

This is an action pursuant to Section 220 of the Delaware General Corporation Law (“DGCL”) seeking the inspection of corporate books and records. The complaint was originally filed on February 8, 2000. It was subject to meritorious technical defenses and was dismissed with leave to refile.’ On November 22, 2000, plaintiff filed his Second Amended Complaint. Trial was held on December 15, 2000.

Having considered the trial testimony and post-trial submissions of the parties, I conclude that plaintiff has not carried his burden of showing a proper purpose for his demand. I reach this conclusion taking into account the paucity of evidence suggesting any wrongdoing or waste of corporate assets, the sweepingly broad scope of the document inspection demanded and the plaintiff’s substantial delay in acting.

I.

Defendant Checkers is a Delaware corporation with its principal place of business in Clearwater, Florida. Checkers develops, produces, owns, operates and franchises quick-service “double drive-thru” restaurants. The Company began operations in 1987 and, since 1991, has

¹ Del. Ch., C.A. No. 17775, Lamb, V.C. (Nov. 15, 2000).

been publicly owned. As of January 3, 2000, the Company's system included 907 restaurants – 464 Rally's restaurants operating in 18 different States and 443 Checkers restaurants operating in 22 different States, the District of Columbia, and elsewhere. Of these, 367 restaurants were company-operated and 540 were operated by franchisees.

In 1991, the Company acquired 100 percent of the stock of Champion Modular Restaurants, Inc. ("Champion"). Champion manufactured and sold modular restaurant packages to franchisees and to the Company for use in its restaurants. Effective February 15, 1994, Champion was merged into the Company.

Plaintiff Craig Mattes was an employee of Checkers for over five years, from 1991 through 1996. During that time, plaintiff held various managerial positions within the Company. In February 1996, after serving more than two years as Director of Operations, responsible for all restaurants in South Florida, Mattes was promoted to Senior Director of Operations.

Shortly thereafter, Mattes quit to become a franchisee. That relationship ended in the spring of 1998. Currently, Mattes is employed in a managerial capacity by a Burger King franchisee that directly competes

with Checkers. Mattes has owned Checkers stock continuously since 1991.

II.

The pertinent demand is contained in a letter dated November 16, 2000 from a Florida attorney representing Mattes. The purported purpose of the demand is to obtain information about various instances of alleged corporate mismanagement and waste, and “to assess the propriety of management decisions. ” Plaintiff testified that he had reviewed some available public records and has knowledge of instances of potential corporate mismanagement and waste of assets through his employment at Checkers between 1991 and 1996.

Plaintiff limited the scope of demand during the course of the proceedings. He now seeks to inspect and copy only the following records:

1. Depreciation schedules that support the Balance Sheets, Statements of Operations and Statement of Cash Flow in the Forms 10-K and Annual Reports [presumably for the years 1992-1997];

2. The Balance Sheets and Statements of Operations for each subsidiary or division of Checkers, especially Champion, for years 1992-1997;

3. The Balance Sheets and Statements of Operations for the 50 percent owned and 75 percent owned joint venture partnerships controlled by Checkers from their inception through 1997;

4. Corporate tax returns for Checkers for years 1992-1997;

5. General Ledgers and Trial Balances (including subsidiaries) that support the Balance Sheets, Statements of Operations and Statements of Cash Flows included in the Forms 10-K and Annual Reports for years 1992-1997;

6. Support for amount allowed for pre-opening costs of restaurants;

7. The original agreement between Checkers and Le Van Hawkins;
and

8. The original agreement between Checkers and Paul Auger.

In support of these demands, Mattes makes claims of waste or mismanagement that can be grouped into six general topics. I will discuss the trial record as it relates to each of these, in turn.

1. Alleged Missing Assets

During the period from 1991 through 1994, (Checkers used the proceeds of public stock offerings to pursue an aggressive growth strategy. According to Mattes, in this period Checkers built four to five new restaurants every month in South Florida alone. Plaintiff claims that, during this extensive build-out program, assets were allocated for accounting purposes to restaurants he managed that were not physically at the restaurant location. Mattes's concern over the whereabouts of these assets arose because their depreciation affected the profit and loss statements of the restaurants he managed. For example, plaintiff testified at trial that he received a store asset list for a Checkers restaurant in Coral Springs which showed that it had 12 tables when, in fact, the store had only four.² Plaintiff estimated that during this time over \$1 million in non-existent assets appeared and were depreciated on the asset sheets of restaurants in South Florida.

² Plaintiff also testified at trial that similar events were occurring in the Tampa area stores, based upon his hearsay testimony that another Checkers employee had encountered the same problems. This hearsay testimony proffered by plaintiff himself cannot create a credible inference of mismanagement. *Thomas & Betts Corp. v. Leviton Mfg. Co.*, Del. Ch., 685 A.2d 702, 710 (1995), *aff'd*, Del. Supr., 681 A.2d 1026 (1996).

Mattes conceded, however, that these “mis-allocated” assets were not necessarily the result of misfeasance on the part of the Company or its bookkeepers, stating that during the Company’s intense build-out “it was hard to keep track of what was going on.”³ Plaintiff also acknowledged that there were assets physically present at his stores that were not listed on the fixed asset sheets. Presumably, those assets may have been listed on the fixed asset sheets of some other Company-owned property. Plaintiff concedes that he: has no knowledge or information that the “missing” assets in question were being given away. Indeed, he admitted at trial that he is merely curious to find out what happened to them.

Mattes argues that the evidence adduced by him about these accounting irregularities entitles him to inspect the following documents for the *entire* company: general ledgers, fixed asset schedules, depreciation schedules, corporate tax returns, and invoices for these assets.

³ Indeed, plaintiff informed certain executives that mis-allocation of assets was an issue, but he did not receive a response. The employees he asked both left the Company.

2. Champion and Construction-Related Costs

Mattes challenges many of the allocations of costs associated with opening new and newly-refurbished Checkers restaurants. He claims that Champion, the Company's construction division, mis-allocated these costs.

a. Change orders

Plaintiff relies on two examples, both of which allegedly occurred during his tenure as Director of Operations, to show that costs **were** not being allocated properly in construction of new restaurants and refurbishment of old ones. His main example is a Checkers in West Palm Beach which plaintiff claims had a specific landscape design package worth \$25,000. Plaintiff testified that two months later, after the store opened, he saw a document ascribing a value of over \$75,000 to that landscape package. He also states that at stores in St. Lucie County certain change orders were made and accounted for, yet the work was never completed. These allegedly uncompleted change orders were depreciated on the stores' profit and loss statements, thereby lowering the stores' profit. Mattes suggests these "missing costs" were the result of intentional waste and self-dealing by the company's officers and directors.

Mattes contends that these allegations entitle him to inspect depreciation schedules of every Checkers restaurant built or refurbished from 1992 to 1996, as well as a record of purchases and invoices from Champion for each such restaurant.

b. Pre-opening costs

Mattes alleges that the Company improperly allocated certain pre-opening costs. ‘These costs were mainly associated with the Rally’s restaurants purchased by the Company and then re-opened as Checkers restaurants. For instance, Mattes claims that one former Rally’s store had only \$20,000 - \$30,000 worth of work done on it, but the store had over \$100,000 in pre-opening charges allocated against it. Mattes also asserts that pre-opening costs were a concern in other restaurants as well.

Mattes was unable to say whether these additional pre-opening costs were attributable to the cost of purchasing these restaurants, although he admits this was a possibility. Nor does he cite any evidence that the money allocated for pre-opening costs was being spent elsewhere or being improperly diverted.

Based on this record, Mattes seeks to inspect the general ledgers, disbursement journals, purchase journals, invoices, and profit and loss statements from each Company-owned store from 1992 to 1997.

3. Vendor rebates

Mattes testified about the treatment of vendor rebates received by the Company for purchases by Company-owned restaurants. His concern originates in the fact that these rebates were not credited back to the individual Company-owned stores on their profit and loss statements.

At the end of the year, certain vendors rebated money to the Company in the form of a marketing reimbursement. This rebate was passed through to franchisees but, as a matter of internal accounting, was not allocated back to the profit and loss statements of Company-owned stores. Mattes questions where this vendor rebate money went. He testified that the former Vice President of Purchasing for Checkers, would “tak[e] that money and do other things with it.” He also claims that the same officer had a “fryolator” given to him by a vendor. Based on these scant “facts, ” plaintiff deduces that the vendor rebates were improperly diverted to the personal use of one or more officer or director of the Company.

Mattes demands the right to inspect all agreements with any and all vendors, as well as any records of rebates paid to the Company needed to trace those rebates through the financial records.

4. The Paul Auger Loan

Late in December 1993, Paul Auger purchased from the Company a restaurant in Mattes's district. At the time, Auger was the father-in-law of a Checkers director who, in turn, was the son of the Chairman of the Board. Mattes claims to know that Auger did not want to purchase the restaurant but did so for "the good of the Company" so it could show a profit. Mattes does not contend that the terms of the transaction were unfair to the Company. Indeed, he admits that the purchase price was "probably . . . close to market price." Rather, he seeks to investigate the transaction because Checkers financed Auger's investment by taking his note for the purchase of the restaurant (the "Paul Auger Loan"). Mattes finds this suspicious because, he says, the Company never financed any other franchisee. Mattes does not know the interest rate on the loan, the size of the loan, or whether the note was ever repaid. His sole complaint is the decision to offer financing terms to Auger while most, if not all, other franchisees had to find other means to pay.

Mattes seeks to inspect the loan agreement, the note, and a repayment schedule so that he can “determine the fairness of the interest rates, the repayment of the loan itself.”

5. La Van Hawkins

La Van Hawkins obtained the exclusive right to develop Checkers restaurants in certain geographical areas. At his deposition, plaintiff took the position that Hawkins’s relationship with the Company was improper and sought to inspect every document evidencing that relationship. After learning that the documents evidencing the Company’s relationship with Hawkins were available publicly, Mattes narrowed his request to a single document he believes exists but is not publicly available. He did not, however, review the publicly filed documents.

Plaintiff testified at trial that he believed Hawkins and the Company entered into a joint venture agreement prior to the publicly disclosed August 10, 1993 joint venture agreement. His basis for believing that such an earlier agreement exists is a conversation he claims to have had in either late 1992 or early 1993 with the Company’s Chief Financial Officer, who told him that Checkers was subsidizing certain of Hawkins’s costs.

The record shows that Hawkins was a franchisee of the company prior to August 10, 1993, but that there is no joint venture: agreement or any other agreement between him and the Company prior to that date other than a standard franchise agreement.

6. The Jim White Transaction

Jim White was a franchisee owning a few Checkers restaurants in Virginia, as well as the land on which the restaurants were situated. White became employed by the Company, eventually serving as President for a while. As a favor to White, Mattes conducted a performance review of the franchise stores owned by White and managed by his son. In doing so, Mattes gained familiarity with those stores. When White left the employ of the Company, the company agreed to purchase the stores from him but did not purchase the land on which the stores were situated (“the Jim White Transaction”).

Plaintiff testified that the rent White charged the Company after that transaction was twice the rent White charged himself when he was a franchisee. Plaintiff admits, however, that he has no idea what the market rate for rent was in the area in which the property owned by White was located, nor does he have any information that the rent being charged was

not a market rent, nor has he attempted to locate this information. Plaintiff also does not assert that White dictated or controlled the terms of such transaction. Furthermore, the transaction in which White sold the stores back to the Company was part of an overall termination of White's relationship with Checkers, as both an employee and a franchisee.

Nonetheless, Mattes contends that he is entitled to not only the lease agreement between the Company and White, but also "lease agreements that the Company may have with other stores that would be similar, where they leased the land, so that we could see that geographically, demographically, these were comparable. "

III.

The evidence at trial did not show "a credible basis to find probable wrongdoing on the part of corporate management." *Security First Corp. v. U.S. Die Casting & Dev. Corp.*, Del. Supr., 687 A.2d 563, 567 (1997). Thus, Mattes has not carried his burden of proving a proper purpose for his demand. *Thomas & Betts Corp. v. Leviton Mfg. Co.*, Del. Supr., 681 A.2d 1026, 1031 (1996); *BBC Acquisition Corp. v. Durr-Fillauer Med., Inc.*, Del. Ch., 623 A.2d 85, 88 (1992). This burden is not insubstantial, and "[m]ere curiosity or a desire for a fishing expedition will not suffice."

Sahagen Satellite Tech. Group, LLC v. Ellipso, Inc., Del. Ch., C.A. No. 18020, mem. op. at 4, Lamb, V.C. (Sept. 27, 2000).

In evaluating the evidence of Mattes's purpose, I am also mindful that he delayed substantially in pursuing his inspection rights. Mattes has been a stockholder of Checkers since 1991. The evidence at trial related entirely to matters occurring before 1996 and, in many cases, much earlier. Mattes testified that he knew about each of these matters at the time. Yet, he **diid** not file his complaint until 2000. Although I need not decide whether, in the circumstances, Mattes's claim is barred by laches, the fact that Mattes did delay so long in asserting his rights weighs in the process of evaluating the evidence of his purpose that was presented at trial.⁴

I am also struck by the incongruity between the narrow scope of the evidence of mismanagement or waste of assets adduced by Mattes and the broad scope of the inspection he seeks. Even if Mattes had carried his

⁴ Decisions of this court have relied on laches in the past to limit the scope of inspection available under Section 220. *Skouras v. Admiralty Enterprises, Inc.*, Del. Ch., 386 A.2d 674, 682 (1978). Nevertheless, other cases have suggested that the equitable defense of laches is not available in the context of a statutory proceeding under that section. *Everett v. Hollywood Park, Inc.*, Del. Ch., C.A. No. 14556, Jacobs, V.C. (Jan. 19, 1996).

burden as to any of the matters he alleged, there was no evidence of such a general mismanagement of the sort addressed in *Skoglund v. Ormand Industries, Inc.*,⁵ for example, to warrant a wide-ranging inspection under Section 220. Instead, the right to inspect would likely have been confined to the particular areas of concern sufficiently proven, at least until some basis was shown in the record to support more general relief.

A. The Asset Allocation Issues

The evidence regarding “missing” assets suggests merely imperfect bookkeeping during a period of rapid expansion. Mattes himself admits there were “extra” assets in his stores that did not appear on his fixed asset lists. In light of this, his testimony about “missing” assets provides scant reason to infer that assets or monies were being misappropriated. Instead, it is likely that the Company had trouble keeping track of which assets were sent to which stores. Mattes admits that he had no personal information that the assets were being given away, and that he is merely “curious” to find out what actually happened to these assets. Curiosity does not satisfy his burden. *E.g., Weiland v. Cent. & S. W. Corp.*, Del. Ch., C.A. No. 9769, slip op. at 3-4, Berger, V.C. (May 9, 1989) (“it is

⁵ Del. Ch., 372 A.2d 204 (1976).

not enough for a stockholder merely to state that he suspects corporate mismanagement. There must be some factual basis for that suspicion; he is not entitled to engage in a fishing expedition. ”).

B. The Construction-Related Claims

Mattes also did not meet his burden with respect to -the accounting for change orders and pre-opening costs. The overall impression gained from Mattes’s trial testimony was that the intense development activity at Checkers in the early 1990s may initially have led to some: errors in tracking contract costs to particular store locations. But Mattes was not in a position to assess whether these errors were the result of venality or not. At best, Mattes testified only to *innuendo* that funds were ‘being diverted by a contractor that had a relationship with a member of the board.

Mattes has no information about how Checkers allocated corporate level costs associated with the development or redevelopment of stores. Instead, his perspective on the subject was that of a manager interested in reporting profits from the stores under his control and, thus, limiting the depreciation amount allocated to them. But this is a limited perspective that omits many relevant considerations. For example, it fails to take into account the allocation of costs necessary to acquire the stores themselves,

even though Mattes admits this was suggested to him by Company management as a possible explanation. In my view, the testimony on this subject simply revealed Mattes's disagreement or even simple misunderstanding over basic business decisions, and lacks the credible support necessary to justify the broad inspection plaintiff seeks. *Everett v. Hollywood Park, Inc.*, Del. Ch., C.A. No. 14556, mem. op. at 11, Jacobs, V.C. (Jan. 19, 1996) (holding plaintiff's opinion that a business decision of the defendant was unwise does not constitute a credible basis to suspect mismanagement).

C. The Vendor Rebates

For similar reasons, Mattes fails to meet his burden with respect to the issue of vendor rebates. Mattes claims that the rebate -money was "being used for other things" and would have me infer that it was being diverted. This claim is without factual support and is not credible evidence for a finding of probable mismanagement.

Mattes's "evidence" was two-pronged. First, he testified that he could not find the rebates in the Company's published financial information. But he did not provide evidence from which I could conclude that detailed information of this sort should have been presented separately

on those financial statements. Second, he suggested that there was something sinister about the fact that the Company passed the rebates through to its franchisees but did not pass them through to the individual Company-owned stores. This amounts to nothing more than a disagreement with a business decision made by the Company, and does not satisfy Mattes's burden under Section 220. *Everett*, mem. op. at 11. In sum, there is no competent evidence that any vendor rebates were ever diverted from the Company's use.⁶

D. The Paul Auger Loan and The Jim White Transaction

Neither the Paul Auger Loan nor the Jim White Transaction have been shown to justify the inspection Mattes seeks.

With respect to the Paul Auger Loan, plaintiff admitted that the purchase price financed by the loan was probably close to the market price. He further conceded that he did not know the size of the loan, the interest rate of the loan, or whether the loan had been repaid. Mattes's sole evidence of wrongdoing or mismanagement is his claim that the Company

⁶ The testimony that a Company official received a "fryolator" as a gift from a vendor does not support any inference that the rebates at issue were either not paid to the Company or were diverted for the personal use of any corporate officer or director.

never financed others' purchases of restaurants. This is insufficient to satisfy plaintiff's burden.

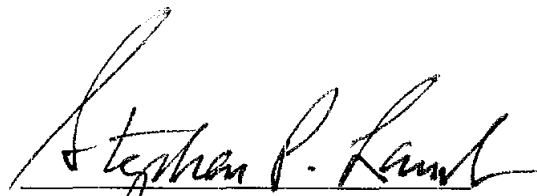
The Jirn White Transaction suffers from a similar lack of credible evidence. Plaintiff's charge amount to this: after selling his restaurants to the Company, White charged the Company a higher rent for the land than he had been charging himself. Yet, plaintiff admits that the sale and the lease were parts of a larger transaction that occurred when White's relationship with the Company was terminated. He does not attack any other aspect of this overall transaction, such as the purchase price for the restaurants or the manner of payment. Mattes does not even offer proof that the rent charged by White after he sold the restaurants, to the Company was higher than the market rate. He also does not suggest that White dictated or could have dictated the terms of any part of that overall transaction. Accordingly, plaintiff's testimony, even if accepted as true, fails to satisfy the burden under Section 220. *See, e.g., Everett*, mem. op. at 12 (denying a request for inspection on the grounds that amount of rent, among other things, is ordinarily a business decision, and plaintiff offered "no specific evidence suggesting impropriety, illegality or irregularity in connection with the board's decisions. ").

E. The La Van Hawkins Contracts

This issue has boiled down to a request to inspect a single contract that the Company says never existed. Moreover, even if the document did exist, Mattes has not established a credible basis to find that there was any probable wrongdoing in the relationship between the Company and Le Van Hawkins. This failure is particularly glaring (and grating) because the material contracts bearing on the relationship between the Company and Hawkins are publicly-filed, and yet Mattes has never reviewed them. In the circumstances, Mattes's mere curiosity or suspicion about the terms of that relationship do not support the entry of an order under Section 220 to compel an inspection of other non-public information,

IV.

For all the foregoing reasons, the court hereby enters JUDGMENT FOR THE DEFENDANT and against the Plaintiff, with costs. IT IS SO ORDERED.


Vice Chancellor