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CORPORATE COUNSEL

Forced Waiver of the Corporate Attorney-Client Privilege

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Communications between corporate counsel and directors and officers are shielded by the attorney-client privilege. However, corporate counsel should be aware that the traditional protection granted privilege is now being weakened. There is a growing line of cases allowing individual defendants—largely former officers and directors—to force an involuntary waiver of the corporate privilege in order to use privileged materials for their personal defense.

When under fire by prosecutors, the Securities and Exchange Commission, or civil plaintiffs, corporate officers and directors often raise a good-faith defense based on their reliance on the advice of counsel. A traditional advice-of-counsel defense requires defendants to show that they presented all material facts to their attorney and acted in accordance with counsel's advice. However, even when that is not possible, reliance on counsel may still be asserted as part of a defense of good faith and lack of fraudulent intent. Unlike the traditional defense, the defense of good faith may be asserted even when defendants have not specifically consulted with an attorney, but instead relied on the involvement of attorneys in corporate decision-making—for example, regarding disclosure issues.

In either scenario, defendants must present supporting evidence—

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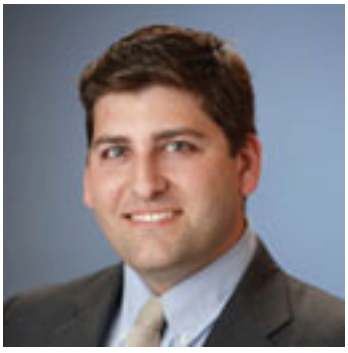

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oral or documentary—of attorney involvement. That information is typically privileged--and the privilege, as noted earlier, usually belongs to the corporation.

Criminal Matters

A number of courts have proven willing to order disclosure of privileged evidence where it is necessary to the defense, particularly in the criminal context. The leading case is United States v. W.R. Grace, 439 F. Supp. 2d 1125 (D. Mont. 2006). In a prosecution for environmental violations, former officers and employees of W.R. Grace & Co, arguing reliance on counsel, sought to introduce documents and testimony over which W.R. Grace asserted the attorney-client privilege.

The Grace court applied a balancing test, weighing the corporation's legitimate privilege against (i) the right to present evidence found in the Sixth Amendment and (ii) the due process rights in the Fourteenth Amendment. The court held that a corporate defendant's attorney-client privilege would have to be "sacrificed in limited instances" where a defendant's constitutional rights outweighed the privilege, and that "in weighing the competing interests it is the exculpatory value of the lost evidence to the accused that weighs most heavily on the scale of fair trial."

Other courts, including the Seventh, Ninth, and Eleventh Circuits, and federal district courts in Arizona and New York, have made similar rulings and statements, generally relying upon the Sixth Amendment's Confrontation Clause—the right to present evidence, the right to cross-examine, the right to present a complete defense, and "fundamental fairness."

Civil Matters

The Sixth Amendment rationale explicated by Grace does not apply in civil cases. Nevertheless, courts have shown flexibility when defendants are subject to allegations of civil fraud—allegations that are "quasi-criminal" in nature and turn on fraudulent intent or good faith.

The few cases addressing the issue—in the Sixth Circuit and federal district courts in New Jersey, New York, Pennsylvania, and Utah—have been less clear than the Grace court in explaining their rationales. The cases typically arise in the context of plaintiffs' document demands. Courts assume without discussion that a reliance-on-counsel defense can override the privilege and bootstrap a waiver of the privilege for the benefit of individual defendants. Ultimately, however, notions of fundamental fairness underlie the decisions.

This issue came squarely to a head in a case our firm litigated in the Southern District of New York several years ago. We represented a former corporate officer in a civil securities fraud suit alleging improper practices by an insurance broker. A key piece of evidence against our client was an anonymous whistle-blower memorandum sent to our client, criticizing a business practice of the company. Company counsel produced that memorandum as part of an email chain in which our client forwarded the memorandum to the company's general counsel, with the substance of the communications between our client and counsel redacted.

Our client had retained possession of an unredacted version of that email exchange which was, in our view, exculpatory. Following our assertion of a defense based in part on general reliance on counsel, plaintiffs sought production of the unredacted document and other documents on which we intended to rely. We joined in that application, which was opposed by company counsel. The special master ruled in favor of production.

Similarly, in the District of Utah, the former president of the Tenfold Corporation asserted a reliance on counsel defense in a civil fraud case brought by the SEC and moved to compel his former employer to disclose privileged documents. A magistrate judge ordered production on the basis of "a finding of a limited exception to the attorney-client privilege."

Procedures and Practicalities

When an individual defendant's counsel thinks that it is in his/her client's interest to use a privileged document, but company counsel declines to waive the privilege, this conflict typically results in a motion to compel, either by the plaintiff, who will naturally want to see that document before any depositions are taken, or by the individual defendant. Courts generally will review the documents in chambers to determine whether a privilege exists and judge the significance of the document to the defense.

To the extent that a court orders production, the court will also have to address the breadth of the forced waiver. Plaintiffs may also seek assurance that defendants have not cherry-picked only favorable privileged documents.

Another difficult issue is whether the corporation is entitled to a separate trial to ensure that the privileged documents and the fruits thereof (for example, deposition testimony) are not used to their detriment. This is no easy task, as illustrated by litigation in criminal cases over the scope of the "fruit of the poisonous tree" doctrine on immunized or improperly obtained evidence.

Conclusions

Corporate counsel should not assume that internal privileged communications will remain inviolate in the face of an assertion of the attorney-client privilege. Courts have shown themselves willing to bend the privilege in favor of individual defendants' right to present a complete defense. Corporations should take this risk of disclosure into account when preparing for and conducting litigation.

Corporate counsel should emphasize to the court the practical collateral consequences of a forced waiver of the privilege. Even if the privilege is overruled, corporations may be able to obtain a severance from the trial of former employees who are allowed to use the privileged documents.

Finally, company counsel and individual defendants' counsel should try to work with each other to avoid those conflicts. And, in the context of a joint defense, company counsel should consider alerting the individual's counsel to harmful privileged documents, of which individual counsel is not aware, that would be turned over to the plaintiff in the event of a subject matter waiver. If counsel for the individual learns the full extent of the potential production, he/she might think twice before pressing for the use of some of the privileged documents.

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