Center of the Circle: In-House Counsel, the Crime-Fraud Exception and "Reasonable Suspicion"

By: Mark J. Fucile

IADC member Mark Fucile of Fucile & Reising LLP in Portland advises lawyers, law firms and legal departments throughout the Pacific Northwest on professional responsibility, risk management and the attorney-client privilege. Before co-founding his current firm in 2005, Mark served as an in-house ethics counsel for a large Northwest regional law firm. Mark also teaches legal ethics as an adjunct for the University of Oregon School of Law at its Portland campus.

"We recognize that corporate counsel coming upon evidence of criminality in communications protected under *Upjohn* are placed in an uncomfortable position."[1]

THE crime-fraud exception to the attorney-client privilege is not unique to in-house counsel. Yet, the very centrality of in-house counsel within their organizations has generated a distinct body of case law applying the exception to conversations between corporate constituents and in-house counsel. One of the unusual features of the exception is that it applies even though the consulted attorney does not know the client's ulterior purpose for the consultation. At the same time, in-house counsel—like their outside counsel counterparts—cannot feign "willful blindness" when there is a reasonable suspicion that a corporate employee is consulting the attorney to further a crime or fraud. Rather, taking appropriate action based on reasonable suspicion over the motive for the consultation can preserve, not lose, the corporation's attorney-client privilege.

[1] *In re* John Doe Corp., 675 F.2d 482, 491 (2d Cir. 1982). "*Upjohn*" refers to Upjohn Co. v. United States, 449 U.S. 383, 101 S. Ct. 677, 66 L.Ed.2d 584 (1981).

This article first surveys the crime-fraud exception generally and then focuses on in-house counsel. On the latter, it both discusses cases applying the exception in the in-house context and examines the closely-associated professional duties to inquire about potential misconduct based on reasonable suspicion and report such misconduct to appropriate officials within the organization for investigation and remedial action that will ordinarily keep the review within the privilege.

I. The Crime-Fraud Exception

As the name implies, the "crime-fraud" exception removes the protection of the attorney-client privilege from communications that further a planned or ongoing crime or fraud.[2] Clients can and do consult lawyers about the potential legal consequences of contemplated conduct. ABA Model Rule of Professional Conduct 1.2(d) notes in this regard that "a lawyer may discuss the legal consequences of any proposed course of conduct with a client and may counsel or assist a client to make a good faith effort to determine the validity, scope, meaning or application of the law."

Both the crime-fraud exception and ABA Model Rule 1.2(d), however, articulate the unremarkable proposition that a client cannot use a lawyer to assist in planning for or committing a crime or fraud.[3] Speaking to privilege, the United States Supreme Court noted: "It is the purpose of the crime-fraud exception to the attorney-client privilege to assure that the 'seal of secrecy' . . . between lawyer and client does not extend to communications 'made for the purpose of getting advice for the commission of a fraud' or crime."[4]

---

[2] *See generally* United States v. Zolin, 491 U.S. 554, 562-565, 109 S. Ct. 2619, 105 L. Ed.2d 469 (1989) (outlining the broad contours of the exception). Although the focus of this article is on the attorney-client privilege, the crime-fraud exception has also been applied to work product protection. *See generally In re* Grand Jury Subpoena, 870 F.3d 312, 316-317 (4th Cir. 2017) (discussing the application of the exception to work product and the differing standards for discovery of fact and opinion work product); Drummond Company, Inc. v. Conrad & Scherer LLP, 885 F.3d 1324 (11th Cir. 2018) (noting application to work product). A reviewing court will generally look to the law controlling, respectively, privilege and work product in assessing the exceptions in a given case. *See generally* Amusement Industry, Inc. v. Stern, 293 F.R.D. 420, 425 (S.D.N.Y. 2013).

[3] This article does not address the evolving accommodation of ABA Model Rule 1.2(d) to state decriminalization of marijuana while it remains prohibited under federal law. States that have decriminalized marijuana have generally accommodated legal advice to state-regulated marijuana businesses through amendments to state equivalents to ABA Model Rule 1.2(d) or associated Rule of Professional Conduct comments or state bar ethics opinions. *See, e.g.,* Oregon RPC 1.2(d); Washington RPC 1.2, cmt. 18; WSBA Advisory Op. 201501 (2015).

[4] *Zolin*, 491 U.S. at 563 (citation omitted).

Comment 9 to ABA Model Rule 1.2, in turn, observes: "There is a critical distinction between presenting an analysis of legal aspects of questionable conduct and recommending the means by which a crime or fraud might be committed with impunity."

Although the crime-fraud exception and ABA Model Rule 1.2(d) dovetail in many respects, the former addresses the application of the client's privilege and the latter regulates lawyer conduct.[5]

The exception may apply even if the lawyer does not know that the purpose of the client's consultation is to further a crime. The Ninth Circuit put it this way:

> [T]he lawyers' innocence does not preserve the attorney-client privilege against the crime-fraud exception. The privilege is the client's, so "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 . . . that [the lawyers] may have been in the dark."[6]

Similarly, the exception only applies to communications relating to a contemplated or ongoing crime or fraud.[7] Other advice on lawful activities—even if occurring during the same time period—does not automatically lose privilege. The U.S. District Court for the Southern District of New York summarized the law on this point:

> If the court finds that the crime-fraud exception is applicable, it "does not extend to all communications made in the course of the attorney-client relationship, but rather is limited to those communications and

[5] By using the terms "crime" and "fraud," both the privilege exception and the ABA Model Rule effectively sweep quite broadly given the range of conduct that falls within one or the other. Restatement (Third) of the Law Governing Lawyers (*Restatement*), Section 82, comment d (2000) notes, however, that decisions vary on whether the exception applies to other intentional torts that do not fit within these definitions. *See also* Lewis v. Delta Airlines, Inc., No. 2:14-cv-01683-RFB-GWF, 2015 WL 9460124 at *2-*5 (D. Nev. Dec. 23, 2015) (unpublished) (surveying authority on this point); Koch v. Specialized Care Services, Inc., 437 F. Supp.2d 362, 372-377 (D. Md. 2005) (discussing *Restatement*, § 82, cmt. d).

[6] United States v. Chen, 99 F.3d 1495, 1504 (9th Cir. 1996) (citation omitted).

[7] The exception also extends to legal advice sought by the client to cover-up a crime or fraud—essentially treating it as part of the client's ongoing misconduct. *See, e.g., In re* Grand Jury Proceedings, 102 F.3d 748, 751-752 (4th Cir. 1996) (attorneys unwittingly used by client to conceal fraud).

> documents in furtherance of the contemplated or ongoing criminal or fraudulent conduct." While there must be a "purposeful nexus" between the crime or fraud and the attorney-client communication, . . . it is sufficient that the attorney-client communication be "reasonably relate[d] to the crime or fraud[.]"[8]

Legal advice about past conduct generally does not fall within the exception unless the client was seeking it as a part of a cover-up.[9] Similarly, investigations undertaken by counsel (whether internal or external) of past conduct ordinarily do not fall within the exception—again unless the investigation itself is found to have been part of a cover-up. In *In re John Doe Corp*., the Second Circuit found that an ostensible internal investigation was actually used to conceal the principal impropriety involved.[10] The Second Circuit in *John Doe* concluded:

> Corporate counsel need not run to the FBI upon the first sign of criminality in an *Upjohn* protected communication. But such communications are protected only for the purpose of the corporate client seeking, and the attorney rendering, legal advice. . . . Use of the fact of an investigation to allay the concerns of third parties about possible criminal acts, to create the appearance of compliance with laws requiring disclosure, or to cover up a crime disclosed through a protected communication in the course of the investigation will cause the corporation to lose the privilege.[11]

When the exception is litigated, courts generally require a *prima*

[8] *Amusement Industry,* 293 F.R.D. at 427 (citations omitted).

[9] *See In re* Grand Jury Subpoena Duces Tecum Dated Sept. 15, 1983, 731 F.2d 1032, 1041 (2d Cir. 1984) (addressing this distinction).

[10] 675 F.2d at 491 ("[T]he . . . [investigation] . . . was used to conceal the criminal scheme[.]").

[11] *Id*. at 491-492 (citation omitted).

facie showing by the party seeking to pierce the privilege that the client was intending to or committing a crime or fraud when the communication was made and the communication was made in furtherance of the asserted crime or fraud.[12] The Supreme Court in *United States v. Zolin* concluded that *in camera* review is permitted to assess potential application of the exception when the moving party shows "'a factual basis adequate to support a good faith belief by a reasonable person' that *in camera* review of the materials may reveal evidence to establish that the crime-fraud exception applies."[13] The Supreme Court in *Zolin* added:

> Once that showing is made, the decision whether to engage in *in camera* review rests in the sound discretion of the district court. The court should make that decision in light of the facts and circumstances of the particular case, including, among other things, the volume of materials the district court has been asked to review, the relative importance to the case of the alleged privileged information, and the likelihood that the evidence produced through *in camera* review, together with other available evidence then before the court, will establish that the crime-fraud exception does apply.[14]

In the criminal context, litigation over the crime-fraud exception is usually framed procedurally around grand jury subpoenas seeking documents, testimony, or both.[15] In the civil context, the crime-fraud exception is usually litigated through motions to compel document production and associated deposition testimony.[16] If the court orders production, the production can extend to both the crime or fraud involved and legal

[12] *See generally In re* Grand Jury, 705 F.3d 133, 151-155 (3d Cir. 2012) (discussing standard of proof). Courts vary in their approach to what constitutes *prima facie* evidence in this context. For an extended practical survey of this point by federal circuit, *see* EDNA SELAN EPSTEIN, I THE ATTORNEY-CLIENT PRIVILEGE AND THE WORK-PRODUCT DOCTRINE, 890-940 (6th ed. 2017).

[13] *Zolin*, 491 U.S. at 572.

[14] *Id*.

[15] *See Chen*, 99 F.3d at 1498 (grand jury subpoenas to outside and in-house counsel).

[16] *See, e.g.,* Ukiah Auto. Investments v. Mitsubishi Motors of North America, Inc., No. C-04-3932 MMC (MEJ), 2006 WL 1530170 (N.D. Cal. June 5, 2006) (unpublished) (motion to compel document production and associated deposition testimony of in-house counsel).

advice obtained in an effort to hide ill-gotten gains.[17]

II. Interplay Between the Exception and "Reasonable Suspicion" For In-House Counsel

In-house counsel is typically consulted about a wide range of legal issues affecting their organizations. The vast majority of these consultations are unquestionably to further the legitimate business objectives of the organizations concerned. A small, inherently unquantifiable number may either be challenged under the crime-fraud exception or fall within it.[18]

It is important to note that not all challenges to privilege under the crime-fraud exception succeed. In *Ukiah Auto Investments v. Mitsubishi Motors of North America, Inc.,*[19] a former automobile dealer pursuing fraud claims against a motor vehicle manufacturer argued that testimony by corporate managers established that they had consulted with the corporate general counsel about alleged "dumping" of vehicles on dealers and sought the general counsel's deposition under the crime-fraud exception. The court found that the executives reported potential misconduct to the general counsel as a precursor to an internal investigation. The court denied the motion because the crime-fraud exception does not apply when corporate employees are reporting past potential misconduct to internal counsel so that it can be investigated.

Consultations with in-house counsel where the crime-fraud exception applied include a wide spectrum of criminal and civil matters involving law departments of varying sizes. *United States v. Chen*[20] involved a small company where the principals used a lone in-house counsel's legal advice (unbeknownst to the lawyer) to further a tax evasion scheme for their personal benefit. *In re A.H. Robins Co., Inc.*[21] involved a large corporation where company management used the legal department to draft memoranda to the company's field sales staff to further the fraudulent concealment of the deficiencies and safety risks of

---

[17] *See, e.g.,* Grassmueck v. Ogden Murphy Wallace, P.L.L.C., 213 F.R.D. 567, 573 (W.D. Wash. 2003) (extending the exception to associated divorce and estate-planning advice used essentially to hide stolen funds).

[18] Prudent practice counsels reminding corporate constituents seeking legal advice that the advice is being rendered on behalf of the organization rather than to them as individuals. *See generally* ABA Model Rule 1.13(f); United States v. Graf, 610 F.3d 1148, 1157-1161 (9th Cir. 2010) (discussing test for determining whether legal advice rendered to corporate constituent qualified for individual attorney-client privilege).

[19] *See Ukiah Auto. Investments*, 2006 WL 1530170.

[20] *See Chen,* 99 F.3d at 1498.

[21] 107 F.R.D. 2 (D. Kan. 1985).

one of the company's key products. Although many cases in this genre involve asserted financial improprieties,[22] others involve a broad range of asserted misconduct that fall within the fairly elastic definitions of "crime"[23] or "fraud."[24]

The central role of in-house counsel often raise two associated issues: (1) what constitutes reasonable suspicion that an organizational constituent is using the organization to commit an ongoing crime or fraud? and (2) what is the duty to the organization when an in-house counsel learns of an ongoing crime or fraud within the organization? On a practical level, these questions of lawyer professional responsibility are closely linked to the crime-fraud exception, because as discussed earlier, a legitimate investigation by corporate counsel will generally stay within the privilege and work product because it is focused on past conduct and rendering legal advice to the corporation about that past conduct.

Reasonable Suspicion. ABA Formal Opinion 491 (2020) wrestles with the difficult question of what constitutes "reasonable suspicion" in this context.[25] As noted earlier, ABA Model Rule 1.2(d) prohibits a lawyer from assisting a client with conduct the lawyer "knows" is criminal or fraudulent. ABA Model Rule 1.0(f), in turn, defines "knows" as "actual knowledge of the fact in question"—but tempers this with

[22] *See, e.g., In re* Bairnco Corp. Securities Litigation, 148 F.R.D. 91, 100-101 (S.D.N.Y. 1993) (securities class action that focused on a legal advice of both in-house and outside counsel regarding potential financial impact of asbestos litigation); United States v. Cohn, 303 F. Supp.2d 672, 682-683 (D. Md. 2003) (applying exception to testimony of former in-house counsel regarding telemarketing scheme).

[23] *See, e.g., In re* Grand Jury Subpoena, 220 F.3d 406, 410 (5th Cir. 2000) (applying exception to in-house counsel memorandum in the context of criminal Clean Air Act investigation); *In re* Sealed Case, 676 F.2d 793, 798, 815-816 (D.C. Cir. 1982) (applying exception to memoranda prepared by former general counsel regarding bribery of foreign government officials).

[24] *See, e.g.,* Craig v. A.H. Robins Co., Inc., 790 F.2d 1, 3 (1st Cir. 1986) (applying the exception to testimony regarding legal department's destruction of documents following punitive damage award in product liability litigation); BP Alaska Exploration, Inc. v. Superior Court, 245 Cal. Rptr. 682, 696-702 (Cal. App. 1988) (remanding for *in camera* inspection to determine applicability of the exception to, in part, in-house counsel memoranda in civil case involving claims asserting fraud).

[25] *See also* NYCBA Formal Op. 2018-4 (2018) (addressing the prohibition on assisting a client in a crime or fraud); ABA Formal Op. 463 (2013) (discussing money laundering and terrorist financing).

the qualifier that actual knowledge can be "inferred from the circumstances." ABA Formal Opinion 491 notes that in most circumstances a lawyer will not have a duty to inquire because the client's activities are clearly legal. The opinion then outlines two broad guidelines for assessing reasonable suspicion and the duty to inquire. First, if the facts as they develop reveal what reasonably appears to be ongoing criminal or fraudulent conduct, the opinion counsels that the lawyer must ask the client directly about the activities involved. Second, the opinion notes that "a lawyer may not ignore the obvious."[26] The opinion reasons that willful ignorance can amount to knowing assistance if the facts point to a high probability that the client is using the lawyer's services to commit a crime or fraud.[27] In additional to the organizational interest in maintaining privilege by undertaking appropriate remedial action, ABA Formal Opinion 491 also suggests a more personal reason for inquiring if the reasonable suspicion threshold is met: "A lawyer may accordingly face criminal charges or civil liability, in addition to bar discipline, for deliberately or consciously avoiding knowledge that a client is or may be using the lawyer's services to further a crime or fraud."[28]

Duty to the Organization. ABA Formal Opinion 491 also discusses "reasonable suspicion" in the organizational context under ABA Model Rule 1.13 that addresses entity representation.[29] ABA Model Rule 1.13(b) requires a lawyer for an organization—whether internal or external counsel—who "knows that an officer, employee or other person associated with the organization is engaged in action, intends to act or refuses to act in a matter related to the representation that is a violation of a legal obligation to the organization, or a violation of law that reasonably might be imputed to the organization, and that is likely to result in substantial injury to the organization, then the lawyer shall proceed as is reasonably necessary in the best interest of the organization."[30] Ordinarily, a lawyer meets this duty under ABA

[26] ABA, Formal Opinion 491, at 4 (2020).
[27] *Id.* at 6.
[28] *Id.*
[29] *Id.* at 8.
[30] In the wake of the Enron scandal of the early 2000s, ABA Model Rule 1.13 was amended in 2003 to include the reporting obligations and options discussed. *See generally* AMERICAN BAR ASSOCIATION, A LEGISLATIVE HISTORY: THE DEVELOPMENT OF THE ABA MODEL RULES OF PROFESSIONAL CONDUCT 1982-2013, 326-332 (2013); *see also In re*

Model Rule 1.13(b) by "reporting up" through the organization to a level sufficient for appropriate corrective action.[31] In unusual circumstances where the highest level of authority fails or refuses to take appropriate corrective action and it is "reasonably certain to result in substantial injury to the organization," ABA Model Rule 1.13(c) vests discretionary authority in the lawyer to "report out" of the organization by alerting appliable external authorities.

If the client either refuses to reveal information to the lawyer in the face of reasonable suspicion or the organization continues to engage in the crime or fraud involved, ABA Formal Opinion 491 concludes that the lawyer must withdraw.[32] "Withdrawal" in the case of in-house counsel is a particularly difficult result. An even harsher result of staying, however, is the combined risk of regulatory, criminal, and civil liability for becoming a knowing participant in the client's crime or fraud.[33]

III. Summing Up

Most consultations with in-house counsel are unquestionably to further the legitimate business objectives of the organization involved. A few, however, are not. Those may trigger the crime-fraud exception unless the attorney acts on reasonable suspicion and reports the concerns involved through channels within the organization so that the organization can take appropriate action. As the opening quote suggests, the latter can be difficult conversations. They are, nonetheless, conversations that must take place.

Enron Corp. Securities, Derivative & ERISA Litigation, 235 F. Supp.2d 549, 598-600 (S.D. Tex. 2002) (discussing the ABA Model Rules before the amendments). The crime-fraud exception also arose in the extensive litigation surrounding the corporate misconduct that led to Enron's collapse. *See, e.g., In re* Enron Corp., 349 B.R. 115, 123-215 (Bankr. S.D.N.Y. 2006) (finding that the exception applied to communications between employees of an Enron affiliate and in-house counsel).

[31] Lawyers can be disciplined for failing to report under state variants of ABA Model Rule 1.13(b)-(c). *See, e.g., In re* DeMers, 901 N.Y.S.2d 858 (N.Y. Sup. Ct., App. Div. 2010).

[32] ABA Model Rule 491, at 10.

[33] *Id*. at 7. ABA Model Rule 1.13(e) states that lawyers who believe they were discharged for investigating or reporting corporate misconduct can inform the highest management level. ABA Formal Opinion 99-415 (1999), in turn, discusses wrongful discharge claims by former in-house counsel. Former in-house counsel have cited to state versions of ABA Model Rule 1.13(b) in framing wrongful discharge claims arguing that they were terminated for confronting their employers over asserted misconduct. *See, e.g.,* Pina v. Henkel Corp., No. 07-4048, 2008 WL 819901 at *3 (E.D. Pa. Mar. 26, 2008) (unpublished); O'Brien v. Stolt-Nielsen Transp. Group Ltd., 838 A.2d 1076, 1086 (Conn. Supp. 2003); *but see* Pang v. International Document Services, 356 P.3d 1190 (Utah 2015) (acknowledging rule but deciding case on substantive employment law).