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Re: Holman v. Northwest Broadcasting, L.P.
C.A. No. 1572-VCN
Date Submitted: November 14, 2006

Dear Counsel:

Plaintiff Rick A. Holman ("Holman") is a limited partner in Defendant Northwest Broadcasting, L.P. ("Northwest"), a Delaware limited partnership in which Holman owns an approximately 4.6% equity interest. In this books and records action, brought under the Delaware Revised Uniform Limited Partnership Act

M. Duncan Grant, Esquire
Philip Trainer, Jr., Esquire
March 29, 2007
Page 2

(“DRULPA”)¹ and Northwest’s Partnership Agreement,² Holman seeks to value his investment and to investigate possible mismanagement. This letter opinion sets forth the Court’s post-trial findings of fact and conclusions of law.

I. BACKGROUND

Holman provided the initial investment banking services that helped create Northwest in 1995 and served as its chief financial officer from 1995 until 2000, when he abruptly resigned in the middle of a meeting of Northwest’s general partner’s board of directors. Northwest operates broadcast television affiliates in Washington, Oregon, and New York. Alta Communications (“Alta”), a venture

¹ 6 *Del. C.* ch. 17. By 6 *Del. C.* § 17-305(a), the DRULPA grants a limited partner: the right, subject to such reasonable standards (including standards governing what information and documents are to be furnished, at what time and location and at whose expense) as may be set forth in the partnership agreement or otherwise established by the general partners, to obtain from the general partners from time to time upon reasonable demand for any purpose reasonably related to the limited partner’s interest as a limited partner:

(1) True and full information regarding the status of the business and financial condition of the limited partnership; . . .

(6) Other information regarding the affairs of the limited partnership as is just and reasonable.

² Northwest’s Amended and Restated Limited Partnership Agreement (JX 1) provides, at § 8.1, that the partners “shall at all reasonable times have access to [Northwest’s] books.” Those books are generally described as “complete and accurate books of account with respect to the operation of [Northwest].” The parties, in this proceeding, have focused upon Holman’s statutory inspection rights.

M. Duncan Grant, Esquire
Philip Trainer, Jr., Esquire
March 29, 2007
Page 3

capital firm specializing in media investments, is the majority owner of Northwest. Tim Dibble serves as Alta's representative on Northwest's governing board.

Holman first filed a books and records action in this Court on September 2, 2003.³ That dispute was settled on November 29, 2003, through the Settlement Agreement and Mutual Release (the "Settlement Agreement").⁴ Northwest agreed to provide Holman, on an ongoing basis, with a schedule of partnership distributions with names redacted in addition to audited annual and quarterly financial statements.⁵ Holman asserts that he later entered into discussions with Tim Dibble in January 2005 concerning a possible buyout of his investment at a price of approximately \$1.8 million.⁶ Those discussions never culminated in a buyout, frustrating Holman's desire to sell his interest in the partnership.⁷

³ *Holman v. Northwest Partner, L.P., et al.*, C.A. No. 20521-NC. The Complaint in that action (the "First Complaint") sought original partnership agreements and/or certificates of incorporation of subsidiaries, the original Securities Agreement executed in connection with the formation of Northwest, financial instruments setting forth the rights of partners, agreements relating to income and loss allocation and distributions among the partners, a list of current equity holders of the partnership, loan or credit agreements of the partnership, its most recent financial statements, and a schedule of cash distributions to partners.

⁴ JX 5.

⁵ *Id.* at ¶¶ 3-4; *see* Tr. at 49-55.

⁶ Tr. at 20-23; Tr. at 119.

⁷ Tr. at 135-36.

M. Duncan Grant, Esquire
Philip Trainer, Jr., Esquire
March 29, 2007
Page 4

Holman now seeks a second inspection of Northwest's books and records. Holman cites two purposes for this inspection: valuation of his investment and investigation of mismanagement. Holman bolsters his valuation claim by noting the absence of a liquidity opportunity during the eleven-year life of his investment and the looming potential of a buyout from the holder of the controlling interest in Northwest. Holman supports his claims of mismanagement by observing that total assets declined by \$248,410 and overhead increased by \$150,001 between 2004 and 2005.⁸ Holman also offers that, over the period of 1999 to 2004, cash flow from the television stations had decreased 19% while overhead increased by 15%.⁹ Holman submits his personal opinion that such an irregularity is usually attributable to the payment of additional executive bonuses. Holman also asserts that, because television stations are frequently priced for sale based on a multiple of cash flows and Alta has discussed the potential of a buyout of his interest, management would have an incentive to keep cash flows artificially low.¹⁰

⁸ See JX 4 at 4, 6.

⁹ See JX 34.

¹⁰ Tr. at 15-21.

M. Duncan Grant, Esquire
Philip Trainer, Jr., Esquire
March 29, 2007
Page 5

To satisfy his purposes, Holman contends that he is entitled to inspect a broad range of Northwest documents addressing the decline in its financial performance during the last several years, efforts to reverse that decline, executive compensation, and liquidity or buyout opportunities.¹¹

II. ANALYSIS

By statute, a limited partner holds the right to inspect partnership books and records for any purpose that is “reasonably related to the limited partner's interest as a limited partner.”¹² In determining whether a specific purpose is “reasonably related to the limited partner's interest” under 6 *Del. C.* § 17-305, this Court has sought guidance from the case law considering a “proper purpose” under 8 *Del. C.* § 220, the Delaware General Corporation Law’s analogue to Section 17-305.¹³ Even if the applicable technical requirements are met and Holman’s purpose is proper, “[t]he

¹¹ See JX 2.

¹² 6 *Del. C.* § 17-305(e). The parties agree that Holman has complied with all of the procedural formalities for his inspection demand. Pretrial Order at ¶ II(C).

¹³ *Forsythe v. CIBC Employee Private Equity Fund (U.S.) I, L.P.*, 2005 WL 1653963, at *4-*5 (Del. Ch. July 7, 2005); see also *Bond Purchase, L.L.C. v. Patriot Tax Credit Props., L.P.*, 746 A.2d 842, 851 (Del. Ch. 1999); *In re Paine Webber Ltd. P’ships*, 1996 WL 535403, at *15 (Del. Ch. Sept. 17, 1996).

M. Duncan Grant, Esquire
Philip Trainer, Jr., Esquire
March 29, 2007
Page 6

scope of such relief will typically be limited only to the inspection of those books and records that are necessary and essential to the satisfaction of the stated purpose.”¹⁴

A. *The Valuation Purpose and the Scope of Inspection Permitted*

The Court finds that valuation of his interest in Northwest is a purpose of Holman and that the purpose is a proper one.

Valuation of one’s interest is a proper purpose for the inspection of limited partnership’s books and records.¹⁵ When inspection is sought to value one’s holdings, “our courts consistently have limited the extent of that inspection to those records which are ‘essential and sufficient’ to accomplish the stated purpose.”¹⁶

However, if a shareholder has been given all the corporate information that he

¹⁴ *Highland Select Equity Fund, L.P. v. Motient Corp.*, 906 A.2d 156, 164 (Del. Ch. 2006).

¹⁵ *CM & M Group, Inc. v. Carroll*, 453 A.2d 788, 792 (Del. 1982). *Madison Ave. Inv. Partners, LLC v. Am. First Real Estate Inv. Partners, L.P.*, 806 A.2d 165, 174 (Del. Ch. 2002) (“Valuing one’s investment is generally considered to be a proper purpose reasonably related to one’s interest.”).

¹⁶ *Tactron, Inc. v. KDI Corp.*, 1985 WL 44694, at *1 (Del. Ch. Jan. 10, 1985). “[T]he scope of the inspection cannot be premised upon the need to perform an audit, but must be narrowed to those documents which the evidence has shown to be essential and sufficient for the [valuation] purpose for which the inspection is sought.” *Helmsman Mgmt. Servs., Inc. v. A & S Consultants, Inc.*, 525 A.2d 160, 168 (Del. Ch. 1987).

M. Duncan Grant, Esquire
Philip Trainer, Jr., Esquire
March 29, 2007
Page 7

reasonably needs to accomplish his stated purpose, his right has been satisfied and no additional disclosure is required on the part of the entity.¹⁷

For purposes of valuation in the context of § 220, a distinction may be drawn between publicly traded companies and closely held companies. With regard to the former, public filings typically provide significant financial information about the company, and inspection rights are narrowly tailored to address specific needs.¹⁸ The Court will limit or deny any inspection to the extent that the requested information is available in a corporation's public filings. In contrast, shareholders of companies which are not publicly traded do not have access to the same quantity of information available from the regulatory filings of publicly traded companies and, accordingly, are given broader access to the corporation's financial records.¹⁹ Northwest, of

¹⁷ *Id.*

¹⁸ See DONALD J. WOLFE, JR. & MICHAEL A. PITTENGER, CORPORATE AND COMMERCIAL PRACTICE IN THE DELAWARE COURT OF CHANCERY § 8.6(e)(1), at 8-83 (2006) (“Thus, to the extent that information sufficient to permit the valuation is contained in publicly available records, the inspection of corporate books and records for the purpose of such a valuation exercise will be denied.”); see also *DPF, Inc. v. Interstate Brands Corp.*, 1975 WL 1963, at *2 (Del. Ch. Oct. 2, 1975) (“[T]he stock is not only traded on the New York Stock Exchange but it is also registered with the Securities and Exchange Commission pursuant to Section 12 of the Securities Act of 1934 [T]he plaintiff could well already have access to all the information that it is reasonably and fairly entitled to receive for the purpose stated [valuation of stock].”). See also *Petition of B & F Towing & Salvage Co., Inc.*, 551 A.2d 45, 51 (Del. 1988).

¹⁹ See, e.g., *Macklowe v. Planet Hollywood, Inc.*, 1994 WL 560804, at *4 (Del. Ch. Sept. 29, 1994).

M. Duncan Grant, Esquire
Philip Trainer, Jr., Esquire
March 29, 2007
Page 8

course, is not publicly traded and, thus, Holman does not necessarily receive a broadly encompassing range of financial data. Holman, however, already receives significant financial information—audited financial statements—as the result of the settlement of his first books and records action.

As part of his current demand, Holman seeks a breakdown of performance-based executive compensation awarded and supporting materials concerning board decisions on performance-based executive compensation.²⁰ These expenditures, as provided to Holman, are not separated out on the financial statements provided, but are lumped together with all corporate overhead.²¹ Executive compensation, in the context of a closely held partnership, is relevant to Holman's valuation of his interest.

²⁰ See Compl. ¶ 9 (listing requested documents):

h. All documents relating to, reflecting, or evidencing any proposals that bonuses or other performance-based or incentive compensation be awarded to any officers of the partnership with respect to any fiscal year starting on or after January 1, 2000, and, in any instances in which such bonuses or incentive compensation have been awarded, documents sufficient to show to recipient(s) and the amount and terms of each such bonus or incentive compensation.

i. All documents relating to, reflecting, or evidencing any consideration by the Partnership, by the Board of Directors of the General Partner of the Partnership, or by the officers of the Partnership, since January 1, 2000, to award bonuses or other performance-based or incentive compensation to any officers of the Partnership, and, if no such bonuses or other performance-based or incentive compensation arrangements have been instituted, the reasons behind the determination not to institute such arrangements.

²¹ See JX 3 at 5; JX 4 at 6.

M. Duncan Grant, Esquire
Philip Trainer, Jr., Esquire
March 29, 2007
Page 9

Whether Northwest's executive compensation is higher or lower than the industry norm may suggest that cash flow should be adjusted for valuation purposes. Therefore, Holman is entitled to receive a schedule of compensation received by the three most highly paid officers or employees of Northwest since 2000, separated into cash and non-cash consideration, as well as performance-based payments, in order to value his investment in Northwest.

Holman also seeks a panoply of additional information beyond the audited financial statements that he is receiving on an annual and quarterly basis in accordance with the partnership agreement, but he has not shown that the financial reports already provided by Northwest omit other information that is necessary, essential, or sufficient for his purpose. This Court finds no basis for questioning the judgment of the independent auditors in assessing what constitutes material financial information or in preparing the financial statement he receives on a quarterly and yearly basis. Except for executive compensation data, Holman has not provided evidence that the financial accounting standards utilized in preparing and auditing those statements should not otherwise coincide with the standards for information

M. Duncan Grant, Esquire
Philip Trainer, Jr., Esquire
March 29, 2007
Page 10

necessary and sufficient for valuation of his interest in this partnership. Because audited quarterly and annual statements of public firms regularly meet that purpose, then by analogy, the same type of reporting should be sufficient for Holman to value his interest.²² Therefore, the Court concludes that additional schedules detailing executive compensation arrangements, combined with the audited annual and quarterly reports he is already receiving, encompass the scope of financial documents necessary and sufficient to allow Holman to value his interest in Northwest.²³

²² The question of whether Holman has the right to inspect the audited statements is not before the Court; that right is the result of the Settlement Agreement.

²³ Holman's current claims must be evaluated in light of the Settlement Agreement. The Settlement Agreement, at Section 7, precluded Holman from bringing another books and records action for claims "asserted or [which] could have [been] asserted against" Northwest in the First Complaint. Because the Court has granted access to documents as far back as 2000 and because the Settlement Agreement was entered into in 2003, the Court must consider whether the Settlement Agreement precludes Holman from gaining access to the documents which the Court would otherwise allow him to inspect. Holman relies upon Section 9 of the Settlement Agreement which relates to documents which "the parties agreed would not be produced at the time of the Settlement Agreement." Those documents, if circumstances change, can be the subject of a books and records action. Holman, however, has not demonstrated that circumstances have changed and, more importantly, it is not clear that the documents which Holman has sought in this action were documents which the parties agreed would not be produced under the terms of the Settlement Agreement. The Court, thus, returns to Section 7 of the Settlement Agreement. The question is whether the documents sought in this action could have been sought under the First Complaint. They were not sought and could not have been sought because they were not set forth in the demand, or so it appears, that led to the First Complaint. Thus, the only documents which were sought, or could have been sought, through the First Complaint were those listed in the demand. The question is not whether some of the documents at issue here could have been listed in the demand leading to the First Complaint. Accordingly, the Settlement Agreement does not preclude

B. Investigation of Mismanagement as a Proper Purpose

A broader inspection of Northwest's books and records would require credible evidence of wrongdoing by the current management.²⁴ Holman, therefore, identifies a second purpose: the investigation of breaches of fiduciary duty and mismanagement. If a books and records demand is to investigate wrongdoing, a plaintiff must prove that he has some credible evidence of possible wrongdoing sufficient to warrant continued investigation.²⁵

The standards for a limited partnership books and records inspection are similarly treated.²⁶ Cases finding proper purpose in the context of mismanagement

Holman's access to the documents sought in this proceeding. *See generally* Tr. of Oral Arg. on Def.'s Mot. to Dismiss and Rulings of the Court at 50-53 (Jan. 18, 2006).

²⁴ Accusations about events five or six years ago, during the time Holman was employed by Northwest, are discounted due to (i) lack of evidence and (ii) remoteness. Also, the Court rejects as a matter of fact any claim by Northwest that Holman intends to use information obtained through this inspection to harm the partnership.

²⁵ *See Seinfeld v. Verizon Commc'ns, Inc.*, 909 A.2d 117, 125 (Del. 2006) ("We remain convinced that the rights of stockholders and the interests of the corporation in a section 220 proceeding are properly balanced by requiring a stockholder to show 'some evidence of *possible* mismanagement as would warrant further investigation.'") (emphasis in original) (citing *Security First Corp. v. U.S. Die Casting & Dev. Co.*, 687 A.2d 563, 568 (Del. 1997)).

²⁶ *Forsythe*, 2005 WL 1653963, at *4-*5. ("While [limited partners] have the burden of coming forward with specific and credible allegations sufficient to warrant a suspicion of waste and mismanagement, they are not required to prove by a preponderance of the evidence that waste and mismanagement are actually occurring.") *Khanna v. Covad Commc'ns Group, Inc.*, 2004 WL 187274, at *6 (Del. Ch. Jan. 23, 2004) (quoting *Sec. First*, 687 A.2d at 568) ("All that the [books

M. Duncan Grant, Esquire
Philip Trainer, Jr., Esquire
March 29, 2007
Page 12

for limited partnership books and records inspections stand in marked contrast to the present request, with either some element of self-dealing sufficiently demonstrated or far greater financial irregularities presented.²⁷ Holman does nothing more than point to moderately disappointing financial performance that one could expect from any investment. Further, Holman's accusation concerning an incentive for management artificially to depress cash flows is nothing more than an assertion that any time a general partner has control over financial statements he will always have some incentive to game them and thus a proper purpose for inspection would always be available. In short, Holman has not supported his claim with "some credible evidence of possible mismanagement." With that, this claim for inspection based on fears of mismanagement fails.

and records] plaintiff must show is a credible basis for claiming that 'there are legitimate issues of wrongdoing.'").

²⁷ *Forsythe*, 2005 WL 1653963, at *5 ("The plaintiffs . . . have shown that the Fund's value has plummeted over the last few years while the General Partner . . . made substantial fees. In addition . . . CIBC made highly profitable investments that the Fund did not participate in [T]hese facts . . . provide a credible basis for inferring mismanagement of the Fund."). See also *Haywood v. Ambase Corp.*, 2005 WL 2130614, at *5 (Del. Ch. Aug. 22, 2005) (holding basis of mismanagement established where chief executive officer with few executive responsibilities had compensation amounting to 10% of market value of the company and in the 100th percentile of comparable companies). A 15% increase in overhead coupled with an 18% decrease in cash flows pales by comparison.

M. Duncan Grant, Esquire
Philip Trainer, Jr., Esquire
March 29, 2007
Page 13

III. CONCLUSION

For the reasons set forth, Northwest shall provide Holman with supplemental schedules of executive compensation, disaggregated into cash, non-cash, and performance-based remuneration, received by the three most highly compensated employees of Northwest since 2000 and on a yearly basis. Otherwise, Holman's request for a broader inspection of Northwest's books and records is denied.

IT IS SO ORDERED.

Very truly yours,

/s/ John W. Noble

JWN/cap
cc: Register in Chancery-NC