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Case No. 7996-ML

IN THE COURT OF CHANCERY OF THE STATE OF DELAWARE

LOUISIANA MUNICIPAL POLICE EMPLOYEES' RETIREMENT SYSTEM,	)	
Plaintiff,	)	
v.	)	C.A. No. 7996-ML
THE HERSHEY COMPANY,	)	
Defendant.	)	

MASTER'S REPORT
(Motion to Dismiss)

Date Submitted: May 21, 2013
Draft Report: August 16, 2013
Final Report:

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LEGROW, Master

A large portion of the world's cocoa originates in two countries in which illegal child labor often is used on farms, including cocoa farms. The plaintiff, a stockholder of the Hershey Company ("Hershey"), is aware that much of Hershey's cocoa is sourced in these two countries, and the stockholder believes that Hershey may purchase some of that raw material directly from growers, and therefore may be complicit in the illegal activity or have knowledge that the company's products are tainted by the illegal conduct of the grower. The stockholder, armed with little more than the undisputed facts that (i) Hershey is a major player in the chocolate industry that uses cocoa beans and products derived from cocoa beans, (ii) child labor is endemic in two countries that produce a large portion of the cocoa beans, and (iii) some of Hershey's cocoa beans and cocoa-derived products originate in those countries, demanded to inspect an expansive list of books and records. The company refused to allow the inspection, and moved to dismiss the Section 220 complaint filed by the stockholder.

The question this case presents is whether illegal conduct within one sector of an industry provides a credible basis from which this Court may infer that wrongdoing or mismanagement may have occurred at a company in that industry. This is not a novel question, having been addressed, for example, in two other cases involving the stockholder who filed this action. In this case, because the stockholder failed to sustain its minimal burden of providing credible evidence from which the Court may infer mismanagement or wrongdoing at Hershey, rather than within the cocoa supply chain, I recommend that the Court dismiss the complaint.

BACKGROUND[1]

The plaintiff, Louisiana Municipal Police Employees' Retirement System ("LAMPERS" or the "Plaintiff"), is a nonprofit organization that provides pension benefits for employees of municipal police departments in Louisiana.[2] The defendant, Hershey, is a Delaware corporation with its principal place of business in Hershey, PA. The Hershey brand is well-known to anyone who experiences even an occasional craving for chocolate, having developed several distinctive consumer products, and having forever cemented the storied connection between chocolate and love with its iconic "Kiss." Shares of Hershey are traded on the New York Stock Exchange, its products are sold in more than 70 countries, and it occupies approximately 42% of the market share for chocolate sold in the United States, making it the largest producer of chocolate in North America.[3] According to the complaint, LAMPERS has continuously owned Hersey stock "at all relevant times."[4]

On October 4, 2012, LAMPERS sent Hershey a letter demanding inspection of Hershey's books and records under 8 *Del. C.* § 220 (the "Demand Letter").[5] The Demand Letter identified six categories of documents that LAMPERS sought to inspect. Some of the categories included several subparts. According to the Demand Letter, the purpose of the demand was to investigate:

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[1] The following facts (as distinguished from a handful of obvious digressions about chocolate) are drawn from the complaint and the documents it incorporates by reference, giving the plaintiff the benefit of all reasonable inferences.
[2] Verified Complaint pursuant to 8 *Del. C.* § 220 to Compel Inspection of Books and Records (hereinafter "Compl.") ¶ 9.
[3] *Id*. ¶ 10.
[4] *Id*. ¶ 9.
[5] *Id*. Ex. A.

(a) mismanagement by the directors and/or officers of Hershey in connection with the matters discussed in the grounds [identified in the Demand Letter];

(b) the possibility of breaches of fiduciary duty by directors and/or officers of Hershey in connection with the matters discussed in the grounds [identified in the Demand Letter]; and

(c) the independence and disinterestedness of the Board, and to determine whether a pre-suit demand is necessary or would be excused prior to commencing any derivative action on behalf of the Company.[6]

The Demand Letter offers a relatively detailed description of the grounds LAMPERS believes support its stated purposes for inspection. All of the stated grounds relate to the undisputed and unfortunate endemic use of child labor on cocoa farms in West Africa. The complaint that LAMPERS filed after Hershey refused to permit inspection (the "Complaint") provides additional background and allegations that LAMPERS argues undergird the validity of the books and records demand.

The facts that LAMPERS contends form a credible basis from which this Court can infer possible mismanagement largely are not disputed. It is a sad and unavoidable fact that, although most Americans likely can catalogue happy childhood memories – whether those of campfires or holidays – that involve chocolate in some form or another, much of the world's cocoa is grown using illegal child labor. This "dark" side of chocolate – and not the semi-sweet variety – became the focus of public attention in 2001.[7] In the wake of press reports on the prevalence of child labor, forced labor, and human trafficking on cocoa farms in West Africa, Congress began considering proposed

[6] *Id*. Ex. A, p. 3.
[7] *Id*. ¶ 15.

legislation that would have required "slave-free" labeling on cocoa products.[8] Concerned about the implications of that labeling, chocolate manufacturers lobbied against the legislation.[9] A compromise ultimately was reached when the Chocolate Manufacturers Association signed the Harkin-Engel Protocol (the "Protocol") on September 19, 2001.[10] The Protocol stated that it was the goal of the chocolate industry, in partnership with other major stakeholders, to "develop and implement [by July 1, 2005] … industry-wide standards of public certification … that cocoa beans and their derivative products have been grown and/or processed without any of the worst forms of child labor."[11] Hershey signed the Protocol to indicate its support for the measure.[12]

The signatories to the Protocol were not successful in achieving their stated goals by 2005. In 2005 and 2008, Senator Harkin and Representative Engel issued joint statements regarding the progress that had been achieved toward completing the goals identified in the Protocol. In 2010, representatives of the United States Department of Labor, the Government of the Republic of Côte d'Ivoire (the "Ivory Coast"), the Government of the Republic of Ghana, and the International Chocolate and Cocoa Industry signed a "Declaration of Joint Action to Support Implementation of the Harkin-

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[8] *Id.*
[9] *Id.* ¶ 16.
[10] *Id.*; Def.'s Br. in Supp. of Mot. to Dismiss (hereinafter "Opening Br.") Ex. A. The Protocol, along with several other documents referenced herein, were extensively cited and quoted in LAMPERS's complaint, and therefore may be considered in the context of Hershey's motion to dismiss. *See In re Gen. Motors (Hughes) S'holder Litig.*, 897 A.2d 162, 169 (Del. 2006) (when a complaint selectively quotes or characterizes a document, the defendant may offer the complete document to the Court on a motion to dismiss); *Solomon v. Armstrong*, 747 A.2d 1098, 1122 n. 72 (Del. Ch. 1999) (in considering a motion to dismiss, the Court may take judicial notice of documents incorporated by reference into the complaint).
[11] Opening Br. Ex. A., p. 3.
[12] Opening Br. Ex. A.

Engel Protocol" (the "2010 Declaration").[13] The 2010 Declaration and the accompanying Framework of Action to support implementation of the Protocol (the "Framework")[14] provided that the participants' goal was that "[b]y 2020, the worst forms of child labor as defined in ILO Convention 182 in the cocoa sectors of Côte d'Ivoire and Ghana will be reduced by 70 percent in aggregate through joint efforts by key stakeholders…."[15]

Despite these commitments from industry members and governments, child labor and human trafficking continue to be a pervasive problem in cocoa farming. Approximately 70 percent of the world's supply of cocoa beans, and the largest percentage of Hershey's supply, comes from West African nations, including Ghana and the Ivory Coast.[16] LAMPERS's Complaint relies on a number of recent news reports to make the undeniable point that child labor continues to be common on cocoa farms in West Africa, with children forced to leave their families and forego schooling to work in horrific conditions.[17]

The documents incorporated by reference in the Complaint, including Hershey's 2011 Corporate Social Responsibility Progress Report (the "CSR Report"),[18] confirm that Hershey cannot certify that all of the 10,000 suppliers from which it sources raw materials produce cocoa without relying on the "worst forms of child labor." Hershey acknowledges that "West Africa is a region of continuing focus for [the] company …

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[13] *Id*. Ex. B.
[14] *Id*. Ex. C.
[15] *Id*. Ex. C., p. 1.
[16] Compl. ¶ 15, Opening Br. Ex. D, p. 20.
[17] Compl. ¶¶ 19-24.
[18] Opening Br. Ex. D.

[because] it is where [Hershey] source[s] the majority of Hershey cocoa ….”[19] The CSR Report identifies Ghana and the Ivory Coast as among Hershey's "major sourcing countries," and acknowledges that ethical sourcing and child labor are among the priorities identified by Hershey's stakeholders.[20] The CSR Report also confirms that Hershey has taken steps to attempt to address those priorities. Those steps include developing and later revising a supplier code of conduct, by which Hershey requires its suppliers to abide.[21] Hershey also undertook an internal risk assessment and supplier audit, in an effort to give preference to suppliers who adequately address human rights concerns and to identify and develop remediation plans for high risk suppliers. To that end, Hershey engages "qualified third part[y]" organizations that assist companies in addressing supply chain performance.[22]

Hershey has acknowledged that child labor is a deep-seated problem in the cocoa industry, and that eliminating the worst forms of child labor is a complex task that involves cultural and economic issues and requires the involvement of both governments and industry leaders.[23] Hershey recently has pledged $10 million over 5 years toward programs that are designed to, among other things, promote ethical labor practices.[24] On October 3, 2012, Hershey announced that by 2020 it will source 100 percent certified

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[19] *Id*. Ex. D, p. 2.
[20] *Id*. Ex. D., p. 8, 11.
[21] *Id*. Ex. D. p. 19; Compl. ¶ 52.
[22] Opening Br. Ex. D, p. 19.
[23] *Id*. Ex. D, p. 20.
[24] *Id*. Ex. D, p. 20.

cocoa for its global chocolate product lines.[25] LAMPERS points to this recent announcement as evidence that Hershey is aware of child labor within its supply chain, but will not take action to end its reliance on ill-gotten cocoa until 2020.[26]

In the Complaint, LAMPERS takes Hershey to task for failing to limit its supply chain to those suppliers Hershey can verify are not relying on child labor. LAMPERS points out that other chocolate manufacturers have adopted such certification requirements,[27] and that Hershey's failure to do so according to the timeline established in the Protocol is subjecting the company to negative publicity and causing retailers to raise concerns. Among other things, LAMPERS points out that one national retailer, Whole Foods, announced it would no longer carry one of Hershey's brands, Scharffen Berger, in its stores due to "Hershey's failure to assure that cocoa is sourced without the use of forced child labor."[28] LAMPERS further alleges that a consortium of retailers sent Hershey's board of directors (the "Hershey Board" or the "Board") a letter voicing concerns over Hershey's failure to remedy child labor problems in the supply chain.[29]

LAMPERS argues that its allegations provide a credible basis from which this Court can infer that the Hershey Board breached its fiduciary duties by actively participating or being complicit in violations of the laws of Ghana, the Ivory Coast, the United States, and California.[30] What LAMPERS's Complaint succeeds in establishing

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[25] Compl. ¶ 35; Compl. Ex. B, p. 3.
[26] Compl. ¶¶ 30, 37, 47, 50.
[27] *Id.* ¶ 36.
[28] *Id.* ¶ 35.
[29] *Id.* ¶ 34.
[30] *Id.* ¶¶ 38-52; Pl.'s Br. in Opp'n to Def.'s Mot. to Dismiss (hereinafter "Opp'n Br.") p. 25.

is that (1) Hershey is a major chocolate manufacturer, and (2) the chocolate industry faces the problem of obtaining raw materials for its products while being aware that certain countries that are major sources of cocoa beans have wide-spread incidence of child labor. Where LAMPERS's Complaint falls short is in its effort to convert those established facts into some evidence of possible mismanagement.

In support of its argument that there is a reasonable basis to believe that Hershey and its Board, "through the purchase and use of cocoa and cocoa-related products originating in Ghana and the Ivory Coast, is actively enabling violations of the law in both Ghana and the Ivory Coast," LAMPERS refers to laws in Ghana and the Ivory Coast that prohibit the use of child labor and human trafficking.[31] The Complaint cites Ghana's "Children's Act," which prohibits the use of exploitive child labor by precluding children under 13 from working altogether and by prohibiting children between 13 and 18 from being employed in "work that poses a danger to the health, safety, or morals of a person."[32] Ghana's Human Trafficking Act seeks to punish those complicit in human trafficking, providing that "[a] person who uses a trafficked person commits an offense and is liable on summary conviction to a term of imprisonment of not less than five years."[33] That law also creates a duty to inform police when a person has knowledge of trafficking:

> (1) A person with information about trafficking
> (a) Shall inform the police, or
> (b) May inform

[31] Compl. ¶¶ 41-47.
[32] *Id.* ¶ 41.
[33] *Id.* ¶ 43.

> (i) the Commission of Human Rights and Administrative Justice,
> (ii) the Department of Social Welfare,
> (iii) the Legal Aid Board, or
> (iv) a reputable Civil Society Organization.
>
> (2) A person who fails to inform the police commits an offense and is liable on summary conviction to a fine of not less than two hundred and fifty penalty units or a term of imprisonment of not less than twelve months or to both.[34]

The Ivory Coast similarly prohibits certain forms of labor for children under the age of 18, including (1) cutting of trees, (2) burning of fields, (3) application of chemicals, (4) application of chemical fertilizer, (5) chemical treatment of fields or plants, and (6) carrying of heavy loads.[35] These activities are among the activities defined as the Worst Forms of Child Labor by the International Labor Organization Convention 138 and 182.[36] The Ivory Coast's Projet de Loi also prohibits trafficking of children and forbids apprenticeships before the age of 14.[37]

In addition to these laws, the Complaint – though not the Demand Letter – also recites certain federal and state laws that LAMPERS contends Hershey may be violating.[38] The Trafficking Victims Protection Reauthorization Act of 2008 (the "VPRA") relevantly provides for criminal charges against:

> (a) Whoever knowingly provides or obtains the labor services of a person by any one of, or by any combination of, the following means:
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> (1) by means of force, threats of force, physical restraint, or threats of physical restraint to that person or another person;

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[34] *Id.* ¶¶ 43-44.
[35] *Id.* ¶ 45.
[36] *See* Opening Br. Ex. D, p. 20.
[37] Compl. ¶ 45.
[38] *Id.* ¶ 49.

> (2) by means of serious harm or threats of serious harm to that person or another person;
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> (3) by means of the abuse or threatened abuse of law or legal process; or
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> (4) by means of any scheme, plan or pattern intended to cause the person to believe that, if that person did not perform such labor or services, that person or another person would suffer serious harm or physical restraint.
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> (b) Whoever knowingly benefits, financially or by receiving anything of value, from participation in a venture which has engaged in the providing or obtaining of labor or services by any of the means described in subsection (a), knowingly or in reckless disregard of the fact that the venture has engaged in the providing or obtaining of labor or services by any such means.[39]

The VPRA defines "venture" as "any group of two or more individuals associated in fact."[40] The Complaint also refers to the California Transparency Supply Chain Act of 2010 (the "CTSCA"), which requires manufacturers with more than $100 million in annual gross receipts to disclose their efforts to:

> (1) Engage in verification of product supply chains to evaluate and address risks of human trafficking and slavery. The disclosure shall specify if the verification was not conducted by a third party.
>
> (2) Conduct audits of suppliers to evaluate supplier compliance with company standards for trafficking and slavery in supply chains. The disclosure shall specify if the verification was not an independent, unannounced audit.
>
> (3) Require direct suppliers to certify that materials incorporated into the product comply with the laws regarding slavery and human trafficking of the country or countries in which they are doing business.

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[39] *Id.* ¶ 49; 18 U.S.C. § 1589.
[40] 18 U.S.C. § 1591.

(4) Maintain internal accountability standards and procedures for employees or contractors failing to meet company standards regarding slavery and trafficking.

(5) Provide company employees and management who have direct responsibility for supply chain management, training on human trafficking and slavery, particularly with respect to mitigating risks within the supply chains of products.[41]

Hershey responded to the Demand Letter on October 12, 2012 (the "Response Letter"). Hershey's Response Letter raised several arguments that Hershey contended supported its decision not to permit LAMPERS to inspect the requested books and records. Among other things, Hershey argued that LAMPERS (i) failed to provide sufficient evidence of beneficial ownership, (ii) failed to state a proper purpose, (iii) sought books and records for an "extraordinarily long and unwarranted timeframe," and (iv) demanded categories of books and records with an "impermissibly broad" scope.[42] LAMPERS filed its Complaint on November 2, 2012, and Hershey promptly moved to dismiss (the "Motion"). The parties briefed that motion and argument was held on May 21, 2013. In its Motion, Hershey argued that this Court should dismiss the Complaint because it fails to allege a credible basis from which the Court can infer any wrongdoing or mismanagement. Hershey also contends that LAMPERS fails to state a proper purpose to inspect books and records created before 2010, and that the scope of the records sought extends far beyond what is permitted under Section 220. LAMPERS, on the other hand, asserts that the undisputed facts alleged in the Complaint, and the reasonable inferences to be drawn there from, more than sustain its burden under the

[41] Compl. ¶ 51; Cal. Civ. Code § 1714.43.
[42] Compl. Ex. B.

"credible basis" standard. LAMPERS also disputes the argument that the scope of the demand, in either timeframe or category, is overly broad, and contends that those issues do not form a basis to dismiss the Complaint.

ANALYSIS

Pursuant to Rule 12(b)(6), this Court may grant a motion to dismiss for failure to state a claim if a complaint does not assert sufficient facts that, if proven, would entitle the plaintiff to relief. The governing pleading standard in Delaware to survive a motion to dismiss is "reasonable 'conceivability.'"[43] That is, when considering such a motion, a court must

> accept all well-pleaded factual allegations in the Complaint as true, accept even vague allegations in the Complaint as "well-pleaded" if they provide the defendant notice of the claim, draw all reasonable inferences in favor of the plaintiff, and deny the motion unless the plaintiff could not recover under any reasonably conceivable set of circumstances susceptible of proof.[44]

This "conceivability" standard asks whether there is a "possibility" of recovery.[45] If the well-pleaded factual allegations of the complaint would entitle the plaintiff to relief under a reasonably conceivable set of circumstances, the Court must deny the motion to dismiss.[46] The Court, however, need not "accept conclusory allegations unsupported by

[43] *Central Mortg. Co. v. Morgan Stanley Mortg. Capital Hldgs. LLC*, 27 A.3d 531, 537 (Del. 2011) (footnote omitted).
[44] *Id.* (citing *Savor, Inc. v. FMR Corp.*, 812 A.2d 894, 896-97 (Del. 2002)).
[45] *Id.* at 537 & n.13.
[46] *Id.* at 536.

specific facts or … draw unreasonable inferences in favor of the non-moving party."[47] A claim may be dismissed if the allegations in the complaint or the documents incorporated by reference therein "effectively negate the claim as a matter of law."[48]

I. LAMPERS HAS NOT ALLEGED A CREDIBLE BASIS FROM WHICH THE COURT CAN INFER POSSIBLE WRONGDOING OR MISMANAGEMENT

Section 220 of the Delaware General Corporation Law allows a stockholder to inspect books and records of a corporation, provided that the stockholder's inspection demand meets the form and manner requirements contained in the statute, and the inspection is demanded for a proper purpose.[49] A proper purpose is one "reasonably related to such person's interest as a stockholder."[50] It is settled Delaware law that investigation of corporate waste, mismanagement, or wrongdoing is a proper purpose to demand inspection.[51] Mere suspicion, however, or a subjective belief of wrongdoing, without more, is not sufficient to state a proper purpose.[52] Instead, a stockholder whose stated purpose is investigation of mismanagement must provide "some evidence" to

[47] *Price v. E.I. duPont de Nemours & Co.*, *Inc.*, 26 A.3d 162, 166 (Del. 2011) (citing *Clinton v. Enterprise Rent-A-Car Co.*, 977 A.2d 892, 895 (Del. 2009)).
[48] *In re Gen. Motors (Hughes) S'holder Litig.*, 897 A. 2d 162, 169-70 (Del. 2006).
[49] 8 *Del. C.* § 220(c); *Louisiana Mun. Police Emps. Ret. Sys. v. Countrywide Fin. Corp.*, 2007 WL 2896540, at *9 (Del. Ch. Oct. 2, 2007); *Highland Select Equity Fund, L.P. v. Motient Corp.*, 906 A.2d 156, 164 (Del. Ch. 2006).
[50] 8 *Del. C.* § 220(b).
[51] *Security First Corp. v. U.S. Die Casting & Dev. Co.*, 687 A.2d 563, 567 (Del. 1997); *Dobler v. Montgomery Cellular Holding Co.*, 2001 WL 1334182, at *3 (Del. Ch. Oct. 19, 2001).
[52] *City of Westland Police & Fire Ret. Sys. v. Axcelis Techs., Inc.,* 1 A.3d 281, 287 (Del. 2010); *Marathon Partners, L.P. v. M&F Worldwide Corp.*, 2004 WL 1728604, at *5 (July 30, 2004).

suggest a "credible basis" from which this Court may infer possible mismanagement, waste, or wrongdoing may have occurred.[53]

This credible basis standard has been described as the "lowest possible burden of proof" under Delaware law.[54] The standard falls far short of requiring a stockholder to prove by a preponderance of the evidence that mismanagement or wrongdoing actually has occurred.[55] The burden, however, is not insubstantial, and although members of both the Delaware Supreme Court and this Court have encouraged stockholders to use the "tools at hand" by making books and records demands before instituting derivative litigation, that recommendation does not alter the requirement that a stockholder present some evidence from which the Court may infer possible mismanagement or wrongdoing.[56] The credible basis standard is designed to strike a balance between granting stockholders access to corporate records and protecting corporations and their stockholders from wasteful fishing expeditions based on mere curiosity.[57]

A. LAMPERS Has Not Alleged a Credible Basis to Infer Violations of Foreign or Domestic Law

LAMPERS's stated purpose in seeking inspection is to investigate mismanagement or wrongdoing by Hershey's corporate officers or directors in connection with purported violations of law by Hershey.[58] LAMPERS contends that it

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[53] *Seinfeld v. Verizon Commc'ns, Inc.*, 909 A.2d 117, 118 (Del. 2006).
[54] *Countrywide Fin. Corp.*, 2007 WL 2896540, at *10.
[55] *Axcelis Techs., Inc.*, 1 A.3d at 287; *Countrywide Fin. Corp.*, 2007 WL 2896540, at *10.
[56] *Marathon Partners, L.P.*, 2004 WL 1728604, at *4.
[57] *Seinfeld*, 909 A.2d at 118.
[58] LAMPERS's third stated purpose, to investigate the independence and disinterestedness of Hershey's directors to determine if demand would be excused as futile, only would be proper if LAMPERS had established a credible basis to investigate mismanagement or wrongdoing that

has carried its burden of establishing a credible basis from which this Court can infer that Hershey has violated federal, state, or international law, and that it likewise has shown a credible basis from which this Court can infer that Hershey's directors or officers permitted or facilitated that wrongdoing.[59] Essentially, LAMPERS argues that a number of undisputed facts provide the necessary quantum of evidence from which this Court can conclude that Hershey may be acting illegally.

Specifically, LAMPERS contends that it is beyond dispute that illegal child labor is a pervasive, long-standing problem on cocoa farms in the Ivory Coast and Ghana, that those countries are "major sourcing countries" for Hershey, that Hershey has 42 percent of the market share of chocolate in the United States, that Hershey signed the Protocol in 2001 but has not certified that its products are not tainted by child labor, and that Hershey has faced public pressure and reputational risk from its failure to source its cocoa from supplies certified as free from the taint of child labor. In making that argument, LAMPERS primarily relies on the Protocol, several news reports regarding child labor in the chocolate industry, and the CSR Report.

Notably, none of those sources – or any other source identified in the Complaint – states that Hershey has violated the law or is under investigation for possible legal violations, nor do they identify any illegal conduct within the company. In *Louisiana Municipal Police Employees' Retirement Sys. v. Lennar Corp.*, this Court recently held

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ultimately could form the basis of a derivative suit. The parties do not address this purpose in their briefs, presumably because it rises or falls on the viability of LAMPERS's other purposes. Having concluded that LAMPERS does not state a credible basis from which the Court can infer mismanagement, this third purpose is moot.

[59] *See* Compl. Ex. A, p. 8; Compl. ¶¶ 67-68; Opp'n Br. p. 12-15.

that negative news articles alone, even when those articles indicate that the Company at issue is under investigation for legal violations, are insufficient to establish a stockholder's burden under the credible basis standard.[60] In this case, the articles and other sources on which LAMPERS relies are even more attenuated. Although those sources detail at length very serious legal violations on many farms in the Ivory Coast and Ghana, none of the articles directly implicate Hershey in that conduct. LAMPERS nevertheless suggests that the conclusion of Hershey's complicity may be drawn from its market share and its failure to source exclusively from certified cocoa. That is, given the prevalence of child labor in countries from which Hershey sources cocoa, Hershey's large market share, and its inability to certify the absence of child labor within the supply line, LAMPERS argues that there is a credible basis from which this Court can determine that (1) Hershey's supply line is partially dependent on cocoa produced using illegal child labor, and (2) Hershey therefore is in violation of a number of laws.

As a preliminary matter, I am doubtful that I can rely upon this statistical "analysis" as evidence to support the credible basis standard LAMPERS must meet. In *Louisiana Municipal Police Employees' Retirement Sys. v. Countrywide Financial Corp.*, this Court held a "statistical correlation, ***if adequately supported by a sound, logical methodology and competent expert testimony***," may constitute "'some evidence' of possible corporate wrongdoing."[61] Even when a statistical correlation meets that standard, however, it forms the "outer limits" of the "minimal quantum of evidence" a

[60] 2012 WL 4760881, at *4 (Del. Ch. Oct. 5, 2012).
[61] *Countrywide Fin. Corp.*, 2007 WL 2896540, at *1 (emphasis added).

shareholder must provide to satisfy the credible basis standard.[62] The statistical analysis relied upon in *Countrywide Financial Corp.* was an economist's analysis and review of certain stock option grants for the company at issue, from which the economist concluded, based on what the Court described as a "tried and true" statistical methodology, that there was a statistically significant chance that some form of option manipulation occurred at the company. That statistical correlation is vastly different from what LAMPERS offers in this case, which is little more than the logical fallacy that, because some cocoa is produced using child labor, and Hershey purchases a large amount of cocoa or cocoa-derived products, Hershey must use cocoa products tainted by child labor.

Even if I could rely on this statistical or logical correlation, however, which arguably I must do on a motion to dismiss, LAMPERS has not alleged a credible basis from which I can infer wrongdoing. At most, LAMPERS has succeeded in alleging that Hershey purchases cocoa, directly or indirectly, from farms that utilize child labor.[63]

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[62] *Id.*

[63] Hershey vigorously denies that it purchases any cocoa directly from the Ivory Coast or Ghana. Although the CSR Report identifies those countries as "major sourcing countries," *see* Opening Br. Ex. D, p. 8, Hershey stated in its Response Letter and in its briefing that Hershey does not "directly" purchase any cocoa beans from West African farms, because most of Hershey's products are processed from cocoa-derived products purchased by Hershey from large, multinational corporations, and that the small amount of cocoa beans purchased from West Africa are purchased from third-party suppliers who must adhere to Hershey's supplier code of conduct. *See* Compl. Ex. B, p. 3. On a motion to dismiss, however, I cannot rely on those factual statements by Hershey, which cannot independently be verified by any document incorporated by reference in the Complaint. Because Hershey does not publicly disclose its suppliers, Hershey cannot defeat the inspection demand by relying on its own representation that it does not directly purchase cocoa beans from the countries at issue. Any other conclusion would turn Section 220 on its head and result in companies litigating, in books and records cases,

Neither that "evidence," nor the other sources on which LAMPERS relies, provide any basis from which the Court could conclude that Hershey has violated the law.

LAMPERS first contends that its sources, and the logical conclusions to be drawn therefrom, provide a credible basis from which I can conclude that Hershey may have violated laws in Ghana and the Ivory Coast. LAMPERS does not allege that Hershey actually operates any farm or other business in those countries, or even that it employs any person within those countries. Accordingly, there is no credible basis from which I can conclude that Hershey may be violating the laws in Ghana or the Ivory Coast that prohibit employing children below a certain age or requiring children to perform certain dangerous or physically-demanding tasks.[64] Nor does the Complaint allege any credible basis to believe that Hershey has violated Ghana's Human Trafficking Act, which creates a "duty to inform" police if any person has knowledge of another person's exploitation of a trafficked person. Other than alleging Hershey's generalized knowledge about the prevalence of illegal labor and human trafficking in these countries, LAMPERS had provided no evidence from which I could conclude that Hershey has knowledge of any person who has violated the Human Trafficking Act. Even if I were to make the inferential leap that Hershey directly purchases cocoa from farms that utilize child labor, there is nothing in the Complaint from which I logically can draw the conclusion that Hershey has knowledge of illegal activity triggering its duty to inform under the Human Trafficking Act.

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merit defenses to the alleged wrongdoing. *See Marmon v. Arbinet-Thexchange, Inc.*, 2004 WL 936512, at *6 (Del. Ch. Apr. 28, 2004).

[64] *See* Compl. ¶¶ 41-45.

Perhaps because LAMPERS recognized the difficulty in establishing a credible basis from which this Court could infer violations of those international laws, the Complaint also asserts that LAMPERS has a credible basis to believe that Hershey may have violated state and federal law. These laws were not mentioned in the Demand Letter, which relied solely on LAMPERS's contention that Hershey potentially was in violation of laws in Ghana and the Ivory Coast.[65] Because federal and state laws were not cited in support of LAMPERS's stated purpose in the Demand Letter, in fairness they should not be included in the Complaint.

Even if I considered the federal and state laws cited by LAMPERS, however, there is no evidence from which I can conclude that Hershey may have violated those laws. LAMPERS first raises the VRPA, which makes it a crime to "knowingly benefit[], financially, or by receiving anything of value, ***from participation in a venture*** which has engaged in providing or obtaining labor or services by force, threat, or intimidation."[66] The statute defines a "venture" as "any group of two or more individuals associated in fact."[67] LAMPERS offers no plausible argument from which this Court could conclude that Hershey participates in a "venture" with any farmer in Ghana or the Ivory Coast. LAMPERS offers no allegation that Hershey is engaged in profit-sharing or any other economic association with any farmer in West Africa, other than a simple buy-sell arrangement. LAMPERS nevertheless argues, implausibly, that the term "venture" should be interpreted to capture within its meaning Hershey's alleged purchase of cocoa

[65] *See Id.* Ex. A, p. 5-8.
[66] *Id.* ¶ 49; 18 U.S.C. § 1589 (emphasis added).
[67] 18 U.S.C. § 1591.

beans from these farmers because using such cocoa allows Hershey to minimize costs and maximize profits.[68] This expansive reading of the term "venture" cannot be squared with the statutory definition of the term as an "association in fact," and LAMPERS's attempt to stretch the statute leads to absurd results. Under LAMPERS's reading of the statute, any retailer who sold Hershey chocolate products after becoming aware that the products were not sourced from certified growers could be liable under the VRPA, since the retailers also arguably benefit if Hershey's lower prices result in increased retail sales. In fact, under LAMPERS's reading of the statute, I – and any person who is reading this report or otherwise is aware of the fact that Hershey's supply may be derived in part from cocoa produced through child labor – arguably will violate the VRPA if we continue to satisfy a chocolate craving with a less expensive Hershey product, rather than a more expensive brand that relies solely on cocoa products certified as free from child labor. It is no more logical to conclude that Congress intended the VRPA to apply to a standard buy-sell supply chain than it is to conclude that Congress intended the statute to apply to globally-aware consumers.

LAMPERS's argument that Hershey has violated the CTSCA is equally strained. The CTSCA is a disclosure law that requires any manufacturer with more than $100 million in gross receipts to disclose the company's efforts to identify and address illegal labor and human trafficking within its supply chain by, among other things, verifying product supply chains to evaluate and address risks of illegal labor or trafficking, auditing suppliers for compliance with company standards, requiring direct suppliers to certify

[68] Opp'n Br. at 16-17.

that materials incorporated in a product comply with the law, maintaining internal accountability standards and procedures for employees and contractors, and providing training to employees with direct responsibility for supply chain management. Notably, the CTSCA does not require companies to do any of these things, but only requires companies to disclose their efforts to manage these risks within their supply chain.

LAMPERS concedes that Hershey has made the required disclosures pursuant to the CTSCA,[69] but contends that Hershey's disclosures are misleading because the company touts its supplier code of conduct as an effective measure to addressing illegal child labor, while LAMPERS contends the code of conduct is not effective because it applies only to Hershey's direct suppliers and not to farmers themselves,[70] and because Hershey does not explain whether it does anything to test the honesty of the signatories to the code, and does not disclose the consequences for violating the code. These *ipse dixit* contentions are not persuasive. Although LAMPERS may believe that the supplier code of conduct is not as effective as Hershey would like it to be, the CTSCA does not require that a company take particular, or even any, action to address illegal labor within its supply chain. The law instead is intended to enable consumers to make informed purchasing decisions with knowledge about companies' "efforts to supply products free from the taint of slavery and trafficking."[71] Consumers can do so on the basis of Hershey's disclosure and the publicly available facts that illegal child labor continues to

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[69] *See Id*. at 18-20.

[70] Notably, this argument directly contradicts LAMPERS's argument that Hershey may purchase cocoa directly from farmers or other suppliers who use child labor.

[71] California Senate Bill No. 657, Ch. 556, § 2.

pervade the cocoa industry and Hershey cannot certify that its products are free from the taint of child labor. LAMPERS's philosophical disagreements with the effectiveness of Hershey's supplier code of conduct do not amount to credible evidence that Hershey has violated California law.

B. Having Failed to Demonstrate any Basis to Infer Illegal Conduct, LAMPERS's Remaining Allegations of Mismanagement Melt Away

LAMPERS's contention that it has provided some evidence from which this Court could infer that Hershey's directors or officers had acted wrongfully or in breach of their fiduciary duties is based entirely on its contention that it has stated a credible basis that Hershey or its employees may have violated the law.[72] LAMPERS has not made any effort to allege any breaches of fiduciary duty outside the alleged violations of law described above, and having failed to set forth any evidence from which the Court can infer that Hershey has violated the law, LAMPERS's bid to investigate mismanagement or breaches of fiduciary duty related to those violations must fail. Any remaining allegations in LAMPERS's Complaint reflect its apparent disagreement with Hershey's decision not to rely exclusively on certified cocoa products, but do not appear to form the basis of any of its stated purposes. A stockholder's disagreement with a business decision is not evidence of wrongdoing and does not satisfy the credible basis requirement.[73]

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[72] *See, e.g.* Compl. ¶ 67; Opp'n Br. at 25-26.
[73] *Seinfeld v. Verizon Commc'ns, Inc.*, 909 A.2d 117, 120 (Del. 2006); *Marathon Partners, L.P. v. M&F Worldwide Corp.*, 2004 WL 1728604, at *4 (July 30, 2004).

II. HERSHEY'S REMAINING ARGUMENTS DO NOT SUPPORT DISMISSAL OF THE COMPLAINT

Having concluded that the Complaint should be dismissed for want of a proper purpose, Hershey's remaining arguments in support of dismissal are moot. For the sake of efficient judicial review, however, I briefly will address Hershey's argument regarding LAMPERS's standing to investigate matters before 2010, and its contention that the Complaint should be dismissed because the scope of the books and records demand is overbroad.

A. LAMPERS's Standing to Inspect Documents before 2010 Cannot be Determined on a Motion to Dismiss

Hershey asserts that LAMPERS lacks standing to inspect documents pre-dating 2010 because the statute of limitations has run for any derivative claim that accrued before that time. In response, LAMPERS contends that, even if claims accruing before 2010 are time-barred, it is entitled to inspect documents before that time because those documents may be relevant to establishing some of its claims, particularly its *Caremark* claim.

As an initial matter, I cannot conclude at this stage of the pleadings, and when drawing all reasonable inferences in favor of LAMPERS, that it is not entitled to inspect documents predating 2010, although LAMPERS apparently concedes that any breach of fiduciary duty claims that arose more than three years ago would be time-barred. When a stockholder seeks inspection to investigate alleged corporate wrongdoing, and the stockholder establishes a credible basis from which the Court may infer that wrongdoing may have occurred, the stockholder is entitled to inspect "enough information to

effectively address the problem."[74] In *Melzer v. CNET Networks, Inc.*, this Court held that, in order for a stockholder to establish a *Caremark* claim by showing a "sustained or systematic failure of the board to exercise oversight," a stockholder may well need to inspect documents that predated the stockholder's ownership, even though the stockholders did not have standing to bring claims that accrued before they owned stock.[75] The Court concluded that those documents were reasonably related to the stockholders' stated purpose, because the stockholders could not effectively address the alleged problem unless they were able to properly plead demand futility.[76] Similar reasoning applies here. Although LAMPERS may not be entitled to bring claims that accrued before the applicable statute of limitations, documents created before that period may be necessary to establish demand futility in any eventual derivative case. At a minimum, under Rule 12(b)(6), it is reasonably conceivable that, if LAMPERS could have established a proper purpose, it could have shown that documents created before 2010 were reasonably related to that purpose.

Whether LAMPERS is entitled to inspect the twelve years of documents it seeks is another matter, but that is not a question that is appropriate to resolve on a motion to dismiss in this case. This Court discourages parties from presenting pleadings-based motions in summary proceedings, including Section 220 proceedings, because such

[74] *Saito v. McKesson HBOC, Inc.*, 806 A.2d 113, 115 (Del. 2002).

[75] 934 A.2d 912, 919 (Del. Ch. 2007). It is significant that, in *Meltzer*, it was undisputed that the stockholders had standing to bring some derivative claims, and were not using the documents predating their ownership to investigate new claims. *Compare Polygon Global Opportunities Master Fund v. West Corp.*, 2006 WL 2947487 (Del. Ch. Oct. 12, 2006) (rejecting stockholder's inspection demand that sought books and records to investigate claims that the stockholder did not have standing to bring).

[76] *Meltzer*, 934 A.2d at 919-20.

motions tend to "promote delay" and undercut "the statutory mandate and policy that the proceeding be summary in character."[77] This is equally, if not more, true of pleadings-based motions that might narrow, but not entirely resolve, a summary proceeding. Even if I were able to select, at this stage of the proceedings, a date before which LAMPERS plainly was not entitled to inspect documents, that decision would not alleviate much, if any, of the burden on the parties to try the case, and likely would only serve to delay a proceeding that requires prompt resolution under the statute. For that reason, and as explained in more detail below, I do not believe that non-dispositive pleadings-based motions have a place in summary proceedings, absent agreement of the parties or a particular showing of good cause.

B. The Scope of LAMPERS's Inspection Demand Does Not Warrant Dismissal of the Action

Finally, Hershey argues that the Complaint should be dismissed because the scope of the documents LAMPERS seeks to inspect is overbroad. The Demand Letter includes 13 categories of documents, including subparts, which LAMPERS contends are necessary and essential to its stated purposes. Although the scope of the documents

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[77] *Louisiana Mun. Police Emps. Ret. Sys. v. Morgan Stanley & Co., Inc.*, 2011 WL 773316, at *3 (Del. Ch. Mar. 4, 2011). *See also Red Oak Fund, L.P. v. Digirad Corp.*, C.A. No. 8559-VCN, slip op. p. 2 (Aug. 5, 2013); *Khanna v. Covad Commc'ns. Gp., Inc.*, 2004 WL 187274, at *4, n.5 (Del. Ch. Jan. 23, 2004). One might justifiably point out that, despite this "rule" of practice, I permitted the parties to brief and argue a motion to dismiss in this case. I did so for two reasons. First, LAMPERS did not oppose the motion on the basis that it was not proper in a books and records case, nor did LAMPERS seek a conference with the Court to address scheduling or motion practice. Second, after reviewing the motion, it seemed likely that deciding the "proper purpose" portion of the motion, one way or the other, would resolve the overarching dispute between the parties, giving them better odds of reaching a negotiated resolution on any remaining issues. As it turns out, because I recommend that the Court grant the motion to dismiss, no issues remain to be negotiated.

LAMPERS seeks is concededly expansive, and LAMPERS ultimately might not be able to sustain its burden of demonstrating that each category is essential to its stated purpose, I cannot conclude that the Demand Letter is so impermissibly broad as to warrant wholesale dismissal of this action under Rule 12(b)(6).

A Section 220 action is not a forum in which to seek the wide-ranging categories of documents that may be appropriate for discovery under Court of Chancery Rule 34.[78] To the contrary, the scope of an inspection is limited to those documents that are necessary, essential, and sufficient to a stockholder's articulated purpose.[79] A document is "essential" under Section 220 "if, at a minimum, it addresses the crux of the shareholder's purpose, and if the essential information the document contains is unavailable from another source."[80] The stockholder bears the burden of justifying each category of the requested inspection.[81]

This Court has wide discretion to determine the proper scope of an inspection given the purpose articulated and demonstrated by the stockholder.[82] In exercising that discretion, the Court's aim is to harmonize the interests of the corporation with those of the inspecting stockholder.[83] The scope of an inspection necessarily is determined by its purpose; an inspection conducted to investigate possible wide-spread mismanagement

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[78] *Highland Select Equity Fund, L.P. v. Motient Corp.*, 906 A.2d 156, 165 (Del. Ch. 2006).
[79] *Marathon Partners, L.P.*, 2004 WL 1728604, at *4.
[80] *Espinoza v. Hewlett-Packard Co.*, 32 A.2d 365, 371-72 (Del. 2011).
[81] *Security First Corp. v. U.S. Die Casting & Dev. Co.*, 687 A.2d 563, 569 (Del. 1997); *Highland*, 906 A.2d at 164.
[82] *Marathon Partners, L.P.*, 2004 WL 1728604, at *4.
[83] *Security First Corp.*, 687 A.2d at 569.

likely would be broader than one conducted in the context of an imminent proxy contest.[84]

Hershey argues that LAMPERS's failure to narrowly tailor its inspection demand with the "rifled precision" required by Delaware precedent is fatal to its demand and demonstrates that this action is nothing more than a fishing expedition. Although Hershey may be correct that, even if LAMPERS could establish a proper purpose, its inspection demand is overbroad, the scope of the inspection sought in the Demand Letter does not reflect the gross overreaching that might lead this Court to entirely foreclose inspection.[85] Although it should not be incumbent on this Court to pick through a boundless demand to ferret out one or two categories that are essential to a stockholder's purpose, it also is common and within this Court's discretion to narrow a request once a stockholder has been afforded an opportunity to carry his burden on this point. Accordingly, it would require a particularly egregious case, in which the limitless scope of the demand demonstrated that Section 220 was being used impermissibly, or as a "tool of oppression," for this Court to dismiss the action entirely under Rule 12(b)(6). This is all the more true in light of this Court's reluctance to consider pleadings-based motion practice in summary proceedings. The scope of LAMPERS's inspection demand does not suggest that it is using this proceeding for impermissible reasons, or is pursuing

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[84] *Highland*, 906 A.2d at 164-65; *Sahagen Satellite Tech. Gp., LLC v. Ellipso, Inc.*, 791 A.2d 794, 797-98 (Del. Ch. 2000) (*citing Skoglund v. Ormand Industries, Inc.*, 372 A.2d 204, 210 (Del. Ch. 1976)).
[85] *See Highland*, 906 A.2d at 168.

inspection in bad faith. I therefore conclude that the motion to dismiss the Complaint on this basis should be denied.

CONCLUSION

For the foregoing reasons, I recommend that the Court dismiss for want of a proper purpose LAMPERS's Complaint seeking inspection of Hershey's books and records. This is my draft report and exceptions may be taken in accordance with Rule 144.