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Recent Attorney-Client Privilege Decisions: Some Cases of Interest to In-House Counsel

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The last year produced a number of attorney-client privilege cases that may be of particular interest to in-house counsel.

I. The Role of In-House Attorneys

In theory, the same rules of attorney-client privilege apply to both outside lawyers and in-house lawyers.[1] Nonetheless, the fact is that courts sometimes scrutinize a claim of privilege by in-house lawyers more closely than a similar claim by outside lawyers.

Georgia-Pacific Corp. v. GAF Roofing Mfg. Corp.[2]

This case revolved around the sale of a business by Georgia-Pacific to GAF. Michael Scott, in-house environmental counsel for GAF, negotiated certain provisions relating to the sale with counsel for Georgia-Pacific. When the parties sued each other, Georgia-Pacific sought to discover Mr. Scott's recommendations to GAF regarding how certain provisions could be changed and what the impact of those changes would be. When GAF opposed this discovery on attorney-client privilege grounds, Georgia-Pacific brought a motion to compel.

The court granted Georgia-Pacific's motion. The court noted that under the controlling principles of New York law, a party who asserts a privilege has the burden of proving its applicability. Relying on *Rossi v. Blue Cross & Blue Shield*,[3] and other cases, the court noted that in-house counsel frequently have mixed business and legal responsibilities. Since the privilege can be an obstacle to the truth, it ought not to be construed in an unnecessarily broad manner. The court went on to find that in his capacity as negotiator, Mr. Scott was not exercising a lawyer's traditional function but that "[a]s a negotiator on behalf of

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1. *See, e.g.*, 3 J. McLaughlin, Weinstein's Federal Evidence § 503.14[1] (2d ed. 1997).
2. No. 93 Civ. 5125 (RPP), 1996 WL 29392 (S.D.N.Y. Jan. 25, 1996).
3. 540 N.E.2d 703 (N.Y. 1989).

management, Mr. Scott was acting in a business capacity."[4] The court then added:

> Since Mr. Scott negotiated the environmental terms of the Agreement, GP is entitled to know what environmental matters he determined would not be covered in the proposed agreement; the extent to which they were covered in the provisions he negotiated in the Agreement; and whether Scott advised GAF management of the degree to which his negotiations had left GAF protected and unprotected. Only by such testimony can it be determined whether GAF, as a matter of business judgment, agreed to assume certain environmental risks when it entered the Agreement.[5]

The court was certainly correct in its conclusion that the party asserting the attorney-client privilege bears the burden of proving the applicability of the privilege. As a general proposition, business advice typically is not covered by the privilege whereas legal advice is.[6] The court's opinion reflects that there is also New York authority to support the proposition that the negotiation portion of a business transaction should be covered by the privilege. Nonetheless, it is troubling that the opinion is silent on the extent, if any, to which statements that would clearly constitute legal advice by Mr. Scott pertaining to the negotiations would be protected by the privilege or whether all aspects of the entire matter would not necessarily be held privileged.

Itoba Ltd. v. LEP Group PLC[7]

This case was a securities action by an investor, Itoba Ltd. ("Itoba"), against London-based LEP Group PLC ("LEP") and several of its officers for allegedly failing to disclose negative information about its American subsidiaries. In responding to the defendants' motions to dismiss for *forum non conveniens*, Itoba offered a memorandum prepared by Martin Ackerman, a lawyer who had been retained to manage one of LEP's troubled American subsidiaries, to LEP's board of directors regarding the subsidiary's operations. Because Mr. Ackerman was an attorney and had labeled his memorandum "Attorney-Client Privilege[d] Information," LEP contended in reply that the production of the Ackerman memorandum during discovery was inadvertent and that the memorandum should be stricken from the record on attorney-client privilege grounds.[8] The court refused to do so.

This court, too, stressed that the burden of demonstrating the applicability of the privilege rests on the proponent. The court then found that LEP had

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4. Georgia-Pacific, *supra* note 2, at *4.
5. *Id.* at *5.
6. *See, e.g.*, THE ETHICAL OREGON LAWYER § 7.3 (OSB CLE 1991 & Supp. 1994).
7. 930 F. Supp. 36 (D. Conn. 1996).
8. *Id.* at 42.

failed to meet its burden for two primary reasons.

First, although Mr. Ackerman was an attorney, the court held that his memorandum dealt "primarily" with the subsidiary's general business affairs rather than specific legal issues relating to those operations.[9]

Second, notwithstanding the label Mr. Ackerman had placed on his memorandum, the court looked to the substance of the document in reaching its conclusion that the memorandum was not was protected from discovery by the attorney-client privilege.[10]

Sackman v. Liggett Group, Inc.[11]

This was a product liability action against Liggett Group, Inc. ("Liggett"), a cigarette manufacturer. The plaintiff alleged that her use of Liggett's Chesterfield-brand cigarettes caused her to develop cancer. During the course of discovery, Liggett sought a protective order covering documents related to scientific research conducted by the "special projects" division of an industry-funded center known as the Council on Tobacco Research ("CTR"). Most of the documents at issue were correspondence from the general counsel of CTR's member companies (including Liggett) to the "special projects" division or related minutes of meetings by the general counsel discussing specific "special projects" being developed in response to joint civil litigation or regulatory concerns. Liggett contended, in pertinent part, that the documents were protected by the attorney-client privilege because they contained legal advice and strategy.[12] The court disagreed. (It also rejected Liggett's argument that the documents were protected from discovery by the work-product rule.)

Following an *in camera* review of the documents involved, the court found that they did not contain confidential legal communications or legal advice that fell within the ambit of the attorney-client privilege. Rather, the court concluded:

> The documents . . . demonstrate that the attorneys were serving a function other than that of a legal advisor. Counsel to the tobacco companies were functioning in a scientific, administrative, or public relations capacity in taking the action that they did. The role delegated to the attorneys was one that could have been performed by the Scientific Advisory Board [a panel of scientists affiliated with the CTR], a doctor or scientist, or a tobacco company executive. Since the documents are not "primarily of a legal character" they do not fall within the attorney-client privilege.[13]

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9. *Id.* at 43.
10. *Id.*
11. 920 F. Supp. 357 (E.D.N.Y. 1996).
12. *Id.* at 363-65.
13. *Id.* at 365 (citations omitted).

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Although the attorney-client privilege applies to both in-house counsel and a corporation's outside attorneys, *Georgia-Pacific, Itoba* and *Sackman* all raise the question of the extent to which internal counsel should be held to a higher standard for the privilege than if the same activities had been conducted by outside counsel on behalf of a corporate client. In light of what appears to be, at minimum, more stringent scrutiny of internal counsel by courts in applying the privilege, these cases suggest that internal counsel who are dealing with both business and legal issues should segregate their legal analysis into a separate document to enhance the likelihood of maintaining its confidentiality.

II. IN-HOUSE COUNSEL AS INVESTIGATORS

It is clear that if a company hires outside or in-house counsel to conduct a factual investigation in aid of providing legal advice to the company, that investigation is potentially subject to protection under attorney-client privilege.[14] *Rowe* and *Holt* suggest that in applying this facet of the privilege, courts will look beyond who conducted the investigation and, will instead, examine the purpose underlying the investigation.

United States v. Rowe[15]

The in-house lawyers in this case were associates at a law firm. They were asked by a partner at the firm to perform a factual investigation, incident to giving legal advice to the firm, in connection with potentially serious wrongdoing by a partner. Subsequently, a grand jury sought information concerning this investigation, and the firm opposed this attempt on attorney-client privilege grounds.[16]

The court upheld the claim of privilege. As the court noted, the associates were effectively acting as in-house counsel.[17] The court held the fact that business entities other than law firms could have chosen to use nonlawyers to conduct such an investigation was not dispositive. Here, lawyers were used and that the fact-finding was a necessary predicate to the giving of legal advice in this case.[18]

Holt v. KMI-Continental, Inc.[19]

This case involved federal civil rights claims by a former in-house counsel against her corporate employer, KMI-Continental, Inc. ("KMI"), for alleged

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14. *See, e.g.,* Upjohn Co. v. United States, 449 U.S. 383 (1981).
15. 96 F.3d 1294 (9th Cir. 1996).
16. *Id.* at 1295-96.
17. *Id.* at 1296.
18. *Id.* at 1297.
19. 95 F.3d 123 (2nd Cir. 1996).

discrimination in pay and promotions. In affirming summary judgment for KMI, the Second Circuit reviewed the assertion of the attorney-client privilege as it related to two internally-generated reports that the plaintiff had offered to support her claims. The first was a study, known as the Braye Report, KMI had prepared analyzing the reasons underlying its difficulties in retaining African-American employees. The second, called the Campbell Report, was an examination of KMI's potential exposure for "equal pay" claims.[20]

The Second Circuit found that the Braye Report's primary purpose was to advance the business objective of employee retention, and, despite its analysis of KMI's difficulties in this area, did not qualify as legal advice. By contrast, the court found that the primary purpose of the Campbell Report was to render legal advice to KMI and held that this study was covered by the attorney-client privilege.[21]

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Rowe and *Holt* suggest that in assessing whether the privilege will apply to internal investigations, the focus will not simply be on who is conducting the investigation. Rather, the courts will look beyond the identities of the investigators to examine the *purpose* of the investigation. If the investigation is for the primary purpose of providing the corporation with legal advice, it will likely be cloaked with the attorney-client privilege. If, however, a court determines that the primary purpose is to assist the corporation in conducting its business operations, the privilege is unlikely to apply.

III. THE PROTECTION OF INTERNAL INVESTIGATIONS THAT RESULT IN PUBLIC REPORTS

Suppose a company which has a report prepared by in-house or outside counsel chooses to make the report public. Does that mean that all investigative notes and related material become public as well? How about uncirculated drafts of the report? The *Kidder Peabody, Aramony* and *Woolworth* courts reached at least partly different conclusions that may or may not be fully reconcilable on a factual basis.

In re Kidder Peabody Sec. Litig.[22]

On the basis of the record before it, the *Kidder Peabody* court held that the investigation and report about the alleged wrongdoing of a former employee had been prepared primarily for the business purpose of reassuring Kidder Peabody's shareholders and customers that the firm was otherwise sound. It was

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20. *Id.* at 134.
21. *Id.*
22. No. 94 Civ. 3954 (BSJ), 1996 WL 263030 (S.D.N.Y. May 31, 1996).

not prepared for the purpose of providing legal advice. The court held that Kidder Peabody might have gone through the same steps in aid of obtaining legal advice if it had not also had a business purpose for doing so was irrelevant to the availability of the privilege.[23] The court also held that privilege was waived as a result of Kidder Peabody's attempts to use the report affirmatively in litigation as a weapon or defense against its adversaries.[24] On the other hand, the *Kidder Peabody* court held that preliminary drafts of the report which had not been submitted to third parties were covered by the privilege and need not be produced.[25]

United States v. Aramony[26]

This was a criminal action against William Aramony, the former chief executive officer of the United Way of America ("UWA"), and two associates. Mr. Aramony argued on appeal that his convictions should be reversed because, in pertinent part, the trial court had admitted into evidence statements he had made to private investigators from Investigative Group, Inc. ("IGI"), which had been hired by UWA's general counsel to conduct an internal inquiry into allegations of financial improprieties. Mr. Aramony contended that, based on his position as UWA's chief executive officer at the time, his statements to IGI should have been protected by the attorney-client privilege because its investigation had been arranged through UWA's general counsel.[27] Both the trial court and the Fourth Circuit rejected Mr. Aramony's argument. The Fourth Circuit noted that Mr. Aramony had no reasonable expectation that his statements to IGI would be kept confidential because UWA had discussed making IGI's report public from the outset in response to stories concerning Mr. Aramony appearing in the *Washington Post*.[28]

In re Woolworth Corp. Sec. Class Action Litig.[29]

In *Woolworth*, two committees of its board of directors commissioned an investigation by outside law and accounting firms of alleged accounting irregularies. The investigation resulted in a public report by the two investigating firms critical of the company's financial reporting practices. The plaintiffs in this securities class action sought the investigating firms' internal notes and memoranda compiled during the investigation and used to create the public report. The court denied their motion. The court found that the investigation at issue

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23. *Id.* at *7.
24. *Id.* at *14-*15.
25. *Id.* at *15-*16.
26. 88 F.3d 1369 (4th Cir. 1996).
27. *Id.* at 1387.
28. *Id.* at 1390.
29. No. 94 Civ. 2217 (RO), 1996 WL 306376 (S.D.N.Y. June 7, 1996).

was not conducted primarily for business purposes and that the report had not been used either as a sword or as a shield in any litigation.[30] The court, therefore, held the investigatory notes privileged except to the extent that particular portions of particular discussions were expressly identified in the report.[31]

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Notwithstanding the *Woolworth* decision, *Kidder Peabody* and *Aramony* suggest that care should be used at the outset of an investigation in defining and documenting its scope and overall objectives. If a corporation wishes to maximize the probability that an investigation will remain confidential, it should take that posture from the beginning of the investigation and channel the report through internal counsel to the appropriate officers or directors who initiated the investigation on behalf of the corporation.

IV. IN-HOUSE COUNSEL AS LITIGANTS: PRIVILEGED COMMUNICATIONS WITH NON-ATTORNEYS

Amatuzio v. Gandalf Systems Corp.[32]

Cases are divided on the question whether, and to what extent, in-house counsel may sue former employers for torts such as wrongful termination and may use ostensibly privileged materials to support their allegations.[33]

The *Amatuzio* case represented an attempt by counsel for a corporate defendant to disqualify counsel for a plaintiff-former employee on the ground that the plaintiff-former employee had revealed information subject to the corporate defendant's attorney-client privilege to his lawyer. The court summarized its holding as follows:

> The court holds that communications with a corporation's attorney made by, to, or in the presence of a non-attorney employee who later becomes adverse to the corporation are not protected by RPC 4.2, RPC 4.4 [the approximate counterparts to DR 7-104 and DR 7-102(A)] or the attorney-client privilege from disclosure by the former employee to his litigation counsel if (i) the litigation involves an allegation by the employee that the corporation breached a statutory or common law duty which it owed to the employee, (ii) the communication disclosed involves or relates to the subject matter of the litigation, and (iii) the employee was not responsible for

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30. *Id.* at *1-*3.
31. *Id.* at *2-*3.
32. 932 F. Supp. 113 (D. N.J. 1996).
33. *See, e.g.,* General Dynamics Corp. v. Superior Court, 876 P.2d 487 (Cal. 1994). This case raises analogous questions with regard to nonlawyer employees who receive privileged communications.

> managing the litigation or making the corporate decision which led to the litigation. We also see no reason why a similar rule would not apply with respect to disputes that have not yet resulted in litigation.[34]

On the facts before it, the court noted that the plaintiff was himself within the category of employees who stood to be terminated as a result of the actions that were discussed in the confidential communications. The plaintiff was not in charge of implementing the decisions relating to the confidential communications and that the corporate employer and other the defendants were aware of the foregoing. The court therefore held that the privilege would not prohibit plaintiff's revelation of this information to his attorney or the use by the attorney of that information in prosecution of the litigation.[35]

V. WHO HOLDS THE PRIVILEGE WHEN A CORPORATION IS SOLD?

Tekni-Plex, Inc. v. Meyner and Landis[36]

Who controls attorney-client privilege when the stock or assets of a corporation are sold? *Tekni-Plex* provides an answer that is largely consistent with prior case law but also contains a point worth noting.

A company by the name of Tekni-Plex had been merged into a company called TP Acquisition Corporation. "Old" Tekni-Plex was then dissolved, and TP Acquisition Corporation changed its name to Tekni-Plex. Subsequently, litigation ensued between "new" Tekni-Plex and Mr. Tang, the sole shareholder of old Tekni-Plex at the time of the transaction, for alleged breaches of representations and warranties pertaining to certain environmental matters.[37]

In accordance with the weight of prior authority, the court held that privilege generally goes with the entity. Thus, where assets are sold, the selling entity retains the privilege. Where stock is sold, however, the new shareholder controls the privilege.[38] Thus, where old and new Tekni-Plex had been merged, the new shareholder controlled the privilege. This meant, *inter alia*, that new Tekni-Plex could deprive Mr. Tang of access to discussions with counsel for old Tekni-Plex about environmental matters unless Mr. Tang could prove that he was a co-client of the firm at that time.[39]

The court drew a distinction, however, between communications directly related to the merger negotiations and other prior communications. As to com-

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34. Amatuzio, *supra* note 32, at 118.
35. *Id.* at 119.
36. 89 N.Y.2d 123 (1996).
37. *Id.* at 128-29.
38. *See, e.g., In re* Sealed Case, 120 F.R.D. 66 (N.D. Ill. 1988); *In re* Grand Jury Subpoenas, 902 F.2d 244 (4th Cir. 1990).
39. Tekni-Plex, *supra* note 36, at 137-38.

munications relating to the merger negotiations, the court held that it was obviously the intention of the parties not to transfer access to those communications from the buyer to the seller and that this was reflected, *inter alia*, in an express agreement that the privilege be preserved in any subsequent dispute regarding the acquisition.[40] As the court stated:

> Where the parties to a corporate acquisition agree that in any subsequent dispute arising out of the transaction the interests of the buyer will be pitted against the interests of the sold corporation, corporate actors should not have to worry that their privileged communications with counsel concerning the negotiations might be available to the buyer for use against the sold corporation in any ensuing litigation. Such concern would significantly chill attorney-client communication during the transaction.[41]

In the absence of an express agreement to that effect, however, it would seem that, consistent with prior cases from other jurisdictions, access to the negotiation-related communications would have had to be granted to new Tekni-Plex.[42] The key point is that provisions regarding access to privileged communications are a worthwhile part of any transaction regarding the sale of an entity to a third party.

It is also interesting to draw possible comparisons between *Tekni-Plex* and *Georgia-Pacific*. As can be seen from the quotation above, the Tekni-Plex court evidently had no difficulty assuming that it is possible to have "privileged communications with counsel concerning [business] negotiations." The *Georgia-Pacific* court, however, applied New York law to reach an arguably contrary result. How the balance between these two cases may be struck over time remains, of course, to be seen. Perhaps the next few years will provide the answer.

VI. THE CRIME/FRAUD EXCEPTION TO THE ATTORNEY-CLIENT PRIVILEGE: WHAT IF CORPORATE COUNSEL DOES NOT KNOW OF THE ALLEGED CRIME OR FRAUD?

"All courts agree that communications by a client to the client's attorney in pursuit of a future criminal or fraudulent act are not privileged."[43] But, in the corporate context, what if the corporate counsel involved is not aware of the alleged crime or fraud? Two recent Ninth Circuit decisions address this question.

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40. *Id.* at 139.

41. *Id.*

42. *See, e.g.*, Polycast Tech. Corp. v. Uniroyal, Inc., 125 F.R.D. 47 (S.D.N.Y. 1989); Medcom Holding Co. v. Baxter Travenol Lab., 689 F. Supp. 841 (N.D. Ill. 1988).

43. 3 J. MCLAUGHLIN, WEINSTEIN'S FEDERAL EVIDENCE, *supra* note 1, § 503.16[1] at 503-80.

In re Grand Jury Proceedings[44]

This case involved a federal grand jury investigation of possible immigration and tax crimes by an unnamed corporation. The government issued a subpoena to two former internal corporate counsel to appear before the grand jury to answer questions concerning their confidential communications with other corporate personnel regarding another corporate employee's immigration status and compensation. The corporation moved to quash the grand jury subpoenas. In doing so, the corporation argued, in pertinent part, that the "crime/fraud" exception could not apply because the government had not shown that the attorneys involved actually knew of the employee's immigration status and, therefore, their advice was not "in furtherance of" the immigration and tax allegations at issue.[45] The district court denied the motion and the Ninth Circuit affirmed.

Both the district court and the Ninth Circuit found that attorney need *not* know of the illegality involved for the "crime/fraud" exception to apply. Rather, the focus of the inquiry is on the *client's knowledge* as the holder of the privilege:

> Inasmuch as today's attorney-client privilege exists for the benefit of the client, not the attorney, it is the client's knowledge and intentions that are of paramount concern to the application of the crime-fraud exception; the attorney need know nothing about the client's ongoing or planned illicit activity for the exception to apply. It is therefore irrelevant, for purposes of determining whether the communications here were made 'in furtherance of' Corporation's criminal activity, that Roe and Doe [the two former in-house counsel] may have been in the dark about the details of that activity.[46]

United States v. Chen[47]

Chen involved a similar procedural setting and the same result. In *Chen*, a corporation and its principals had moved to quash subpoenas issued to both internal and outside counsel by a federal grand jury investigating possible customs and tax charges. The district court found specifically that neither attorney had committed any wrongdoing. Nonetheless, the district court went on to find that the government had made a *prima facie* showing that the corporation had used its attorneys as unwitting conduits to make false statements to the Customs Service. Accordingly, the district court refused to quash the subpoenas.[48] The Ninth Circuit affirmed.

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44. 87 F.3d 377 (9th Cir. 1996).
45. *Id.* at 380-81.
46. *Id.* at 381-82 (footnote omitted).
47. 99 F.3d 1495 (9th Cir. 1996).
48. *Id.* at 1499.

Citing *In re Grand Jury Proceedings*, the Ninth Circuit held:

> The district judge found that the lawyers in this case were innocent of any wrongful intent, and had no knowledge that their services were being used to trick the Customs Service or the IRS. But the lawyer's innocence does not preserve the attorney-client privilege against the crime-fraud exception. The privilege is the client's . . . .[49]

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In re Grand Jury Proceedings and *Chen* make plain that the "crime/fraud" exception is no longer a stranger to the corporate setting. With the increasing criminalization of a wide variety of conduct—environmental, tax and employee immigration issues to name only a few—corporate counsel will need to become more familiar with this once obscure exception to the attorney-client privilege. Moreover, and as *In re Grand Jury Proceedings* and *Chen* demonstrate, an internal counsel's own honesty does not guarantee that the privilege will be maintained. Rather, in-house counsel may be placed in the uncomfortable position of assessing why their advice is being sought on a particular issue to ensure both that the corporation's conduct does comply with the law and that the attorney-client privilege will be preserved.

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49. *Id.* at 1504.