IN THE COURT OF CHANCERY OF THE STATE OF DELAWARE
IN AND FOR NEW CASTLE COUNTY

IN RE FREEPORT-MCMORAN SULPHUR, INC. SHAREHOLDER LITIGATION.	)))	Consolidated C.A. No. 16729

MEMORANDUM OPINION AND ORDER

Submitted: January 20, 2005
Decided: January 26, 2005

Pamela S. Tikellis, Esquire, Robert J. Kriner, Jr., Esquire, Brian D. Long, Esquire, A. Zachary Naylor, Esquire, Robert R. Davis, Esquire, CHIMICLES & TIKELLIS, LLP, Wilmington, Delaware, *Lead Counsel for the Plaintiffs and Delaware Liaison Counsel.*

Norman M. Monhait, Esquire, ROSENTHAL, MONHAIT, GROSS & GODDESS, P.A., Wilmington, Delaware, *Counsel for the Plaintiffs.*

Lewis H. Lazarus, Esquire, Michael A. Weidinger, Esquire, Thomas E. Hanson, Jr., Esquire, MORRIS, JAMES, HITCHENS & WILLIAMS, LLP, Wilmington, Delaware; Robert B. Bieck, Jr., Esquire, Amy L. Glovinsky, Esquire, JONES, WALKER, WAECHTER, POITEVENT, CARRERE & DENEGRE, L.L.P, New Orleans, Louisiana, *Attorneys for McMoRan Oil & Gas Co.*

Alan J. Stone, Esquire, Natalie J. Haskins, Esquire, MORRIS, NICHOLS, ARSHT & TUNNELL, Wilmington, Delaware; Benjamin S. Kaminetzky, Esquire, DAVIS POLK & WARDWELL, New York, New York, *Attorneys for Richard C. Adkerson, James R. Moffett, B. M. Rankin, Jr., R. M. Wohleber, Rene L. Latiolais, and Freeport-McMoRan Sulphur, Inc.*

Allen M. Terrell, Jr., Esquire, Brock E. Czeschin, Esquire, RICHARDS, LAYTON & FINGER, P.A., Wilmington, Delaware; Terance M. Murphy, Esquire, Michael L. Rice, Esquire, Greg L. Weselka, Esquire, JONES DAY, Dallas, Texas, *Attorneys for J. Terrell Brown and Thomas D. Clark.*

LAMB, Vice Chancellor.

I.

The plaintiffs move to compel the production of certain documents contained on the defendants' privilege log. The plaintiffs claim that the requested documents are subject to an exception to the attorney-client privilege due to the mutuality of interest that they share with the defendant corporation. The defendant corporation denies that a mutuality of interest existed between the parties when the contested documents were created. In addition, the defendant corporation claims that, even if a mutuality of interest existed, the plaintiffs cannot show the requisite good cause as to why they are entitled to the documents.

For the reasons below, the motion to compel is granted in part and denied in part.

II.

A. Background[1]

In 1998, the plaintiffs, former shareholders of Freeport-McMoRan Sulphur, Inc. ("FSC"), filed suit against the defendants, former FSC directors, FSC, and McMoRan Oil & Gas Co. ("MOXY"), in connection with the 1998 merger between FSC and MOXY, two sister companies. The plaintiffs allege that the former FSC directors breached fiduciary duties owed to FSC stockholders by approving the merger and that MOXY aided and abetted those breaches of duty.

[1] For purposes of this motion, the court includes only the background necessary for this motion. An extensive recounting of the facts is available in the previous opinions discussed in notes 2 and 3.

The defendants moved to dismiss the complaint and the Court of Chancery granted the motion.[2] That decision was later reversed by the Delaware Supreme Court.[3] The parties have now returned to the Court of Chancery and are preparing for trial.

B. The Dispute

The plaintiffs contend that certain documents on the defendants' privilege log were created when a mutuality of interest existed between FSC and its shareholders. The plaintiffs argue that, as shareholders of FSC during the relevant time period, they are entitled to the production of these documents, even if the documents may otherwise be privileged from non-shareholders.

In an effort to resolve the disagreement, the defendants produced several documents listed on the privilege log. The plaintiffs are not satisfied by the defendants' selective production and now seek the production of 15 additional documents from the log. The contested documents fall into two categories: those that relate to litigation with IMC Global, Inc. ("IGL") and those that relate to the FSC shareholder repurchase plan.

The IGL litigation arose out of a merger between IGL and Freeport-McMorRan, Inc. ("FTX"), which was effectively FSC's parent company. After the merger, there was a dispute about the sale of a joint venture between MOXY and

[2] *See In re Freeport-McMoRan Sulphur, Inc. S'holders Litig.*, 2001 WL 50203 (Del. Ch. Jan. 5, 2001). In the motion to dismiss, the court granted the plaintiffs leave to amend their complaint, which they did. The amended complaint was also dismissed. *See In re Freeport-McMoRan Sulphur, Inc. S'holders Litig.*, C.A. No. 16729-NC, slip op. (Del. Ch. Sept. 10, 2002), *rev'd, Krasner v. Moffett*, 826 A.2d 277 (Del. 2003).

[3] *See Krasner*, 826 A.2d 277.

the subsidiary of FTX that spun off FSC into a separate publicly traded entity. IGL brought suit against several FTX directors, some of whom are also defendants in this case, alleging breaches of fiduciary duty. IGL also sued MOXY for aiding and abetting the breaches of those duties. The plaintiffs maintain they had a mutuality of interest with FSC, and they may therefore compel production of documents relating to the IGL litigation, up until the date that the proxy statement for the MOXY merger was issued, October 9, 1998.[4] In response, the defendants claim that the mutuality of interest that existed between FSC and its shareholders ended when the MOXY merger was announced on August 3, 1998.

The share repurchase plan for FSC relates to odd-lot purchases of common stock. The plaintiffs seek the production of one plan-related document that was created on October 10, 1997. They claim that this document should be treated as within the mutuality of interest time period despite it being created before FSC issued public stock. The defendants argue that since FSC did not have stockholders when the document was created, there can be no mutuality of interest with FSC shareholders.

[4] The plaintiffs also argue that the production of the IGL litigation documents can be compelled because the defendants waived the attorney-client privilege by disclosing the documents to directors who served on multiple boards of directors, thereby exposing confidential communication to third parties, i.e. the other company on whose board the director sits. The court does not need to reach this issue based on its ruling that mutuality of interest and good cause have been shown.

The defendants have produced the contested documents *in camera* for the court, but the court finds that, based on its analysis, a review of the documents is unnecessary.

III.

A. The IGL Documents

1. Mutuality Of Interest

"[Attorney-client] privilege, as reflected in Rule 502 of the Delaware Rules of Evidence, 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 of the privilege may be restricted or denied entirely."[5] "Under the so-called fiduciary duty exception to the attorney-client privilege, shareholders who enjoy a 'mutuality of interest' with corporate management may obtain access to the corporation's confidential communications with counsel upon a showing of 'good cause.'"[6] "Although there is little Delaware case law on the subject, and no bright-line rule that identifies the point in time when mutuality of interest diverges in each case, that divergence must necessarily occur at the point in time when the parties can reasonably anticipate litigation over a particular action."[7] In order to succeed

[5] *Zirn v. VLI Corp.*, 621 A.2d 773, 781 (Del. 1993).
[6] *Oliver v. Boston Univ.*, 2004 WL 944319, at *2 (Del. Ch. Apr. 26, 2004). *See also Kosachuk v. Harper*, 2000 WL 1946664, at *1 (Del. Ch. Dec. 19, 2000) ("Delaware courts recognize that a stockholder litigating against his or her corporation may be entitled to discover attorney-client privileged or attorney-work product privileged documents in the possession of the corporation or its counsel where 'good cause' is shown.").
[7] *In re Fuqua Indus., Inc. S'holder Litig.*, 2002 WL 991666, at *3 (Del. Ch. May 2, 2002).

in their motion to compel, the plaintiffs bear the burden of demonstrating the mutuality of interest.[8]

In this case, the plaintiffs claim that the divergence in interest did not occur until October 9, 1998, the day that the proxy statement was issued. They base their argument on the original complaint and the deposition of Daniel Krasner, the named plaintiff shareholder. In his deposition, Krasner repeatedly states that the proxy statement gave him the first indication that he should sue.[9] The plaintiffs assert that Krasner's deposition shows that before the proxy statement, "there was no identified dispute between the parties, and insufficient indication of a deal that would necessitate litigation."[10]

In response, the defendants claim that the divergence in interest happened earlier, on August 3, 1998, the day of the merger announcement. The defendants argue that the plaintiffs conceded in a letter from A. Zachary Naylor, plaintiffs' counsel, that August 3rd is the correct date.[11] This argument is unsupportable for

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[8] *Id.* ("[T]he litigant must first establish that a mutuality of interest existed between the parties.") (quoting *Continental Ins. Co. v. Rutledge & Co.*, 1999 WL 66528, at *2 (Del. Ch. Jan. 26, 1999)).

[9] Krasner Dep. at 65, line 22:

Q: When did you become aware that the boards of the two companies had approved the merger?

A: I don't recall the exact date I became aware. It was in the proxy statement, I believe.

Krasner Dep. at 67, line 16:

Q: And when did you form the opinion that you were opposed to the merger?

A: When I read the merger proxy statement.

[10] Pls.' Motion to Compel Mem. at 5.

[11] Letter from A. Zachary Naylor to Lewis H. Lazarus of May 24, 2004 ("Naylor Letter") .

two reasons. First, Naylor did not waive any rights with regard to the privilege log, so any purported admission does not restrict the plaintiffs' right to assert claims against the log. At the beginning of his letter, Naylor clearly declared his intention not to waive any of his clients' rights.[12] Additionally, in the sentence immediately preceding, Naylor indicated that his letter covered only documents created before August 3rd.[13]

Second, the purported admission is not an affirmative admission. The plaintiffs' letter stated only that communications made prior to August 3rd would be construed as generated during the period of mutuality.[14] Nowhere do the defendants demonstrate that this statement precludes the assertion that the mutuality continued beyond August 3rd.

Moreover, the defendants' substantive argument does not disprove the plaintiffs' position regarding the existence of a mutuality of interest. The defendants allege that because the merger announcement contained facts included in the complaint, the parties' interests diverged upon the announcement. The defendants maintain that the announcement of the merger exchange ratios provided

[12] Naylor Letter at 1 (declaring that he was writing the letter "without waiving or intending to waive any of Plaintiff's rights with respect to any entry on Defendants' privilege logs.").
[13] Naylor Letter at 1 ("After a review of these privilege logs, it is apparent to Plaintiff that privilege has been claimed with respect to a number of documents dating from prior to the August 3, 1998 agreement for which no privilege is available.").
[14] Naylor Letter at 3 ("Plaintiff believes that attorney/client privilege is inapplicable to those documents generated prior to the execution of the August 3, 1998 merger agreement [that] were created at a time where mutuality of interest existed between Plaintiff, Freeport and its directors.").

a reasonable basis for them to anticipate litigation with any shareholders from either company. The defendants do not argue any facts beyond the merger exchange ratio. They rely on this solitary fact to support their claim that all corporate communication with counsel after the merger announcement should remain confidential. Based on the facts before it, the court finds that the mere publication of merger exchange ratios, without more, is not the point in time at which the divergence in the mutuality of interest occurred.

The court reaches this conclusion mindful of the fact that the parties' mutuality of interest may diverge earlier than any potential work product protection begins, even though both doctrines direct the court to look to the phrase "in anticipation of litigation" in order to determine whether documents should be produced. As the court found in *Continental*, "the lack of a mutuality of interest may preclude production of counsels' advice, legal memoranda, or other documents long before the work product doctrine is ever effective."[15] Here, however, the plaintiffs have met their burden. They have established a mutuality of interest during the time leading up to August 3, 1998. Indeed, the defendants concede as much in their brief. The dispute over documents related to the IGL litigation concerns only the time period between August 3rd and October 9th. The plaintiffs have introduced evidence from the named shareholder that he did not consider litigation before receiving the proxy, and the defendants have not

[15] *Continental*, 1999 WL 66528, at *4.

produced any evidence to counter the plaintiffs' position. Therefore, the court finds that there was a mutuality of interest between the parties from August 3, 1998 to October 9, 1998.

2. Good Cause

Next, the plaintiffs must show good cause for the court to allow them access to the contested documents. Of the seven non-exclusive factors listed in *Garner*,[16] courts in Delaware have focused on these three factors as particularly salient: (i) "the nature of the shareholders' claim and whether it is obviously colorable;" (ii) "the apparent necessity or desirability of the shareholders having the information and the availability of it from other sources;" and (iii) "the extent to which the communication is identified versus the extent to which the shareholders are blindly fishing."[17] "Plaintiffs bear the burden of showing good cause as to why the attorney-client privilege should be set aside."[18]

[16] *Garner v. Wolfinbarger*, 430 F.2d 1093, 1104 (5th Cir. 1970) ("There are many indicia that may contribute to a decision of presence or absence of good cause, among them 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 is obviously colorable; the apparent necessity or desirability of the shareholders 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 related to past or to prospective actions; whether the communication is of advice concerning the litigation itself; the extent to which the communication is identified versus the extent to which the shareholders are blindly fishing; the risk of revelation of trade secrets or other information in whose confidentiality the corporation has an interest for independent reasons.").

[17] *Sealy Mattress Co. of New Jersey v. Sealy Inc.*, 1987 WL 12500, at *4 (Del. Ch. June 19, 1987) (quoting *Garner*, 430 F.2d at 1104). *See also Kosachuk*, 2000 WL 1946664, at *1.

[18] *In re Fuqua Indus., Inc. S'holder Litig.*, 1999 WL 959182, at *3 (Del. Ch. Sept. 17, 1999).

After a review of the record, the court finds that the plaintiffs have met their burden of demonstrating good cause under Delaware's interpretation of *Garner*. First, their claim for breaches of fiduciary duty is colorable, especially given the earlier litigation reversing the motion to dismiss. Second, the documents requested are unavailable from other sources because they are communications between the defendants and their counsel. Third, the plaintiffs are not blindly fishing. They have identified specific documents that relate to the IGL litigation. Additionally, the plaintiffs have explained how the documents relate to the merger between FSC and MOXY through the relationship between FSC and FTX, as well as the relationship between MOXY and IGL.

Although the defendants argue that the plaintiffs have failed to link the IGL litigation to the value of the merger between FSC and MOXY, the court finds that the documents requested may shed more light on the potential liability of the IGL litigation than the plaintiffs were able to discern from the depositions of the defendants. This case is factually dissimilar to *Oliver*, in which the court found the plaintiffs did not identify specific documents that could overcome the deponents' lack of knowledge.[19] Here, unlike in *Oliver*, the plaintiffs have identified specific documents that may be more informative than the depositions already conducted.

[19] *Oliver*, 2004 WL 944319, at *3 ("[T]he Plaintiffs have not identified what documents they believe would be helpful in remedying [the] knowledge shortfall [from the depositions of the individual defendants].").

The plaintiffs seek a discrete set of documents that could arguably better inform them regarding the liability of the IGL litigation.

Thus, after weighing the factors for good cause, the court finds that the plaintiffs have met their burden for compelling the production of the IGL litigation documents.

B. The Shareholder Repurchase Plan

In addition to the IGL litigation documents, the plaintiffs seek the production of one document related to the shareholder repurchase plan of FSC. As this court has previously held, "Delaware law is stingy about affording fiduciary protections to those who do not clearly qualify for them."[20] With regard to motions to compel, "the fiduciary duty exception will not apply absent a fiduciary relationship."[21]

Looking to the shareholder repurchase plan document, the issue is not whether the mutuality of interest had ended, but whether it had begun. The contested document was created before FSC issued public stock. Thus, there was no fiduciary duty owed to the future FSC stockholders and there could not have been a mutuality of interest between FSC and its stockholders.

[20] *Continental*, 1999 WL 66528, at *5.
[21] *Id.* *Continental* lists several cases that find *Garner* does not apply to communications between a defendant and its counsel before the establishment of a fiduciary relationship with a plaintiff.

The plaintiffs have not met their burden for compelling production of the shareholder repurchase document. They cite several cases from other states that they claim have extended *Garner* to facts similar to those before this court,[22] but those cases do not directly address the issue as *Continental* does. Therefore, the court declines to extend the mutuality of interest exception to communications that were created before the fiduciary relationship could have arisen, since there was no public stock issued.

IV.

For the foregoing reasons, the motion to compel is granted in part and denied in part. IT IS SO ORDERED.

[22] *See Cohen v. Uniroyal, Inc.*, 80 F.R.D. 480, 484 (E.D. Pa. 1978) (differentiating between shareholders and subsequent purchasers in a situation where *the common stock had already been issued*); *Bairnco Corp. Sec. Litig. v. Keene Corp.* (*In re Bairnco Corp. Sec. Litig.)*, 148 F.R.D. 91, 98-99 (S.D.N.Y. 1993) (same).