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Record Keeping And Forum Selection Can Limit ESI Requests

By **Daniel Schiau and Tod Northman** (March 22, 2019, 4:09 PM EDT)

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For at least a decade, Silicon Valley darling Palantir Technologies treated corporate governance as an afterthought. Among its laundry list of infirmities, Palantir's management conducted by email what should have been board business, didn't formalize corporate decisions into board resolutions (if the board was consulted at all) and forewent annual shareholder meetings.

Palantir even attempted to amend corporate documents retroactively and without notice — perhaps not complying with the documents themselves. Because these allegations arose in a summary proceeding (and thus the record wasn't fully developed), they were enough to convince the Delaware Supreme Court that a dissident shareholder should be permitted to review electronically stored information, or ESI, in response to its Section 220 books and records request.

In KT4 Partners LLC v. Palantir Technologies Inc.,[1] the Delaware Supreme Court analyzed the circumstances in which emails are obtainable by a shareholder. The court's opinion clarified the law governing requests for ESI review, and underscored the importance of forum selection clauses in corporate documents, refusing to limit the jurisdictional use of materials disclosed under such a records request without a compelling (or contractual) reason.

Ultimately, diligent corporate governance will go a long way to protecting a corporation from having to disclose ESI — so long as it has traditional records available.

A Request for Corporate Records

The controversy in KT4 Partners arose out of a game of corporate finger-pointing. In 2003, KT4 invested in Palantir. For the next decade, Marc Abramowitz, KT4's principal, acted as a trusted advisor to Palantir's CEO Alex Karp, resulting in free access to the corporation's meetings and executives.

This relationship foundered in 2015 when Karp accused Abramowitz of stealing Palantir's intellectual property and sued him, triggering KT4 to attempt to sell its shares in Palantir to a private equity fund. The sale fell through because of what KT4 suspected was tortious interference by Palantir; to investigate, KT4 requested corporate books and records under an Investor Rights Agreement and 8 Del. C. § 220.

KT4's request contained 20 specific documents requests and one general request for access to Palantir's books and records, "including hardcopy and electronic documents and information."[2] After negotiations regarding the scope of Palantir's disclosure failed, KT4 initiated an action in the Delaware Court of Chancery.

The Initial Litigation

To prevail on a request for corporate books and records under 8 Del. C. § 220, a stockholder must prove, by a preponderance of the evidence, that the stockholder has a proper purpose for seeking disclosure — a purpose that is "reasonably related to the stockholder's interests as a stockholder."[3] Additionally, the stockholder must show that the records requests are "necessary and essential" to the stockholder's stated purpose.[4]

Of the six purposes set forth in KT4's request, the Court of Chancery found three to be proper, and permitted KT4 to inspect Palantir's books and records, which are "essential to fulfill" its three proper "investigative purposes."[5]

Following the decision, the parties were unable to agree on the disclosure of email. KT4 argued that emails should be produced as part of Palantir's disclosure, but the Court of Chancery ruled against it, saying that emails were not included within the definition of "electronic documents and information" because KT4's initial request was not a targeted request for emails.

Applying an interpretive expressio unius[6] argument, the court believed that KT4 acknowledged the exclusion of emails from its request by specifically requesting "emails" in addition to electronic documents in another of its 20 unrelated document requests. In ruling on jurisdictional use of the produced records, the court summarily adopted Palantir's proposed jurisdictional use restriction, limiting KT4's ability to bring any action arising out of the produced records to Delaware venues only, without explanation.

The Appeal: Precedent for Corporate Records Requests

KT4 challenged the Court of Chancery's rulings regarding the disclosure of emails and the jurisdictional use of records produced. At the outset of the appeals proceedings, the parties agreed that the appropriate standard of review for whether the court's declaration of the scope of relief was appropriate should be abuse of discretion.

However, the Supreme Court of Delaware adopted a de novo standard of review to determine which specific books and records were included in KT4's initial demand, an interpretation urged by KT4. From this standard, the court excepted only circumstances where "the written demand is ambiguous and there are factual determinations underlying the Court of Chancery's resolution of that ambiguity," to which deference must be given.[7]

A Clear Standard for Electronic Mail Production

As its first point of error, KT4 argued that the production of emails was appropriate, stressing that KT4's explicit references to "electronic documents" were sufficient. Acknowledging that both the general request and the preface to the specific requests referenced "electronic documents and information," the Supreme Court of Delaware posited that "[e]mails, of course, are a type of electronic document," as if to suggest Palantir's argument was altogether uninspiring.

The court proceeded with an in-depth analysis of the "necessary and essential" standard, which requires that a stockholder be provided all documents deemed paramount to the stockholder's stated purposes over which the corporation has control.[8] In the instance of emails, precedent suggests that the Court of Chancery should not order the production of emails when traditional corporate governance materials — such as bylaws, minutes or record books — would satisfy the requesting corporation's proper purpose.[9] Emails should be produced only if these traditional records are insufficient.[10]

In the Supreme Court of Delaware's view, KT4 made an ample showing that emails were necessary to investigate wrongdoing by Palantir, given that Palantir had routinely conducted business informally via email, and otherwise failed to document such business through traditional forms of corporate record keeping, such as minutes and resolutions. In the words of the court: "If the only documentary evidence of the board's and company's involvement in the [alleged wrongdoing] comes in the form of emails, then those emails must be produced."[11]

Although earlier Chancery Court decisions have permitted ESI review, this decision is important in that it sets forth clear guidance from the Delaware Supreme Court about when emails and other ESI must be produced in a request for corporate records. The standard is narrow, requiring disclosure only when the corporation does not have traditional records documenting corporate action. Corporations that actively maintain formal records, which may be proactively "sanitized" to omit informal banter or commentary, will continue to be protected from such disclosure.

Jurisdictional Use — Emphasis on Forum Selection Clauses

In its second point of error, KT4 argues that Palantir's jurisdictional use restriction, which restricts KT4's ability to bring a lawsuit arising out of its record inspection to the Delaware Court of Chancery, improperly limited KT4's remedies. Applying a constitutional framework, a plaintiff generally should be permitted to bring a suit in any jurisdictional venue that can obtain personal jurisdiction over a defendant.

In its analysis, the Supreme Court of Delaware acknowledges this limitation and, applying a practical approach, notes that stockholders must be permitted to bring actions against the fiduciaries of a corporation, which, in the context of a Delaware corporation, may not be located in Delaware.

The only precedent on this issue lies in another recent case — United Technologies Corp. v. Treppel.[12] In that case, the Supreme Court of Delaware announced five factors to which the Court of Chancery is permitted to give weight when determining whether a jurisdictional use restriction is appropriate.[13]

However, Treppel had a key difference: the presence of a forum selection clause in its subject documentation. Because the respondent corporation in Treppel had voluntarily decided to subject the corporation to suit solely in Delaware, and a previous derivative suit had already been filed there, the Supreme Court of Delaware, concerned about conflicting rulings, determined that a jurisdictional use restriction was appropriate.

In KT4 Partners, the subject contracts did not contain forum selection clauses and were governed by California law. Moreover, the presence of both Karp and Abramowitz in California made it likely that duplicative litigation could occur in both jurisdictions if the jurisdictional use provision was permitted.

Ultimately, the Supreme Court of Delaware found no reason to limit KT4's use of Palantir's records to

Delaware, highlighting the fact that the parties are well within their rights to bind themselves to a specific jurisdiction via contract, and that limiting jurisdiction to Delaware might increase jurisdictional inefficiency since there was already litigation in California over related issues.

Practical Advice for Corporations

Corporate law generally permits shareholders to request a vast array of corporate books and records to investigate wrongdoing by company officials. Prior to KT4 Partners LLC v. Technologies Inc., the issue of if and when emails would be granted as part of a request was unsettled.[14] The Supreme Court of Delaware's decision in KT4 Partners proclaimed a straightforward rule for the production of emails, providing stockholders yet another weapon for their arsenal, while still limiting the aggressive use of such production to circumstances in which the corporation's record keeping is deficient.

Corporations should read KT4 Partners to incentivize the proper keeping of corporate records in order to prevent stockholders from accessing more "informal" documents, such as emails, in a request for corporate books and records. KT4 Partners also emphasizes the strength of forum selection clauses in directing any litigation arising from the review of any corporate books and records, including a corporation's core organizational documents, to a specific venue.

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[1] KT4 Partners LLC v. Palantir Technologies Inc., No. 281, 2019 WL 347934 (Del. Jan. 29, 2019).

[2] Id. at *5 (emphasis added).

[3] KT4 Partners LLC v. Palantir Technologies Inc., No. 2017-0177-JRS, 2018 WL 1023155, at *7 (Del. Ch. Feb. 22, 2018) (citing Seinfeld v. Verizon Commc'ns Inc., 909 A.2d 117, 121 (Del. 2006)), rev'd in part, Delaware SC Opinion, 2019 WL 347934; 8 Del. C.§ 220(b).

[4] Mudrick Capital Mgmt. LP v. Globalstar Inc., No. 2018-0351-TMR, 2018 WL 3625680, at *7 (Del. Ch. July 30, 2018) (quoting Saito v. McKesson HBOC Inc., 806 A.2d 113, 114-15, 118 (Del. 2002)).

[5] Chancery Opinion, 2018 WL 1023155, at *17.

[6] A constitutional canon of construction, which can be translated as "the expression of one thing implies the exclusion of others."

[7] Delaware SC Opinion, 2019 WL 347934, at *7.

[8] For example, see Tod Northman and Daniel Schiau, "How can stockholders overcome hurdles to make a books and records request under state corporate law?", Lingua Negoti blog, Tucker Ellis LLP (February 8, 2019), https://www.tuckerellis.com/lingua-negoti-blog/how-can-stockholders-overcome-hurdles-to-make-a-books-and-records-request-under-state-corporate-law; see also Delaware SC Opinion, 2019 WL 347934, at *9 (citing Saito, 806 A.2d at 114–15).

[9] Delaware SC Opinion, 2019 WL 347934, at *10. See, e.g., In re Plains All American Pipeline LP, No. 11954-VCMR, 2017 WL 6016570, at *4–5 (Del. Ch. Aug. 8, 2017) (ORDER).

[10] Delaware SC Opinion, 2019 WL 347934, at *10. See, e.g., Wal-Mart Stores Inc. v. Indiana Elec. Workers Pension Trust Fund IBEW, 95 A.3d 1264, 1273 (Del. 2014); Indiana Elec. Workers Pension Trust Fund IBEW v. Wal-Mart Stores Inc., No. 7779-CS, 2013 WL 5636296, at *2 (Del. Ch. Oct. 15, 2013) (ORDER); Amalgamated Bank v. Yahoo! Inc., 132 A.3d 752, 791–93 (Del. Ch. 2016).

[11] Delaware SC Opinion, 2019 WL 347934, at *13.

[12] 109 A.3d 553 (2014).

[13] The factors are:

> (i) the fact that [the stockholder seeking inspection] seeks to file claims arising out of the same corporate conduct that was already the subject of derivative litigation in the Court of Chancery and this Court; (ii) [the corporation's] legitimate interest in having consistent rulings on related issues of Delaware law, and having those rulings made by the courts of this state; (iii) [the corporation's] adoption of a forum selection bylaw that represents a non-case-specific determination by its board of directors that internal affairs litigation involving the company should proceed in a single forum; and (iv) the investment the corporation has already made (which comes at a cost to its stockholders) in defending not only the prior derivative litigation in the Court of Chancery, but also this § 220 action.

Delaware SC Opinion, 2019 WL 347934, at *15 (citing Treppel, 109 A.3d at 560).

[14] Whether intentional or not, counsel for Palantir contradicted this notion at oral argument by stating that jurisdictional use restrictions were the “norm” in the Court of Chancery, before quickly backtracking after being pressed on the statement. This seemingly insignificant mishap left a lasting impact; Chief Justice Leo Strine highlighted the statement in his opinion. See Delaware SC Opinion, 2019 WL 347934, at *16, *16 n. 112.