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STOCKHOLDER INSPECTION RIGHTS AND AN “INCREDIBLE” BASIS: SEEKING DISCLOSURE RELATED TO CORPORATE SOCIAL RESPONSIBILITY

Gabrielle Palmer*

I. INTRODUCTION

Corporations are creatures of state law.2 The state of incorporation determines the rights of shareholders and managers.3 As part of this regulatory process, state law provides shareholders with the right to inspect the books and records of corporations. Described by courts as a “powerful right,”4 the authority is “an important part of the corporate governance landscape.”5

The federal securities laws also regulate the disclosure by public companies. In the 1930s, Congress assigned to the Securities and Exchange Commission (SEC) the authority to develop an affirmative disclosure regime for these companies.6 Under the Securities Act of 1933 and the Securities Exchange Act of 1934, the SEC adopted a comprehensive framework that required “issuers to disclose information about the company, its business, and its management periodically and upon the occurrence of specified events.”7

Neither system has proved particularly hospitable to the disclosure of information related to matters of corporate social responsibility. Inspection rights have traditionally been limited to matters of corporate wrongdoing. Similarly, the securities laws focused on information material to investors, a category that generally does not include socially responsible activities.8 Pressure has, however, increased for the disclosure of this type of information. In 2010, Congress sought to promote corporate social transparency. The Dodd-Frank Wall Street and Consumer

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3. Id.
Protection Act (Dodd-Frank)\(^9\) required affirmative disclosure about conflict minerals\(^{10}\) and natural resource extraction payments.\(^{11}\) Although relatively narrow topics, they represented examples of Congress imposing on the SEC the obligation to write disclosure rules on matters designed to promote social well-being.

In the aftermath of these changes at the federal level, Delaware law has arguably undergone a shift, making information on corporate social responsibility accessible through inspection rights.\(^{12}\) In *Louisiana Municipal Employees’ Retirement System v. Hershey*, the Chancery Court denied a motion to dismiss an inspection request seeking information about the use of child labor and human trafficking in the defendant’s supply chain.\(^{13}\) The court indicated that shareholders could meet the standards for inspection through the use of public information about child labor on cocoa farms in West Africa.\(^{14}\) As evidence of the “possibility of mismanagement,” the court accepted an inference that arose from a correlation between public information about human rights abuses in West Africa and the company’s acknowledgment of concern about the issue.\(^{15}\)

This article seeks to examine inspection rights in Delaware, with a particular emphasis on the availability of materials relating to corporate social responsibility. Part II discusses the requirements of the governing law—namely, Section 220 of the Delaware General Corporation Law. Part III concerns the incredible pleading standards that Section 220 imposes on shareholders requesting information about public companies. Part IV explores the relationship between inspection rights and corporate social responsibility. Finally, Part V discusses the *Hershey* decision and Part VI analyzes the possible shift in Delaware standards when issues of social responsibility are involved.

**II. THE GOVERNING LAW: DELAWARE CODE SECTION 220**

**A. Overview**

Inspection rights have long existed under Delaware law.\(^{16}\) Common law provided that stockholders were “entitled to know . . . how [their] agents were conducting the affairs of the corporation of which [the

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\(^{11}\) Id. § 78m(q)(2)(A).


\(^{13}\) Id. at 3-4.

\(^{14}\) Id. at 17-22.

\(^{15}\) Id.

stockholder] was a part owner."  

Enforcement of these rights required a writ of mandamus from the Delaware Superior Court. In 1967, the legislature codified the common law right of inspection in Section 220 of the Delaware General Corporation Law. Under the provision, stockholders have the right to inspect the corporation’s books and records “for any proper purpose.” Shareholders must submit a written demand that specifies the requisite purpose. The corporation has five days to respond to, and comply with, the demand. In the absence of a timely response, “the stockholder may apply to the Court of Chancery for an order to compel such inspection.” When seeking inspection of corporate books and records other than a corporate stock list, shareholders bear the burden of establishing a proper purpose.

B. Proper Purpose

Proper purpose has been described as “[t]he paramount factor in determining” entitlement to inspection rights. The requirement prevents access to corporate records out of “sheer curiosity” and avoids harassment to the corporation. A proper purpose must be “reasonably related to such person’s interest as a stockholder” and not “adverse to the best interests of the corporation.” In general, this requires an allegation of wrongdoing by the board.

Examples of proper purpose include contentions that: corporate assets were comingledd with those of a controlling shareholder; fiduciary

21. tit. 8, § 220(b).
22. Id.
23. Id.
24. Id.
25. Skouras v. Admiralty Enters., 386 A.2d 674, 678 (Del. Ch. 1978) (noting under Section 220, the “burden of proving a proper purpose is on the stockholder, where, as here, the demand is for inspection of books and records rather than for a stock list”).
27. Id.
28. tit. 8, § 220(b).
29. Skouras, 386 A.2d at 678.
duties were violated in connection with related party transactions; and executives were excessively compensated for performing minimal duties. The standard is generally met where the stockholder pleads mismanagement in the context of self-dealing transactions or “financial irregularities.”

On rare occasions, Delaware courts have recognized that shareholders need not allege mismanagement. Instead, shareholders, as owners, have the inherent right to obtain certain types of information irrespective of fault. For example, Delaware courts have allowed shareholders to obtain documents relating to the valuation of their shares absent allegations of wrongdoing.

Shareholders also need not allege mismanagement when exploring director qualifications. In City of Westland Police & Fire Retirement System v. Axcelis Technologies, Inc., the company had in place a “plurality-plus” voting provision requiring any director failing to receive majority vote to tender a letter of resignation to the Nominating and Governance Committee, which then recommends board action with respect to the resignation. Pursuant to the provision, three directors resigned and submitted the required letter. The board, however, did not accept their resignations.

In the aftermath, a stockholder filed a Section 220 action alleging that the Board’s rejection of such directors’ resignations “established a credible basis to infer that the Board intended to entrench those three directors (and indeed the entire Board) in office.” The Chancery Court disagreed, concluding that the shareholders had not presented credible evidence supporting the claim of entrenchment.

35. See, e.g., CM & M Grp. v. Carroll, 453 A.2d 788, 792 (Del. 1982) (valuation of shares is a proper purpose).
36. See generally id. (granting inspection rights where stockholder sought valuation in order to sell his stock where the corporation was closely held with no publicly traded shares and where shares were subject to substantial restrictions on resale). Moreover, intent to solicit proxies is sufficient to meet the proper purpose threshold without allegations of wrongdoing by the Board. W. Air Lines, Inc. v. Kerkorian, 254 A.2d 240, 241 (Del. 1969).
38. Id. at 283.
39. Id. at 284.
40. Id.
41. Id. at 283.
On appeal, the Delaware Supreme Court found director suitability to be a proper purpose, even absent allegations of mismanagement. Stockholders had an inherent right to information regarding director qualifications because, with regard to governance issues, they “may express dissatisfaction only through the electoral check.” Nonetheless, because the Axcelis stockholder relied on allegations of entrenchment and not suitability, the court affirmed the lower court’s decision.

A proper purpose, therefore, must relate to a stockholder’s status as part owner of the company. In general, the courts have limited these rights to allegations of mismanagement. Nonetheless, some issues, such as director qualifications and share valuation, are viewed as inherently important to stockholders such that they do not need to be accompanied by allegations of wrongdoing.

III. DELAWARE COMMON LAW AND THE NEED FOR A CREDIBLE BASIS

In pleading a “proper purpose,” neither allegations of “general mismanagement” nor “mere suspicions” of wrongdoing will suffice. Instead, courts have grafted on an additional requirement not contained in the statute. Shareholders must allege a “credible basis” for any such claim. A credible basis requires “some evidence of possible mismanagement as would warrant further investigation of the matter . . . .”

Stockholders can meet this threshold by presenting “documents, logic, testimony or otherwise” that suggest “legitimate issues of wrongdoing.” The standard does not require affirmative evidence of mismanagement but rather a showing that corporate wrongdoing is possible based on a preponderance of the evidence.

Although described as setting “the lowest possible burden of proof,” the credible basis standard is not insubstantial. In Shamrock

43. Axcelis, 1 A.3d at 290.
44. Id. (quoting Pershing Square, L.P. v. Ceridian Corp., 923 A.2d 810, 817–18 (Del. Ch. 2007)) (internal quotation marks omitted).
45. Id.
46. DEL. CODE ANN. tit. 8, § 220(b) (2010).
50. Id. Note, however, that information widely available through the media may not be sufficient to meet this standard. See Beam ex rel. Martha Stewart Living Omnimedia, Inc. v. Stewart, 833 A.2d 961, 981 (Del. Ch. 2003) (aff’d, 845 A.2d 1040 (Del. 2004)) (en banc).
51. Rulings of the Court From Oral Argument on Exceptions to the Master’s Final Report, supra note 12 (“Stockholders need only show by a preponderance of the evidence a credible basis from which the Court of Chancery can infer that there is possible mismanagement that would warrant further investigation, a showing that may ultimately fall well short of demonstrating that anything wrong occurred.” (emphasis added)).
Activist Value Fund, L.P. v. iPass Inc., stockholders asserted as a proper purpose that the company board failed to achieve certain projected benefits as a result of a merger with GoRemote.53 As evidence of mismanagement, stockholders pointed to “the divergence between projections and results . . . .”54 The court refused to infer mismanagement based on incorrect projections.55 Stockholders instead had to show “something more.”56

Shareholders did, however, succeed in showing “something more” with respect to the claim that the Company failed to plan for GoRemote’s integration.57 Specifically, the complaint alleged that the company formulated a plan only after the Plaintiff wrote a letter asking about one, that the company’s website directed unhappy customers on how to convert from the Company’s services to GoRemote, and that shortly after execution of the merger, the officer responsible for overseeing the integration of the two companies left the company.58 This evidence, the court concluded, “provide[d] the basis for an inference that mismanagement possibly occurred.”59

Credible basis can also be met through expert testimony. In Dobler v. Montgomery Cellular Holding Co., Inc.,60 a stockholder sought documents to determine, among other things, whether mismanagement or waste had occurred with respect to transactions engaged in or authorized by the company’s single board member.61 To meet the credible basis requirement, the stockholder presented testimony from an expert in valuation and forensic accounting that identified “red flags” in the financial statements.62 The red flags focused on advances made by the company to affiliates.63 The red flags coupled with concern over “the apparent lack of documentation for significant transactions with affiliates”64 was sufficient to establish the requisite credible basis.65

54. Id. at *2.
55. Id. (“Predictions of the consequences of implementing corporate decisions (i.e., the taking of risk) and the failure of those predictions to materialize do not, without more, share a logical nexus with mismanagement.”).
56. Id.
57. Id.
58. Id. at *2 n.14.
59. Id. at *2. Accordingly, the company’s motion to dismiss was denied because the stockholder pled a credible basis from which the court could infer wrongdoing with respect to the merger. Id.
61. Id. at *4.
62. Id. at *2, *4.
63. Id. at *4.
64. Id. at *5.
65. Id. at *4. The court in Magid v. Acceptance Insurance Co. found that expert testimony was sufficient to meet the credible basis threshold. See No. Civ.A. 17989-NJ, 2001 WL 1497177, at *7 (Del. Ch. Nov. 15, 2001). Specifically, the plaintiff’s expert testified that “management’s failure to adjust on a timely basis the Company’s loss reserves in response to” a California Supreme Court
Stockholders have met the credible basis threshold by presenting a variety of other types of evidence, including: potential misconduct identified in SEC orders; the presence of transactions that allegedly imparted a “personal material benefit” on directors and which “carried serious adverse consequences” to the company; an unusually quick settlement of a derivative action; and the failure to hold a stockholders meeting over a three year period, especially when combined with allegations that the corporation’s founder made statements about unauthorized loans and an intent to dilute shares.

Mere disagreements with management’s judgment, however, will not suffice to create an inference of wrongdoing. In Seinfeld v. Verizon Communications, a shareholder filed a Section 220 action alleging the compensation paid to Verizon’s three highest officers “was excessive and wasteful.” The plaintiff asserted that compensation totaling $205 million over three years was unwarranted.

The shareholder acknowledged, however, that he lacked any factual support for the claims of wrongdoing. Nonetheless, requiring a credible basis of wrongdoing would impose an “insurmountable barrier” to the exercise of inspection rights under Section 220. As a result, the plaintiff argued that “minority shareholders who have access only to public documents and without a whistle blower or corporate documents should be permitted to have limited inspection based upon suspicions, reasonable beliefs, and logic arising from public disclosures.”

decision that “significantly expanded” the company’s risk exposure “constituted a reasonable basis for concluding that mismanagement may have occurred.” Id. at *3.


70. 909 A.2d 117 (Del. 2006) (en banc).

71. Id. at 118.

72. Id. at 119.

73. Id. (“During his deposition, Seinfeld acknowledged he had no factual support for his claim that mismanagement had taken place. He admitted that the three executives did not perform any duplicative work. Seinfeld conceded he had no factual basis to allege the executives ‘did not earn’ the amounts paid to them under their respective employment agreements.”).

74. Id. at 120–21. Specifically, “by requiring evidence, the shareholder is prevented from using the tools at hand” to obtain information about the corporation. Id. at 121 (internal quotation marks and citations omitted).

The Delaware Supreme Court disagreed finding that the credible basis “standard achieves an appropriate balance between providing stockholders who can offer some evidence of possible wrongdoing with access to corporate records and safeguarding the right of the corporation to deny requests for inspections that are based only upon suspicion or curiosity.”

Plaintiff was “concerned about the large amount of compensation paid to the three executives.” Such a “disagreement” with the company’s business judgment was not sufficient evidence of wrongdoing.

The credible basis standard necessarily creates barriers for stockholders alleging corporate mismanagement. As Seinfeld illustrates, stockholders seeking inspection of corporate books and records must offer something more than concern over board behavior. The threshold requires affirmative evidence that permits an inference of mismanagement. Practically, however, it can be difficult for stockholders to obtain this type of information because whether corporate actions are consistent with directors’ fiduciary duties is a matter of the process by which decisions are made.

IV. INSPECTION RIGHTS AND CORPORATE SOCIAL RESPONSIBILITY

Corporations are sometimes said to “have a responsibility to society at large.” Corporate social responsibility signifies “the ethical and responsible methods of corporate operations and business practices.” Although “[t]here is no single universal framework describing the activities that are part of [corporate social responsibility] initiatives,” the approach generally refers to good business practice in the areas of “environmental sustainability . . . stakeholder responsiveness, human rights, labor conditions, and social accountability.” Pressure to engage in socially responsible behavior often comes from non-shareholders, including “consumers, human rights groups, domestic and international labor

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76. Seinfeld, 909 A.2d at 118.
77. Id. at 120.
78. Id. (affirming the Chancery Court’s finding that the Plaintiff offered no evidence from which the court could infer that wrongdoing was in fact occurring).
79. See Aronson v. Lewis, 473 A.2d 805, 812 (Del. 1984) overruled on other grounds by Brehm v. Eisner, 746 A.2d 244 (Del. 2000) (finding that the business judgment rule shields the board from liability for corporate decisions if “the directors of a corporation acted on an informed basis, in good faith and in the honest belief that the action taken was in the best interests of the company”).
82. Chandra, supra note 80, at 111.
groups, and increasingly the media. In particular, corporate social responsibility "is attractive to consumers."

Socially responsible behavior can, however, promote profit maximization. Consequently, shareholders often apply pressure through the proxy process in an effort to increase corporate social involvement. Although "the specifics of any given corporate social responsibility issue vary by industry," common areas of concern include "environmental protection[,] . . . sustainable development[,] and labor" conditions. These concerns center around "the relationships between corporate economic activity and the health and welfare of the people and environment with which the corporate actor interacts."

The issue can become even more complicated with the outsourcing of production. Although companies may act in a socially responsible manner, their suppliers may not. Suppliers may have an incentive to lower costs and gain profits "at the expense of workers' health and lives."

Shareholders seeking information about socially responsible activities, including those of suppliers, have traditionally had few meaningful avenues. With respect to inspection rights, shareholders as owners were not automatically entitled to information about these types of activities but must allege some sort of wrongdoing by the company and the board. In addition, the credible basis standard required some affirmative evidence of mismanagement with respect to socially responsible activities. This is true despite the fact that "directors must, within the constraints of

84. Harrington, supra note 81, at 490.
86. Socially irresponsible business practices may impact shareholder return; for example, "a corporation which aids and abets human rights abuse exposes the company to" significant legal risks which may in turn impact dividend distributions. Eric Engle, Article, What You Don't Know Can Hurt You: Human Rights, Shareholder Activism and SEC Reporting Requirements, 57 SYRACUSE L. REV. 63, 79 (2006).
87. Rule 14a-8 of the Securities Exchange Act of 1934 allows shareholders to submit to the company proposals for mandatory inclusion in the proxy materials, subject to certain exclusions. 17 C.F.R. § 240.14a-8 (2015); see also Virginia J. Harnisch, Note, Rule 14a-8 After Reagan: Does It Protect Social Responsibility Shareholder Proposals?, 6 J.L. & POL. 415, 446 (1990) (noting that social responsibility proposals "sensitize management to important issues, subject management to checks, provide information, and offer a forum for shareholder communication. These social responsibility proposals also serve a broader purpose because they afford shareholders the opportunity to communicate with each other and management about how major corporations are behaving in a variety of areas which significantly impact the public and society at large.").
89. Harrington, supra note 81, at 483. In extractive industries, corporate social responsibility issues also include "companies' 'entanglement' with repressive governments in infrastructure development or security arrangements." Williams, supra note 88, at 722.
90. Williams, supra note 88, at 723.
92. Id.
the law, make the best interests of stockholders the end goal of the governance of a for-profit corporation.\textsuperscript{93} While some directors may seek “to pursue profits in a high-minded manner that respects the best interests of other corporate constituencies[,]\textsuperscript{94} they may feel a need “to compromise [their] sense of integrity because of a fear that stockholders will demand that [they] keep pace with . . . competitors who are less other-regarding.”\textsuperscript{95}

Likewise, federal law provided few mechanisms for disclosure of this type of information. Disclosure under the securities laws has traditionally focused on financial information deemed important to investors.\textsuperscript{96} Topics related to corporate social responsibility do not necessarily meet this criteria.\textsuperscript{97} As a result, companies did not need to make robust disclosure with respect to these issues.\textsuperscript{98} To the extent that they do so,\textsuperscript{99} disclosure is often voluntary and motivated by groups other than shareholders.\textsuperscript{100}

Nonetheless, pressure on Congress has resulted in some mandatory disclosure of socially responsible behavior even absent a strong nexus to

\begin{footnotesize}
\textsuperscript{93} Leo E. Strine, Jr., Essay, Can We Do Better By Ordinary Investors? A Pragmatic Reaction to the Dueling Ideological Mythologists of Corporate Law, 114 COLUM. L. REV. 449, 452 (2014).
\textsuperscript{94} Leo E. Strine, Jr., Article, Making it Easier for Directors to “Do the Right Thing?”, 4 HARV. BUS. L. REV. 235, 241 (2014).
\textsuperscript{95} Id.
\textsuperscript{97} Arguably, some social disclosure directly implicates shareholder interests. Id. at 237 (“First, the Conflict Minerals Rule represents real financial consequences for companies engaged in illicit trading practices. Second, socially responsible investing has shifted the traditional materiality definition into nonfinancial factors such as morality.”). In addition, investors are increasingly concerned with social information in making investment decisions such that this “information is clearly material to them, irrespective of its economic implications.” Cynthia A. Williams, The Securities and Exchange Commission and Corporate Social Transparency, 112 HARV. L. REV. 1197, 1288–89 (1999).
\textsuperscript{99} Companies committed to social responsibility may choose to adopt “codes of conduct that purport to regulate their suppliers’ labor practices with respect to” workers in developing countries. Claire Moore Dickerson, Human Rights: The Emerging Norm of Corporate Social Responsibility, 76 TUL. L. REV. 1431, 1437 (2002). In addition, companies can address operations in countries with no or insufficient labor laws by committing to pay “workers a decent wage.” Harrington, supra note 81, at 489.
\textsuperscript{100} Harrington, supra note 81, at 489–90 (“The pressures on multinational corporations, industries, and the international community to create and implement corporate social responsibility rules, especially in regard to labor practices, are many. These pressures typically center on social expectations of the multinational corporation; in turn, these social expectations are the result of pressures from consumers, human rights groups, domestic and international labor groups, and increasingly the media.”).
\end{footnotesize}
the financial interests of shareholders.\textsuperscript{101} Dodd-Frank required the SEC to promulgate rules mandating public companies to disclose their use of “conflict minerals” originating in the Democratic Republic of the Congo and adjoining countries.\textsuperscript{102} In addition, Dodd-Frank required the SEC to adopt rules governing the disclosure of payments made to the federal or foreign governments in connection with the commercial development of oil, natural gas, or minerals.\textsuperscript{103} The information was potentially important to investors who were “more interested in investing ethically than in maximising [sic] the profitability of their investments.”\textsuperscript{104}

Whatever the benefits, the approach imposes costs. Unlike inspection rights, which affect companies on a case-by-case basis, federal disclosure requirements are categorical and apply to all companies subject to the obligation, even where shareholders and the public have little interest in the information. Published reports indicate the total cost of compliance with the conflict minerals rule to be over $700 million.\textsuperscript{105} Moreover, the approach has engendered criticism from some at the SEC. One chair of the agency described efforts to mandate this type of disclosure as “more directed at exerting societal pressure on companies to change behavior, rather than to disclose financial information that primarily informs investment decisions.”\textsuperscript{106} Nonetheless, future intervention by Congress remains a strong possibility.\textsuperscript{107}

V. HERSHEY AND THE POSSIBLE SHIFT IN DELAWARE STANDARDS

The need for federal disclosure requirements may at least in part have been related to the apparent unavailability of state law inspection rights with respect to social responsibility. A recent decision in Delaware, however, suggests the possibility that the courts are becoming


\textsuperscript{103} 15 U.S.C. § 78m(q)(2)(A).


\textsuperscript{106} Mary Jo White, Chair, Securities and Exchange Comm’n, 14th Annual A.A. Sommer, Jr. Corporate Securities and Financial Law Lecture, Fordham Law School: The Importance of Independence (Oct. 2, 2013).

\textsuperscript{107} Dodd-Frank was “but one example of an emerging trend” of mandated disclosure relating to corporate social responsibility. Galit A. Sarfaty, Human Rights Meets Securities Regulation, 54 VA. J. INT’L L. 97, 100 (2013). Public outcry has led to Congressional intervention in other areas as well. In Citizens United v. Federal Election Commission, the Supreme Court held “that the Government may not suppress political speech on the basis of the speaker’s corporate identity” thereby approving of corporate personhood. 558 U.S. 310, 365 (2010). In the aftermath of Citizens United, the Shareholder Protection Act was introduced to Congress. H.R. 1734, 113th Cong. (2013). The Act would require shareholder approval before corporations may engage in political spending. \textit{id.}.
more amenable to the use of inspection rights to obtain information on these types of activities. The case arose in the context of a request by a shareholder of The Hershey Company seeking information about the use of child labor by cocoa producers in Africa.108

According to the court decision (based upon the allegations in the complaint), most of the world’s cocoa (approximately 70%) came from West Africa, particularly Ghana and the Ivory Coast.109 In 2001, the use of child labor in the production of cocoa received significant public attention.110 Press reports indicated “the prevalence of child labor, forced labor, and human trafficking on cocoa farms in West Africa.”111 As a result, Congress considered mandatory “‘slave-free’ labeling on cocoa products.”112

Apprehensive of such labeling, chocolate manufacturers opposed the proposal.113 As a compromise, the Harkin-Engel Protocol provided that major stakeholders in the chocolate industry would work to implement certification requirements to ensure that cocoa beans were grown and processed without the use of child labor by July 1, 2005.114 The Hershey Company supported this measure and signed the Protocol.115

The date came and went without implementation.116 In 2010, the United States Department of Labor, the governments of Ghana and the Ivory Coast, and the International Chocolate and Cocoa Industry adopted a new deadline and provided for a 70% reduction in the use of child labor by 2020.117

On October 4, 2012, Louisiana Municipal Employees’ Retirement System (LAMPERS) demanded inspection of the corporate books and records concerning Hershey’s awareness of possible human rights violations within its supply chain.118 In describing the purpose, the demand indicated an intent to investigate mismanagement, possible fiduciary duty violations, and “the independence and disinterestedness of the Board” in connection with “the undisputed and unfortunate endemic use of child labor on cocoa farms in West Africa.”119 The investigation

109. Id. at 5.
110. Id. at 3.
111. Id.
112. Id. at 3–4.
113. Id. at 4.
114. Id.
115. Id.
116. Id.
117. Id. at 4–5.
118. Id. at 1–2.
119. Id. at 2–3.
sought to examine the company’s failure “to limit its supply chain to
those suppliers Hershey can verify are not relying on child labor.”

The complaint relied on Hershey’s public statements, media reports,
journal articles and reports by the United States Department of Labor
“to make the undeniable point that child labor continues to be common
on cocoa farms in West Africa, with children forced to leave their fam-
ilies and forego schooling to work in horrific conditions.” LAMPERS
also referenced Hershey’s inability to certify, in accordance with Harkin-
Engel, that all of its suppliers were free from child labor and asserted
that the company all but admitted knowledge of the violations by an-
nouncing that 100% of its cocoa supplies would be certified as free from
human rights abuses by 2020. LAMPERS claimed that Hershey’s fail-
ure to adhere to the Protocol’s initial timeframe subjected the company
to negative publicity and market backlash.

Hershey denied the inspection request and LAMPERS filed an ac-
tion under Section 220. The Master assigned to the case found the al-
legations established at best that Hershey obtained raw materials from
countries known to use child labor. The complaint, according to the
Master, failed to “convert those established facts into some evidence of
possible mismanagement” sufficient to constitute a credible basis for the
purpose alleged. Accordingly, the Master recommended the complaint
be dismissed.

120. Id. at 7.
121. Verified Complaint Pursuant to 8 Del. Ch. § 220 to Compel Inspection of Books and
2013).
122. Masters Report, supra note 108, at 5; see also Verified Complaint Pursuant to 8 Del. Ch. § 220 to Compel Inspection of Books and Records, supra note 121, at 19–24.
124. Id. at 6–7.
125. Id. at 7. In fact, Whole Foods discontinued a particular Hershey’s brand because of its
possible production through child labor. Id. Furthermore, Hershey’s 2011 Corporate Social Respon-
sibility Progress Report acknowledged that child labor was endemic in West Africa and identified
Ghana and the Ivory Coast as Hershey’s “major sourcing countries.” Id. at 5–6. Hershey “has taken
steps to attempt to address” ethical sourcing and child labor within the supply chain, including
a requirement that suppliers sign and adhere to a code of conduct. Id. at 6. Arguably, Hershey’s at-
tempt to address human rights violations within the supply chain is subject to the business judgment
standard, which merely requires the board to act in the best interests of the corporation. See Barnali
Choudhury, Serving Two Masters: Incorporating Social Responsibility into the Corporate Para-
corporate managers can consider non-shareholder interests . . . so long as the decision furthers the
best interests of the corporation.”); see also Seinfeld v. Verizon Commc’ns, Inc., 909 A.2d 117, 120
(Del. 2006) (en banc) (Plaintiff’s “disagreement” with Verizon’s business judgment in determining
the amount of compensation for corporate officers was not sufficient evidence of wrongdoing).
127. Id. at 14–15.
128. Id. at 7–8.
129. Id. at 28.
The Plaintiff took exception and sought review by the Chancery Court. The Vice Chancellor rejected the Master’s recommendation that the action be dismissed. In doing so, he found that the complaint sufficiently alleged both a proper purpose and a credible basis. The stockholder only had to show “a possibility” of mismanagement, not prove that such behavior had actually occurred. As a result, in the presence of “two competing inferences . . . the plaintiff gets the inference.”

The complaint supported inferences “of possible violations of law in which Hershey may be involved.” The factual allegations made it reasonable to conclude “Hershey’s products contain cocoa and cocoa-derived ingredients that were the result of child labor and human trafficking” and “that the board knows some of its . . . ingredients are sourced from farms” engaging in labor exploitation.

Moreover, Hershey’s failure to implement certification requirements by July 1, 2005, combined with the company’s subsequent announcement of its intention to do so by 2020 supported the inference that at least some of the company’s cocoa was the product of child labor. As the Vice Chancellor reasoned:

If I call up, you know, my daughter's school and I say, "Can you confirm for me that there’s no one on the payroll with a criminal record?" and they say to me, "We're not going to do that now, but we hope to be able to do so in 2020." I'm going to draw the inference that they can't do it right now and there's probably someone at the school with a criminal record.

The inference was further supported by Hershey’s “market-leading status and dominant market share.” Accordingly, the court denied Hershey’s motion to dismiss, allowing the complaint to move forward from the pleadings stage to a merits hearing. The case, however, was voluntarily dismissed by the parties before such a hearing was held.

VI. HERSHEY AND THE IMPLICATIONS UNDER SECTION 220

In some respects, Hershey broke no new ground. The court applied the traditional analysis. LAMPERS had to sufficiently allege misman-

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130. Rulings of the Court From Oral Argument on Exceptions to the Master’s Final Report, supra note 12, at 3.
131. Id. at 22.
132. Id. at 13.
133. Id. at 17.
134. Id. at 18.
135. Id. at 19.
136. Id. at 8.
137. Id.
138. Id. at 9-10. The court requested that the parties schedule a hearing within 60 days. Id.
139. Id. at 22.
agement in order to meet the proper purpose requirement. In addition, the allegations of wrongdoing had to be supported by a credible basis.

Nonetheless, the decision in practice went beyond the traditional approach taken by Delaware courts under Section 220 and has the potential to significantly improve the accessibility of information concerning a corporation’s socially responsible (or irresponsible) behavior. First, the court accepted claims of mismanagement that Hershey “support[ed] the use of unlawful child labor” and “integrat[ed] this illegal conduct into its business model” largely from the widespread knowledge of the problems of child labor in the cocoa production process.\footnote{Verified Complaint Pursuant to 8 Del. Ch. § 220 to Compel Inspection of Books and Records, supra note 121, at 1.}

Similarly, the court relied on a flexible approach towards the credible basis standard. LAMPERS essentially used the common knowledge of child labor violations in the cocoa industry coupled with the company’s commitment to reduce the instances of these actions to create an inference that the board was aware of the problem. Absent were any specific allegations of actual knowledge of violations by suppliers or allegations that the specific suppliers used by Hershey relied on child labor.

This analysis could be repeated with respect to other human rights abuses or matters of social responsibility that are likely to affect the supply chain. Widespread concern exists over worker safety in the garment industry.\footnote{Julifkar Ali Manik & Jim Yardley, Building Collapse in Bangladesh Leaves Scores Dead, N.Y. TIMES, (Apr. 24, 2013), http://www.nytimes.com/2013/04/25/world/asia/bangladesh-building-collapse.html?pagewanted=all&_r=2&.} Bangladesh, second only to China in textile production, manufactures goods for a significant number of large retailers.\footnote{Id.} In 2013, a fire killed 112 factory workers in the country.\footnote{Id.} Government officials and multinational corporations pledged to take steps “to ensure the safety of factories where goods they sell are manufactured.”\footnote{Id.} Despite the pledges, problems remain. More than 100 factory workers died in a building collapse shortly after the fire.\footnote{Id.}

Similarly, concerns have arisen in Indonesia and Malaysia with deforestation that results from the production of palm oil. Most of the world’s supply of palm oil is produced in the two countries.\footnote{ConAgra Palm Oil 2014, CERES, http://www.ceres.org/investor-network/resolutions/conagra-palm-oil-2014 (last visited Apr. 18, 2015).} The palm oil production process results in deforestation because the resource thrives in “consistently high humidity and temperatures.”\footnote{Id.} Accordingly, palm oil “plantations are often established at the expense of rainfor-
As a result of deforestation in Indonesia, the country is now the “3rd largest emitter of greenhouse gases globally.” Some companies that make significant use of palm oil have pledged by a specific date to ensure that production is through sustainable sources.

Whether the use of palm oil or conditions in textile producing countries, environmental or labor concerns are widely known, some companies have made pledges to address these abuses in the supply chain. The widespread nature of the problem coupled with the future commitment to address the concerns arguably provides both a proper purpose and credible basis that would justify the inspection of documents related to these matters. Moreover, as Hershey indicated, violations not directly attributable to the company but that occurred in supply chain would not be a complete defense. To the extent corporations rely on a supply chain that is directly tied to human rights violations, the “possibility” of corporate involvement exists.

VII. CONCLUSION

Section 220 of Delaware Corporate Law provides a way for shareholders to obtain non-public information about companies where they invest. The statute requires only that the request be “reasonably related to such person’s interest as a stockholder.” The courts, however, have added a number of interpretive glosses that make inspection rights difficult. They largely assume that a shareholder’s interest is limited to mismanagement. Moreover, the courts have added the requirement that the allegations of management must be supported by a credible basis.

Hershey, however, signals a more flexible approach, at least with respect to the inspection of materials related to corporate social responsibility. In these circumstances, shareholders may be able to meet the credible basis threshold by showing, through media reports or otherwise, widespread public awareness of legal violations in the production process and attribute the knowledge to the board.

Congressional intervention in this area has been characterized “as a consequence of state law.” To the extent that inspection rights are more accessible for such information, however, Congress and the SEC may have less incentive to impose affirmative obligations requiring disclosure of the same type of information. The result will be disclosure not

149. Id.
150. ConAgra Palm Oil 2014, supra note 147.
151. Id.
152. DEL. CODE ANN. tit. 8, § 220 (b) (2010).
in a categorical fashion but on a case-by-case basis depending upon the needs and interests of shareholders.

Of course, the case is only one decision and reflects the views of only one Vice Chancellor, albeit a jurist stating that he was simply relying on existing precedent in Delaware.\(^\text{154}\) Moreover, because the parties agreed to dismiss the case, the applicable issues were not reviewed by the Delaware Supreme Court.\(^\text{155}\) Nonetheless, the case did not alter the legal framework but instead adopted a flexible approach to existing legal standards. That subsequent decisions may do the same remains, therefore, a distinct possibility.

\(^{154}\) Rulings of the Court From Oral Argument on Exceptions to the Master’s Final Report, supra note 12, at 22 (“What I think I have to do is follow Seinfeld. Seinfeld is the Delaware Supreme Court. That’s why I have to follow him.”).

\(^{155}\) See Stipulation of Dismissal, supra note 140, at 1.