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

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| MURIEL P. KAUFMAN, | ) | |
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| Plaintiff, | ) | |
| | ) | |
| v. | ) | C.A. No. 699-N |
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| COMPUTER ASSOCIATES INTERNATIONAL, INC., | ) | |
| | ) | |
| | ) | |
| Defendant. | ) | |

***MEMORANDUM OPINION AND ORDER***

**Submitted: November 16, 2005**
**Decided: December 13, 2005**
**Cover Page Revised: December 21, 2005**

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LAMB, Vice Chancellor.

This case presents the question of whether to stay a books and records action under 8 *Del. C.* § 220 at the request of a special litigation committee when a derivative action encompassing substantially the same allegations of wrongdoing filed by different plaintiffs is pending in another jurisdiction. For reasons that have much to do with the light burden imposed by the plaintiff's demand in this case, the court concludes that the special litigation committee's motion to stay the books and records action should be denied.

## I.

Computer Associates International, Inc. ("CA") is a Delaware corporation that designs, markets, and licenses computer software products that allow businesses to coordinate their information technology operations. CA is one of the largest software companies in the world, doing business with more than 95% of all Fortune 500 companies. In 2003, the CA board of directors approved a settlement of a shareholder derivative action and related federal class action litigation both filed in the United States District Court for the Eastern District of New York.[1] These cases arose out of accusations of accounting fraud and related insider trading committed by current and former officers and directors of CA that had come to

[1] The shareholder derivative action was captioned *Federman v. Artzt, et al.,* No. 03-CIV-4199 (E.D.N.Y. filed Oct. 22, 2002) and the related federal class action litigation captioned *In Re Computer Associates 2002 Class Action Securities Litigation,* No. 02-CIV-1226 (E.D.N.Y. filed Feb. 25, 2002).

light in the wake of similar corporate scandals at Enron and Worldcom. The proposed settlement was approved by U.S. District Judge Thomas C. Platt in December 2003. In connection with the settlement, CA issued 5.7 million shares of its common stock (valued at $133 million) to its shareholders, and also gave all current and former officers and directors releases from liability to CA for all claims arising from the settled lawsuits.

This, however, was not the end of litigation arising out of the alleged accounting fraud at CA. In June and July of 2004, certain former CA executives were indicted by the U.S. Attorney for the Eastern District of New York on charges of obstructing justice, among other counts. As a result, three separate plaintiffs filed derivative actions on behalf of CA, again in the Eastern District of New York, seeking a wide range of damages as well as disgorgement of compensation from 22 current and former CA officers and directors.[2] These actions were consolidated by Judge Platt and refiled on January 7, 2005, as the 2005 Derivative Litigation.

Muriel P. Kaufman is a beneficial stockholder of CA. On September 14, 2004, Kaufman filed a Section 220 action in this court, after having issued a written stockholder's demand to determine:

[2] Only a subset of the 22 defendants were actually criminally charged by the federal authorities.

> [W]hether any or all of the Individual Officers and/or directors have breached fiduciary duties and wasted corporate assets by a) causing the company to pay all the consideration in connection with the resolution in August 2003 of certain security and ERISA class action litigation, in which those who committed the accounting manipulations were fully released from liability, and the Company was caused to give up its rights of contribution against the responsible parties; and b) participating and/or aiding and abetting the obstruction of a government investigation, thereby exacerbating the penalties the Company is likely to be assessed in connection with any resolution of that investigation.

While the allegations contained in the 2005 Derivative Litigation and the purpose expressed by Kaufman in her Section 220 action are not identical, in that the New York litigation includes many allegations outside the scope of the Section 220 request, the parties agree that Kaufman's potential claims are substantially encompassed in the 2005 Derivative Litigation.

Kaufman is not a party to the New York litigation. Nevertheless, in October 2004, she filed a motion in the District Court pursuant to Rule 60(b) of the Federal Rules of Civil Procedure seeking to vacate or rescind the releases given by CA in connection with the 2003 settlement. Judge Platt has allowed limited discovery in that case, through which Kaufman has received 177 boxes of information.[3]

In response to these developments, on February 1, 2005, CA's board of directors established a special litigation committee ("SLC") comprised of two

[3] Kaufman disputes the usefulness of this discovery. Pl.'s Opposing Br. 9.

independent board members: William E. McCracken, a former general manager of the printing division of IBM, and Renato Zambonini, former CEO and Chairman of Cognos, Inc. The SLC retained the law firm of Fried, Frank, Harris, Shriver, & Jacobson LLP as its counsel. On February 14, 2005, the SLC moved to stay the 2005 Derivative Litigation and the Rule 60(b) proceeding. These motions remain pending.

The SLC, acting on behalf of CA, now moves this court to stay Kaufman's books and records action until the committee has completed its investigation into the matters alleged in the 2005 Derivative Litigation. In its view, allowing Kaufman to proceed with her Section 220 action while the SLC is at work violates the basic understanding of Delaware corporate law that allows independent committees to control derivative litigation. If Kaufman is allowed to proceed, the SLC argues, Kaufman will have in essence eviscerated the authority of the SLC to control litigation under Delaware law.

Kaufman responds on several grounds. First, she notes that the right under Section 220 to inspect books and records for a proper purpose is an independent right, unrelated to ordinary discovery. Second, Kaufman notes that she is not a party to the 2005 Derivative Litigation, and therefore should be allowed to pursue her own interests without reference to some other litigant's claim. Finally,

Kaufman argues that by filing a Section 220 action before filing a derivative action she is following the express directions of the Delaware courts to use all the tools at hand to direct her later legal action in the most efficient way possible. Therefore, she argues, staying the Section 220 action in these circumstances would work against the policy objectives of Delaware law.

**II.**

As a general matter, 8 *Del. C.* § 220 provides that any record or beneficial stockholder has the right to inspect the stock ledger, a list of the corporation's stockholders, or other corporate books and records for a purpose reasonably related to his or her interest as a stockholder. The statute requires that the demand be written, that it be under oath, that it state the purpose for the inspection sought, and that it be directed to the corporation at its registered office in Delaware or its principal place of business.[4] Section 220 books and records actions are often used to investigate claims of mismanagement to assess whether or not derivative litigation is warranted.

[4] DONALD J. WOLFE, JR. & MICHAEL A. PITTENGER, CORPORATE AND COMMERCIAL PRACTICE IN THE DELAWARE COURT OF CHANCERY, § 8.6(a) (2005).

A special litigation committee formed in accordance with the landmark decision in *Zapata Corp. v. Maldonado*[5] has broad powers to control litigation filed nominally on behalf of a corporation.[6] Once such a committee is formed and takes control of a derivative litigation, the committee typically moves for a stay of all proceedings to allow it to complete its investigation promptly and without undue interference.[7]

This general power to control litigation, however, is less obvious when the corporation (or a SLC) seeks a stay of a Section 220 action, as opposed to a stay of the underlying litigation itself. Fundamentally, the right to proceed under Section 220 to inspect books and records exists independently of any claim the stockholder might ultimately choose to bring. Therefore, while there are circumstances in which a Section 220 action can be understood to interfere with the workings of a special litigation committee of a corporation's board of directors, courts have generally allowed Section 220 actions to proceed despite the presence of even a well constituted committee.

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[5] 430 A.2d 779 (Del. 1981) (concluding that although a board, as a whole, has been found disqualified to respond objectively to a demand, or has failed to conduct a reasonable good faith investigation prior to refusing a demand, the corporation may nonetheless seek dismissal of derivative litigation if such a course of action is found to be in the best interests of the corporation by an independent board committee).
[6] *Id.*
[7] *Id.*

In *Freund v. Lucent Technologies*,[8] for example, this court permitted a Section 220 action to proceed even though the same plaintiff had previously filed (and dismissed) a claim, noting the crucial point that "[the plaintiff] dismissed his federal securities litigation nearly a year ago and has not initiated any other proceedings against Lucent. Thus, there is no reason to infer that he is prosecuting this demand in order to obtain evidence for use in some other pending proceeding."[9]

In another case, *Khanna v. Covad Communications Group*,[10] the court allowed a Section 220 action to continue where the same plaintiff filed his derivative action when the Section 220 action was still pending. As the court explained, the defendant corporation was responsible for the overlap between Section 220 and the derivative case due to its failure to respond properly to the plaintiff's Section 220 demand when it was made. Allowing the board to stay the action, the court concluded, would "encourage corporations to shirk their Section 220 duties and to engage in dilatory conduct in the hopes that the passage of time . . . would allow them to avoid their obligations altogether."[11]

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[8] 2003 Del. Ch. LEXIS 3 (Del. Ch. Jan. 9, 2003).
[9] *Id.* at *11.
[10] 2004 Del. Ch. LEXIS 11, *13 (Del. Ch. Jan. 23, 2004).
[11] *Id.* at *13.

Finally, in *Romero v. Career Education Corp.*,[12] this court refused to stay a Section 220 action where a special litigation committee had been formed to investigate a series of related derivative and securities claims, but where the Section 220 plaintiff was uninvolved with the already filed claims and it was "certainly conceivable that any resulting claim for violation of fiduciary duties . . . would be entirely different from the pending federal claims."[13]

The holdings in these cases are consistent with the teachings of the Delaware Supreme Court as recently reiterated in *Security First Corp. v. U.S. Die Casting*,[14] to "encourage the use of Section 220" as an "information-gathering tool in the derivative context," provided a proper purpose is shown.[15] Certainly, there are rare cases in which courts might stay books and records actions in favor of internal investigations.[16] But Delaware courts have never found that Section 220 actions are conclusively precluded by the filing of related derivative litigation.

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[12] 2005 Del. Ch. LEXIS 112, *4 (Del. Ch. Jul. 19, 2005).
[13] *Id.* at *4.
[14] 687 A.2d 563 (Del. 1997).
[15] *Id.* at 567 n.3.
[16] Such a case might arise, for example, if a court in a different jurisdiction has already granted a stay of discovery to a special litigation committee, and the same plaintiff comes before this court to investigate identical claims through a Section 220 request. *See, e.g,* Trial Tr., *Parfi Holding, AB v. Mirror Imagine Internet, Inc.*, No. 18457 (Del. Ch. Mar. 23, 2001), Hennes Aff. Ex. G at 211.

This case is not one where a Section 220 action must be stayed in favor of a SLC investigation. It is doubtless true that the task facing the SLC here is a complicated one, involving closely interrelated criminal and civil charges against a large number of former officers or employees of CA. Furthermore, Kaufman's counsel frankly conceded at oral argument that the allegations of mismanagement underlying the Section 220 claim are encompassed by the allegations of wrongdoing found in the 2005 Derivative Litigation. Thus, the documents that would be produced in response to the Section 220 demand are unlikely to lead to the assertion of new or different claims.

Yet, the documents that are the subject of the Section 220 action constitute a relatively discrete set of papers, and have been provided to the government in the past. While the possibility of furnishing these documents to Kaufman will likely raise issues of privilege that might somewhat distract the SLC or its attorneys from its primary task of investigating the claims raised by the derivative plaintiffs,[17] this distraction is likely to be relatively minimal in the context of a large investigation conducted by experienced counsel. Such a minimal burden should not be the basis of a stay that deprives a stockholder of her statutory right to inspect the books and

[17] The defendant asserts, for example, that certain materials prepared by CA's audit committee during the course of its investigation have been requested by the plaintiff, and may well be privileged. Def.'s Reply Br. 6 n.6.

records of a corporation. But in denying this stay, the court does not mean to imply any prejudice to any defenses that CA might raise in this litigation.

The court's emphasis on the light burden this Section 220 action imposes on the defendant means, of course, that the situation would be quite different if this plaintiff, or some other plaintiff, were to file derivative litigation on these same issues. In that case, the court notes that a stay in favor of the SLC might be a "foregone conclusion."[18] Even so, the plaintiff would still have the opportunity to show that the SLC was improperly constituted. As this court's colloquy during oral argument on a similar motion to stay in *In Re Audiovox Derivative Litigation* suggests, a sham SLC that is established merely as a device for delaying litigation will receive little respect from the court.[19] At the moment, of course, the court has no reason to believe that the purpose of CA's SLC is anything other than to conduct a full investigation of the serious charges laid against the company.

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[18] *Kaplan v. Wyatt*, 484 A.2d 501, 510 (Del. Ch. 1984).

[19] No. 787-N (Del. Ch. Apr. 22, 2005). During oral argument, the court expressed considerable concern about the validity of a special litigation committee composed largely of the same people whose conduct was under scrutiny:

> Well, these are four people who are themselves named defendants, and who are at least alleged to have participated in the approval of . . . the agreement that is the subject of this litigations. They are, as I understand it . . . members of the compensation committee. They are members of the audit committee. They have known about the allegations in this complaint since last November. Rather than taking steps to investigate at the time the allegations were brought, they filed a motion to dismiss. How can I ignore that? They filed proxy material in which they report the fact that they have moved to dismiss and report to the stockholders that they mean to defend against this action vigorously. How can I square that with them now being appointed members of the special litigation committee charged with investigating their own alleged misconduct? *Id.*, Tr. at 7-8.

In sum, the court finds this Section 220 action will impose only a minimal burden on the defendant's SLC. Thus, in the exercise of its discretion, the court declines to issue a stay.

## III.

For the foregoing reasons, the defendant's motion to stay is DENIED. IT IS SO ORDERED.