

Delaware Supreme Court Confirms Chancery Court's Broad Authority to Impose Use Restrictions on Information Obtained From Section 220 Books and Records Inspections

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In [United Technologies Corp. v. Treppel](#), No. 127, 2014, 2014 Del. LEXIS (Del. Dec. 23, 2014), the [Delaware Supreme Court](#) held that the Delaware Court of Chancery is authorized regulate how stockholders use information obtained through books and records inspections under [Section 220](#) of the Delaware General Corporation Law ("Section 220"). The defendant corporation, in opposing a stockholder's Section 220 proceeding, had sought to bar the stockholder from using any obtained information in any legal action brought outside of Delaware. The Vice Chancellor, however, expressed the belief that the Chancery Court lacked the statutory authority to impose such a restriction. The Delaware Supreme Court reversed and identified the factors the Chancery Court should consider in exercising its discretion to impose the restriction on remand. United Technologies reaffirms the Chancery Court's important role in regulating books and records inspections in a manner that avoids inflicting unnecessary costs and burdens on corporations and their stockholders.

Following United Technologies' settlement of a United States Department of Justice investigation, a stockholder, Lawrence Treppel, sent a letter demanding that United Technologies commence litigation against certain officers and directors. At about the same time, another stockholder made a Section 220 inspection demand relating to the same investigation, which demand United Technologies' board approved. That inspection led to a derivative action in the Delaware Court of Chancery, which was eventually dismissed based on plaintiff's failure to first make a litigation demand or to show demand was excused. While this derivative suit was pending, United Technologies' board considered Treppel's litigation demand letter and rejected it. Treppel then made a Section 220 inspection demand, purportedly to enable him to evaluate the board's decision rejecting his litigation demand. United Technologies, as a condition to allowing the inspection, sought to negotiate terms by which Treppel would agree to commence any litigation arising out of the inspection in Delaware. Treppel refused and filed a Section 220 action in the Court of Chancery.

At trial, the record confirmed that Treppel had a history of filing derivative suits outside the corporation's state of incorporation. United Technologies requested the Chancery Court restrict Treppel from using any obtained information in any litigation outside Delaware. The Chancery Court

allowed the inspection, but ruled that it lacked authority to impose the restriction. Instead, it identified a charter or by-law provision as the proper mechanism for a Delaware corporation to protect its interest in litigating in Delaware. After Treppel filed his Section 220 action, United Technologies had in fact adopted such a provision — designating Delaware as the exclusive forum for any derivative or stockholder litigation. Treppel, however, insisted this provision would not apply to any subsequent derivative action by him because the provision post-dated his purchase of shares in United Technologies.

The Delaware Supreme Court reversed the Chancery Court's decision that it lacked authority to impose the requested use restriction, noting that Section 220(c) authorizes the Chancery Court in the exercise of discretion to prescribe "any limitations or conditions . . . as the Court may deem just and proper." The statute imposes no limits on the Chancery Court's authority to restrict the use of information gained from an inspection when the corporation's legitimate interests are threatened. Hence, the Supreme Court found the Chancery Court had erred, and remanded the case to the Chancery Court.

In remanding, the Supreme Court identified, "case-specific" factors for the Chancery Court's consideration bearing on "the legitimate concern on United Technologies' part that it and its stockholders could face excessive costs and the risk of inconsistent rulings if Treppel were to file suit elsewhere." These factors included Treppel's investigation of the same corporate conduct that derivative litigation had already addressed, United Technologies' interest in avoiding inconsistent rulings and having Delaware law issues decided by Delaware courts, and Treppel's inability to explain why he needed to file in a non-Delaware forum. The Supreme Court also noted the importance of ensuring Section 220 actions "do not get bogged down in collateral issues," such as Treppel's argument that United Technologies' new forum selection by-law would not apply to future suits by him. The Supreme Court deemed that argument meritless on its face.

United Technologies recognizes the Chancery Court's broad authority to impose use restrictions on information acquired from books and records inspections. It also reflects the Delaware Supreme Court's concern that stockholders may misuse books and records inspections in a manner that will impose undue burdens on Delaware corporations and their stockholders.

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