EFiled: Jul 13 2005 4:33PM EDT
Filing ID 6197796

IN THE COURT OF CHANCERY OF THE STATE OF DELAWARE

IN AND FOR NEW CASTLE COUNTY

DEEPHAVEN RISK ARB TRADING LTD.,	)	
Plaintiff,	)	
v.	)	Civil Action No. 379-N
UNITEDGLOBALCOM, INC.,	)	
Defendant.	)	

MEMORANDUM OPINION

Submitted: July 8, 2005
Decided: July 13, 2005

John L. Reed, Esquire, John H. Newcomer, Jr., Esquire, Matt Neiderman, Esquire, DUANE MORRIS LLP, Wilmington, Delaware, *Attorneys for Plaintiff*

Michael Hanrahan, Esquire, Tanya P. Jefferis, Esquire, PRICKETT, JONES & ELLIOTT, P.A., Wilmington, Delaware, *Attorneys for Defendant*

PARSONS, Vice Chancellor.

Plaintiff, Deephaven Risk Arb Trading, Ltd. ("Deephaven"), is an investment fund and claims to have brought this action as a stockholder of UnitedGlobalCom, Inc., a Delaware corporation ("UGC").[1] Deephaven's Complaint seeks to compel inspection of UGC's books and records pursuant to 8 *Del. C.* § 220.

This matter was tried on September 24, 2004, and argued on March 14, 2005. UGC was merged into another entity on June 15, 2005. Thereafter, the parties filed supplemental briefs addressing the impact of the merger on Deephaven's claims. This Memorandum Opinion reflects the Court's post-trial findings of fact and conclusions of law. For the reasons discussed below, I find that Deephaven was a beneficial owner of UGC stock and is entitled to a limited inspection, notwithstanding the recent merger. I therefore grant Deephaven's demand in part.

I. FACTS

Deephaven is an investment fund that utilizes market-neutral investment strategies designed to deliver risk-adjusted returns with low volatility.[2] Market-neutral strategies seek to capture mispricings or spreads between related capital instruments without being exposed to absolute price movements. These objectives are often achieved by combining long and short positions.

---

1 Deephaven has never been a stockholder of record, but instead, claims it was a beneficial owner within the meaning of 8 *Del. C.* § 220(a) at all relevant times.

2 Trial Transcript ("Tr.") at 7. All cites to the Trial Transcript refer to the testimony of David Halbower, the only witness presented at trial.

UGC is a large international broadband communications provider. On January 12, 2004, UGC announced a $1 billion rights offering (the "Rights Offering"). On the record date of the Rights Offering, UGC had outstanding 293,107,030 shares of Class A common stock ("Class A" or "Stock"), 8,198,016 shares of Class B common stock ("Class B") and 303,123,542 shares of Class C common stock ("Class C"). The Class A stock was publicly traded on the NASDAQ National Market and widely held. Liberty Media Corporation owned all of the Class B and Class C shares, giving it approximately 55% of the outstanding common stock and 92% of the cumulative voting power.

A. Deephaven's Dealings in UGC Stock and Rights

Following the announcement of the Rights Offering on January 12, 2004, Deephaven began actively trading UGC Stock. To do so, Deephaven utilized at least five brokerage accounts, at Barclays, Deutsche Bank, Goldman Sachs, Morgan Stanley and Salomon Smith Barney. It was often Deephaven's practice to borrow UGC shares in one of its accounts with the intention of short-selling them to itself in another Deephaven account.[3] The result of that type of transaction is that Deephaven's purchase and sale prices are identical and no economic interest in UGC Stock is created—that is, Deephaven is not exposed to fluctuations in the value of UGC shares.

---

[3] A short-sale is "any sale of a security which the seller does not own or any sale which is consummated by the delivery of a security borrowed by, or for the account of, the seller." *In re Digex Inc. S'holders Litig.*, 2002 WL 749184, at *2 (Del. Ch. Apr. 16, 2002) (quoting 17 *C.F.R.* § 240.3b-3) (internal quotations omitted).

Not all of Deephaven's UGC trades, however, were matched short-sales and purchases. Beginning January 13, 2004, and in earnest on January 22, Deephaven amassed a substantial net short position across its accounts. For example, on February 18, 2004, just two days before the final results of the Rights Offering were released, Deephaven was net short 4,615,071 shares of UGC.

Throughout that period, however, Deephaven's Barclays account consistently held a long position in UGC Stock. On January 13, 2004, Deephaven established a position of 2,050,000 shares in the Barclays account and that figure swelled to a high of 9,338,592 on March 3.[4] In fact, aside from a three day period between March 5 and March 8, following the liquidation of the UGC position in its Barclays account, Deephaven held UGC shares long in the Barclays account at all times between January 13 and August 23, 2004.[5]

In addition to buying and selling UGC shares, Deephaven also actively participated in the market for rights, purchasing millions of rights on the open market.

B. The Rights Offering

The Rights Offering prospectus identified Mellon Investment Services LLC ("Mellon") as the subscription agent. Mellon was to receive all correspondence relating to the subscriptions on behalf of UGC. UGC retained the discretion to determine the timeliness, validity, form and eligibility of all exercises of rights. In addition, UGC

---

[4] Joint Trial Exhibit ("JX") 5; Deephaven's Demonstrative Exhibit ("DDX") 1.

[5] Between March 5 and 8, 2004, Deephaven was long UGC stock in a Goldman Sachs account. JX 7; DDX 1.

retained the right to extend the offering period for any reason, at least up until the most recently announced expiration time.

The rights were distributed on January 21, 2004, and were freely tradable on the NASDAQ. Under the terms of the Rights Offering, each right entitled its holder to a basic subscription privilege and an oversubscription privilege. Each share of Class A stock entitled stockholders to receive .28 rights and approximately 83 million Class A rights were distributed.

The basic subscription privilege of each full Class A right allowed the holder to purchase one share of Class A stock at a price of $6.00—a 40% discount to the then-current market price of approximately $10.00. The oversubscription privilege also entitled rightsholders who had exercised their basic subscription privilege in full to purchase additional shares of Stock. The number of shares available for oversubscription was to be equal to the number of shares made available by rightsholders that failed to exercise their basic subscription privileges. In other words, UGC sought to sell all of the Stock offered in the rights offering either through basic subscriptions or a combination of basic and oversubscriptions.

To subscribe to the Rights Offering, stockholders were required to take certain steps. They had to deliver a rights certificate together with payment of the full subscription price before the expiration date. Stockholders wishing to exercise their rights, but who were unable to deliver rights certificates by the expiration date were required to provide full payment and a notice of guaranteed delivery before expiration.

The corresponding rights certificates were due within three business days thereafter. Foreign holders were required to take additional steps in order to exercise their rights.[6]

The Rights Offering originally was set to expire on February 6, 2004, but on January 23 UGC announced that it had extended the expiration date to February 12. The Rights Offering deadline apparently was not extended again, and February 12 was the final deadline for submission of all rights certificates and notices of guaranteed delivery. In addition, rightsholders that submitted notices of guaranteed delivery were to provide the completed subscription certificates by February 18.

Before the expiration date, Deephaven submitted 5,190,700 rights certificates, a request for 1 million oversubscription rights, and full payment for the requested shares.

C. Preliminary Results from the Rights Offering

The subscription period for the Rights Offering expired at 5:00 pm on February 12. At 6:19 that evening, Mellon emailed its "PRELIMINARY FINAL Report

---

[6] The Rights Offering provided that:

> To exercise or transfer their rights, foreign holders must notify the subscription agent before 11:00 a.m., New York City time, on Friday, January 30, 2004, five business days prior to the expiration time and must establish to our satisfaction that such exercise or transfer is permitted under applicable law. In the case of Class A rights, if a foreign holder does not establish to our satisfaction that such exercise or transfer is permitted under applicable law, and notify, and provide acceptable instructions to, the subscription agent by such time (and if no contrary instructions have been received by such time), the subscription agent will seek to sell the foreign holder's Class A rights, subject to the subscription agent's ability to find a purchaser. JX 1 at 43.

as of February 12, 2004" to counsel for UGC.[7] The report showed 63,668,383 shares subscribed pursuant to basic rights and 66,820,883 subscribed pursuant to oversubscription rights. In addition, the body of the email stated:

> Please note: We have 25,500,477 Protected Rights
>
> 20,298,886 Protected Oversubscription Rights

The next morning at 10:26 am, Mellon emailed its "Final Report as of February 12, 2004" to counsel for UGC.[8] This report included the exact same figures for subscriptions and oversubscriptions as the Preliminary Final Report from the previous day. The email did not include, however, any reference to Protected Rights.

On February 13, 2004, UGC issued a press release announcing preliminary results of the Rights Offering. The press release stated:

> The subscription agent for the Class A Rights Offering has informed UGC that Class A rightsholders have subscribed for approximately 63.7 million shares of UGC Class A common stock pursuant to the basic subscription privilege and approximately 66.8 million shares of UGC Class A common stock pursuant to the oversubscription privilege. Due to the substantial oversubscription, UGC will issue 100% of the approximately 83.0 million shares of the UGC Class A common stock offered in the rights offering.
>
> * * *
>
> Shares of UGC Class A common stock requested pursuant to the oversubscription privilege will be allocated among the approximately 19.3 million shares of UGC Class A common stock available to satisfy oversubscription requests in

---

7 JX 44.

8 JX 45.

> accordance with the proration procedures described in the prospectus for the rights offering.[9]

Deephaven's portfolio manager overseeing its trades in UGC stock and rights was Matthew Halbower. Based on the preliminary figures, Deephaven stood to receive the entire 1 million shares it requested from oversubscription rights. Halbower was surprised, however, by the large number of rights apparently left unexercised and made a series of phone calls to confirm the figures in the press release. On February 17, 2004, the first business day after the press release, Halbower called Mellon's Ed Eismont to confirm that the figures remained accurate. Eismont verified that 19 million rights still appeared available for oversubscription and that the numbers were accurate "in light of notice[s] of guaranteed delivery as well."[10] That same day, Halbower telephoned UGC's Rich Abbott, who also confirmed the press release's numbers.[11]

On February 19, 2004, Halbower again contacted Eismont to confirm the continued accuracy of the press release's numbers. In particular, Halbower wanted to confirm that over 19 million rights were unsubscribed for and available for oversubscription requests. Eismont did confirm the numbers, but explained: "we are trying to run through all the numbers to make sure that we're in line with what they're

---

9 JX 3.

10 Tr. at 69–70.

11 Tr. at 72–73. It is unclear from Halbower's testimony whether Abbott told him that the figures included notices of guaranteed delivery or that notices of guaranteed delivery were going to be immaterial. Regardless, Halbower testified that he was led to believe that 19.3 million shares would be available for oversubscription notwithstanding notices of guaranteed delivery. Tr. at 164–65.

showing before we come out with the numbers."[12] According to Halbower, Eismont also communicated to him

> that a large number of rights failed to exercise the oversubscription privilege because those rights were held by foreign holders; that rights held by foreign holders in this rights offering had to jump through additional hoops, which are very atypical. . . . And there were lots of discussions going on with their internal legal folks about the fact that these foreign holders weren't going to be allowed to exercise their rights. And that created, in my [Halbower's] mind, a great deal of suspicion.[13]

Halbower's suspicions led him to begin recording the call.[14] During the recorded portion of the conversation, Eismont explained: "Logic would dictate that's the logical answer. That a lot of the foreign holders couldn't participate due to not providing the appropriate paperwork."[15] Moreover, Eismont noted that the deadline to exercise rights came a number of days after it would have been too late to sell the rights on the open market, implying that foreign holders who intended to exercise their rights but were unable to in the end, would not have had the opportunity to then sell their rights.

D. The Final Results of the Rights Offering are Released

On February 20, 2004, UGC issued a final press release stating that it had received subscriptions for approximately 82 million of the 83 million rights, leaving only about 1 million shares available for oversubscription. This news represented a substantial

---

12 JX 16.

13 Tr. at 76.

14 JX 16. Halbower recorded approximately the second half of the phone call.

15 *Id.*

departure from the figures disclosed in the February 13 press release and later confirmed by Mellon and UGC. The February 20 press release explained the discrepancy by stating that the February 13 press release had excluded shares subscribed pursuant to guaranteed delivery procedures.

Halbower immediately contacted both Eismont and Abbott for an explanation, recording both calls. Eismont explained that the February 13 press release's exclusion of shares subscribed pursuant to guaranteed delivery was due to a mistake by UGC and its attorneys. Halbower asked Eismont about the foreign holders explanation he previously had used to account for the large number of unsubscribed rights. Eismont described that explanation as merely the most logical explanation at the time because he had been informed by UGC's counsel that the figures included notices of guaranteed delivery.

That same day, Eismont also called Abbott. Abbott's explanation was that Mellon had mistakenly informed UGC that the notices of guaranteed delivery number "wasn't going to be material."[16]

The rights were exchanged for Stock on February 25, 2004; shortly thereafter, the proration for oversubscription requests was announced. Deephaven received just 34,603 oversubscription shares based on its exercised position of 5,190,700 basic rights and its request for 1,000,000 oversubscription rights.

---

[16] JX 18.

E. Deephaven's Books and Records Request

On February 24, 2004, Deephaven's counsel wrote to UGC to express its concern over the sudden change in available rights and to request that all relevant files, documents, and other information be preserved. UGC responded on March 1, 2004, and denied any "wrongful actions after the delivery deadline."[17] Subsequently, on March 24, Deephaven wrote to UGC demanding inspection of certain categories of UGC's books and records pursuant to 8 *Del. C.* § 220 (Deephaven's "Demand Letter").[18] Specifically, the Demand Letter requested eleven categories of documents relating to various aspects of the Rights Offering and the manner in which it was executed.[19]

---

[17] JX 27.

[18] JX 29.

[19] The categories of documents requested are:

1. All records including copies of taped phone conversations reflecting or referring to all elections of oversubscription rights in the Rights Offering;
2. All records reflecting or referring to all notices of guaranteed delivery received by the Company or its agents in connection with the Rights Offering;
3. All records reflecting or referring to the extension of the subscription period for the Rights Offering;
4. All records reflecting or referring to the subscriptions and notices of guaranteed delivery received by the Company or its agents in connection with the Rights Offering, including, without limitation, all records reflecting or referring to the date and time at which all such subscriptions and notices of guaranteed delivery were received by the Company or its agents;
5. All records reflecting or referring to communications concerning the receipt by the Company or its agents of subscriptions and/or notices of guaranteed delivery in connection with the Rights Offering, including, without limitation, any requests or demands that subscriptions or notices of guaranteed delivery be accepted or honored by the Company or its agents after the subscription deadline;
6. All memoranda, publications, manuals or other documents reflecting or referring to the Company's policies, procedures or guidelines concerning the

Deephaven stated four purposes for its demand: (1) to investigate possible corporate wrongdoing or mismanagement, including breaches of fiduciary duty, misuses of corporate assets, misuses of corporate information and/or other wrongdoing in connection with the handling of the Rights Offering; (2) to investigate and assess the veracity and legality of UGC's public and private disclosures made in connection with the Rights Offering; (3) to determine whether the rights of Deephaven and other similarly situated stockholders of UGC were impermissibly interfered with or denied by UGC or its agents in connection with the Rights Offering; and (4) to determine whether Deephaven and other similarly situated stockholders are in fact entitled to additional oversubscription privileges in connection with the Rights Offering.

Following UGC's receipt of the Demand Letter, Deephaven and UGC engaged in discussions in an attempt to resolve Deephaven's demand. When Deephaven concluded

---

2004 Rights Offering, including, without limitation, all policies, procedures, or guidelines concerning the receipt of subscriptions after the deadline;

7. All records reflecting or referring to Rights Offering subscriptions received after the subscription deadline;

8. All records reflecting or referring to Rights Offering notices of guaranteed delivery received after the deadline for such notices;

9. All records reflecting or referring to the number of Rights Offering subscriptions received at all times during the Rights Offering subscription period, including, without limitation, all calculations, tabulations, charts, running totals, spreadsheets, and raw data; and

10. All documents and other information provided by the subscription agent for the Company's class A shares concerning the number of Rights Offering subscriptions received and/or the number of oversubscription rights available at all times during the Rights Offering.

11. All records, including recorded phone conversation logs between the Company, its subscription agent, and any individual referencing or relating to the oversubscription rights.

the discussions would not be fruitful, it filed its Complaint. UGC moved to dismiss the Complaint under Court of Chancery Rule 12(b)(6), raising issues related to Deephaven's technical compliance with § 220, its status as a beneficial holder and the purpose for its demand. The Court denied UGC's motion,[20] and the case later was tried.

On June 15, 2005, UGC and Liberty Media International consummated a business combination whereby they combined their businesses under a newly formed parent corporation, Liberty Global, Inc. (the "Merger"). Each share of UGC Stock was converted into the right to receive either $9.58 in cash or .2155 shares of Liberty Global stock. UGC contends that the Merger mooted this action because Deephaven no longer is a stockholder and no longer has a proper purpose to seek inspection. Deephaven disputes that contention.

II. ANALYSIS

A. Standing

Section 220 provides inspection rights of a corporation's books and records to all of its stockholders.[21] As amended (effective August 1, 2003), the statute defines the term "stockholder" to include "a person who is the beneficial owner of shares of such stock held . . . by a nominee on behalf of such person."[22] A stockholder is required only to

---

20 *Deephaven Risk Arb Trading Ltd. v. UnitedGlobalCom, Inc.*, 2004 WL 1945546 (Del. Ch. Aug. 30, 2004).

21 8 *Del. C.* § 220(b).

22 8 *Del. C.* § 220(a)(2). Before amendment, § 220 rights were available only to stockholders of record, and as a result, beneficial owners whose stock was held on their behalf were required to either have shares re-issued in their names before issuing a demand letter or request that the action be prosecuted on their behalf by

provide "documentary evidence of beneficial ownership" and to state that such documentary evidence is "a true and correct copy of what it purports to be."[23]

1. Is ownership of individual shares of stock negated by a net short position?

Deephaven asserts that it has owned UGC Stock since January 13, 2004 in its Barclays account. It argues that any short positions in UGC Stock are immaterial to determining whether it beneficially held the UGC shares in its Barclays account. UGC challenges Deephaven's beneficial ownership on two primary grounds. First, UGC argues that at the time of the Rights Offering, "as a short seller, Deephaven was not a beneficial owner of UGC stock."[24] Thus, UGC effectively contends that the Court must analyze Deephaven's UGC holdings in the aggregate to determine beneficial ownership. Second, UGC argues that borrowing shares does not give rise to beneficial ownership and that the act of selling borrowed shares to one's self does not change the shares' status as borrowed.

At the time of the Rights Offering, Deephaven held over 4 million UGC shares long in its Barclays account. At the same time, Deephaven's *net* position across all of its brokerage accounts was more than 4 million shares short. According to UGC, because Deephaven was net short, "Deephaven did not <u>own</u> any UGC stock; it <u>owed</u> over 4

---

the record holder. The 2003 amendment to § 220 liberalized the statute in order to obviate such technical hurdles. *See* Donald J. Wolfe, Jr. & Michael A. Pittinger, *Corporate and Commercial Practice in the Delaware Court of Chancery*, § 8-6[b] (2004).

[23] 8 *Del. C.* § 220(b).

[24] UGC's Post-trial Br. ("UPB") at 23.

million shares to others."[25] In other words, UGC contends that if an investor simultaneously holds a long position in a security and a larger short position in the same security, the investor does not "own" the shares held long. UGC offers no authority for this proposition, however, and it is unsupported by either the statute or practical considerations.

As Halbower explained at trial, the simultaneous ownership of long and short positions is akin to an individual who has an outstanding loan for $1 million, while at the same time maintaining $1 million in cash in a bank account. While both positions may be relevant when calculating the person's net worth, the fact of the loan does not negate her "ownership" of the $1 million in cash, which she owns and may dispose of as she wishes.[26]

Section 220 is a summary proceeding.[27] Historically, only record holders had standing to seek inspection rights. Proof that the plaintiff was a stockholder of record generally ended that portion of the analysis.[28] For example, it has been held that "§ 220 does not require that a shareholder have a 'direct' economic interest in the stock she owns

---

25 *Id.* (emphasis in original).

26 This example assumes the cash has not been pledged as collateral against the loan. In this case, there is no evidence that the shares held in Deephaven's Barclays account were in any way directly encumbered by obligations in other accounts.

27 8 *Del. C.* § 220(d).

28 *See Holtzman v. Gruen Holding Corp.*, 1994 WL 444756, at *3 (Del. Ch. Aug. 5, 1994) ("A current stockholder of record in a Delaware corporation has standing to seek inspection rights under § 220, provided a proper purpose is stated.").

of record to be entitled to enforce the inspection right."[29] In addition, record holders have inspection rights "even though the possibility exists that a stockholder may later be divested of this stock in some other proceeding or be declared in some future proceeding to be holding his stock contrary to law or private agreement."[30]

The statute was amended in 2003 to, among other things, extend inspection rights to beneficial owners of stock. In describing the pertinent portion of the legislation, the bill explains: "inspection rights are extended to a person who beneficially owns stock through either a voting trustee or a nominee who holds the stock of record on behalf of such person."[31] Importantly, neither the newly-amended statute nor the legislation itself indicates an intent to create two classes of inspection rights: one for record holders and one for beneficial holders. I interpret the 2003 amendment to afford to beneficial holders *all* § 220 rights previously held by record holders. Therefore, established law that record holders need not have an economic interest in stock to have inspection rights applies with equal force to beneficial holders such as Deephaven.

Practically, requiring an analysis of why and under what circumstances a § 220 plaintiff came to hold a company's shares could significantly complicate the nature of this summary and often expedited proceeding. To give effect to UGC's position potentially would force courts to undertake a complex analysis to determine the

---

29 *Macklowe v. Planet Hollywood, Inc.*, 1994 WL 560804, at *3 (Del. Ch. Sept. 29, 1994).

30 *See Holtzman*, 1994 WL 444756, at *3.

31 S.B. 127, 142d Gen. Assem. (Del. 2003).

plaintiff's financial position net of stock, options and other derivatives. One can imagine cases in which financial experts might be necessary to make such a determination. Moreover, the specter of being forced to disclose sophisticated and proprietary trading techniques could have a chilling effect on the use of § 220 by a substantial segment of stockholders. Finally, unlike in other situations such as voting, the § 220 analysis includes its own safeguard against plaintiffs with economic incentives that are not aligned with other stockholders: the proper purpose analysis. For all of these reasons, I see no grounds to discount Deephaven's beneficial ownership of UGC shares held at Barclays because it also held off-setting short positions.

2. Is a purchaser of one's own short sales a beneficial owner?

UGC argues that "[a]s a short seller, Deephaven was not a beneficial owner of UGC stock"[32] and that "Deephaven's transfer of shares and cash from one pocket to the other pocket does not alter its status as a short seller and does not establish beneficial ownership."[33] UGC's argument has two components. First, UGC argues that because a short sale involves borrowing shares in order to sell them, the short seller never "owns" the shares and never becomes a "beneficial owner." UGC then argues that Deephaven's transfer of borrowed shares to another of its brokerage accounts did not change their status as borrowed shares.

---

32 UPB at 23.

33 *Id.* at 26.

The first component of UGC's argument raises the interesting question of whether one who merely borrows shares, and does not sell them, becomes a beneficial owner. One would think not, but for present purposes the Court need not answer that question. It is sufficient to note that under Delaware law a purchaser of shares from a short seller is a beneficial owner.[34] This result enables short selling in modern markets without necessitating quasi-title searches in connection with each stock purchase.

The remaining question is whether Deephaven's short-sales to itself constitute normal sales or, as UGC argues, some other type of transfer. UGC's position is without merit. All transfers of Stock into Deephaven's Barclays account involved an exchange of cash for Stock. More importantly, once in the Barclays account, the shares were not linked to, or otherwise encumbered by, the short positions in the other Deephaven accounts. Once Deephaven paid for the shares in its Barclays account, it had all of the rights of ownership, including the right to dispose of them and to receive the corresponding subscription rights. UGC's interpretation would differentiate between stockholders that purchased shorted shares on the open market and those that purchased such shares from themselves. I question the wisdom of treating those two situations differently in determining beneficial ownership. Therefore, I hold that regardless of the method Deephaven used to finance the shares in its Barclays account, having paid for and

---

[34] *In re Digex*, 2002 WL 749184, at *2 ("With regard to the share borrowed, both the shareholder from whom it was borrowed and the third party to whom the share was sold are beneficial owners.").

held them, Deephaven beneficially owned the shares and had the necessary standing to bring this action.[35]

B. Effect of the Merger

UGC contends that the Merger on June 15, 2005 has mooted this action for two reasons. First, UGC argues that as a result of the Merger Deephaven is no longer a UGC stockholder and thus is not entitled to UGC's books and records pursuant to § 220. This position, however, is contrary to a previous decision of this Court. In *Cutlip v. CBA Int'l, Inc.*, the court unequivocally rejected the notion that a merger after commencement of a § 220 action nullifies the plaintiff's standing.[36] Like the situation in *Cutlip*, Deephaven has established that it was a stockholder at the time of its demand and therefore has standing to maintain this action. Just as the subsequent merger in *Cutlip* did not divest

---

[35] UGC attacks Deephaven's beneficial ownership on two other grounds. UGC argues that Deephaven has not proven that it maintained beneficial ownership at all relevant times, such as when it made its demand and filed the Complaint. UGC bases this argument on two premises, neither of which is persuasive. First, UGC argues that Deephaven has not proven it was a stockholder at the time of its demand because some of the shares in its Barclays account were obtained as a result of the Rights Offering and were actually owed to other stockholders as a result of related short sales. As discussed *supra*, however, concurrent short obligations do not alter the beneficially owned status of shares held long.

UGC also argues that Deephaven did not beneficially own any shares until after June 15, 2004. This argument rests on admittedly mistaken Deephaven interrogatory answers. Deephaven's account records, now in evidence, show near continuous beneficial ownership in its Barclays account from January 13, 2004 through August 23, 2004 and a net long position since March 1, 2004. The only break of continuous ownership in the Barclays account occurred between March 5 and 8, and is immaterial because at that time Deephaven owned shares in its Goldman Sachs account and was net long across all of its accounts.

[36] 1995 WL 694422, at *2 (Del. Ch. Oct. 27, 1995) (Steele, V.C.).

the plaintiffs of standing in that case, the recent Merger here has no bearing on Deephaven's standing in this case.

Second, UGC argues that Deephaven's purposes for inspection are moot because Deephaven is no longer a UGC stockholder. Specifically, UGC relies on *Grimes v. DSC Communications Corp.*, for the proposition that a purpose of investigating claims of waste and mismanagement do not survive a merger because only stockholders have standing to pursue derivative actions.[37] The situation in *Grimes* is distinguishable, however, because in *Grimes* the stated purpose of the requested inspection was to investigate whether a pre-suit demand was wrongfully refused and, if so, to assist the plaintiff in meeting the particularized pleading requirement for a derivative action under Court of Chancery Rule 23.1. Therefore, by obviating the possibility of a derivative suit, the merger mooted Grimes' proper purpose.

In this case an active dispute remains notwithstanding the Merger. UGC incorrectly attempts to portray Deephaven's demand as primarily seeking to investigate claims of waste and mismanagement to determine whether or not it wanted to continue to own UGC stock.[38] To the contrary, the primary purposes for Deephaven's investigation

---

[37] C.A. No. 16145-NC, letter op. at 2–3 (Del. Ch. Nov. 6, 1998).

[38] Even if this were considered a primary purpose of Deephaven's demand, it still might support a continuing proper purpose in the circumstances of this case. As a result of the Merger, Deephaven received 28,946 shares of the resulting entity, Liberty Global, of which UGC is now a wholly-owned subsidiary and asset. *See* Korn Aff. ¶¶ 3–4. Thus, according to Deephaven, the value of its investment in the surviving entity still will be affected by the suspected pre-Merger mismanagement or wrongdoing of UGC. Because Deephaven has asserted other proper purposes, however, I need not address this argument further.

also have included "determin[ing] whether the rights of Deephaven and other, similarly-situated stockholders of the Company were impermissibly interfered with or denied by the Company or its agents in connection with the 2004 Rights Offering" and "determin[ing] whether Deephaven and other, similarly-situated stockholders are in fact entitled to additional oversubscription privileges in connection with the 2004 Rights Offering."[39]

Under Delaware law, the essential inquiry when distinguishing between direct and derivative claims is: "Who suffered the alleged harm—the corporation or the suing stockholder individually—and who would receive the benefit of the recovery or other remedy?"[40] The harm to Deephaven and similarly situated stockholders from misallocation of shares during the Rights Offering was suffered only by the affected stockholders and not by UGC, which stood to receive equal proceeds regardless of the distribution. Further, any relief obtained in a future suit would benefit Deephaven or a class of similarly situated stockholders, and not UGC.[41] Thus, although the Merger may have removed the possibility of derivative claims stemming from the Rights Offering, the

---

[39] Deephaven's Demand Letter. JX 29.

[40] *Tooley v. Donaldson, Lufkin & Jenrette, Inc.*, 845 A.2d 1031, 1035 (Del. 2004).

[41] Causes of action for the misallocation of shares among competing stockholders or for discrimination against specific stockholders have often been found to be direct and not derivative in nature. *See Acker v. Transurgical, Inc.*, 2004 WL 1230945, at *1 (Del. Ch. Apr. 22, 2004) (reorganization of a corporation's capital structure to the benefit of one shareholder and the detriment of another gave rise to a direct claim); *Gatz v. Ponsoldt*, 2004 WL 3029868, at 8 (Del. Ch. Nov. 5, 2004) (claim that transaction favored certain preferred stockholders to the detriment of other classes of stockholders was direct).

potential still exists for Deephaven to assert a class action claim or individual claims based on a misallocation of shares in the Rights Offering. I turn now to whether Deephaven has demonstrated a proper purpose for its § 220 demand, taking into account the recent Merger.

C. Proper Purpose

Section 220 requires that a stockholder seeking inspection of books and records state a proper purpose for the inspection. Section 220(b) defines a "proper purpose" as one "reasonably related to such person's interest as a stockholder."

To demonstrate a proper purpose when seeking to investigate possible mismanagement, a stockholder must "present some credible basis from which the Court can infer that waste or mismanagement may have occurred."[42] "The threshold for a plaintiff in a Section 220 case is not insubstantial."[43] Stockholders are not required to show actual mismanagement, but they must show, by a preponderance of the evidence, that there is a "credible basis to find probable corporate wrongdoing."[44] Stockholders

---

42 *Thomas & Betts Corp. v. Leviton Mfg. Co.*, 681 A.2d 1026, 1031 (Del. 1996).

43 *Sec. First Corp. v. U.S. Die Casting & Dev. Co.*, 687 A.2d 563, 568 (Del. 1997).

44 *Id.* at 565.

cannot satisfy this burden merely by expressing a suspicion of wrongdoing[45] or a disagreement with a business decision.[46]

Deephaven suggests that UGC may have issued false or misleading information in connection with either or both of the February 13 and 20, 2004 press releases. Deephaven also alleges that UGC may have treated certain foreign or other stockholders preferentially during the Rights Offering. The preferential treatment could have included granting extensions of applicable deadlines for exercising rights or waiving technical requirements to which foreign stockholders or rightsholders were subject. I find that the two press releases are sufficiently inconsistent to raise questions regarding what actually happened. As explained below, the press releases together with other evidence adduced by Deephaven constitute credible evidence from which the Court can infer that wrongdoing may have occurred. Therefore, Deephaven is entitled to a limited production of what is essential and sufficient to evaluate the timing of receipt of rights certificates, notices of guaranteed delivery and payment, and thereby determine what occurred.

The February 13 press release stated that the preliminary numbers showed rightsholders had subscribed for only 64 million of a possible 83 million shares. Although the February 13 press release did not specifically mention notices of guaranteed

---

[45] *See Weiland v. Cent. S.W. Corp.*, 1989 WL 48740, at *2 (Del. Ch. May 9, 1989) (dismissing § 220 action for failure to provide the necessary factual basis for plaintiff's suspicions of wrongdoing).

[46] *See Everett v. Hollywood Park, Inc.*, 1996 WL 32171, at *5–6 (Del. Ch. Jan. 19, 1996) (rejecting challenges to business judgments without a credible basis from which the Court could infer self-dealing or failure to exercise due care).

delivery, it did imply that notices of guaranteed delivery had been included in the figures by estimating that 19.3 million shares would be available to satisfy oversubscription requests. In contrast, the February 20 press release substantially revised the number of basic subscription requests to 82 million and reported a reduction in the number of shares available for oversubscription to 1 million. The only explanation for the reduction provided in the press release was that notices of guaranteed delivery had *not* been included in the preliminary figures. Specifically, the February 20 press release stated:

> As previously reported on February 13, 2004, the subscription agent for the Class A rights offering had informed UGC of the preliminary results whereby Class A rights holders had subscribed for approximately 63.7 million shares of UGC Class A common stock pursuant to the basic subscription privileged and approximately 66.8 million shares of UGC Class A common stock pursuant to the oversubscription privilege. These figures excluded shares unsubscribed pursuant to guaranteed delivery procedures.[47]

The reported omission may have occurred as stated and been the result of a relatively benign mistake. For example, there may have been a miscommunication between Mellon and UGC on or about February 12 that caused UGC to publish the preliminary numbers as it did.[48] By February 20, UGC realized the preliminary figures did not include the notices of guaranteed delivery and explicitly stated that fact. If this

---

[47] JX 4.

[48] A February 12 email from Mellon to UGC attaching the preliminary numbers later reported in the February 13 press release arguably supports this explanation. JX 44. The body of the email, but not the attached report, includes a cryptic reference to having received 25 million "Protected Rights." It is not entirely clear, however, what the email reference means, and UGC did not offer any testimony explaining it.

were all that occurred, Deephaven admits that it might not even be interested in investigating further.

Several facts, however, provide a credible basis to infer that that is not the whole story and that wrongdoing may have occurred. First, the magnitude of the change itself is significant—from approximately 19 million shares reportedly available for oversubscription rights according to the February 13 press release to about 1 million shares as of February 20. The initial report that the rightsholders of more than twenty percent of the available shares failed to exercise their basic subscription privileges immediately surprised experienced market participants such as Halbower and Eismont. Between February 13 and 19, a skeptical Halbower questioned both Eismont and Abbott about the figures and whether they included notices of guaranteed delivery. Eismont himself asked UGC's counsel the same question. Both were told the preliminary figures *did include* notices of guaranteed delivery.

Furthermore, the apparently low subscription rate caused Eismont and, perhaps, others to wonder whether foreign holders of rights had difficulty complying with the requirements for exercising them. Based on Eismont's comments Deephaven alleges that UGC may have treated certain foreign or other stockholders preferentially during the Rights Offering. Deephaven focuses on a conversation Halbower had with Mellon's Eismont on February 19. Eismont offered a possible explanation for the low subscription rate, stating: "[l]ogic would dictate . . . [t]hat a lot of the foreign holders couldn't

participate due to not providing the appropriate paperwork."[49] Deephaven contends that such foreign holders could have pressured UGC and Mellon to allow subscriptions that were submitted after the expiration date or that otherwise failed to meet the applicable requirements.

Collectively, the foregoing facts reasonably create suspicion when one considers that all subscription requests, including notices of guaranteed delivery, were due by 5:00 pm on February 12. Therefore, as of February 13, UGC and Mellon should have had all the information they needed to give accurate preliminary results. At a minimum, it is reasonable to expect that UGC or Mellon would have discovered the mistake in the week between the February 13 and 20 press releases, especially in the face of specific questions about whether or not notices of guaranteed delivery were included. In the context of a transaction affecting a large number of shares and, presumably, numerous shareholders, their failure to do so is sufficiently troubling to justify further inquiry. Eismont's remarks concerning foreign holders of rights, although inconclusive standing alone, provide further support for a limited investigation.

For these reasons I find Deephaven has proven by a preponderance of the evidence a credible basis from which the Court can infer that mismanagement or other wrongdoing may have occurred in connection with the Rights Offering and that it is possible that

---

[49] JX 16. According to Halbower, Eismont said that foreigners who held rights had to jump through additional hoops, which were atypical. Eismont also allegedly said that "there were lots of discussions going on with internal legal folks about the fact that those foreign holders weren't going to be allowed to exercise their rights." Tr. at 76.

Deephaven and similarly situated stockholders may have been entitled to additional shares in connection with the Rights Offering. Thus, Deephaven has presented a proper purpose for investigating when UGC and Mellon received the subscriptions and notices of guaranteed delivery and any written or electronic communications between Mellon and UGC on that subject. This should enable Deephaven to determine what happened. Because of its limited showing, however, Deephaven's investigation does not need to encompass all communications between stockholders and rightsholders on the one hand and UGC and Mellon on the other relating to the Rights Offering or the exercise of rights under it.

D. Scope

A § 220 plaintiff is entitled to those records that are "essential and sufficient" to the shareholder's purpose.[50] A stockholder is not entitled to the wide ranging discovery that would be available in support of litigation, and the records available are those within the "corporation's possession, custody or control."[51]

In its Demand Letter and this action, Deephaven seeks to inspect 11 categories of corporate books and records that relate to the Rights Offering. Many of the requests are overlapping and too broad for the limited investigation warranted. Based on a review of the requests, I find the documents Deephaven is entitled to receive are those called for in

---

50 *Helmsman Mgmt. Servs., Inc. v. A & S Consultants, Inc.*, 525 A.2d 160, 167 (Del. Ch. 1987).

51 *Saito v. McKesson HBOC, Inc.*, 806 A.2d 113, 115 (Del. 2001).

categories 4 and 9, subject to the following modifications.[52] First, the language "or referring to" should be deleted from both categories, because it is too broad. In addition, in connection with category 9, UGC need only produce those documents and records actually in its possession. In conformance with this ruling, UGC is required to produce all of the rights certificates, notices of guaranteed delivery and any related documentation delivered to UGC or Mellon by rightsholders in connection with the Rights Offering. To the extent the dates those documents were received by UGC or Mellon are not self-evident, UGC shall also produce sufficient additional records to show the dates and times at which such subscriptions and notices of guaranteed delivery were received. As to the remaining categories of documents requested, Deephaven has failed to demonstrate a proper purpose for their production. Accordingly, I deny Deephaven's request with respect to all other categories.

Because Mellon acted as Deephaven's transfer agent for the Rights Offering, all rights certificates, related documentation and payments of the subscription price were to be delivered directly to Mellon. Presumably many, if not all, of those documents remain in Mellon's possession. UGC resists production of those documents, however, on the ground that they are not within UGC's "control."

Section 220 contemplates production by a subject corporation of documents within its "possession, custody or control" in generally the same sense that language is used in Rule 34 of the Federal Rules of Civil Procedure and Court of Chancery Rule 34. In the

---

[52] The two categories to be produced (4 and 9), as modified, subsume the portions of requests 1, 2, 5, 7, 8, and 10 supported by a proper purpose.

Rule 34 context, "[c]ontrol has been defined to include 'the legal right to obtain the documents requested upon demand.'"[53] Thus, the key inquiry is whether the company has the power, unaided by the court, to force production of the documents.[54]

Mellon acted as UGC's agent for the Rights Offering. In that capacity, Mellon was to receive all of the rights certificates, related documentation and payments for the shares. It is logical to conclude, therefore, that those documents are under UGC's control. The same is true for any additional documents that might be necessary to show the date of receipt of those documents.

III. CONCLUSION

Deephaven has established that it has standing to prosecute this action as a beneficial owner of UGC Stock. I find that Deephaven has presented a credible basis for the Court to infer that mismanagement or wrongdoing may have occurred in connection with the implementation of the Rights Offering. Therefore, Deephaven is entitled to the limited production discussed above of the documents sought by its requests 4 and 9, as modified in this Memorandum Opinion.

IT IS SO ORDERED.

---

53 *7 Moore's Federal Practice* § 34.14[2][b] (3d ed. 2005).

54 *See Weinstein v. Orloff*, 870 A.2d 499, 510 (Del. 2005) (holding that even in the context of a subsidiary, the company must have actual power to cause the subsidiary to produce the documents); *see also Dobler v. Montgomery*, 2001 WL 1334182, at *10 (Del. Ch. Oct. 19, 2001) ("rights of shareholders secured by § 220 cannot be defeated simply by having another entity hold the records").