> We reverse because the record reflects insufficient evidence upon which to evaluate the thoroughness of the report or the independence of the receiver's attorney, whose recommendation was accepted by the court. In addition, the record reflects inadequate sworn testimony or evidence from which to make any findings.

Id. at 645. Thus, *De Moya* stands for the principle that the same substantive and procedural standards of review should apply under § 7.12 as govern a motion under § 7.08.

ANALYSIS AND RECOMMENDATION

§ 7.13 Judicial Procedures on Motions to Dismiss a Derivative Action Under § 7.08 or § 7.11

(a) *Filing of Report or Other Written Submission.* Upon a motion to dismiss an action under § 7.08 (Dismissal of a Derivative Action Against Directors, Senior Executives, Controlling Persons, or Associates Based on a Motion Requesting Dismissal by the Board or a Committee) or § 7.11 (Dismissal of a Derivative Action Based Upon Action by the Shareholders), the corporation shall file with the court a report or other written submission setting forth the procedures and determinations of the board or committee, or the resolution of the shareholders. A copy of the report or other written submission, including any supporting documentation filed by the corporation, shall be given to the plaintiff's counsel.

(b) *Protective Order.* The court may issue a protective order concerning such materials, where appropriate.

(c) *Discovery.* Subject to § 7.06 (Authority of Court to Stay a Derivative Action), if the plaintiff has demonstrated that a substantial issue exists whether the applicable standards of § 7.08, § 7.09, § 7.10, § 7.11, or § 7.12 have been satisfied and if the plaintiff is unable without undue hardship to obtain the information by other means, the court may order such limited discovery or limited evidentiary hearing, as to issues specified by the court, as the court finds to be (i) necessary to enable it to render a decision on the motion under the applicable standards of § 7.08, § 7.09, § 7.10, § 7.11, or § 7.12, and (ii) consistent with an expedited resolution of the motion. In the absence of special circumstances, the court should limit on a similar basis any discovery that is sought by the plaintiff in response to a motion for summary judgment by the corporation or any defendant to those facts likely to be in dispute. The results of any

such discovery may be made subject to a protective order on the same basis as under § 7.13(b).

(d) *Burdens of Proof.* The plaintiff has the burden of proof in the case of a motion (1) under § 7.08 where the standard of judicial review is determined under § 7.10(a)(1) because the basis of the claim involves a breach of a duty set forth in Part IV (Duty of Care and the Business Judgment Rule) or because the underlying transaction would be reviewed under the business judgment rule, or (2) under § 7.07(a)(1) (suits against third parties and lesser corporate officials). The corporation has the burden of proof in the case of a motion under § 7.08 where the standard of judicial review is determined under § 7.10(a)(2) because the underlying transaction wouid be reviewed under a standard other than the business judgment rule, except that the plaintiff retains the burden of proof in all cases to show (i) that a defendant's conduct involved a knowing and culpable violation of law, (ii) that the board or committee as a group was not capable of objective judgment in the circumstances as required by § 7.09(a)(1), and (iii) that dismissal of the action would permit a defendant or an associate [§ 1.03] thereof to retain a significant improper benefit under § 7.10(b). The corporation shall also have the burden of proving under § 7.10(b) that the likely injury to the corporation from continuation of the action convincingly outweighs any adverse impact on the public interest from dismissal of the action. In the case of a motion under § 7.11 (Dismissal of a Derivative Action Based Upon Action by the Shareholders), the piaintiff has the burden of proof with respect to § 7.11(b), (c), and (d), and the corporation has the burden of proof with respect to § 7.11(a).

(e) *Privilege.* The plaintiff's counsel should be furnished a copy of related legal opinions received by the board or committee if any opinion is tendered to the court under § 7.13(a). Subject to that requirement, communications, both oral and written, between the board or committee and its counsel with respect to the subject matter of the aetion do not forfeit their privileged character, and documents, memoranda, or other material qualifying as attorney's work produet do not become subject to discovery, on the grounds that the action is derivative or that the privilege was waived by the pro-

duction to the plaintiff or the filing with the court of a report, other written suhmission, or supporting documents pursuant to § 7.13.

Comment:

a. Comparison with existing law. Although a number of decisions place the burden on the corporation to demonstrate the adequacy of the procedures used by, and the independence of, the board or committee, § 7.13(d) allocates the burden of proof te the corporation under § 7.10 only in those cases that would not be reviewed under the standard of the business judgment rule. This is consistent with the adoption of a "universal demand" standard because those jurisdictions that place the burden on the corporation would not require the use of a committee procedure in instances when demand would be required. Instead, the board's refusal to sue would be often protected by the business judgment rule.

Fewer cases have dealt with issues of discovery, but § 7.13(c) is consistent with the practice in those jurisdictions that permit the court to assess the merits of the action. Even fewer decisions have considered the issues of privilege and work product in this context, but § 7.13(e) is supported by recent federal decisions.

b. Implementation. Section 7.13 can be implemented by judicial decision.

c. Discovery. Section 7.13(c) provides for a set of procedures under which the plaintiff can obtain limited discovery under defined circumstances, but the corporation is protected against abusive or dilatory discovery requests that seek to give a derivative action a nuisance value independent of its merits. The restrictions on discovery in § 7.13(c) reflect the basic purpose of § 7.08: namely, an early screening mechanism to filter out actions having little prospect of benefiting the corporation. It would defeat the purpose of this procedure if the plaintiff could stretch out the proceeding or otherwise engage in fishing expeditions through expansive discovery requests that made a low-cost settlement preferable to the corporation. Decisions have generally recognized that stricter restrictions on plaintiffs' discovery requests are appropriate in the context of the derivative action than in other cases. See, e.g., Segan v. Dreyfus Corp., 513 F.2d 695 (2d Cir.1975); Segal v. Gordon, 467 F.2d 602 (2d Cir.1972). Under the test fashioned by the New York courts, before the plaintiff in the derivative action may receive extensive discovery, "there must appear a basis for inquiry on the face of the complaint, established by factual allegations of evidentiary value." See Resnick v. Karmax Camp Corp., 112 A.D.2d 206, 491 N.Y.S.2d 692, 693–94 (2d Dept.1985). Section

7.13(c) takes a position that is similar to these New York decisions. See Reportor's Note 2.

At the same time, a number of decisions have held that before summary judgment is granted for the defendants, the plaintiffs in a well-pleaded action should normally receive some opportunity to obtain discovery from the corporation and the defendants. As these cases have acknowledged, "plaintiff's proof must come mainly from sources largely within the control of the defendants and from the mouths of the alleged wrongdoers." See Alabama Farm Bureau Mut. Casualty Co., Inc. v. American Fidelity Life Ins. Co., 606 F.2d 602, 609 (5th Cir.1979). In short, even meritorious actions often cannot be successfully prosecuted without discovery because the plaintiff typically lacks access to the information that the defendants possess. Thus, to strike a sound balance, § 7.13(c) interposes the court between the plaintiff and the defendants and subjects all requests for discovery te prior judicial approval. Before granting a request for discovery under § 7.13(c), the court must determine that the following conditions have been satisfied: (1) the plaintiff has shown "that a substantial issue exists whether the applicable standards of § 7.08, § 7.09, § 7.10, § 7.11, or § 7.12 have been satisfied," (2) the "plaintiff is unable without undue hardship to obtain the information by other means," and (3) the discovery is "necessary to enable [the court] to render a decision on the motion under the applicable standards of § 7.08, § 7.09, § 7.10, § 7.11, or § 7.12."

Even when these conditions are satisfied, the court should further determine that the requested discovery is "consistent with an expedited resolution of the motion." Thus, if the requested discovery seems overbroad or unfocused, the court should narrow its scope by specifying those issues as to which depositions or interrogatories will assist the court in reviewing the board's or committee's determinations. Also, it is appropriate for the court to set time limits, to limit multiple or redundant depositions, and to ensure that efficient use is made of less costly techniques, such as written interrogatories. In particular, the court should consider reasonable measures to reduce the burden of discovery on disinterested directors, such as by limiting the number of interrogatories and permitting their depositions only after less intrusive methods of discovery have first been adequately utilized.

In determining whether to permit discovery and the extent thereof, the court should consider, among other factors, the degree of particularity with which plaintiff's allegations are framed, whether the plaintiff has proffered any information that corroborates these allegations, and whether the plaintiff has identified any

specific deficiencies in the board's or committee's report or other written submission that merit discovery. An implication of § 7.13(c) is that when the plaintiff applies to the court to take discovery, it will need to submit not only a specific and limited discovery plan, but also a pleading or memorandum that is responsive to the board's or committee's determinations, indicating with particularity any respects in which the determinations of the board or committee fail to meet the requirements of § 7.10, such as by not being "based on grounds that ... warrant reliance," if required by § 7.10(a)(2).

Section 7.13(c) does not require an evidentiary hearing, but the use of such a hearing is within the sound discretion of the court. Instances will arise when the conflicting views of experts or other witnesses can be most efficiently tested through cross-examination. As always, however, control of such hearings remains with the court and the scope of any such hearing should be focused on the criteria of §§ 7.08 and 7.10.

Section 7.13(c) does not adopt the distinction made in some cases that permits discovery as to the independence of a litigation committee or the adequacy of its procedures, but precludes discovery as to the merits of the action. See Reporter's Note 2. Rather, § 7.13(c) conditions the plaintiff's ability to obtain discovery on the court's need for information "necessary to enable it to render a decision on the motion under the applicable standards of § 7.08, § 7.09, § 7.10, § 7.11, or § 7.12." No implication is intended by this phrase that discovery as to the merits will usually be necessary. The burden is on the plaintiff to show not simply that there are legitimate factual issues, but that these issues should affect the court's judgment. Thus, even when plaintiff has made a strong factual showing as to weaknesses in the board's or committee's report or other written submission, the court may still find that adequate justifications for dismissal of the action have been advanced that are independent of the merits of the action and that have not been effectively controverted by the plaintiff.

In cases where there is a substantial issue as to self-dealing or where a significant improper benefit has been retained so as to trigger § 7.10(b), the critical inquiry will normally focus on the action's merits. To the extent that the board's or committee's determinations depend to a material degree on an assessment of the action's merits, some discovery as to the action's merits is more likely to be justified, once the requisite showing under § 7.13(c) is made by the plaintiff. In such cases, there is little reason to give a board or litigation committee the exclusive right to develop evidence

as to the merits, particularly once the plaintiff has demonstrated inadequacies in its report.

In cases where the board or the litigation committee advances business justifications for dismissal that are independent of the merits of the action, merits discovery may not be necessary, but discovery as to these justifications, which often are conclusory in character, may be appropriate. Accordingly, the court may in its discretion limit discovery to these justifications or, alternatively, may require that the plaintiff make a showing of specific need before granting discovery relating to the merits of the action.

Section 7.13(c) also provides that, in the absence of special circumstances, the court should limit, on a similar basis, any discovery that is sought by the plaintiff in response to a motion for summary judgment by the corporation or any defendant. The court may determine that special circumstances exist when the plaintiff, against whom summary judgment is sought, although lacking admissible evidence to resist the motion, makes particularized allegations in the complaint or particularized statements in an affidavit from which it appears to the court that the plaintiff can produce evidence sufficient to resist the motion if discovery is allowed. In such a case, discovery should be limited to that evidence. More generally, discovery by all parties should be limited to facts involved in directly establishing or directly controverting the elements of a claim under Parts IV–VI.

d. Burden of proof with respect to procedures. Subsection (d) of § 7.13 allocates the burden of proof applicable to a motion to dismiss. Section 7.13(d) draws a basic distinction consistent with the general philosophy underlying these Principles: When the claim is that the defendants breached the duty of care (or the transaction is otherwise protected by the business judgment rule), the burden is placed on the plaintiff. When the action is against third parties or lower-echelon corporate officials and is therefore covered by § 7.07(a)(1), the burden of persuasion similarly falls on the plaintiff. Only in cases involving alleged breaches of the duty of fair dealing by senior corporate officials, directors, and controlling persons does the burden of persuasion fall on the corporation. Even then, that burden is simply to show that under § 7.10(a)(2) the board or committee "reasonably determined that dismissal was in the best interests of the corporation." This burden does not necessitate proof of the intrinsic fairness of the transaction.

Even when the burden of persuasion falls on the corporation to show the reasonableness of the board's or committee's conclusions, the burden of persuasion remains on the plaintiff with respect to

allegations (1) that defendants engaged in a knowing and culpable violation of law, (2) that the board or committee was not capable of "objective judgment in the circumstances" as required by § 7.09(a)(1), and (3) that dismissal of the action would permit a defendant or an associate to retain a significant improper benefit under § 7.10(b). In these instances, it is impractical to ask the corporation to prove, for example, that the defendants made full disclosure or that the defendants did not engage in illegal behavior, because in essence this would require the corporation to prove a negative.

Under the procedure required by § 7.13(a), a "report or other written submission" will have been filed with the court. This report or other written submission should describe the review and evaluation that the board or committee undertook pursuant to § 7.09(a)(3) and should under § 7.09(a)(4) set forth the board's or committee's "determinations in a manner sufficient to enable the court to conduct the review required under § 7.10." Although a number of decisions have placed the burden on the corporation to establish the independence of committee members (see Reporter's Note 1), these decisions were not in the context of a "universal demand" regime, and thus § 7.13 does not require the board's or committee's report affirmatively to establish the independence of its members.

e. Disclosure and the attorney-client privilege. The cases have recognized a potential exception to the attorney-client privilege when an action is derivative, on the ground that the plaintiff is seeking to represent the client and the privilege may not be asserted by the attorney against the client. See Garner v. Wolfinbarger, 430 F.2d 1093 (5th Cir.1970), cert. denied, 401 U.S. 974, 91 S.Ct. 1191, 28 L.Ed.2d 323 (1971); Valente v. Pepsico, Inc., 68 F.R.D. 361 (D.Del.1975). This doctrine does not deem the privilege to be unavailable; it simply permits the plaintiff to show "good cause" why the privilege should not be applied against him or her. *Garner* specified nine criteria that the court should balance in making this good cause determination, and virtually all subsequent cases have adopted these factors. Two of these factors are: "whether the communication is of advice concerning the litigation itself" and "whether the communication related to past or prospective actions." 430 F.2d at 1104. Those decisions that have found "good cause" to pierce the veil of the attorney-client privilege have involved communications that were roughly contemporaneous with the events giving rise to the litigation. Courts appear uniformly to have refused to subject post-event atterney-client communications to disclosure, particularly those communications advising with re-

spect to a pending litigation. See Reporter's Note 3. In this light, there is no conflict between the position taken in § 7.13(e) and the *Garner* line of cases. Section 7.13(e) provides that the special counsel's communications with the board or committee with respect to a pending litigation shall be privileged and not subject to plaintiff's inspection, except as provided in § 7.13(a), which only requires disclosure to the plaintiff of the report or other written submission to the court and any supporting documentation. The position of counsel to a board or a litigation committee considering a demand or a derivative action is substantially different from that of a general counsel or other corporate attorney who is giving advice with respect to a prospective transaction. The special counsel has undertaken to serve only a narrowly defined client—the disinterested members of the board, or a litigation committee—and counsel's communications uniquely relate to the appraisal of the pending litigation. Moreover, the functioning of the disinterested members of the board or the litigation committee might be severely hampered if communication between them and their counsel could not be conducted with reasonable candor and confidence on both sides.

Submission of the board's or committee's report or other written submission to the court waives the privilege as to such documents and, to a more limited extent, as to the process of their preparation. The established law of the attorney-client privilege has long provided that invocation of the reliance-on-counsel defense waives the privilege. See Reporter's Notes 3–5. Thus, it would be unfair if the board or committee could rely on legal advice from its counsel that the action was not meritorious as a ground for dismissing the action and then deny plaintiff access to the substance of that advice. Accordingly, § 7.13(e) requires the disclosure of any formal opinion (including an oral opinion summarizing written advice) or other written legal advice given by counsel to the board or to the committee with regard to the action if any legal opinion is tendered to the court. The decision belongs to the corporation whether to submit such an opinion to the court, but once one is tendered, all other formal legal opinions (including those in draft or oral form) given to the board or committee and pertaining to the same general subject matter must be given to the plaintiff. This rule is intended to discourage opinion shopping without chilling the board's or committee's access to confidential legal advice. Otherwise, absent special circumstances, the plaintiff should not be permitted to depose the counsel or to reconstruct the dialogue between the board or the committee and its counsel. To the extent that under the prevailing law in a jurisdiction the attorney-client privilege is waived by the submission of the attorney's opinion or

other report to the court (see Reporter's Note 5), the goal of protecting counsel te the board or committee from non-essential discovery can also be achieved under § 7.13(c), rather than § 7.13(e). Under § 7.13(c), "limited discovery" is available only to the extent "necessary to enable ... [the court] to render a decision on the motion" and only if it is "consistent with an expeditod resolution of the motion." In applying this discretionary power to grant discovery, the court should disfavor depositions or other discovery of the board's or committee's counsel, at least with respect to such attorney's representation of the board or committee regarding the instant litigation, beyond discovery concerning formal opinions when such an opinion is tendered to the court.

Section 7.13(e) also addresses the problem of waiver as it applies more generally to third parties, including the press. In Joy v. North, 692 F.2d 880, 893 (2d Cir.1982), the Second Circuit stated in broad terms that "a motion for judgment based on the [litigation committee's] report waives the privilege" even as to the public. This rule, however, may produce a serious dilemma for the corporation: if it seeks to terminate the action, it must disclose the confidential data whose sensitive nature constituted the very basis for finding the action adverse to the corporation's interests. Also, disclosure to the public may subject the corporation itself to suit; for example, the data may suggest corporate liability for a past failure to disclose material information under the federal securities laws. Thus, to protect its officials, the corporation might be required to expose itself to liability.

As a justification for this rule, *Joy v. North* pointed to the effect on investor confidence of a contrary rule:

> We simply do not understand the argument that derivative actions may be routinely dismissed on the basis of secret documents. We cannot say what the effect on investor confidence would be if special litigation committees were routinely allowed to do their work in the dark of night.

692 F.2d 880, 893.

This understandable concern does not, however, justify a complete waiver of the privilege. In a more recent and narrower decision dealing with the same fact pattern, the Seventh Circuit declined to find that submission of the litigation committee's report to the court waived the privilege. However, the court did conclude that the normal presumption of public access to court records implies that "special litigation committee reports used in the adjudication stages of derivative litigation should be available for public inspection, unless exceptional circumstances require confidentiali-

ty." In re Continental Illinois Securities Litigation, 732 F.2d 1302, 1314 (7th Cir.1984). The Seventh Circuit recognized that public disclosure might jeopardize important corporate interests, but suggested "that procedures can be developed whereby these interests can be accommodated." Id. at 1316. In a footnote, the court suggested that this accommodation might be achieved by "editing out portions of the Report that might be particularly sensitive." Id. at 1315 n.21. Although § 7.13 contains no black letter provision on this point, the Seventh Circuit's position is consistent with its general approach. The court could excise confidential matter under § 7.13(b), but still disclose the substance of it on a "generic" basis, much as the Securities and Exchange Commission has permitted disclosure of the fact that questionable payments were made, along with their approximate amount, but without requiring specific disclosure of sensitive details.

Section 7.13(a) gives greater information to the plaintiff than need be publicly disclosed, both because the plaintiff has a direct interest and because the plaintiff can be made subject to a protective order. When necessary, disclosure of confidential material under § 7.13(b) can be limited to the plaintiff's attorneys. Also, under the combined effect of § 7.13(b) and (c), no waiver of the privilege need result with respect to other actions brought by a third party against the corporation (such as, for example, a class action for damages under the federal securities laws).

f. The work product doctrine. Section 7.13 recognizes the applicability of the work product doctrine to derivative litigation. See Reporter's Note 5. The work product doctrine creates a qualified immunity from disclosure, rather than an absolute privilege, in order to ensure a zone of privacy for attorneys and their clients to prepare their case for litigation. See, e.g., United States v. Nobles, 422 U.S. 225, 238, 95 S.Ct. 2160, 2170, 45 L.Ed.2d 141, 153 (1975); Hickman v. Taylor, 329 U.S. 495, 67 S.Ct. 385, 91 L.Ed. 451 (1947). Discovery is permitted when the party seeking discovery can show "substantial need" for the materials and that the party is unable "without undue hardship to obtain the substantial equivalent of the materials by other means." Fed. R. Civ. P. 26(b)(3). However, in Upjohn Co. v. United States, 449 U.S. 383, 101 S.Ct. 677, 66 L.Ed.2d 584 (1981), the Supreme Court held that material that reflected counsel's mental processes, such as notes and memoranda related te the interview of witnesses, could not be obtained merely because of the adversary's inability te obtain equivalent material without undue hardship. Id. at 400–402. The rationale for this nearly absoluto standard of protection has been that the work product doctrine is intended less to protect privileged communica-

tions than to maintain the vitality of the adversary system. See also In re Sealed Case, 676 F.2d 793, 809 (D.C.Cir.1982); United States v. AT & T, 642 F.2d 1285, 1299 (D.C.Cir.1980). Such a broader purpose in turn implies that, in the context of an investigation under § 7.09, the work product doctrine should not be subject to waiver under the *Garner* exception to the attorney-client privilege simply because the action is derivative, and cases have so held. See Reporter's Note 4. In the typical intornal corporate investigation that is conducted with respect to a derivative action, the special counsel to the litigation committee may interview dozens of witnesses. If the resulting interview notes and other memoranda were subject to discovery (subject only to the attorney/client privilege), the special counsel would be severely hampered in gathering or reporting facts to the litigation committee or in estimating the probable value of the litigation. For the litigation committee to conduct a thorough investigation, it must of necessity rely on its counsel, and counsel's effectiveness depends in substantial measure on the availability of the work product doctrine. Thus, counsel's notes, internal drafts, correspondence with witnesses, and similar materials should normally be protected from disclosure under the work product doctrine, regardless of the availability of the attorney-client privilege.

REPORTER'S NOTE

1. For decisions holding that the corporation bears the burden of proving the independence of the committee members and the adequacy of the procedures employed, see, e.g., Zapata Corp. v. Maldonado, 430 A.2d 779, 788 (Del.1981); Will v. Engebretson & Co., 213 Cal. App.3d 1033, 261 Cal.Rptr. 868, 872-73 (1989); Rosengarten v. Buckley, 613 F.Supp. 1493 (D.Md. 1985); Auerbach v. Bennett, 47 N.Y.2d 619, 625, 634, 419 N.Y.S.2d 920, 923, 929, 393 N.E.2d 994, 997, 1002 (1979); Holmstrom v. Coastal Ind., Inc., 645 F.Supp. 963, Fed. Sec. L. Rep. (CCH) ¶ 91,486 (N.D.Ohio 1984); Stein v. Bailey, 531 F.Supp. 684 (S.D.N.Y.1982) ("strong evidence" of the litigation committee's independence must be shown). Although agreement exists that the burden is on the corporation, there is less consensus about whether a presumption of independence applies to committee members. Some decisions read *Auerbach* as expressing such a presumption, while others do not. See DeMott, Shareholder Derivative Actions: Law and Practice, § 5.06, p. 99 (1991 Cum. Supp.). Nor is there agreement about the nature of the showing that will satisfy this burden. Few decisions have had to face this issue squarely, because most cases have involved directors who were not defendants in the action and who had no close business or personal relationships with the defendants. See, e.g., Auerbach v. Bennett, 47 N.Y.2d 619, 625, 419 N.Y.S.2d 920,

923, 393 N.E.2d 994, 997 (1979); Zapata Corp. v. Maldonado, 430 A.2d 779, 781 (Del.1981); Abella v. Universal Leaf Tobacco Co., 546 F.Supp. 795, 800 (E.D.Va.1982); Gall v. Exxon Corp., 418 F.Supp. 508, 510 n.2 (S.D.N.Y.1976). However, where a member of the litigation committee had a long-time association with a principal defendant, although one that did not rise to the level covered by § 1.23's definition of "interested," the Delaware Chancery Court found that the committee's report had to be rejected because the corporation had not shown this director to be "independent." Lewis v. Fuqua, 502 A.2d 962, 967 (Del.Ch.1985). In contrast, one federal district court decision has taken a seemingly more relaxed attitude to such potential conflicts by adopting a "direct benefit" test, under which a director who voted to approve a self-dealing transaction, but who received no benefit from it, could serve on the committee. See Lewis v. Anderson, 615 F.2d 778, 783 (9th Cir.1979), cert. denied, 449 U.S. 869, 101 S.Ct. 206, 66 L.Ed.2d 89 (1980). The facts of *Lewis* involved, however, only one director out of three who was subject to such a potential conflict because of his potential liability as a non-benefiting participant in the prior transaction.

In contrast to *Lewis*, the Sixth Circuit in Hasan v. CleveTrust Realty Investors, 729 F.2d 372 (6th Cir. 1984), concluded that "a presumption against independence" might be justified:

> The problems of peer pressure and group loyalty exist *a fortiori* where the members of a special litigation committee are not antagonistic, minority directors, but are carefully selected by the majority directors for their advice. Far from supporting a presumption of good faith, the pressures placed upon such a committee may be so great as to justify a presumption against independence.

Id. at 377. See also Joy v. North, 692 F.2d 880, 888 (2d Cir.1982).

Section 7.13(d) avoids an either/or approach to the question of the burden of proof, by separately allocating the burden on specific issues. In duty of care cases, the burden is placed on the plaintiff, while in some duty of fair dealing cases, it rests partially on the defendants, except that the burden on some special issues—such as the existence of a "knowing and culpable violation of law" or the inability of directors to be "capable of objective judgment"—also rests on the plaintiff. This allocation reflects both the difficulty facing the defendants of proving a negative (i.e., that one did not commit a crime or was not incapable of exercising objective judgment) and the lower probability of these factors applying in the typical case. Also, the allocation of the burden to the plaintiff in duty of care cases is intended to avoid any incentive to bring these cases in the belief that the burden of proof would lead defendants to settle easily.

2. Jurisdictions currently differ on the degree of discovery they will permit prior to the resolution of the court's decision on the board's or committee's report. In New York, plaintiffs may inquire at this stage only into the independence and good faith of the committee and the adequacy of its investigative procedures and methodologies. See Par-

koff v. General Tel. & Electronics, 53 N.Y.2d 412, 442 N.Y.S.2d 432, 425 N.E.2d 820 (1981); Rosen v. Bernard, 108 A.D.2d 906, 485 N.Y.S.2d 791 (2d Dept. 1985) (granting "limited issue hearing" on independence and procedures and permitting discovery in connection therewith); General Electric Co. v. Rowe, 1991 WL 111173 (E.D. Pa. June 18, 1991). Delaware distinguishes between the "demand required" and "demand excused" contexts, and in the latter context allows for discovery that may inquire into the reasonableness of the committee's conclusions. See Kaplan v. Wyatt, 484 A.2d 501, 510 (Del.Ch. 1984), aff'd, 499 A.2d 1184 (Del. 1985); Peller v. The Southern Co., 707 F.Supp. 525 (N.D.Ga.1988), aff'd 911 F.2d 1532 (11th Cir.1990). In "demand refused" cases, Levine v. Smith, 591 A.2d 194, 208–10 (Del. 1991), seems to hold that discovery is inappropriate, although this has been questioned by a later decision. See Zitin v. Turley, 1991 WL 283814, 1991 U.S. Dist. LEXIS 10084 (D. Ariz. June 20, 1991). Federal decisions have generally been more liberal about granting discovery. See Joy v. North, 692 F.2d 880, 889 (2d Cir.1982); Zitin v. Turley, supra; Farber v. Public Service Company of New Mexico, Fed. Sec. L. Rep. (CCH), ¶ 96,106 (D.N.M. 1991). *Zitin*, for example, reasoned that even if discovery was normally premature in a demand refused case, it could be appropriate once the corporation moved for summary judgment based on the report.

Even those courts that have held substantive judicial review of the board's or committee's determinations to be generally available have, however, recognized the need for meaningful limits on the plaintiff's ability to obtain discovery. Thus, on remand following the North Carolina Supreme Court's decision in *Alford v. Shaw*, supra, the trial court required the plaintiffs to file a written statement of the issues plaintiffs planned to contest at the hearing held to consider the litigation committee's recommendations. In approving such a procedure for focusing the issues and limiting discovery, the appellato court noted that the hearing might otherwise have turned into "an unmanageably chaotic theater of accusations." Alford v. Shaw, 327 N.C. 526, 398 S.E.2d 445, 457 (1990).

3. The status of the attorney-client privilege and of work product in derivative litigation continues to be disputed. Following its decision in Garner v. Wolfinbarger, 430 F.2d 1093 (5th Cir.1970), the Fifth Circuit revisited the same issues in Ward v. Succession of Richard W. Freeman, 854 F.2d 780 (5th Cir.1988), and again held that "in litigation involving a corporation and its shareholders, the shareholders may have access to otherwise privileged information after a showing of good cause," because "shareholders stand in the shoes of a client when management seeks counsel on matters that ultimatoly should benefit shareholder interests." 854 F.2d at 784, 785. *Ward* identified the following non-exclusive factors for determining when good cause exists to waive the privilege in favor of shareholders:

> The number of shareholders and the percentage of stock they represent; the bona fides of the shareholders; the nature of the shareholders' claim and whether it was obviously colorable; the

> apparent necessity or desirability of the shareholder having the information and the availability of it from other sources; whether, if the shareholders' claim is of wrongful action by the corporation, it is of action criminal, or illegal but not criminal, or of doubtful legality; ... whether the communication is of advice concerning the litigation itself; the extent to which the communication is identified versus the extent te which the shareholders are blindly fishing; tbe risk of revelation of trade secrets or other information in whose confidentiality the corporation has an interest for independent reasons.

854 F.2d at 784 (citing Garner v. Wolfinbarger, 430 F.2d at 1104). *Garner*'s good faith exception to the privilege in a derivative action "has become accepted doctrine." See In re Sunrise Sec. Litig., 130 F.R.D. 560, 567 (E.D.Pa.1989); Helt v. Metropolitan Dist. Comm'n, 113 F.R.D. 7, 9–10 (D.Conn.1986). Some decisions have placed special emphasis on evidence showing a meritorious cause of action, declining to find good cause to waive the privilege even when the other factors were present "in the absence of a stronger showing of breach of fiduciary duty." See Gerrits v. Brannen Banks of Florida, Inc., 138 F.R.D. 574, 579 (D.Colo.1991). Notwithstanding *Garner*, some decisions have also recognized a privileged status for internal evaluation studies that were prepared after the termination of the events giving rise to the litigation. See In re LTV Securities Litigation, 89 F.R.D. 595, 608 (N.D.Tex.1981); In re Dayco Corp. Derivative Securities Litigation, 99 F.R.D. 616, 620 (S.D.Ohio 1983).

4. Case law has consistently held that when a defendant in litigation seeks to invoke the defense of reliance on the advice of counsel, this invocation waives the privilege. See Panter v. Marshall Field & Co., 80 F.R.D. 718 (N.D.Ill.1978); Broad v. Rockwell International Corp., Fed. Sec. L. Rep. (CCH), ¶ 95,894 (N.D.Tex.1977); Haymes v. Smith, 73 F.R.D. 572 (W.D.N.Y.1976); Garfinkle v. Arcata National Corp., 64 F.R.D. 688 (S.D.N.Y.1974). Because a special litigation committee inherently relies on its counsel in assessing the merits of litigation, an overly aggressive reading of this exception to tbe attorney-client privilege could render the privilege inapplicable to the litigation committee as a practical matter. Some decisions have approached this result by broadly inferring waiver. See Zitin v. Turley, Fed. Sec. L. Rep. (CCH), ¶ 96,123 (D.Ariz. June 20, 1991). ("By filing its motion for summary judgment based on the report of the committee, the corporation has waived any claims of privilege and any work product immunity to the extent that counsel communicated the information or documents to the committee"). *Zitin* also found the practice of conducting the investigation under the supervision of counsel so as to claim the protection of the privilege and work product immunity "to be an indication of the lack of good faith of the Committee and Counsel in investigating the allegations." Id. at ¶ 90,684. See also Peller v. The Southern Co., 707 F.Supp. 525, 529 (N.D.Ga.1988), aff'd, 911 F.2d 1532 (11th Cir.1990). In contrast, to achieve a sensible compromise be-

tween the rule and its most important exception, § 7.13(a) gives the plaintiff's counsel full access to the board's or committee's report and all supporting documentation, and § 7.13(e) further specifies that any legal opinions (including certain oral opinions) must also be furnished to the plaintiff's counsel if a legal opinion is tendered to the court. See Comment *e* to § 7.13. Subject to the "good cause" exception of *Garner v. Wolfinbarger*, additional discovery of the board's or committee's counsel is not intended by § 7.13(e), even though the tender of the opinion to the court might be deemed a waiver of the privilege under traditional formulations of the privilege. The privilege is not, however, applicable to questions relating to the counsel's independence, background, experience, and compensation from, or other financial relationships with, the corporation. Other exceptions to the privilege—such as the crime/fraud exception and the waiver doctrine—are not addressed by § 7.13. See, e.g., In re John Doe Corp., 675 F.2d 482, 489–93 (2d Cir.1982); In re Sealed Case, 676 F.2d 793, 813 (D.C.Cir.1982); In re International Systems and Controls Corporation Securities Litigation, 693 F.2d 1235, 1242–43 (5tb Cir.1982).

5. Since Upjohn Co. v. United States, 449 U.S. 383, 401, 101 S.Ct. 677, 688, 66 L.Ed.2d 584, 598 (1981), which held that witness interview notes "cannot be disclosed simply on a showing of substantial need and inability to obtain the equivalent without undue hardship," subsequent decisions have given nearly absolute protection to what has been termed "opinion work product"—that is, materials that reveal the mental processes of the attorney in evaluating the potential cause of action. See In re Internationa1 Systems and Controls Corp. Securities Litigation, supra, at 1240; In re Sealed Case, 676 F.2d 793, 809–10 (D.C.Cir.1982); In re Grand Jury Investigation, 599 F.2d 1224, 1231 (3d Cir.1979); Duplan Corp. v. Moulinage et Retorderie de Cbavanoz, 509 F.2d 730, 734 (4th Cir. 1974). This higber level of protection would typically apply to the work product of a special counsel to a litigation committee to the extent the materials sought evaluated the potential strengths and weaknesses of the cause of action or the credibility of important witnesses. It also seems clear that the "anticipation of litigation" requirement of the work product doctrine would be satisfied once a plaintiff made demand or otherwise indicated an intent to sue. For decisions that have held that the *Garner* rule is inapplicable to work product, see In re International Systems and Controls Corp. Securities Litigation, 693 F.2d 1235, 1239–41 (5th Cir.1982); In re Dayco Corp. Derivative Securities Litigation, 99 F.R.D. 616, 620 (S.D.Ohio 1983). Section 7.13 does not address the special issue of waiver when work product materials are disclosed to a governmental agency, such as the S.E.C. For an overview of this important topic, see Crisman and Matthews, Limited Waiver of the Attorney-Client Privilege and Work-Product Doctrine in Internal Corporate Investigations: An Emerging Corporate 'Self-Evaluative' Privilege, 21 Am. Crim. L. Rev. 123, 174–77 (1983).

6. With respect to the standards for protective orders, see Marcus, Myth and Reality in Protective Or-

der Litigation, 69 Cornell L. Rev. 1, 41–46 (1983). In general, "nonparty access to protected discovery [is] almost universally den[ied] ... unless intended to garner information for use in other litigation." Id. See also Note, Non-Party Access to Discovery Materials in the Federal Courts, 94 Harv. L. Rev. 1085 (1981). Although there is today a constitutionally based "presumption of access to court records," see, e.g., In re Continental Illinois Securities Litigation, 732 F.2d 1302, 1308–16 (7th Cir.1984), it is also clear tbat courts can afford broad confidentiality to pretrial discovery proceedings, because they are not public and the information is obtained under the compulsion of judicial enforcement. See Seattle Times Co. v. Rhinehart, 467 U.S. 20, 104 S.Ct. 2199, 81 L.Ed.2d 17 (1984). In *Seattle Times*, however, the Supreme Court implied that once information is introduced into evidence, the presumption of public access normally applies. Cf. Landmark Communications, Inc. v. Virginia, 435 U.S. 829, 839, 98 S.Ct. 1535, 1541, 56 L.Ed.2d 1, 10 (1978) ("The operations of the courts and the judicial conduct of judges are matters of utmost public concern."). Section 7.13(e) follows *Continental Illinois* in assuming that the "presumption of public access" is not irrebuttable, although only a strong showing of likely injury should justify expungement. The editing procedure that § 7.13 contemplates would be similar to that followed by sentencing courts under Rule 32(c) of the Federal Rules of Criminal Procedure, which permits the court to expunge certain confidential material from the presentence report before its disclosure to the defendant.

ANALYSIS AND RECOMMENDATION

§ 7.14 Settlement of a Derivative Action by Agreement Between the Plaintiff and a Defendant

(a) A derivative action should not be settled, discontinued, compromised, or voluntarily dismissed by agreement between the plaintiff and a defendant, except with the approval of the court.

(b) The court should approve a proposed settlement or other disposition if the balance of corporate interests warrants approval and the settlement or other disposition is consistent with public policy. In evaluating a proposed settlement, the court should place special weight on the net benefit, including pecuniary and nonpecuniary elements, to the corporation.

(c) In the absence of circumstances leading the court to find that the interests of the shareholders will not be substantially affected by the settlement or otber disposition, the court's approval should be preceded by notice (which should be on an individual basis to the extent practicable) to, and an opportunity of a hearing