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Amended Brief of Professor Nancy Gertner and Professor Kent Greenfield as *Amici Curiae* in Support of Plaintiff, Louisiana Municipal Police Employees' Retirement System v. The Hershey Company, C.A. No. 7996-ML

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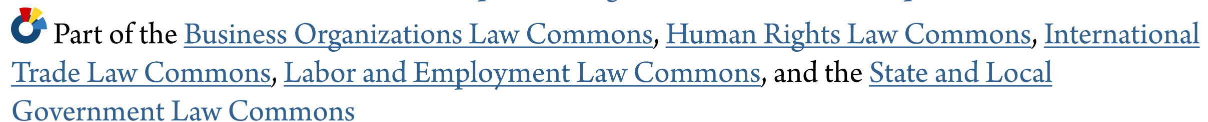
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IN THE COURT OF CHANCERY OF THE STATE OF DELAWARE

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

AMENDED BRIEF OF PROFESSOR NANCY GERTNER AND PROFESSOR KENT GREENFIELD AS *AMICI CURIAE* IN SUPPORT OF PLAINTIFF

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TABLE OF CONTENTS

TABLE OF AUTHORITIES II

INTERESTS OF THE AMICI CURIAE 1

SUMMARY OF ARGUMENT 2

ARGUMENT 4

I. Delaware Corporations Have A Duty To Obey The Law, Enforceable Through Corporate Law, And Determining Whether Illegality Is Occurring Is A Proper Purpose For A Section 220 Inspection 4

II. The Court Of Chancery Should Use This Case To Develop The Law Surrounding The Liability Of Delaware Corporations For Illegalities Committed Overseas And By Third Parties 8

III. Conclusion 12

TABLE OF AUTHORITIES

CASES

Page(s)

Guttman v. Huang,
823 A.2d 492, 506 n. 34 (Del. Ch. 2003) 4

In re Caremark Int'l Inc. Deriv. Litig.,
698 A.2d 959 (Del.Ch.1996) 7

In re Goldman Sachs Group, Inc. S'holder Litig.,
2011 WL 4826104 (Del. Ch. Oct. 12, 2011) 4

In re Massey Energy Co.,
2011 WL 2176479, (Del. Ch. May 31, 2011) 4, 5, 6

In re Walt Disney Co. Derivative Litigation,
906 A. 2d 27, 67 (Del. 2006) 4

Seinfeld v. Verizon Comm. Inc.,
909 A.2d 117 (Del. 2006) 11

Solomon v. Armstrong,
747 A.2d 1098, 1114 n.45 (Del. Ch. 1999) 6

Stone v. Ritter,
911 A.2d 362, 370 (Del.2006) 7

STATUTES

8 Del. C. § 101(b) 4

8 Del. C. § 124 4

8 Del. C. § 220 .... passim

OTHER AUTHORITIES

Stephen M. Flanagan, 7A FLETCHER CYCLOPEDIA OF THE LAW OF PRIVATE CORPORATIONS sec. 3400, at 12 (1997) 5

Kent Greenfield, *Ultra Vires Lives! A Stakeholder Analysis of Corporate Illegality (With Notes on How Corporate Law Could Reinforce International Law Norms)*, 87 Va. L. Rev. 1279 (2001) 1, 5, 6

PRINCIPLES OF CORPORATE GOVERNANCE: ANALYSIS AND RECOMMENDATIONS § 2.01(b)(1) (1992) 5

Adam Sulkowski & Kent Greenfield, *A Bridle, a Prod, and a Big Stick: An Evaluation of Class Actions, Shareholder Proposals, and the Ultra Vires Doctrine as Methods for Controlling Corporate Behavior*, 79 St. John's L. Rev. 929, 949 (2006) 5

Adam J. Sulkowski, *Ultra Vires Statutes: Alive, Kicking, and a Means of Circumventing the Scalia Standing Gauntlet in Environmental Litigation*, 14 J. Envir. Law & Litig. 75, 103-107 (2009) 5

INTERESTS OF THE AMICI CURIAE

Professor Nancy Gertner, Professor of Practice at Harvard Law School, served as Judge on the United States District Court for the District of Massachusetts from 1994 until 2011. She has dedicated her career–before, during, and after serving on the bench–to the proper administration of justice. She has lectured around the world on the topic of judicial independence and judicial accountability, and her interest in this case springs from her scholarly and professional interest in the role of courts in creating and administering legal rules in a democracy. In 2008, the American Bar Association recognized her contributions to advancing human rights and civil liberties by naming her the recipient of its Thurgood Marshall Award.

Professor Kent Greenfield is a leading scholar of corporate governance and corporate accountability. He is Professor of Law and Law Fund Research Scholar at Boston College, and a former chair of the Section on Business Associations of the American Association of Law Schools. In his article Ultra Vires Lives! A Stakeholder Analysis of Corporate Illegality (With Notes on How Corporate Law Could Reinforce International Law Norms), 87 Va. L. Rev. 1279 (2001), and in his book The Failure of Corporate Law: Fundamental Flaws and Progressive Possibilities (Chicago University Press, 2006), he first articulated the argument that Delaware corporate law provides a mechanism for shareholders to ensure that corporations abide by international law.

The amici file this brief on their own behalf. No party's counsel authored the brief in whole or in part. No party or party's counsel contributed money that was

intended to fund preparing or submitting the brief. No person—other than the amici or its counsel—contributed money that was intended to fund preparing or submitting the brief.

SUMMARY OF ARGUMENT

There is no question that corporations chartered in Delaware have a duty to obey the law. There is also no question that such duty is enforceable within corporate law, both vis-à-vis fiduciaries and the company itself. With fiduciaries, unlawful behavior is a breach of fiduciary duty. With the company itself, illegal acts are ultra vires. Ensuring that Delaware companies and their fiduciaries maintain respect for the rule of law has, laudably, been a focus of the Delaware Chancery for some time. To satisfy the requirement that the demanded inspection have a "proper purpose," a plaintiff only needs to show a "credible basis" that illegality for which Hershey is responsible has occurred or is occurring.

Delaware courts have not to date made clear the responsibility of companies for illegalities committed by suppliers and business partners. Certainly a company cannot protect itself from legal accountability simply by hiding behind an assertion that an illegality was committed by a separate legal entity or middleman. Rather, the determination of legal accountability necessarily depends on a more nuanced calculus, and good corporate governance—not to mention fairness—will require there to be something of a continuum of responsibility.

The proper calibration of this continuum of accountability will require careful deliberation by the Delaware courts, the nation's most important judicial monitor of multinational companies. These calibrations will take time, and will depend on the

equities and facts of specific cases. But the Delaware courts cannot shy away from this important task.

Establishing this continuum is a matter of increasing importance for Delaware courts, because a growing number of US companies chartered in Delaware are engaged in business practices globally. Also, an increasing number of Delaware companies are working through contractors and middlemen to occupy stages of the supply chain that would have traditionally been occupied by the company itself or by wholly-owned subsidiaries. The instant case is a perfect example of both the need for companies to be mindful of their legal and ethical responsibilities in a global economy, and the need for the Delaware Chancery to continue its efforts to delineate the responsibilities of Delaware corporations to respect the rule of law wherever and through whatever vehicle they do business.

The reality of chocolate production in western Africa, linked with the dominant role of defendant Hershey corporation in the world chocolate market, gives rise to a more-than-reasonable presumption that Hershey is toward the top end of the continuum of accountability for illegal acts, providing a more than "credible basis" for the shareholder plaintiff's claim for inspection. It may be impossible to know at this juncture the precise extent or nature of the board's knowledge of, or the company's role in, furthering or benefiting from the ongoing illegal use of child labor or from child trafficking. But that is exactly the purpose of a § 220 inspection.

ARGUMENT

I. DELAWARE CORPORATIONS HAVE A DUTY TO OBEY THE LAW, ENFORCEABLE THROUGH CORPORATE LAW, AND DETERMINING WHETHER ILLEGALITY IS OCCURRING IS A PROPER PURPOSE FOR A SECTION 220 INSPECTION.

As the Delaware courts have long recognized, corporations chartered in Delaware have a duty to obey the law. There is no question that such duty is enforceable within corporate law, both vis-à-vis fiduciaries and the company itself. Indeed, ensuring that Delaware companies and their fiduciaries maintain respect for the rule of law has, laudably, been a focus of the Delaware Chancery for some time.

With fiduciaries–directors, officers, and senior management–ensuring the company acts lawfully is a material component of fiduciary duty. In re Massey Energy Co., 2011 WL 2176479, at *20 (Del. Ch. May 31, 2011) ("A fiduciary of a Delaware corporation cannot be loyal to a Delaware corporation by knowingly causing it to seek profit by violating the law."); In re Goldman Sachs Group, Inc. S'holder Litig., 2011 WL 4826104, at *20 (Del. Ch. Oct. 12, 2011) ("Illegal corporate conduct is not loyal corporate conduct."); In re Walt Disney Co. Derivative Litigation, 906 A. 2d 27, 67 (Del. 2006) ("A failure to act in good faith may be shown . . . where the fiduciary acts with the intent to violate applicable positive law."); Guttman v. Huang, 823 A.2d 492, 506 n. 34 (Del. Ch. 2003) ("[O]ne cannot act loyally as a corporate director by causing the corporation to violate the positive laws it is obligated to obey.").

Illegalities are not only enforceable by means of a fiduciary duty suit against individuals. Because Delaware corporations (including defendant The Hershey Company) are chartered only for "lawful" acts or activity, 8 Del. C. § 101(b), illegalities

committed by the company are considered ultra vires and may be the proper source of both direct shareholder suits and injunctive actions by the state Attorney General. Delaware law is explicit on this point. A "lack of capacity or power may be asserted . . . [i]n a proceeding by a stockholder against the corporation to enjoin the doing of any act or acts" or "[i]n a proceeding by the Attorney General to dissolve the corporation, or to enjoin the corporation from the transaction of unauthorized business." 8 Del. C. § 124. See generally Kent Greenfield, Ultra Vires Lives! A Stakeholder Analysis of Corporate Illegality (With Notes on How Corporate Law Could Reinforce International Law Norms), 87 Va. L. Rev. 1279 (2001) ("corporations are not authorized under their charters to commit crimes or otherwise act unlawfully. . . . [B]ecause unlawful acts are ultra vires . . . such activities become subject to the enforcement powers of corporate law."); Stephen M. Flanagan, 7A FLETCHER CYCLOPEDIA OF THE LAW OF PRIVATE CORPORATIONS sec. 3400, at 12 (1997) ("If an act or contract is illegal . . . it is doubtless ultra vires in the broad sense as being 'without power.'"). See also Adam Sulkowski & Kent Greenfield, A Bridle, a Prod, and a Big Stick: An Evaluation of Class Actions, Shareholder Proposals, and the Ultra Vires Doctrine as Methods for Controlling Corporate Behavior, 79 St. John's L. Rev. 929, 949 (2006) ("a court could be asked to enjoin the illegal conduct or to exercise its powers in equity and order the company to achieve certain benchmarks or engage in certain remedial or preventative programs to prevent further illegalities"); Adam J. Sulkowski, Ultra Vires Statutes: Alive, Kicking, and a Means of Circumventing the Scalia Standing Gauntlet in Environmental Litigation, 14 J. Envir. Law & Litig. 75, 103-107 (2009) (reviewing modern cases). The ALI

Principles of Corporate Governance provide additional support for this position. “[T]he corporation, in the conduct of its business . . . [i]s obliged, to the same extent as a natural person, to act within the boundaries set by law.” PRINCIPLES OF CORPORATE GOVERNANCE: ANALYSIS AND RECOMMENDATIONS § 2.01(b)(1) (1992). The comment to that section clarifies that “[t]he appropriate vehicle to remedy an alleged violation of the principles stated in § 2.01 would be an action for injunctive or other equitable relief by a shareholder.” Id. § 2.01 cmt. j.

This Court’s recent comments in In re Massey Energy Co., supra, go to this point:

> Delaware law does not charter law breakers. Delaware law allows corporations to pursue diverse means to make a profit, subject to a critical statutory floor, which is the requirement that Delaware corporations only pursue “lawful business” by “lawful acts.”

In re Massey Energy Co., supra, at *20. See also Solomon v. Armstrong, 747 A.2d 1098, 1114 n.45 (Del. Ch. 1999) (“[i]n the context of defining void acts, ultra vires acts . . . include[] acts specifically prohibited by the corporation’s charter, for which no implicit authority may be rationally surmised, or those acts contrary to basic principles of fiduciary law”).

In other words, the corporation is empowered under Delaware law only to conduct lawful activities, and when it engages in unlawful activities as an entity it is acting beyond its chartered powers. The ultra vires doctrine may be extinct with regard to limiting corporations to engage in only certain lines of business. But with regard to unlawful activities, a vestige of the doctrine survives. As one of us said over a decade ago,

> While the [ultra vires] doctrine has fallen away in the main, loosening corporations from the obligation of staying within narrowly prescribed purposes, a remaining sliver of the doctrine seeks to ensure that corporate activities stay within legal bounds. The existence of such a doctrine is consistent with statutory texts, typical articles of incorporation, background norms of contract law, and with what the major firm stakeholders would want in an ex ante negotiation.

Greenfield, 87 Va. L. Rev. at 1351.

The implication of the requirement that corporations not engage in illegalities in this case cannot be overstated. Shareholders have an interest in monitoring whether the corporation is acting unlawfully even if there is insufficient evidence to show that directors or other fiduciaries should be subject to personal liability for a failure to monitor under Caremark and Stone v Ritter. See In re Caremark Int'l Inc. Deriv. Litig., 698 A.2d 959 (Del.Ch.1996); Stone v. Ritter, 911 A.2d 362, 370 (Del.2006). In order to show a "proper purpose" for its inspection demand, 8 Del. C. § 220, it is emphatically not necessary for the shareholder plaintiff in this case to show that any individual fiduciary stood in breach of those duties, because even if a fiduciary has not breached her duty to monitor, the company itself may nevertheless be acting ultra vires. And such activity would be a concern of shareholders, as it would provide a basis for a shareholder injunctive actions or enforcement actions by public officials or agencies. So to satisfy the requirement that the demanded inspection have a "proper purpose," a plaintiff should only be required to show a "credible basis" that illegality for which Hershey is responsible has occurred or is occurring, not a "credible basis" that a fiduciary is in breach.

II. THE COURT OF CHANCERY SHOULD USE THIS CASE TO DEVELOP THE LAW SURROUNDING THE LIABILITY OF DELAWARE CORPORATIONS FOR ILLEGALITIES COMMITTED OVERSEAS AND BY THIRD PARTIES.

The reality of cocoa farming and chocolate production in western Africa raises a compelling inference that significant illegality is occurring. While it is impossible at this stage of the litigation for us—or this Court—properly to evaluate the evidence, it certainly appears very likely that cocoa and cocoa-related products are being produced in Ghana and Cote d'Ivoire, two important sources for Hershey, in violation of international law as well as of the laws of those countries and of the United States. Moreover, given the dominant role of defendant Hershey corporation in the world chocolate market, and its admitted sourcing of cocoa from the region in question, it is reasonable to doubt defendant Hershey's assertions that it is not in any way knowledgeable of, willfully blind to, or complicit with such illegalities.

In all fairness, however, there are two gaps in the argument that would hold Hershey and its directors responsible under Delaware corporate law for the illegalities alleged in the complaint. The first gap is informational, and the second is doctrinal.

Informational. The nature of the illegalities alleged, the business model of cocoa production that relies on mostly family farms, and the foreign and distant locale of the alleged illegalities all make it quite difficult to gather evidence about the role of Hershey in furthering the illegalities alleged or benefitting therefrom. The extent of knowledge or involvement of Hershey management and of The Hershey Corporation in these illegalities is yet murky. But gathering this kind of information is a very purpose of a § 220 inspection.

As argued above, it is a proper purpose for shareholders to concern themselves with whether the company is engaging in, or is complicit in, unlawful activities. Shareholders have standing to concern themselves with possible illegalities not only because such illegalities are ultra vires and would give rise to injunctive actions brought by shareholders or the Attorney General. Shareholders also have standing to concern themselves with possible illegalities because of the potential of serious reputational harm to the company in which they have invested.

This case is an apt example of the importance of a § 220 inspection. Given the defendant's laudable history and values, the high value of its brands, and its beloved status with children in the United States, the company would suffer devastating reputational harm if a public agency in the United States or elsewhere initiated proceedings against the company on the basis of the illegalities alleged in the complaint. The shareholders have a right (assuming the "credible basis" standard is met) to use a § 220 inspection to investigate proactively the nature of Hershey's knowledge or complicity in the alleged illegality, both to protect their own interests as shareholders and to protect the company itself.

Doctrinal. Though the matters alleged in this case are terribly serious, this suit is more important than the merits of this sole dispute. In an increasingly global world economy, Delaware corporations are involving themselves more deeply in the laws and cultures of other national economies. As a result, they will increasingly be required to answer to a range of legal and cultural obligations that may be unfamiliar. Also, because of the nature of the global economy, an increasing number of Delaware companies are

working through subcontractors, suppliers, and middlemen to occupy stages of their production and supply chains that would have traditionally been occupied by the company itself or by wholly-owned subsidiaries. Because of this, Delaware corporations are increasingly asked to answer for behavior that may not be their own in a strict sense, but on which their international reputation and their shareholder and customer relationships rely.

Meanwhile, the Delaware judiciary has not yet defined the contours of corporations' responsibility for illegalities committed by suppliers, business partners, or other third parties. Certainly a company and its board cannot protect itself from legal accountability simply by hiding behind an assertion that an illegality was committed by a separate legal entity or middleman. Rather, the determination of legal accountability will necessarily depend on a more nuanced calculus, and good corporate governance—not to mention fairness—will require there to be something of a continuum of responsibility.

On one end will be situations in which there is de facto unity between a Delaware corporation and a subcontractor, supplier, or middleman acting illegally, or when a Delaware corporation is acting in partnership with entities acting illegally. The responsible end of the continuum would also capture situations in which a Delaware corporation and its fiduciaries were knowingly complicit in such illegalities, even if managerial unity or partnership did not exist. On the other end of the continuum, it would be unjust for corporations and their management to be held responsible for the behavior and decisions of independent actors committing illegalities without the complicity, benefit, or knowledge of the corporation.

The proper calibration of this continuum of accountability will require careful deliberation by the Delaware courts, the nation's most important judicial monitor of multinational companies. In establishing the levels of accountability, attention will need to be paid to both the ex ante effects of legal rules on behavior, and on the ex post considerations of fairness and just desert. These fine calibrations will take time, and will depend on the equities and facts of specific cases. But the Delaware courts cannot shy away from this important task.

The calibration of this continuum is a matter of increasing importance for Delaware courts. In a sense, as Delaware corporations become more global, the Delaware judiciary must concern itself with the global implications of its corporate law doctrines. (Chancellor Strine has been vocal on this front. See Transcript of Oral Argument and The Court's Ruling in In re Puda Coal, Inc. Stockholders Litigation, C.A. No.6476-CS, February 6, 2013 (available at http://www.delawarelitigation.com/files/2013/02/puda-case.pdf)).

The instant case is a perfect example of the need for boards and the corporations they steward to be mindful of their legal and ethical responsibilities in a global economy, and the need for the Delaware Chancery to continue its efforts to delineate the responsibilities of Delaware corporations to respect the rule of law wherever they do business. With evidence of the realities of chocolate production in Western Africa, coupled with the dominant role of the Hershey corporation in that market, the shareholders have certainly presented sufficient information to satisfy the requirement of showing a "proper purpose" for such inspection and "credible basis" to believe that

mismanagement or wrongdoing has occurred. 8 Del. C. § 220; Seinfeld v. Verizon Comm. Inc., 909 A.2d 117 (Del. 2006). Once the inspection is ordered and completed, the shareholders and the court will have a much greater ability to evaluate where on the continuum of responsibility Hershey lies. And this case would then provide an excellent juridical vehicle for the Court of Chancery to clarify the obligations of Delaware corporations acting globally.

III. CONCLUSION

This Court should compel the defendant to grant the plaintiff's § 220 inspection request.

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