2015

Delaware Shareholders with Enough "Skin in the Game:" Choice of Law and Other Concerns in the Aftermath of Wal-Mart Stores v. IBEW

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DELAWARE SHAREHOLDERS WITH "ENOUGH SKIN IN THE GAME:" CHOICE OF LAW & OTHER CONCERNS IN THE AFTERMATH OF WAL-MART STORES V. IBEW

Alexander T. Yarbrough*

PART I: INTRODUCTION

In April 2012, *The New York Times* published an article outlining reports of alleged illegal conduct that took place between the years of 2002 and 2005 by Wal-Mart officials in Mexico.[1] This illegal conduct included bribery payments made to Mexican government officials in exchange for building permits.[2] These permits were allegedly made at the direction of senior company executives.[3] If proven, these actions would violate United States law.[4]

Wal-Mart Shareholders initiated a Section 220 books and records inspection request to investigate wrongdoing on the part of Wal-Mart's board of directors and management and also to analyze the possibility of a derivative action.[5] Wal-Mart refused to produce some documents, stating that the requested records were not necessary and essential to the shareholders' demand and also that the documents were subject to the attorney-client privilege and therefore protected.[6] The shareholders petitioned the Court

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[1] David Barstow, *Vast Mexico Bribery Case Hushed Up by Wal-Mart After Top-Level Struggle*, N.Y. TIMES, Apr. 21, 2012, at A1 ("Wal-Mart de Mexico had orchestrated a campaign of bribery to win market dominance. In its rush to build stores . . . the company had paid bribes to obtain permits in virtually every corner of the country.").

[2] *Id.*

[3] *Id.*

[4] *See id; see also* the *Foreign Corrupt Practices Act* ("FCPA"), 15 U.S.C. §§ 78dd-1, et seq. The FCPA makes it unlawful for certain classes of persons and/or entities to make payments to foreign government officials to assist in obtaining or retaining business.

[5] Wal-Mart Stores, Inc. v. Ind. Elec. Workers Pension Trust Fund (IBEW), 95 A.3d 1264, 1269-70 (Del. 2014).

[6] *Id.* at 1269.

of Chancery to enforce their request and what resulted was the adoption of the "*Garner* Fiduciary Exception:" a doctrine which allows shareholders of a corporation to pierce the corporation's attorney-client privilege in order to corroborate fiduciary violations by corporate management upon proof of good cause.[7] Delaware's highest court in *Wal-Mart Stores v. IBEW* affirmed the chancery court, formally subscribing the state to the doctrine.[8]

This Note first argues that the Delaware Supreme Court's decision in *Wal-Mart* yields critical choice of law concerns for both plaintiffs and defendants embroiled in shareholder derivative litigation. Specifically, plaintiff shareholders will receive less favorable treatment outside of Delaware even with the Delaware Supreme Court's adoption of *Garner*. Further, the *Garner* exception creates the incentive for corporations to reincorporate in other state jurisdictions in order to limit derivative suit liability.

Under the internal affairs doctrine, both state and federal courts apply the substantive corporate law of the jurisdiction where the corporation is incorporated.[9] Procedural aspects of the law — where privileges are located — of the instant jurisdiction remain intact.[10] Therefore, even though *Garner* is now the law in Delaware, plaintiffs may receive less favorable treatment in other jurisdictions.

Corporations may seek to mitigate these new litigation risks by incorporating in another state jurisdiction. Differences in substantive statutory corporate law have long affected the choices corporations face when they choose jurisdictions to incorporate

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[7] Ind. Elec. Workers Pension Trust Fund (IBEW) v. Wal-Mart Stores, Inc., 2013 WL 5636296 (Del. Ch. 2013) (order enforcing plaintiff's § 220 books and records request).
[8] *Wal-Mart*, 95 A.3d at 1275.
[9] VantagePoint Venture Partners 1996 v. Examen, Inc., 871 A.2d 1108, 1112 (Del. 2005). The internal affairs doctrine is important as it "prevent corporations from being subjected to inconsistent legal standards, [and] the authority to regulate a corporation's internal affairs should not rest with multiple jurisdictions." *Id.*
[10] *See id.*

within. The application of the *Garner* exception to the corporation's attorney-client privilege creates the potential opportunity for the production of highly sensitive and potentially damaging documents during the course of litigation. Firms will undoubtedly be adverse to such potential liability.

Given Delaware's predominance in substantive corporate law, this Note further argues that other jurisdictions should be cautious when looking to follow Delaware's lead in applying the *Garner* doctrine to their respective statutory schemes. The application of the *Garner* doctrine stresses the relationship between a corporation and its corporate counsel. Corporate executives will be dis-incentivized to engage in full, open communication with their legal counsel. Likewise, a corporation's attorney will be deterred in their efforts to engage in internal investigations of corporate malfeasance.

In Part II, this Note begins by summarizing the history and scope of Section 220 shareholder demands, the attorney-client privilege, and the work product doctrine. This Note then addresses and analyzes the creation of the *Garner* Fiduciary Exception by the United States Court of Appeals for the 5th Circuit. The Part ends with an in-depth look into the Delaware Supreme Court's decision in *Wal-Mart*.

Part III provides analysis and explores the choice of law concerns that come with the adoption of the *Garner* Exception. This Part advocates and recommends the filing of shareholder derivative actions in Delaware state courts by plaintiffs in order to maintain *Wal-Mart*'s significance. Finally, although the fiduciary exception can have immense beneficial results for shareholder plaintiffs, this Part ends by noting the pitfalls that might materialize with the adoption of the *Garner* exception by a jurisdiction.

PART II: BACKGROUND

An analysis of the *Wal-Mart* decision involves the review of traditional notions of the attorney-client privilege, the work-product doctrine, § 220 demands, and relevant case law.[11]

A. § 220 Right to Inspect Corporate Documents and Records

Shareholders of Delaware corporations have long enjoyed a powerful right to inspect the books and records of companies in which they hold equity.[12] Initially, the power of a shareholder to demand production of company information arose out of state common law.[13] Courts would therefore issue writs of mandamus to enforce requests to inspect corporate documents.[14] In 1967 the Delaware General Assembly formally codified a statutory right upon shareholders to inspect corporate books and records in the Delaware General Corporate Law ("DGCL").[15] In 2003, the legislature expanded the right to beneficial owners of shares.[16]

§ 220 actions are a critical part of the corporate governance backdrop in the state of Delaware.[17] A shareholder has a statutory right to, at the very least, a narrow review of corporate books and records when they have provided some reliable foundation to

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[11] *See* D.G.C.L. § 220 for a "§220 demand."

[12] Under the common law, a stockholder had the right to examine the books and records of the company, and that right could not be take away except by statute that expressly or by necessary implication authorized it. *See* State ex rel. Cochran v. Penn-Beaver Oil Co., 143 A. 257 (Del. 1926); State ex rel. Healy v. Superior Oil Corp., 13 A.2d 453 (Del. 1940).

[13] Historically, this proved difficult for shareholders as writs of mandamus are within the individual discretion of the courts. *See* S. Mark Hurd and Lisa Wittaker, Article, *Books and Records Demands and Litigation: Recent Trends and Their Implications for Corporate Governance*, 9 DEL. L. REV. 1 (2006).

[14] *Id.*

[15] *See generally* 2-27 Delaware Corporation Law and Practice § 27.01; 8 Del. C. § 220

[16] Stephen A. Radin, *Developments in the Law: the New Stage of Corporate Governance Litigation: Section 220 Demands – Reprise*, 28 CARDOZO L. REV. 1287, 1288 (2005). *See also* 2-27 Delaware Corporation Law and Practice § 27.01. The DGCL is firm in its requirement to allow § 220 requests: a corporation is forbidden from waiving this right in its certificate of incorporation or its bylaws.

[17] Security First Corp. v. U.S. Die Casting & Dev. Co. 687 A.2d 563, 571 (Del. 1997).

establish that there has been some form of wrongdoing.[18] In truth, a § 220 proceeding may serve a beneficial undertaking as the first step in a derivative suit even though it may sometimes "invite mischief to open corporate management to indiscriminate fishing expeditions."[19] Trial courts, therefore, typically endeavor to strike a proper balance between legitimate corporate management concerns and a shareholder's statutory right to inspect.[20]

In order to make a proper § 220 demand, a shareholder must establish that (1) he or she is a stockholder of the company; (2) the stockholder has complied with the DGCL in the manner and form of making a demand for inspection of such documents; and (3) the stockholder made the demand for a proper purpose.[21] Courts primarily focus their analysis on the third element: whether a shareholder's demand for inspection was for a "proper purpose."[22] While this statutory provision confers an absolute right, the shareholders themselves bear the burden of proving by a preponderance of the evidence that the purpose to inspect is proper.[23] Thus, if analysis reveals a demand made in bad faith, the Chancery Court will deny relief.[24]

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[18] *Id.*

[19] *Id. In re Walt Disney Co. Derivative Litigation* provides an example of a § 220 request that ultimately lead to the acquisition of important facts which persuaded a court to excuse a derivative demand to be made on the corporation's board. In that case, shareholder plaintiffs used the newly gained information to draft a complaint which portrayed the company's directors in a markedly different light. In re Walt Disney Co. Derivative Litig., 825 A.2d 275, 279 (Del. Ch. 2003).

[20] *See, e.g., id.*

[21] Radin, *supra* note 16 at 1288 (citing Seinfeld v. Verizon Communs., Inc., 2005 Del. Ch. LEXIS 185, 5 (Del. Ch. Nov. 23, 2005)).

[22] *See* § 220(b)(2) "Any stockholder . . . shall, upon written demand under oath stating the purpose thereof, have the right during the usual hours for business to inspect for *any proper purpose* . . ." (emphasis added).

[23] James L. Hallowell, *Chancery Court Continues Close Scrutiny in Section 220 Actions*, DEL. BUS. CT. INSIDER (Nov. 28, 2012), http://www.gibsondunn.com/publications/Documents/Hallowell-ChanceryCourtContinuesCloseScrutinyinSection220Actions.pdf. *See also* § 220(b)(2)(b.)(2.). The DGCL describes a proper as any purpose reasonably related to the requester's interest as a shareholder. *Id.*

[24] *See* 2-27 Delaware Corporation Law and Practice § 27.04 (citing Highland Select Equity Fund, L.P. v. Motient Corp., 906 A.2d 156 (Del. Ch. 2006), *aff'd*, 922 A.2d 415 (Del. 2007) ("[A] Section 220 right is bound by a requirement of good faith and lack of abuse . . . . [w]here those factors are in doubt or missing, the court must use its statutory powers to deny relief.")).

Once a shareholder asserts a proper purpose, a court will initiate an inquiry into the scope of the § 220 demand.[25] In addition to scope, the burden of proof shifts to the corporation to explain why the shareholder's purpose is improper.[26] It is well established that a purpose to investigate corporate wrongdoing can be a valid, proper purpose in the context of a § 220 demand.[27]

Documents that are available to shareholders upon a successful demand include: a corporation's stock ledger, a list of stockholders and the corporation's other books and records.[28] While a "book" or "record" may be interpreted broadly, the purpose of a § 220 demand must not be so broad in nature as to constitute a wide range discovery; absent a detailed request for specific information or document(s), Delaware courts are inclined not to enforce a shareholder's general § 220 request.[29] The state's Supreme Court established a standard to this effect: a demand must be particular in nature and specify with "rifled precision" the documents sought. [30] A shareholder will be allowed to inspect the requested documents only upon proof that their demand is both *necessary* and *essential* to achieve the stated purpose.[31] Courts typically consider documents to be necessary and essential when they address the "crux of the shareholder's purpose" and when they

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[25] *See* Saito v. McKesson HBOC, Inc., 606 A.2d 113, 114 (Del. 2002).
[26] *Security First*, 687 A.2d at 570.
[27] *See* City of Westland Police & Fire Ret. Sys. v. Axcelis Techs., Inc., 1 A.3d 281, 285 (Del. 2010) (investigating a board's handling of two acquisition proposals and the refusal to accept the resignations of three directors who failed to receive an affirmative majority vote at an annual meeting); Seinfeld v. Verizon Commc'n, Inc., 909 A.2d 117, 121 (Del. 2006) (investigating mismanagement and corporate waste regarding the compensation of three corporate executives).
[28] § 220 (b)(1).
[29] *See Saito*, 606 A.2d at 114.
[30] *See, e.g.*, Brehm v. Eisner, 746 A.2d 244, 266-67 (Del. 2000) ("Plaintiffs may well have the 'tools at hand' to develop the necessary facts for pleading purposes. For example, plaintiffs may seek relevant books and records of the corporation under Section 220 of the Delaware General Corporation Law, if they can ultimately bear the burden of showing a proper purpose and make specific and discrete identification, with rifled precision, of the documents sought. Further, they must establish that each category of books and records is essential to the accomplishment of their articulated purpose for the inspection.").
[31] *Id.* (emphasis added).

cannot be obtained from another source.[32] Whether or not a specific document is essential to a given inspection by shareholders is necessarily fact dependent, based on the context in which the § 220 demand arises.[33]

In the face of potential derivative litigation, corporations are sometimes unwilling to turn over corporate documents to shareholders.[34] Many shareholders will often need to utilize the courts in order to effectuate § 220 demands.[35] Historically, however, Delaware courts have been wary of granting every request made by shareholders, routinely applying careful scrutiny to the purposes equity holders provide in their demands.[36] Indeed, Delaware courts "have evidenced a somewhat greater willingness to scrutinize the credibility of the stated purpose when the stockholder's demand is for books and records rather than merely a stockholder's list."[37] As such, there is an expanding judicial concern with the potential for expensive and seemingly unnecessary fishing expeditions by shareholders through corporate books and records requests.[38]

Moreover, the Delaware Supreme Court itself has repeatedly emphasized the availability of § 220 claims as a possible "method of securing facts to support a demand futility claim."[39] With the potential for shareholders to acquire sensitive corporate

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[32] Espinoza v. Hewlett-Packard Co., 32 A.3d 365, 371 (Del. 2011).
[33] *Id.* at 372.
[34] *See, e.g., Wal-Mart*, 95 A.3d at 1270 (providing an example of a corporation providing redacted documents to comply with the § 220 demand in the most narrow way possible).
[35] *See, e.g., Saito*, 606 A.2d at 114.
[36] *See e.g.*, La. Mun. Police Employees'. Ret. Sys. v. Lennar Corp., 2012 Del. Ch. LEXIS 230 (Del. Ch. Oct. 5, 2012) (requiring a shareholder to produce "some evidence of possible mismanagement as would warrant further investigation of the matter" when rejecting a shareholder'; Rock Solid Gelt Ltd. v. SmartPill Corp., 2012 Del. Ch. LEXIS 234 (Del. Ch. Oct. 10, 2012) (denying a § 220 demand because the shareholder had not demonstrated a proper purpose within the meaning of § 220 (b)(2)(b.)(2.)).
[37] 2-27 Delaware Corporation Law and Practice § 27.04 (quoting Sutherland v. Dardanelle Timber Co., 2006 Del. Ch. LEXIS 88 (Del. Ch. May 16, 2006)).
[38] James L. Hallowell, *Chancery Court Continues Close Scrutiny in Section 220 Actions*, DEL. BUS. CT. INSIDER (Nov. 28, 2012), http://www.gibsondunn.com/publications/Documents/Hallowell-ChanceryCourtContinuesCloseScrutinyinSection220Actions.pdf.
[39] Beam v. Stewart, 845 A.2d 1040, 1056 n. 51 (Del. 2004).

information, it is unsurprising that some corporations may attempt to comply with the scope of a § 220 demand in the most narrow way possible.

B. Attorney-Client Privilege and the Work-Product Doctrine in the Corporate Context

As a separate legal entity from its shareholders, a corporation enjoys an independent right to protection under the attorney-client privilege as well as the work product doctrine.[40] Critically, the privilege lies with the corporation itself, and not with any officer or employee.[41] When management or control changes occur, the new management has the authority to assert and waive the protection.[42] Both the attorney-client privilege and the work product doctrine advance the same central tenant of efficient administration of fairness and the continuation of the attorney-client relationship.[43]

In Delaware, the courts have enshrined the attorney-client privilege within their evidentiary rules: it begins when a person, public officer, *corporation*, or other organization consults with a lawyer or a person reasonably believed to be an attorney with the purpose of obtaining legal counsel in a confidential setting.[44]

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[40] *See generally*, Jaclulin Aaron & Stephen Marzen, *Feature: Privilege In Corporate Family Representations*, 32 DEL. LAWYER at 20 (2014). *See also* United States v. Louisville & Nashville R.R., 236 U.S. 318, 336 (1915).

[41] Cindy A Shipani, *Article: The Future of the Attorney-Client Privilege In Corporate Criminal Investigations*, 34 DEL. J. CORP. L. 921, 931 (2009).

[42] *See* Commodity Futures Trading Comm'n v. Weintraub, 471 U.S. 343, 349 (1985) ("[W]hen control of a corporation passes to new management, the authority to assert and waive the corporation's attorney-client privilege passes as well. New managers installed as a result of a takeover, merger, loss of confidence by shareholders, or simply normal succession, may waive the attorney-client privilege with the ordinary course, a parent corporation can ultimately control a respect to communications made by former officers and directors.").

[43] Bufkin Alyse King, *Commentary: Preserving the Attorney-Client Privilege in the Corporate Environment*, 53 ALA. L. REV. 621, 622 (2002).

[44] D.R.E. 502(a)(1), (a)(3) (emphasis added).

Both the law and public policy have long held the relationship between an attorney and his/her client to be paramount.[45] Corporations, just like individuals have a general duty to provide any and all testimony in a court preceding which the public has the right to know.[46] Like many facets of the law, these rules are subject to several exceptions.[47] "An exception [to the general rule] is justified if, and only if, policy requires it be recognized when measured against the fundamental responsibility of every person to give testimony."[48] Therefore, the attorney-client privilege is present when: (1) a client; (2) makes a communication; (3) in confidence; (4) to an attorney; (5) for the purpose of seeking legal counsel.[49]

While the attorney-client privilege focuses on the promotion of the client's unfettered access to legal advice in a confidential setting, the work product doctrine promotes the interests of the attorney in the litigation process.[50] In Delaware, the work-product doctrine can be found in Chancery Court Rule 26(b)(3).[51] The protection defends the "mental impressions, conclusions, opinions, and legal theories of lawyers in their work."[52]

The work product protection in Delaware extends quite expansively.[53] Courts commonly apply either the broader "because of litigation" test or the more narrow

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[45] *See generally*, Alexander C. Black, *Determination of Whether a Communication is from a corporate Client for Purposes of the Attorney-Client Privilege – Modern Cases*, 26 A.L.R. 5th 628, 628.
[46] 8 Wigmore, Evidence § 2192 at 70.
[47] *Wal-Mart*, 95 A.3d at 1280. (citing Ct. Ch. R. 26(b)(3)).
[48] 8 Wigmore, Evidence § 2285 at 527.
[49] Richard J. Morvillo, *Upjohn Warnings: Recommended Best Practices When Corporate Counsel Interacts With Corporate Employees*, *in* INTERNAL INVESTIGATIONS 2009: HOW TO PROTECT YOUR CLIENTS OR COMPANY 669, 682 (2009).
[50] Cindy A Shipani, *Article: The Future of the Attorney-Client Privilege In Corporate Criminal Investigations*, 34 DEL. J. CORP. L. 921, 931 (2009).
[51] Ct. Ch. R. 26(b)(3).
[52] Mennen v. Wilmington Trust Co., 2013 Del. Ch. LEXIS 204, at *20-21 (Del. Ch. July 25, 2013)
[53] Carlyle Inv. Mgmt. L.L.C. v. Moonmouth Co. S.A., 2015 Del. Ch. LEXIS 42, at *26 (Del. Ch. Feb. 24, 2015).

"primary purpose" test.[54] Delaware applies the "because of" test.[55] Therefore, protection extends only to a document produced because of litigation.[56] Rule 26(b)(3) permits a party to a suit to overcome work product protection and access to non-opinion work product upon a showing that the party pursuing discovery has "substantial need of the materials in the preparation of the party's case and that the party is unable without undue hardship to obtain the substantial equivalent of the materials by other means."[57] Thus, the outcome of any work-product inquiry necessarily depends upon whether documents sought were created in the first instance.[58] "If the document was created for some other reason, such as a business purpose, then it is likely not protected."[59]

C. The *Garner* Fiduciary Exception

In 1970, the United States Court of Appeals for the Fifth Circuit recognized a fiduciary exception to the attorney-client privilege.[60] The court-created fiduciary

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[54] *Id.*
[55] *Id.*
[56] *Id.*
[57] Rule 26(b)(3) reads in full: "Trial preparation: Materials. -- Subject to the provisions of paragraph (b) (4) of this rule, a party may obtain discovery of documents, electronically stored information, and tangible things otherwise discoverable under paragraph (b)(1) of this rule and prepared in anticipation of litigation or for trial by or for another party or by or for that other party's representative (including the other party's attorney, consultant, surety, indemnitor, insurer, or agent) only upon a showing that the party seeking discovery has substantial need of the materials in the preparation of the party's case and that the party is unable without undue hardship to obtain the substantial equivalent of the materials by other means. In ordering discovery of such materials when the required showing has been made, the Court shall protect against disclosure of the mental impressions, conclusions, opinions, or legal theories of an attorney or other representative of a party concerning the litigation. A party may obtain without the required showing a statement concerning the action or its subject matter previously made by that party. Upon request, a person not a party may obtain without the required showing a statement concerning the action or its subject matter previously made by that person. If the request is refused, the person may move for a Court order. The provisions of Rule 37(a)(4) apply to the award of expenses incurred in relation to the motion. For purposes of this paragraph, a statement previously made is (A) a written statement signed or otherwise adopted or approved by the person making it, or (B) a stenographic, mechanical, electrical, or other recording, or a transcription thereof, which is a substantially verbatim recital of an oral statement by the person making it and contemporaneously recorded." Ct. Ch. R. 26(b)(3).
[58] Carlyle Inv. Mgmt. L.L.C. v. Moonmouth Co. S.A., 2015 LEXIS 42, at *25-26 (Del. Ch. Feb. 24, 2015).
[59] JPMorgan Chase & Co. v. Am. Century Cos., 2013 LEXIS 101, 2013 WL 1668393, at *3 (Del. Ch. 18, 2013).
[60] Garner v. Wolfinbarger, 430 F.2d 1093, 1093 (5th Cir. 1970).

exception applies in derivative lawsuits initiated by the shareholders of a corporation.[61] Although corporations are entitled to the attorney-client privilege when the issue concerns communications between management and its corporate attorney(s), the privilege has not been held absolute where shareholders are seeking to pierce the privilege.[62] Various jurisdictions, both on the state and federal level, adopt the doctrine.[63] In some circumstances, courts extend the doctrine to direct suits such as class actions.[64]

In order for the exception to apply, a shareholder must satisfy a two-part test.[65] First, a shareholder must confirm that a fiduciary-duty relationship actually exists.[66] Second, the shareholder must then show "good cause" for disclosure of the otherwise privileged information.[67] Notably, however, the fiduciary exception does not apply to a corporation's communications concerning the defense of a derivative lawsuit; those communications enjoy a separate and independent right of protection as they pertain to

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[61] Olga Leier, *Fiduciary Exception To The Attorney-Client Privilege: The Rationale Behind The Exception And The Need For Corporate Responsibility Suggest That The Exception Should Apply To Both Derivative And Non-Derivative Actions*, 40 SW. L. REV. 199, 203-04 (2010).

[62] *Id.*

[63] *See, e.g.*, In re PWK Timberland, LLC 2015 Bankr. LEXIS 248 at *6 (Bankr. W.D. La. Jan. 27, 2015); Omega Consulting Group v. Templeton, 805 So.2d 1058, 1060 (Fla. Dist. Ct. App. 2002); Solis v. Bruister, 2013 U.S. Dist. LEXIS 29108, at *9-10 (S.D. Miss. Jan. 22, 2013); Penn, LLC v. Prosper Bus. Dev. Corp., 2012 U.S. Dist. LEXIS 117067, at *34-36 (S.D. Ohio Aug. 20, 2012); Cox v. Administrator United States Steel & Carnegie, 17 F.3d 1386, 1416 (11th Cir. 1994) (application of *Garner* in a union dispute).

[64] *See, e.g.*, RMED Int'l, Inc. v. Sloan's Supermarkets, Inc., 2003 U.S. Dist. LEXIS 71, at *12-21 (S.D.N.Y. Jan. 3, 2003) (class action alleging federal securities laws violation); Moore v. Lender Processing Servs., 2012 U.S. Dist. LEXIS 158387, at *7 (M.D. Fla. Nov. 5, 2012) ("[T]he simple fact that the instant case does not involve a shareholder action is not sufficient to completely disregard the Garner analysis.").

[65] *Garner*, 95 A.3d at 1102.

[66] *Id.*

[67] *See id.* at 1103-04. The court provided a non-exhaustive list of factors that courts could consider in their "good cause" balance test. Leier, *supra* note 42, at 205 (citing *Garner*, 430 F.2d at 1103-04) ("(1) the number of shareholders (plaintiffs) and the percentage of stock they represent; (2) the legitimacy of the claim; (3) the necessity of obtaining the information and its availability from other sources; (3) whether the communication related to the past or prospective action, i.e., whether the communication was part of an ongoing wrongdoing or fraud, or whether the communication related to a defense; (6) whether the communication was for advice concerning the litigation itself; (7) whether the shareholders were "blindly fishing; and (8) the risk of revealing trade secrets and other confidential information.").

the legal defense of corporate management.[68] This is in contrast to communications made concerning the corporate conduct being questioned by shareholders. There the corporation itself holds the attorney-client privilege, not management.[69]

In *Garner,* a group of plaintiff shareholders filed suit against a defendant insurance corporation and its directors over alleged violations of several federal securities laws.[70] While the district court denied the corporation's assertion of the attorney-client privilege protection, the Fifth Circuit disagreed and held that the privilege did apply under both federal and state law.[71] However, the circuit court still held for the plaintiffs, crafting a new judicially-created fiduciary exception to the corporation's attorney-client privilege: when a corporation is accused of acting axiomatically to the interest of shareholders in a derivative action, and relevant information cannot be obtained from another source, the protection of the attorney-client privilege should be restricted.[72]

The court in *Garner* recognized the critical difference between a corporation and an individual when the attorney-client privilege is invoked.[73] Compared to an individual managing his/her own affairs, corporations, their officers, and their directors do not share the same reality: "the beneficiaries of . . . [a corporation's] action are the stockholders" not the corporation itself.[74] The court also recognized the possibility that, in some circumstances, management can have a valid interest adverse to some or all stockholders.[75] However, in the context of a derivative suit, managerial judgment and the

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[68] A yield of the privilege concerning communications in anticipation of derivative litigation would also defeat the adversarial system that courts employ.
[69] Shipani, *supra* note 41, at 931.
[70] *Garner*, 430 F.2d at 1095.
[71] *Id.* at 1098.
[72] *Id.* at 1101.
[73] *Id.*
[74] *Id.* ("[W]hen all is said and done, management is not managing for itself.").
[75] *Id.*

advice they seek from counsel may not hide "behind an ironclad veil of secrecy which under all circumstances preserves it from being questioned by those for whom it is at least in part, exercised."[76]

Ultimately noting the intrinsic nature and structure of corporations themselves and the applicable analogies of historic exceptions to the attorney-client privilege, the *Garner* court crafted what has been termed the "*Garner* Exception" to the attorney-client privilege: where corporate management is engaged in a derivative action against the corporation's shareholders suing on behalf of the corporation, the protection of those specific interests, the public, as well as those of the company require the conclusion that the attorney-client privilege be subject t the right of the shareholders to show cause why it should not be invoked in the particular instance.[77]

The court looked to two traditional exceptions to the attorney-client privilege for guidance: (1) the crime-fraud exception; and (2) the exception for communications by parties to a joint attorney.[78] First, plaintiff shareholders in *Garner* claimed to have been the victims of what they termed "improprieties" in the issuance and sale of the corporation's stock. [79] The improprieties were potentially illegal and thus any communication before or during the commission of those improper actions for the

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[76] The Court also found persuasive two English cases, which advance the notion that there are "obligations, however characterized, that run from corporation to shareholder and must be given recognition in determining the applicability of the privilege. "*See Garner*, 430 F.2d at 1101 (citing Gouraud v. Edison Gower Bell Telephone Co., 57 L.T. Ch. 498 (Eng. 1888); W. Dennis & Sons Ltd. v. West Norfold Farmers' Manure & Chem. Co., 169 L.T. 64 (Eng. 1943). The Court also found persuasive two historical exceptions to the attorney client privilege: communication in contemplation of a crime or fraud and communication to a joint attorney. In those situations, attorney client privilege does not apply because the goals of the privilege and the law itself are frustrated. *See id.* at 1102 (citing Union Camp Corp. v. Lewis, 385 F.2d 143 (4th Cir. 1967); Pollock v. United States, 202 F.2d 281, 281 (5th Cir. 1953); United States v. Bob, 106 F.2d 37, 37 (2d Cir.), cert. denied, 308 U.S. 589, 589 (1939)).

[77] *Garner*, 430 F.2d at 1103-04.

[78] *Garner*, 430 F.2d at 1101.

[79] *Id.* at 1103.

purpose of assisting in the commission of those actions were not privileged.[80] The court recognized that the differences between crime-fraud and "questionable legality" are "differences of degree, not of principle."[81]

Second, in circumstances where an attorney provides counsel to parties with the same interests, neither party may exercise the privilege in a subsequent controversy against one another.[82] In the corporate setting, the attorney acts on behalf of management *and* the shareholders to whom that corporate management, both officers and directors, owe a fiduciary duty. As the corporation's management and shareholders have a "mutuality of interest," and corporate counsel acts on behalf of each, the corporation cannot assert an absolute privilege not to disclose to the shareholders.[83] Thus, the *Garner* Court crafted the fiduciary exception to apply even if the corporate misconduct did not reach the level of criminal or fraudulent conduct.[84]

The *Garner* exception relies on the unique situation that corporations face when embroiled in a derivative suit.[85] Shareholders bring derivative suits, acting on behalf of

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[80] In the intersection of the interests of management, shareholders, and the derivative lawsuit, the court noted that a corporation has a fundamental duty to the stockholders and public to act lawfully. *Id.*

[81] *Id.*

[82] This is the case even when counsel acts jointly for two or more parties having no formal business agreements between them. *Id.* (citing Grand Trunk W.R.R. v. H.W. Nelson Co., 116 F.2d 823, 835 (6th Cir. 1941)); further, this exception applies to many other situtations. *Garner*, 430 F.2d at 1103 (citing Billias v. Panageotou, 76 P.2d 987, 987 (Wash. 1938) (partners); Boyle v. Kemplin, 9 N.W.2d 589, 589 (Wis. 1943) (joint trustors); Hoffman, v. Labutzke, 289 N.W. 652, 57 (Wis. 1940) (insured and insurer in an automobile death action)).

[83] The Fifth Circuit relied on a Colorado case that focused on the relationship between a certified public accountant and his corporate client to make its point. There, the Colorado court found that the joint attorney exception was properly applicable to the invocation of the attorney-client privilege when used in a derivative lawsuit filed by their shareholders. *See Garner*, 430 F.2d at 1103 (citing Pattie Lea, Inc. v. District Court, 423 P.2d 27 (Colo. 1967)).

[84] *Leier, supra* note 61, at 207 (citing *Garner*, 430 F.2d at 1103). This decision however, did not constrain the scope of the exception to prospective criminal action; rather, the court found little weight in the differences between prospective criminal activity and prospective action of questionable legality, or prospective fraud. *Garner*, 430 F.2d at 1103.

[85] Leier, supra note 61, at 208 (citing ARTHUR R. PINTO & DOUGLAS M. BRANSON, UNDERSTANDING CORPORATE LAW 423, 425-27 (2d ed. 2004)).

the corporation.[86] Typically, shareholders commence a derivative suit to address a suspected wrong to the corporation committed by the corporation's management, board or both.[87] Central to a derivative suit is the idea that a corporation, its directors and its officers, owe fiduciary duties to the corporation, and by extension, shareholders.[88]

The issue, therefore, in a derivative suit, is that both the shareholders and the board of directors seek to represent the interests of the corporation.[89] *Garner* represents the notion that it would be axiomatic to deny shareholder plaintiffs access to information or communications which are the impetus for management's actions taken allegedly on behalf of the corporation.[90] Once there is a merging of interest in the corporation — the individual interests of shareholder and of management — the corporation's attorney-client privilege yields to shareholder plaintiffs seeking to represent the corporation's interest in a derivative action.[91]

Unsurprisingly, the *Garner* decision itself has been in controversy ever since the court handed the case down for publication, with many critics arguing the original purpose of the privilege is counteracted.[92] Discussed *infra* in Part III, the concerns that worry some *Garner* critics are equally valid when applied to the *Wal-Mart* decision.

D. Wal-Mart Stores, Inc. v. Ind. Elec. Workers (IBEW)

The specific facts of *Wal-Mart* provide guidance in the analysis of the Delaware Supreme Court's rationale for the recent adoption of the *Garner* exception.

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[86] *Id.*
[87] *Id.*
[88] *Id.*
[89] *Id.*
[90] *Id.*
[91] *Id.*
[92] *See* King, *supra* note 43 at 628. *See, e.g.*, Jack P. Friedman, *Is the Garner Qualification of the Corporate Attorney-Client Privilege Viable after Jaffee v. Redmond?*, 55 BUS. L. 243, 244 (1999).

Wal-Mart Stores, Inc. ("Wal-Mart") is a publicly traded, American-based multinational retail corporation that is headquartered in Bentonville, Arkansas.[93] While the corporation has its headquarters in Arkansas, Wal-Mart remains incorporated under the laws of Delaware.[94] A commercial giant, the company is consistently rated as the number one corporation worldwide in terms of revenue.[95]

Plaintiff Indiana Electrical Workers Pension Trust Fund ("IBEW") is a retirement system that provides benefits during retirement to member electrical workers in the state of Indiana.[96] At the time of the alleged wrongdoing, IBEW was a shareholder of Wal-Mart.[97] Wal-Mart operates stores in Mexico through a subsidiary of the American parent corporation called "Wal-Mart de Mexico" ("WalMex").[98]

In 2012, a former WalMex executive, Sergio Cicero Zapata informed the general counsel of Wal-Mart International,[99] Maritza Munich, of "irregularities" authorized by the WalMex executives, whom he described were at the "highest levels."[100]

Wary of potential violations under United States Federal Law, Munich promptly notified the senior leadership and board of directors of the parent company in the U.S. and then initiated an investigation at their direction.[101] At the urging of an independent firm which Munich retained in order to evaluate the allegations, Munich suggested that

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[93] *Wal-Mart*, 95 A. 3d at 1267.
[94] *Id.*
[95] *See* FORTUNE, http://fortune.com/global500/ (last visited Jan. 23, 2015). Forbes Fortune Magazine lists Wal-Mart Stores, Inc. at the top of its annual Global 500 list. It is estimated that Wal-Mart serves more than 100 million customers worldwide in 26 countries per week.
[96] Wal-*Mart*, 95 A. 3d at 1267; *see also* http://www.ibew.org/.
[97] *Wal-Mart*, 95 A. 3d at 1267.
[98] As the parent company, Wal-Mart Stores, Inc. owns a substantial and controlling interest in WalMex. *Wal-Mart*, 95 A. 3d at 1267.
[99] Wal-Mart operates stores under three main categories: Wal-Mart U.S., Wal-Mart International, and Sam's Club. *See* http://fortune.com/company/wmt/. As a subsidiary operating in a foreign country, WalMex falls under the Wal-Mart International banner.
[100] Barstow, *supra* note 1.
[101] *Id.*; *see also* the FCPA, 15 U.S.C. §§ 78dd-1, et seq.

the U.S. company initiate a "thorough investigation" in order to limit any liability the company might face. Senior leadership, who, instead, opted to conduct a "far more limited" internal, preliminary investigation, rejected this proposal.[102] The Board appointed Roland Hernandez, head of the Board's Audit Committee to supervise the inquiry.[103] Throughout the investigation, Munich informed senior leadership in the United States while Hernandez apprised her of developments via electronic mail and other detailed memoranda.[104]

In December 2005, an internal memo from company investigators to Wal-Mart executives outlined the graveness of the situation: "[t]here is reasonable suspicion to believe that Mexican and USA laws have been violated."[105] Instead of heeding this warning, WalMex executives rebuked the investigators as being what they termed as "overly aggressive."[106] In response, Wal-Mart Executives in the United States then ordered a revised internal investigation protocol.[107] With this new protocol, the supervision of the investigation was transferred to José Luis Rodríguezmacedo, Wal-Mart's general counsel. This move was seen as highly irregular and questionable, as Rodríguezmacedo himself was an early target of the internal investigation.[108] Thereafter, Rodríguezmacedo quickly wrapped up the company's investigation, coming to the conclusion that "[t]here is no evidence or clear indication of bribes paid to Mexican

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[102] Barstow, *supra* note 1.
[103] *Id.*
[104] *Id.*
[105] *Wal-Mart*, 95 A. 3d at 1268.
[106] Barstow, *supra* note 1.
[107] *Wal-Mart*, 95 A. 3d at 1268.
[108] Barstow, *supra* note 1; *see also Wal-Mart*, 95 A. 3d at 1268. Munich resigned soon after this appointment. ("[Munich] complained to senior Wal-Mart executives, noting that 'the wisdom of assigning any investigative role to management of the business unit being investigated escapes me.").

government authorities with the purpose of wrongfully securing any licenses or permits."[109]

After *The New York Times* article was published, the IBEW filed a § 220 demand on Wal-Mart in June 2012 and requested inspection of a number of internal documents in connection with the bribery allegations.[110] IBEW explained that its proper purpose for the § 220 demand centered on seeking information concerning the company's mismanagement of the WalMex allegations, the possibility of a breach of the fiduciary duty of care by Wal-Mart or WalMex's respective corporate management, and to assess the possible futility of filing a pre-derivative suit demand on Wal-Mart's board of directors.[111]

Wal-Mart responded to the inspection request with a limited number of board materials, minutes, agendas, and presentations relating to the allegations published by the *Times* article and the company's policies as they relate to the Foreign Corrupt Practices Act.[112] Critically, however, Wal-Mart refused to provide documents that they claimed were not necessary to IBEW's purpose and those documents they claimed to be covered by the attorney-client privilege and/or work product doctrine.[113]

a. Procedural History

Finding the produced documents unsatisfactory, IBEW filed a complaint with the Delaware Chancery Court in August 2012 citing various issues it held with documents

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[109] *Wal-Mart*, 95 A. 3d at 1268.
[110] *Id.*
[111] *Id.*
[112] At this juncture, Wal-Mart produced well over 3000 documents to the IBEW in response to their § 220 inspection request. This proved limiting, however, because these documents were highly redacted "without any explanation for the redactions." *Id.*
[113] *Id.*

sent by Wal-Mart.[114] Wal-Mart produced additional documents to satisfy the IBEW with less redactions, however IBEW became frustrated and noticed Wal-Mart with depositions of specific Wal-Mart records custodians. In response, Wal-Mart moved for a protective order from the Chancery Court, which it granted in part and restricted the scope of IBEW's inspection request.[115]

Thereafter, IBEW lodged an additional complaint with the court alleging that Wal-Mart did not comply with the court's order to produce documents.[116] Both parties agreed to initiate a § 220 trial with the sole issue for the court's consideration of whether or not Wal-Mart produced all of the documents that were responsive to the § 220 inspection request.[117] The trial's result did not bode well for Wal-Mart: The chancery court issued a final order requiring Wal-Mart to produce all documents in the custody of its record keepers in connection to IBEW's allegations.[118] Invoking the *Garner*

fiduciary exception, the Chancery Court ordered Wal-Mart to produce documents protected by the attorney-client privilege and the work product doctrine: "it's a classic application of *Garner*, because it's a situation where, you know, has there been—I think the shareholders—and I take them—given their role in the thing, I think they've got enough skin in the game to qualify under *Garner*."[119]

b. The Delaware Supreme Court

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[114] *Id.*

[115] Around the same time, IBEW received an anonymous package of whistleblower documents that pertained to the WalMex Investigation. In accordance with ethics guidelines, IBEW's counsel immediately disclosed the documents to Wal-Mart's counsel. *Id.*

[116] *Id.* at 1270.

[117] *Id.* at 1270-71.

[118] *Id.* at 1270. The Court also required Wal-Mart to produce relevant documents which were in possession of Roland Hernandez, former member of Wal-Mart's Board Audit Committee.

[119] *Id.* at 1270-76.

On appeal, Wal-Mart's main argument centered on the position that the Chancery Court abused its discretion when ordering the production of privileged, and therefore protected, documents.[120] Arguing that their production of non-privileged documents satisfied the necessary and proper purpose of IBEW's § 220 demand, Wal-Mart asked the court to reverse the Chancery Court and limit the number discoverable documents.[121] IBEW responded, stating that its derivative action against Wal-Mart was entirely dependent on the release of these privileged documents and that the Court should adopt the *Garner* doctrine.[122]

i. *Garner* Doctrine Adopted

The Court ultimately found for IBEW and explicitly adopted the *Garner* doctrine.[123] Citing two cases, the Court recognized its previous use of the *Garner* doctrine, at least in dicta.[124] According to the Court, the attorney-client privilege 'is not absolute and, if the legal advice relates to a matter which becomes the subject of a suit by a shareholder against the corporation, the invocation may be restricted or denied

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[120] *Id.* at 1274.
[121] *Id.*
[122] "[A] key category of responsive documents essential to [IBEW's] proper purpose are documents concerning the Company's ongoing compliance activities and changes to its operative compliance procedures, such as changes to the Audit Committee's charter. These documents, including documents reflecting changes in the wake of the WalMex investigation, will bear on director and officer knowledge of the investigation, and thus liability. Indeed, Wal-Mart's privilege log confirms that responsive documents exist from September 2005 through at least May 2012." *Id.* at 1274.
[123] *Id.* at 1275-78.
[124] While the Delaware Supreme Court had not adopted the *Garner* exception previously in any context, other lower Delaware courts have done so in a § 220 books and records proceeding. *See* Grimes v. Communications Corp., 724 A. 2d 561 (Del. Ch. 1998); Khanna v. Covad Communs. Group, 2004 Del. Ch. LEXIS 11 (Del. Ch. Jan. 23, 2004); Saito v. McKesson HBOC. Inc., 2002 Del. Ch. LEXIS 125, at *12-13 (Del. Ch. Nov. 13. 2002).

entirely."[125] If there is good cause for the disclosure of privileged communications, the invocation of the privilege would be set aside.[126]

The Court explained that the application of the *Garner* doctrine was justified in the context of § 220 demands and in plenary proceedings.[127] When documents that are sought by a shareholder are unavailable from any other source while at the same time their production is integral to the [shareholder's] ability to assess whether the board wrongfully refused [their derivative suit] demand," [128] the doctrine of attorney-client privilege does not avail the corporation of protection.[129] Although the Court adopted *Garner*, it also made clear that the threshold question in a § 220 demand is whether a document request satisfies a necessary and essential inquiry.[130] Only then may a court consider the merits of a *Garner* fiduciary exception.[131] The question of whether or not a specific document is necessary or essential to a given inspection purpose is fact sensitive and will necessarily depend on the circumstance in which the shareholder's §220 inspection demand arises.[132]

ii. *Garner* Applied

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[125] *Wal-Mart*, 95 A.3d at 1276 (citing Zirn v. VLI Corp., 621 A.2d 773 (citing Valente v. PepsiCo, Inc. 68 F.R.D. 361 (D. Del. 1975))).

[126] *Id.* at 1276-77. The Court also referenced Espinoza v. Hewlett-Packard Co., 32 A. 3d 365 (Del. 2011) in which the Court was presented with the issue of applying the *Garner* doctrine in the context of a § 220 demand. The Court did not have to reach the application of *Garner* in order to craft a holding for that case. Rather, the Court held that the documents requested by the shareholder were not shown to be "essential" to the proper purpose of outlined in the shareholder's § 220 demand. Therefore, the shareholder could not rely on *Garner* because it did not meet the threshold question of essentiality.

[127] *Id.* at 1278 (quoting *Grimes*, 724 A.2d at 569).

[128] *Id.*

[129] *Id.* at 1278 ("Accordingly, the *Garner* doctrine fiduciary exception to the attorney-client privilege is narrow, exacting, and intended to be very difficult to satisfy. It achieves a proper balance between competing legitimate interests.").

[130] *Id.*

[131] *Id.*

[132] *Id.* at 1283; Courts must act with "rifled precision" when crafting orders granting inspection. *Id.* (citing *Brehm*, 746 A.2d at 266-67).

In applying *Garner*, the Court held that the Chancery Court did not abuse its discretion in ordering Wal-Mart's production of protected documents, stating that the order did not include documents or communications containing "advice concerning the litigation itself," but instead information concerning the purported payments to Mexican government officials and the company's internal inquiry.[133]

The Court, addressing the work product doctrine, emphasized that the *Garner* doctrine only applied to information protected by the attorney-client privilege; work-product must be analyzed pursuant to Court of Chancery Rule 26(b)(3).[134] A party may gain access to protected work product only if "the party seeking discovery has *substantial need* of the materials in the preparation of the party's case and that the party is unable without due hardship to obtain the substantial equivalent of the materials by other means."[135] Although this test creates a substantial overlap with the *Garner* doctrine, the Court found that the Chancery Court properly bifurcated the issues and rendered two separate, legitimate dispositions.[136] Approving the lower court's observation that "there is a colorable basis that part of the wrongdoing was in the way the investigation itself was conducted" and that it is "very difficult to find those documents by other means," the Court held that IBEW had met the "substantial need" standard for production of Wal-Mart's work product.[137]

PART III: ANALYSIS OF CHOICE OF LAW CONCERNS & OTHER SECONDARY EFFECTS

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[133] *Id.* at 1280.
[134] *See* Del. Ch. Ct. R. 26(b)(3); *Wal-Mart*, 95 A.3d at 1280.
[135] *Wal-Mart*, 95 A.3d at 1280 (emphasis added).
[136] *Id.* at 1281. "In this case, the record reflects that the Court of Chancery's workd product ruling was properly and solely based upon Rule 26(b)(3) and only referred to the privilege rationale of *Garner* as overlapping with its own separate work product analysis."
[137] *Id.* at 1279-81.

Corporation law in the United States is free flowing: corporations are constantly motivated to consider domestication in other jurisdictions on a somewhat frequent basis.[138] This section focuses on the choice of law implications for shareholder plaintiffs as well as other potential secondary and unintentional effects that may result in the aftermath of the Delaware Supreme Court's decision in *Wal-Mart v. IBEW.*

a. Choice of Law – Forum Shopping Implications

Shareholder plaintiffs who wish to engage in derivative litigation against corporate management should rejoice in Delaware's adoption of the *Garner* doctrine. Sensitive documents that are critical to a shareholder plaintiff's case become potentially available. Forum shopping, however, remains especially important when a shareholder plaintiff decides to initiate her suit.[139]

A shareholder plaintiff may only file suit against a defendant whom the court has personal jurisdiction over.[140] Through its personal jurisdiction, a court exercises authority to make decisions binding on the persons involved in a civil case, including derivative actions.[141] Generally, each state has personal jurisdiction over persons within its territory; thus, no state can exercise personal jurisdiction and authority over persons outside its territory unless such persons manifest some contact with the state.[142] Critically, courts exercising jurisdiction over a state where a corporation is incorporated,

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[138] Depending on the state, the action of transferring an already incorporated entity to a different jurisdiction's corporate law is sometimes called domestication. Other jurisdictions refer to this as a "re-incorporation."

[139] *See generally*, Debra Lyn Bassett, Article, *The Forum Game*, 84 N.C.L. REV. 333, 334 (2006) (addressing strategies of plaintiffs when selecting forums for their claims).

[140] *See* Int'l Shoe Co. v. Wash., 326 U.S. 310, 316 (1945) (citing Pennoyer v. Neff, 95 U.S. 714, 733 (1878) ("Historically the jurisdiction of courts to render judgment . . . is grounded on their de facto power over the defendant's person. Hence his presence within the territorial jurisdiction of a court was prerequisite to its rendition of a judgment personally binding him." *see also* Kate Bonacorsi, Note, *Not at Home with "At-Home" Jurisdiction*, 37 Fordham Int'l L.J. 1821, 1822-23 (2014).

[141] *Id.*

[142] *Id.*

exercise personal jurisdiction over such corporations.[143] Therefore, a shareholder may file a derivative suit in either the state of incorporation or where the defendants (i.e. the corporation or the directors named in the derivative suit) have sufficient contacts.[144]

Shareholder plaintiffs of Delaware corporations must file in Delaware state court in order to assure themselves the availability of the *Garner* doctrine. Failure to do so may result in a jurisdiction refusing to apply the fiduciary exception, regardless of the internal affairs doctrine. The attorney-client privilege in Delaware rests within the state's rules of evidence, rather than Delaware's corporate statutory scheme.[145] Under the internal affairs doctrine, both state and federal courts will apply the substantive corporate law of the jurisdiction where the corporation is incorporated.[146] However, this doctrine typically does not apply to court rules and procedures.[147] Thus, although a plaintiff filing a derivative suit in a jurisdiction will be forced to adhere to the substantive law of the corporation's state of incorporation, the evidentiary rules of the instant jurisdiction will apply.[148]

Take, for example, a corporation based in the state of Florida, but is incorporated (for various reasons) in the state of Delaware. Further assume that a shareholder wishes to address an alleged wrong by filing a derivative suit against the corporation and the shareholder files suit in a Florida state court. The Florida court will apply the law of

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[143] *See Int'l Shoe*, 326 U.S. at 319 ("[T]o the extent that a corporation exercises the privilege of conducting activities within a state, it enjoys the benefits and protection of the laws of that state. The exercise of that privilege may give rise to obligations, and, so far as those obligations arise out of or are connected with the activities within the state, a procedure which requires the corporation to respond to a suit brought to enforce them can, in most instances, hardly be said to be undue.").

[144] If the directors or corporation have sufficient contacts with a jurisdiction, they can be within the personal jurisdiction of that jurisdiction. *See* Burger King Corp. v. Rudzewicz, 471 U.S. 462, 473 (U.S. 1985). An in-depth analysis of when a director or corporation has sufficient contacts with a jurisdiction is beyond the scope of this Note.

[145] *See* Del. R. Evid. 502.

[146] VantagePoint, 871 A.2d at 1112.

[147] *See* Chaplake Holdings, Ltd. v. Chrysler Corp., 766 A.2d 1, 5 (Del. 2001).

[148] *Id.*

Delaware for derivative demand and other corporate law issues. However, the court will apply the evidentiary and privilege rules of Florida, *not* of Delaware. If Florida does not recognize the *Garner* fiduciary exception, a plaintiff may not be able to gain access to privileged information the same way IBEW was able to in the *Wal-Mart* decision. Under such a circumstance, shareholder plaintiffs are much more inclined to file a suit in Delaware state court.

Similarly, defendant boards or officers named in derivative suits may attempt resistance to such a forum selection. One such option for defendants may be a removal to federal court under federal diversity jurisdiction.[149] Things may prove difficult however, as there must be "complete diversity" in order to achieve federal jurisdiction. Federal law provides that in a case with multiple plaintiffs and defendants, "the presence in the action of a single plaintiff from the same State as a single defendant deprives the district court of original diversity jurisdiction over the entire action."[150] In a derivative action, directors and officers named individually in the suit, by their residence in various states, at least in theory, may create the complete diversity necessary for federal diversity jurisdiction. However, boards of multinational corporations often involve dozens of individuals, both foreign and domestic, who may disrupt the completeness of diversity and terminate the ability of federal courts to adjudicate the dispute.[151]

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[149] *See* 28 U.S.C. § 1332(a) for statutory authority on federal diversity jurisdiction. The federal diversity statute also provides that "a corporation shall be deemed a citizen of any state by which it has been incorporated and of the state where it has its principal state of business." Hertz Corp. v. Friend, 559 U.S. 77, 80 (2010). The Court in *Hertz* held that a principal place of business is where the "nerve center" of the corporation exists. This is where the corporation's executive officers direct, control and coordinate. *Id.* at 95.

[150] Exxon Mobil Corp. v. Allapattah Servs., 545 U.S. 546, 553 (2005) (citing Wisconsin Dept. of Corrections v. Schacht, 524 U.S. 381 (1998); Newman-Green, Inc. v. Alfonzo-Larrain, 490 U.S. 826 (1989)).

[151] Wal-Mart, for example, currently has 16 members on their board of directors. These directors reside in various jurisdictions. WAL-MART STORES, INC., *Board of Directors*, http://corporate.walmart.com/our-story/leadership/board-of-directors/ (last visited Apr. 24, 2015).

b. Choice of Law – Incorporation Decisions For Delaware Corporations

Additionally, the *Wal-Mart* decision may incentivize corporations to leave the corporate legal framework of Delaware in search of more favorable jurisdictions. Differences in substantive statutory corporate law have long affected the choices corporations face when they choose jurisdictions to incorporate within.[152]

The statutory structure of a state's corporation law necessitates the existence of an informed choice of law consideration on the part of a corporation. Frameworks regulating corporate issues such as indemnification, insurance, minority shareholder protection, freeze-outs, and majority shareholder rights all require the careful attention and comparison between jurisdictions.[153] As jurisdictions compete for the patronage of firms, a "race-to-the-bottom" ensues.[154]

For example, in contrast to most state jurisdictions, Delaware requires that all domestic corporations pay an annual franchise tax to the state as a requirement of their incorporation.[155] To large corporations, this can be a *de minimus* expense as the tax is capped out at a maximum of $180,000.[156] To both small and micro-cap corporations, however, this can be financially crippling. Thus, smaller corporations will typically have an incentive to incorporate in the state in which they operate rather than Delaware.[157]

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[152] *Id.* at 9.
[153] *Id.* at 10.
[154] *See* Daniel J.H. Greenwood, Article, *Democracy and Delaware: The Mysterious Race to the Bottom/Top*, 23 YALE L. & POL'Y REV. 381, 381 (2005).
[155] Domestic corporations include those who are currently incorporated in the state of Delaware. The Franchise Tax is calculated based on a number of factors. *See* http://corp.delaware.gov/frtax.shtml.
[156] http://corp.delaware.gov/frtax.shtml.
[157] Issues of control also factor into a corporation's decision. The grander the variety of corporate law, choice of law becomes important, especially in a takeover setting.

Just as statutory changes can provoke corporations to leave a jurisdiction, so too can a wide reaching court decision.[158] The history of corporate jurisprudence in Delaware is littered with decisions that have made corporations uneasy in their continued incorporation in that state.[159] Illustrating this principal is the seminal case of *Smith v. Van Gorkom.*[160] In *Van Gorkom*, the Delaware Supreme Court recognized the personal liability of directors for their decision to accept a buyout offer from other entities.[161] Fearful of firms re-incorporating elsewhere, the Delaware General Assembly took steps to reverse the State Supreme Court's decision by enacting § 102(b)(7) in the General Corporation Law.[162] Under the new law, corporations gained the ability to limit the liability of directors in the company's articles of incorporation from liability concerning the fiduciary duty of care.[163]

Delaware corporations are not alone in their concern. The *Garner* exception, although broad in its federal judicial acceptance, remains inconsistently applied by those federal courts.[164] Various courts continue to apply the doctrine to different facts and circumstances, far beyond corporate book and records requests.[165] *Garner* has been applied to a varying amount of situations, including (but not limited to) class actions, individual suits, ERISA[166] claims, corporate bondholders, real estate transactions, union

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[158] *See* Henry N. Butler, Article, *Smith v. Van Gorkom, Jurisdictional Competition, and the Role of Random Mutations in the Evolution of Corporate Law*, 45 WASHBURN L.J. 267, 272 (2006) ("Because many other states closely follow Delaware decisions, Van Gorkam also adversely affected many of Delaware's competitors.").

[159] *See, e.g.*, Cede & Co. v. Technicolor, Inc., 634 A.2d 345 (Del. 1993); Paramount Comn's, Inc. v. QVC Network Inc., 637 A.2d 34 (Del. 1993).

[160] Smith v. Van Gorkom, 488 A.2d 858, 858 (Del. 1985).

[161] *Van Gorkom*, 488 A.3d at 872.

[162] Butler, *supra* note 158, at 274.

[163] *Id.*

[164] Benjamin Cooper, *An Uncertain Privilege: Reexamining Garner v. Wolfinbarger and its Effect on Attorney-Client Privilege*, 35 CARDOZO L. REV. 1217, 1229 (2014)

[165] *Id.* at 1229.

[166] The Employee Retirement Income Security Act (ERISA), Pub. L. 93-406 (1974).

members/officers, and purchasers of stock.[167] In addition, some courts apply the exception to other business entities including general and limited partnerships.[168]

Without correction, the *Wal-Mart* decision stands to have an effect similar to *Van Gorkom* prior to the Delaware legislature's intervention. The application of the *Garner* exception to the corporation's attorney-client privilege creates the potential opportunity for the production of highly sensitive and potentially damaging documents during the course of litigation. Firms will undoubtedly be adverse to such potential liability.

i. Opportunity For Other Jurisdictions

If risk-averse firms choose to leave Delaware and domesticate elsewhere, where would they go? The trend for many firms, at least in recent days, is the State of Nevada.[169] In addition to Nevada having not adopted *Garner*, many commentators point to the extraction of private benefits, the saving of incorporation taxes, and the minimization of litigation costs as the main motivations behind corporate entities choosing to incorporate in the Silver State.[170]

Further, Nevada allows directors and officers to face almost no liability. Compared to Delaware, Nevada provides a great deal more protection from derivative

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[167] *Id.* at 1229 (citing, e.g., In re Int'l Sys. & Controls Corp. Sec. Litig., 693 F.2d 1235 (5th Cir. 1982); RMED Int'l, Inc. v. Sloan's Supermarkets, Inc., 94 Civ. 5587PKLRLE, 2003 WL 41996 (S.D.N.Y. Jan. 6, 2003); In re Pfizer Inc. Sec. Litig., No. 90 Civ. 1260, 1993 WL 561125 (S.D.N.Y. Dec. 23, 1993); Panter v. Marshall Field & Co., 80 F.R.D. 718 (N.D. Ill. 1978); Cohen v. Uniroyal, 80 F.R.D. 480 (E.D. Pa. 1978)).

[168] *See* Cooper, *supra* note 164, at 1230. ("Extending the [*Garner*] exception beyond shareholder suits to circumstances in which there is not a well-established fiduciary relationship between the parties is inherently problematic and inconsistent with the logic of *Garner*."); *see also, e.g.*, Fortson v. Winstead, McGuire, Sechrest & Minick, 961 F.2d 469, 475 n.5 (4th Cir. 1992); Lugosch v. Congel, 219 F.R.D. 220, 229, 242–43 (N.D.N.Y. 2003); Ferguson v. Lurie, 139 F.R.D. 362 (N.D. Ill. 1991).

[169] Michael Barzuza, Article, *Market Segmentation: The Rise of Nevada as a Liability-Free Jurisdiction*, 98 VA. L. REV. 935, 937 (2012).

[170] *See id.* at 937. Nevada claims the nickname the "Silver State." THE NEVADA LEGISLATURE, https://www.leg.state.nv.us/General/NVFacts/.

liability for officers and directors.[171] Three years after the Nevada legislature enacted these additional protections for directors and officers, the state's market share of out-of-state corporations rose nearly twenty-five percent. [172]

c. The Incentive For Covert Attorney Communication

It is easy to review the facts of *Wal-Mart* and justify the Delaware Supreme Court's holding. However, the holding has implications for law-abiding corporations who may consult counsel in the ordinary course of business. Such corporations certainly rely heavily on the assistance of an attorney, now more than ever, to help them comply with the numerous laws and regulations on both a state and federal level.[173] If an employee or officer remains un-assured that any communication will be protected in every circumstance, they will be cautious in providing information. Thus, the purposes of the privilege would not be sustained.[174]

The recognition of the *Garner* fiduciary exception in the context of Delaware shareholder derivative suits will entice corporations, theirs boards, officers and counsel to engage in "covert" attorney communication, lest their interactions be potentially discoverable during litigation. Many courts, including the United States Supreme Court, have rightly noted some of the potential pitfalls of an abrogation of the attorney-client privilege.[175]

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[171] Unlike Delaware's § 102(b)(7) provision, which only allows for companies to opt out of liability for breaches of the duty of care, Nevada law provides for entities to waive out of liability for everything short of actions that constitute "[i]ntentional misconduct, fraud, or a knowing violation of the law." Barzuza, *supra* note 161, at 950-51.
[172] Barzuza, *supra* note 169, at 948-949.
[173] *See* King, *supra* note 43, at 623.
[174] *Id.* at 632.
[175] *See* Upjohn Co. v. United States, 449 U.S. 383, 383 (1981).

Upjohn Co. v. United States presents facts that bear a striking resemblance to the facts of *Wal-Mart*.[176] There, the United States Supreme Court the scope of the corporate attorney-client privilege and work product derived in anticipation of litigation.[177] *Upjohn* centered on a general counsel's internal investigation into reports of company employees bribing foreign officials in order to obtain business permits.[178] The United States government initiated an action against Upjohn, demanding the disclosure of its internal investigation.[179] When Upjohn refused, the government sought an order to produce from the courts.[180]

Both the District Court and the Sixth Circuit upheld the government's demand, holding that a corporation's attorney-client privilege only extended to the "control group" of the company.[181] The Sixth Circuit specifically noted that accepting Upjohn's claim "for broader application of the privilege would encourage upper-echelon management to ignore unpleasant facts and create too broad a 'zone of silence."[182] The Supreme Court reversed, finding that the purpose behind the attorney-client privilege was "to encourage full and frank communication between attorneys and their clients and thereby promote broader public interests in the observance of law and administration of justice."[183] Thus, the Supreme Court in *Upjohn* articulated twin goals of the attorney client privilege: (1) to

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[176] *Id.*
[177] *See* King, *supra* note 43, at 629-30.
[178] *Upjohn*, 449 U.S. at 383.
[179] For the more information on the FCPA, *see supra* note 94. *Id.* at 386.
[180] *Id.* at 388.
[181] *Id.*
[182] *Id.*
[183] *Id.* at 389.

encourage full communication to corporate counsel in order to facilitate sound legal advice; and (2) to encourage corporate compliance with laws and regulations.[184]

The justifications and warnings that the United States Supreme Court expressed in *Upjohn* apply equally to the disposition in *Wal-Mart*. "The first step in the resolution of any legal problem is ascertaining the factual background and sifting through the facts with an eye to the legally relevant."[185] A new fear of the discovery of normally privileged information may entice Delaware firms to engage in covert legal communications, or not communicate at all. Further, corporate counsels may be deterred in their efforts to root out illegal activity through internal investigations, fearing that their findings become discoverable. This is worrisome, especially given the recent increase in financial regulation.[186]

If the discussions between attorney and corporation are subject to a balancing test, how can a client accurately predict the potential protection afforded? A client, in all forms, should be able to rely on the notion that their communications seeking legal advice from counsel will be protected and confidential. Indeed, the *Garner* test is premised on a balancing test that weighs the court's need to discover otherwise privileged communications between lawyer and corporate client against the value of protecting the

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[184] Brian E. Hamilton, *Conflict, Disparity, and Indecision: The Unsettled Corporate Attorney-Client Privilege*, 1997 ANN. SURV. AM. L. 629, 636 (1997).

[185] *Id.* at 390-91. The Court referenced ABA Code of Professional Responsibility, Ethical Consideration 4-1: "A lawyer should be fully informed of all the facts of the matter he is handling in order for his client to obtain the full advantage of our legal system. It is for the lawyer in exercise of his independent professional judgment to separate the relevant and important from the irrelevant and unimportant. The observance of the ethical obligation of a lawyer to hold inviolate the confidences and secrets of his client not only facilitates the full development of facts essential to proper representation of the client, but also encourages laymen to seek early assistance."

[186] *See, e.g.*, Sarbanes-Oxley Act of 2002 ("Sarbanes-Oxley"), PUB. L. 107-204, 107th CONG. (July 30, 2002); *see also*, Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank"), PUB. L. 111-203, 111th CONG. (July 21, 2010).

confidentiality of the communications.[187] Such a test intrinsically counteracts the justifications for the protections afforded by the privilege in the first place. "If the purpose of the attorney client privilege is to be served, the attorney and client must be able to predict with some degree of certainty whether particular discussions will be protected."[188]

IV. CONCLUSION

The *Wal-Mart* decision presents a cautionary story to shareholder plaintiffs, corporate defendants, and corporate attorneys alike. Where there is a credible basis for challenging the adequacy of a corporation's internal investigation, corporate documents and communications can become available for inspection – and, in some cases, result in liability for Delaware firms. It thus becomes critical for plaintiffs to file their derivative actions in Delaware state court. Otherwise, these shareholder plaintiffs may potentially lose the benefits of the *Garner* exception as an advantage in their litigation war chest.

While plaintiffs benefit from the Delaware Supreme Court's decision, Delaware firms will no doubt be opposed to the liability that the *Garner* fiduciary exception creates. The *Wal-Mart* decision yields an important factor for firms to consider when they look to incorporate in Delaware. With states moving towards more standardized corporate legal schemes, firms have their pick of the "corporate law litter." Thus, Delaware is not alone in its expansive legal protection and flexibility. The door is wide open for firms to leave the their traditional home of Delaware and move to other jurisdictions which offer the same corporate protection without the liability of *Garner*.

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[187] Jack P. Friedman, *Is the Garner Qualification of the Corporate Attorney-Client Privilege Viable After Jaffee v. Redmond*, 55 BUS. LAW. 243 (1999).
[188] *Upjohn*, 449 U.S. at 402 (Burger, C.J. concurring).

Finally, given the potential discovery of sensitive corporate documents via the fiduciary exception, firms will be incentivized to engage in covert attorney-client communication. The justifications for the attorney-client privilege are undermined when a corporate client cannot place full confidence in the protected nature of its discussions with its attorney. Moreover, corporate counsels engaged in internal investigations will be deterred in their efforts to confront corporate malfeasance. The motivations of privacy and quick resolution behind a general counsel's inquiry to root out corporate wrongdoing are negated when courts do not protect the fruits of internal investigations they conduct. Generally, such internal investigations are purposed at ensuring a corporation's compliance with the law. The law should encourage such behavior, not inhibit it.