioners responding to or litigating such demands in the future. Delaware corporations should carefully consider such demands, the circumstances under which they are made, and consult with experienced Delaware counsel on how best to respond.

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<sup>3</sup> Mem. Op. at 4.

<sup>4</sup> Mem. Op. at 6-7.