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CONFIDENTIALITY OF COMMUNICATIONS BY IN-HOUSE COUNSEL FOR FINANCIAL INSTITUTIONS

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I. INTRODUCTION

In 1974, Joel Dolkart ran into serious trouble with the New York law firm where he was a partner. His colleagues accused him of siphoning off more than \$2.5 million of fees paid to the firm by Gulf & Western Industries, a major corporate client that Dolkart had served as “outside general counsel” for sixteen years.¹

When the lawyers’ accusations led to an eighty-nine-count criminal indictment, Dolkart told the New York District Attorney that he had “concrete information about serious misconduct

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1. *Sec. & Exch. Comm’n v. Gulf & W. Indus., Inc.*, 518 F. Supp. 675, 678 (D.D.C. 1981).

committed by officers of prominent corporations.”² The prosecutors contacted the Securities and Exchange Commission, where they encountered “intense interest” in Dolkart and what he knew,³ and eventually entered into a plea agreement promising Dolkart a recommendation for a probationary sentence in exchange for his full cooperation with the SEC.⁴ Dolkart did cooperate fully, and the SEC launched a three-year investigation of Gulf & Western’s financial affairs that culminated in a civil complaint charging the company and two of its top executives with numerous violations of federal securities laws. Gulf & Western challenged the propriety of the complaint, arguing among other things that the SEC had “solicited and extracted confidential and privileged information” from its outside general counsel.⁵

Gulf & Western lost its argument. Judge Barrington Parker found the claim of privilege “lacking in support, both factually and legally.”⁶ The court stressed that Dolkart “wore several hats” during his tenure as outside general counsel, including service as a director, corporate secretary, and a member of the company’s pension advisory committee.⁷ “Because of Dolkart’s many roles and the large amount of time he spent at Gulf & Western’s offices, it cannot be assumed that all of his discussions with corporate officials involved legal advice.”⁸ Moreover, even if some of the challenged communications were privileged, Judge Parker noted, “[t]he Commission, as protector of the public interest, could possibly show good cause to justify disclosure of any privileged information obtained from Dolkart.”⁹

2. *Id.* It should be noted that Dolkart voluntarily revealed information seemingly related to the perpetration of a possible fraud on the part of his client. Thus, while this case generally can be read as a restriction of the attorney-client privilege, it might be possible to distinguish it on its particular facts.

3. *Id.*

4. *Id.*

5. *Id.* at 677. Gulf & Western also advanced an affirmative defense that “the Commission deliberately leaked information about its investigation to the New York Times and aired the matter in the public media,” thus “stripping [defendants] of their due process rights.” *Id.* at 677-78. The court rejected this defense, finding insufficient evidence that the SEC or its staff was responsible for the leaks. *Id.* at 685.

6. *Sec. & Exch. Comm’n v. Gulf & W. Indus., Inc.*, 518 F. Supp. 675, 678 (D.D.C. 1981).

7. *Id.*

8. *Id.* at 683.

9. *Id.* at 686.

* * * *

Because of Dolkart's unusually close relationship with Gulf & Western, his case illustrates two issues that should be of great concern to in-house corporate counsel, and particularly to in-house counsel in heavily regulated areas such as financial institutions. First is the danger that the attorney-client privilege will not apply to communications with a lawyer when he or she is performing "non-legal" roles for the corporate client. Second is the danger that a regulatory agency may assert the public policy claim that the agency's need for information overrides the policies underlying both the attorney-client privilege and work product immunity.

This article will explore these two major areas of concern for in-house counsel of financial institutions. Part II provides a brief background of two of the fundamental protections of confidentiality for communications with lawyers, the attorney-client privilege and work product immunity, and the policies that justify these protections.¹⁰ Part III explores the application of both protections to corporations as opposed to individual clients.¹¹ Part IV examines the special complications that surface as courts attempt to apply the privilege and immunity to communications and work of in-house counsel as opposed to outside lawyers.¹² Part V discusses the special policy concerns that some courts weigh when examining the application of disclosure bars in the context of attorneys for regulated industries, particularly financial institutions.¹³ Finally, Part VI sets out some practical issues for consideration by in-house counsel as they seek to provide the most effective advice and representation to their employer-clients.¹⁴

10. See *infra* notes 15-36 and accompanying text.

11. See *infra* notes 37-75 and accompanying text.

12. See *infra* notes 76-178 and accompanying text.

13. See *infra* notes 179-216 and accompanying text.

14. See *infra* notes 217-46 and accompanying text.

II. ATTORNEY-CLIENT PRIVILEGE AND WORK-PRODUCT IMMUNITY IN GENERAL

A. *The Attorney-Client Privilege*

The attorney-client privilege is the oldest common law privilege sanctioned by the courts.¹⁵ Its purpose is to encourage clients to communicate fully and frankly with their attorneys in order to permit ascertainment of the clients' rights and duties under the law.¹⁶ Because the privilege has the effect at times of hindering the courts' quest for evidence and the truth, the privilege is strictly construed to apply only where necessary to protect its underlying policy aims.¹⁷ The burden of persuading a court that the attorney-client privilege applies rests on the party asserting the privilege.¹⁸ The Rules of Evidence do not govern the substantive application of the privilege, but rather incorporate without comment the privilege as it has developed under common law.¹⁹

The privilege is absolute, and unlike the work product doctrine, unqualified.²⁰ Its elements have been set forth in various ways. One example is Wigmore's classic formulation of the privilege, which provides that: "(1) [w]here legal advice of any kind is sought (2) from a professional legal adviser in his capacity as such, (3) the communications relating to that purpose, (4) made in confidence (5) by the client, (6) are at his instance permanently protected (7) from disclosure by himself or by the legal adviser, (8) except the protection be waived."²¹

15. See 8 WIGMORE, EVIDENCE § 2290 (McNaughton rev. 1961); MCCORMICK ON EVIDENCE § 87 (5th ed. 1999); Brian M. Smith, Note, *Be Careful How You Use it or You May Lose it: A Modern Look at Corporate Attorney-Client Privilege and the Ease of Waiver in Various Circuits*, 75 U. DET. MERCY L. REV. 389, 391 (1998).

16. *Upjohn Co. v. United States*, 449 U.S. 383, 389 (1981).

17. See, e.g., MCCORMICK, *supra* note 15, § 87.

18. See *In re Grand Jury Proceedings*, 727 F.2d 1352, 1355 (4th Cir. 1984); *Burroughs Wellcome Co. v. Barr Labs., Inc.*, 143 F.R.D. 611, 615 (E.D.N.C. 1992); *N.C. Elec. Membership Corp. v. Carolina Power & Light Co.*, 110 F.R.D. 511, 515 (M.D.N.C. 1986).

19. FED. R. EVID. 501; N.C. R. EVID. 501.

20. PAUL RICE, ATTORNEY-CLIENT PRIVILEGE IN THE UNITED STATES § 2.2 (2d ed. 1999); *Willis v. Duke Power Co.*, 291 N.C. 19, 35, 229 S.E.2d 191, 201 (1976).

21. 8 WIGMORE, *supra* note 15, §2292 at 554. Under federal common law, the attorney-client privilege applies only if the following conditions are met:

- The asserted holder of the privilege is, or seeks to become, a client.

Although the various formulations suggest that the privilege would apply only to communications *from* the client *to* the attorney, most cases have extended its protection to

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- The person to whom the communication is made is a member of a bar (or the member's agent), and the member is acting as an attorney in receiving the communication.
 - The communication relates to a matter of which the attorney is informed by the client.
 - The communication is made without the presence of third parties.
 - The communication is made for the primary purpose of obtaining legal advice.
 - The communication is not made for the purpose of committing a crime or tort.
 - The privilege is asserted by the party seeking its protection.

Better Gov't Bureau, Inc. v. McGraw (*In re Allen*), 106 F.3d 582, 600 (4th Cir. 1997); *Burroughs Wellcome Co.*, 143 F.R.D. at 615; *N.C. Elec. Membership Corp.*, 110 F.R.D. at 513. If a party fails to assert the privilege, courts may find the party has waived it. *In re Allen*, 106 F.3d at 600; *Burroughs Wellcome Co.*, 143 F.R.D. at 615; *N.C. Elec. Membership Corp.*, 110 F.R.D. at 513.

In North Carolina, the privilege applies if,

- (1) the relation of attorney and client existed at the time the communication was made, (2) the communication was made in confidence, (3) the communication relates to a matter about which the attorney is being professionally consulted, (4) the communication was made in the course of giving or seeking legal advice for a proper purpose although litigation need not be contemplated, and (5) the client has not waived the privilege.

State v. McIntosh, 336 N.C. 517, 523-24, 444 S.E.2d 438, 442 (1994); *State v. Murvin*, 304 N.C. 523, 531, 284 S.E.2d 289, 294 (1981); *Evans v. United Servs. Auto. Ass'n*, 142 N.C. App. 18, 32, 541 S.E.2d 782, 791 (2001).

A recent statement of the scope of the privilege is set forth in Rule 502 of the Revised Uniform Rules of Evidence, which has not been adopted in North Carolina:

A client has a privilege to refuse to disclose and to prevent any other person from disclosing confidential communications made for the purpose of facilitating the rendition of professional legal services to the client (1) between himself or his representative and his lawyer or his lawyer's representative, (2) between his lawyer and the lawyer's representative, (3) by him or his representative or his lawyer or a representative of the lawyer to a lawyer or a representative of a lawyer representing another party in a pending action and concerning a matter of common interest therein, (4) between representatives of the client or between the client and a representative of the client, or (5) among lawyers and their representatives representing the same client.

REV. UNIFORM R. EVID. 502 (1986 amendment); *see* McCORMICK, *supra* note 15, § 87.1.

communications from the attorney to the client as well.²² In essence, then, the privilege requires: (1) a client, (2) a lawyer, (3) a communication between them, (4) made in confidence, (5) for the purpose of securing legal advice.²³ There are several exceptions to the privilege, perhaps the most important being that the privilege will not protect communications that can foster an ongoing crime or fraud.²⁴

State law governs the application of the privilege in state courts; interpretations of the scope and application of the privilege for corporations vary from state to state.²⁵ Federal courts apply federal common law to federal claims and, except in diversity cases, to state law claims in federal court.²⁶ Within the federal courts, interpretations are far from consistent in many respects.²⁷

B. Work Product Immunity Generally

The work product doctrine, first recognized in the United States Supreme Court case of *Hickman v. Taylor*,²⁸ is codified in Rule 26(b)(3) of both the Federal and North Carolina Rules of Civil Procedure. The federal rule provides as follows:

[A] party may obtain discovery of documents and tangible things otherwise discoverable [under other provisions of Rule 26] and prepared in anticipation of litigation or for trial by or for another party or by or for that other party's representative . . . only upon a showing that the party seeking discovery has

22. See, e.g., *In re LTV Sec. Litig.*, 89 F.R.D. 595, 601-03 (N.D. Tex. 1981); see MCCORMICK, *supra* note 15, § 89. See *News & Observer Pub. Co. v. Poole*, 330 N.C. 465, 482, 412 S.E.2d 7, 31 (1992) (finding "confidential communications between attorney and client, from either one to the other, are protected by the traditional attorney-client privilege mandated by common law").

23. See *In re Grand Jury Investigation*, 842 F.2d 1223, 1224 (11th Cir. 1987); JOHN K. VILLA, *CORPORATE COUNSEL GUIDELINES* § 1.01 (2001).

24. See generally RICE, *supra* note 20, § 8.

25. Brian E. Hamilton, *Conflict, Disparity, and Indecision: The Unsettled Corporate Attorney-Client Privilege*, 1997 ANN. SURV. AM. L. 629, 630 (1997); VILLA, *supra* note 23, § 1.01.

26. See FED. R. EVID. 501; VILLA, *supra* note 23, § 1.01.

27. Sherman L. Cohn, *The Organizational Client: Attorney-Client Privilege and the No-Contact Rule*, 10 GEO. J. LEGAL ETHICS 739, 755-60 (1997).

28. *Hickman v. Taylor*, 329 U.S. 495 (1947).

substantial need of the materials in the preparation of the party's case and that the party is unable without undue hardship to obtain the substantial equivalent of the materials by other means. In ordering discovery of such materials when the required showing has been made, the court shall protect against disclosure of the mental impressions, conclusions, opinions, or legal theories of an attorney or other representative of a party concerning the litigation.²⁹

The doctrine generally protects only documents prepared by an attorney *in anticipation of litigation*.³⁰ Unlike the attorney-client privilege, the immunity is qualified: it may be overcome by a showing that an opposing party has a substantial need for the materials and that the party would not be able to obtain the "substantial equivalent" without undue hardship.³¹ Mental impressions, conclusions, opinions, and legal theories of an

29. FED. R. CIV. P. 26(b)(3). The parallel provision in the North Carolina Rules of Civil Procedure states:

[A] party may obtain discovery of documents and tangible things otherwise discoverable under subsection (b)(1) of this rule and prepared in anticipation of litigation or for trial by or for another party or by or for that other party's consultant, surety, indemnitor, insurer, or agent only upon a showing that the party seeking discovery has substantial need of the materials in the preparation of his case and that he is unable without undue hardship to obtain the substantial equivalent of the materials by other means. In ordering discovery of such materials when the required showing has been made, the court may not permit disclosure of the mental impressions, conclusions, opinions, or legal theories of an attorney or other representative of a party concerning the litigation in which the material is sought or work product of the attorney or attorneys of record in the particular action.

N.C. R. CIV. P. 26(b)(3).

30. 8 CHARLES ALAN WRIGHT, ARTHUR R. MILLER & RICHARD L. MARCUS, FEDERAL PRACTICE & PROCEDURE § 2023 (2d ed. 1994); VILLA, *supra* note 23, § 2.05; RESTATEMENT (THIRD) OF THE LAW GOVERNING LAWYERS § 87 cmt. i (1993).

31. Nat'l Union Fire Ins. Co. v. Murray Sheet Metal Co., 967 F.2d 980, 983-85 (4th Cir. 1992); *see* VILLA, *supra* note 23, § 2.13.

attorney are, however, afforded special protection that is treated essentially as an absolute prohibition.³²

The policy rationale of the work product doctrine is not protection of the attorney-client relationship, but rather enhancement of the integrity of the litigation process.³³ As the Supreme Court stated in *Hickman v. Taylor*:

Historically, a lawyer is an officer of the court and is bound to work for the advancement of justice while faithfully protecting the rightful interests of his clients. In performing his various duties, however, it is essential that a lawyer work with a certain degree of privacy, free from unnecessary intrusion by opposing parties and their counsel.³⁴

Federal law governs work product issues in all federal court cases, including diversity cases.³⁵ Most states, including North

32. *Duplan Corp. v. Moulinage et Retorderie de Chavenoz*, 509 F.2d 730, 734 (4th Cir. 1974); see *Nat'l Union Fire Ins. Co.*, 967 F.2d at 984; VILLA, *supra* note 23, § 2.13. In a recent Second Circuit decision, *Doe v. United States*, the court upheld a claim of work-product protection as applied to an attempt to compel an attorney to “testify to her client’s admissions as evidence of his commission of [crimes] . . . , on which the attorney was representing him during the interview.” Nos. 01-6250, 01-6251, 01-6252, 2002 WL 253828, at *3 (2d Cir. Feb. 21, 2002). The court noted that to subpoena the attorney to testify to the observations made in the course of preparing to represent a client, “in order to help the putative adversary prove the offense as to which the attorney was providing representation would do substantial injury to the values that justify the work product doctrine.” *Id.* The court observed that the prohibition of the compulsion of such testimony “falls comfortably within the black letter definition of work product.” *Id.* This case seems to indicate that in some circumstances, not only are documents covered by work-product protection, but client communications may be as well. *Id.*

33. VILLA, *supra* note 23, § 2.01.

34. *Hickman v. Taylor*, 329 U.S. 495, 510-11 (1947). The rationale is that allowing access to an attorney’s trial preparation would be unfair because opposing counsel with an insight into the other side’s preparation and strategy would have an obvious tactical advantage unrelated to the merits of the case. *Id.* at 510. Transparency of preparatory work would also discourage extra effort if it would benefit the adversary as much as the client. See *id.* “The work-product doctrine also protects client interests in obtaining diligent assistance from lawyers. A lawyer whose work-product would be open to the other side might forgo useful preparatory procedures” RESTATEMENT (THIRD) OF THE LAW GOVERNING LAWYERS § 87 cmt. b (1998).

35. 4 MOORE’S FEDERAL PRACTICE, §26.15[5] (2d ed. 1996).

Carolina, have enacted a state rule of evidence identical or very similar to Federal Rule 26(b)(3).³⁶

III. ATTORNEY-CLIENT PRIVILEGE AND WORK PRODUCT IMMUNITY FOR CORPORATIONS

A. *Privilege and the Corporate Client*

Courts have almost universally assumed that the attorney-client privilege is available to corporations, and the principle was never seriously questioned until 1962, when the Seventh Circuit Court of Appeals overturned a federal district court decision that had held the privilege unavailable to a corporate client.³⁷ The district court had been “convinced that without adequate decisional precedent or legislative authority [it] should not indulge extension of the [attorney-client] privilege to a corporation.”³⁸ After reviewing the history of the privilege and its underlying policy, the Seventh Circuit respectfully disagreed:

We turn now to the application of this deep rooted privilege—recognized for more than a century as existing between attorney and client for the benefit of a natural person—to a corporate client. The ruling of the district court under scrutiny here is without precedent. We find nothing improper in the action of the district court in raising the question. However, it is obvious to us that no litigant has heretofore thought there was merit enough in the proposition to warrant a challenge to the availability of the privilege to a corporation. That the privilege has been recognized as available to corporations for more than a century is not open to serious question.³⁹

36. 8 WRIGHT ET AL., *supra* note 30, § 2023 at 334-35; *see supra* note 29 and accompanying text.

37. *Radiant Burners, Inc. v. Am. Gas Ass'n*, 320 F.2d 314, 322-23 (7th Cir.), *cert. denied*, 375 U.S. 929 (1963); *see VILLA, supra* note 23, § 1.01.

38. *Radiant Burners, Inc.*, 320 F.2d at 318.

39. *Id.* at 319.

The policy for the privilege is conceptually the same for corporate clients as for individual clients: "to encourage full and frank communication between attorneys and their clients and thereby promote broader public interests in the observance of law and administration of justice."⁴⁰ Although the underlying considerations are identical, courts and commentators have frequently expressed the concern that the privilege not be used by corporations to create a large "zone of secrecy" for communications whose probative value could be important to a fair resolution of disputes.⁴¹

The availability of the privilege to corporations as clients thus appears well settled, and it is very unlikely that a serious challenge to a corporation's ability to assert the privilege will be mounted again.⁴² Still, commentators continue to question whether corporations should always be able to prevent disclosure by asserting the privilege:

There is no simple answer to the question of whether courts should extend the attorney-client privilege to corporations. This is because the standards for assessing applicability are not certain, and empirical bases for applying those standards have never been proven or disproven. Like so many other evidence rules, the very existence of the privilege is based on intuition, instinct, assumptions, and hunches about the conduct of individuals.⁴³

40. *Upjohn Co. v. United States*, 449 U.S. 383, 389 (1981).

41. *See, e.g., Am. Cyanamid Co. v. Hercules Powder Co.*, 211 F. Supp. 85, 88 (D. Del. 1962); VILLA, *supra* note 23, § 1.01; David Simon, *The Attorney-Client Privilege as Applied to Corporations*, 65 YALE L.J. 953, 956 (1956). Perhaps as a consequence of this practical concern for abuse, the courts have often emphasized a policy of encouraging corporations' voluntary compliance with the law as a justification for applying the privilege to corporations, particularly in the context of internal corporate investigations. *Upjohn*, 449 U.S. at 392 (observing that compliance with the many governmental regulations that apply to a corporation may require special legal expertise); Cohn, *supra* note 27, at 745-47; RICE, *supra* note 20, § 4.10.

42. MCCORMICK, *supra* note 15, § 87.1; RUSSELL ROBINSON, ROBINSON ON NORTH CAROLINA CORPORATION LAW § 3.03(c), 3-9 to 3-10, n.14 (6th ed. 2000).

43. RICE, note 20, § 4.10 at 36; *see* Elizabeth G. Thornburg, *Sanctifying Secrecy: The Mythology of the Corporate Attorney-Client Privilege*, 69 NOTRE DAME L. REV. 157 (1993) (arguing that the "myths" upon which the attorney-client privilege is based should come to an end). As a creature of statute, a corporation has only such rights and powers as the legislature bestows upon it. *Columbus Mills v. Williams*, 33

While it is generally conceded that the privilege for corporations will not be successfully assaulted as a matter of principle or underlying policy,⁴⁴ the fundamental concerns about the propriety of affording such protection to corporate clients will continue to be debated as courts seek to apply the privilege in specific circumstances. For example, in *Garner v. Wolfinbarger*,⁴⁵ the Fifth Circuit Court of Appeals ruled that shareholders in a derivative action against a corporation should be given the opportunity to show cause why the privilege should not be available to a corporation to block disclosure of sensitive communications between corporate counsel and management.⁴⁶ The court went "back to basics"⁴⁷ in requiring a balancing of the important interests at stake: "The privilege must be placed in perspective. The beginning point is the fundamental principle that the public has the right to every man's evidence, and exemptions from the general duty to give testimony that one is capable of giving are distinctly exceptional."⁴⁸ The "*Garner Doctrine*," which has become "accepted law,"⁴⁹ emphasizes the courts' heightened recognition of conflicting principles in applying the attorney-client privilege to corporations.⁵⁰

The privilege developed historically in cases involving individual clients, discrete legal problems, and conventional private practitioners, and its application "to the large and complex

N.C. (11 Ired.) 558, 561 (1850) ("[A] corporation is an artificial body, possessing such powers, and having such capacities, as may be given to it by its maker."); see ROBINSON, *supra* note 42, § 3.01.

44. *Id.* at 38.

45. *Garner v. Wolfinbarger*, 430 F.2d 1093 (5th Cir. 1970).

46. *Id.* at 1103-04.

47. VILLA, *supra* note 23, § 1.27.

48. 430 F.2d at 1100.

49. VILLA, *supra* note 23, § 1.27; see *Sandberg v. Virginia Bankshares, Inc.*, 979 F.2d 332, 352 n.20 (4th Cir. 1992). Section 55-7-49 of the North Carolina Business Corporation Act rejects the "*Garner Doctrine*" for North Carolina corporations: "In any derivative proceeding, no shareholder shall be entitled to obtain or have access to any communication within the scope of the corporation's attorney-client privilege that could not be obtained by or would not be accessible to a party in an action other than on behalf of the corporation." N.C. GEN. STAT. § 55-7-49 (1999); see ROBINSON, *supra* note 42, § 3.03(c) at 3-11.

50. RICE, *supra* note 20, § 8.17.

nature of modern corporate business transactions”⁵¹ has led to numerous interpretive difficulties.⁵² Corporations are “inanimate entities,” which must act through agents, typically individuals, who speak with the company’s lawyers and make decisions based on legal advice.⁵³ Courts have thus struggled with questions regarding which corporate “agents” and which communications are covered by the privilege in various contexts.

Courts have taken different approaches to this question, depending on whether the privilege is sought to protect communications *from* an attorney to representatives of the corporation or *to* an attorney by corporate representatives.⁵⁴ The early decisions focused on communications *to* the attorney and extended the privilege “expansively” to cover communications by or from any officer or employee of a client corporation.⁵⁵ In 1962, however, the court in *City of Philadelphia v. Westinghouse Electric Corp.*,⁵⁶ considering communications *from* the attorney to corporate decision makers, dramatically narrowed the scope of the privilege by allowing its application only to a “control group” within a corporation. Under this control group test, only corporate officers or employees who are in a position to control or take a substantial part in a decision to be taken on an attorney’s advice could invoke the privilege on behalf of a corporate client.⁵⁷

The control group test was widely, though not universally, applied by the courts for nearly twenty years.⁵⁸ The test proved inadequate, however, in protecting communications from employees, especially lower level employees who could not be characterized as part of any control group, to counsel in many situations where the courts deemed such communications worthy of encouragement. Courts thus developed a second, more

51. *Radiant Burners, Inc. v. Am. Gas Ass’n*, 320 F. 2d 314, 318 (7th Cir.), *cert. denied*, 375 U.S. 929 (1963).

52. VILLA, *supra* note 23, § 1.01; MCCORMICK, *supra* note 15, § 87.1.

53. Hamilton, *supra* note 25, at 629.

54. MCCORMICK, *supra* note 15, § 87.1.

55. *United States v. United Shoe Machinery Corp.*, 89 F. Supp. 357 (D. Mass. 1950); *Zenith Radio Corp. v. Radio Corp. of America*, 121 F. Supp. 792 (D. Del. 1954); MCCORMICK, *supra* note 15, §87.1.

56. *City of Philadelphia v. Westinghouse Elec. Corp.*, 210 F. Supp. 483 (E.D. Pa. 1962), *cert. denied*, 372 U.S. 943.

57. *Id.*

58. MCCORMICK, *supra* note 15, § 87.1.

expansive, test that extended the privilege to lower echelon employees so long as the communication related to the subject matter of the communication.⁵⁹ The "subject matter test" has three major components: (1) the employee's communication must be at the direction of his or her superior; (2) the communication must be on the subject matter about which the corporation is seeking legal advice; and (3) the subject matter must concern the employee's duties.⁶⁰

In 1981, the Supreme Court of the United States considered this issue in *Upjohn Co. v. United States*, a case dealing with a corporate investigation into potential illegal payments by corporate employees to foreign government officials.⁶¹ Upjohn's general counsel, directed by the company's chairman to look into allegations of wrongdoing and to work with outside counsel, prepared a questionnaire that he sent to all overseas managers in the corporation.⁶² The letter advised the managers that the chairman had asked the general counsel to conduct an investigation into the payments and instructed the managers to answer the questionnaires and to treat the investigation as highly confidential.⁶³ Upjohn later voluntarily reported the illegal payments to the IRS.⁶⁴ When the IRS began its own investigation, it requested the completed questionnaires.⁶⁵ Upjohn refused to turn them over, citing the attorney-client privilege.⁶⁵

The Supreme Court decided in favor of Upjohn and specifically rejected the application of the control group test.⁶⁷ The Court did not, however, expressly adopt the subject-matter test. Rather, it "eschewed . . . any bright-line test at all,"⁶⁸ and adopted instead a "functional" test to be applied on a case-by-case

59. *Harper & Row Publishers, Inc. v. Decker*, 423 F.2d 487, 491-92 (7th Cir. 1970), *aff'd by equally divided court*, 400 U.S. 348 (1971); VILLA, *supra* note 23, § 1.03[A].

60. Cohn, *supra* note 27, at 750.

61. *Upjohn Co. v. United States*, 449 U.S. 383 (1981).

62. *Id.* at 386-87.

63. *Id.* at 387.

64. *Id.*

65. *Id.* at 387-88.

66. *Id.* at 388; see Cohn, *supra* note 27, at 752-53.

67. *Upjohn*, 449 U.S. at 397.

68. VILLA, *supra* note 23, § 1.03[B].

basis.⁶⁹ The Court considered the following factors persuasive in *Upjohn*:

- the communications were made by employees to corporate counsel in order for the corporation to secure legal advice;
- the employees were cooperating with corporate counsel at the direction of corporate superiors;
- the communications concerned matters within the employees' scope of employment; and
- the information sought was not available from senior management who might have been part of *Upjohn*'s control group.⁷⁰

The *Upjohn* decision "does not . . . definitively resolve the issue of whose communications are protected."⁷¹ Rather, the Supreme Court chose a functional, case-by-case analysis that sacrifices predictability to achieve a weighing of the policy considerations applicable in each situation. Even in federal cases in which the courts will apply federal common law, *Upjohn* leaves many questions open. For example, courts have not been unanimous as to whether communications not made at the specific direction of corporate superiors are covered by the privilege.⁷²

69. Cohn, *supra* note 27, at 753-54.

70. See VILLA, *supra* note 23, § 1.03[B].

71. *Id.*

72. Compare *Sequa Corp. v. Gelmin*, 1993 WL 276081 (S.D.N.Y. July 16, 1993), with RESTATEMENT (THIRD) OF THE LAW GOVERNING LAWYERS § 73 cmt. h (1998). The *Upjohn* "requirement" that the communication concern matters within the scope of the employee's employment has not always been considered a predicate for application of the privilege. See RESTATEMENT (THIRD) OF THE LAW GOVERNING LAWYERS § 73 cmts. b, d (1998). This issue, however, has been troubling to the courts and commentators. In *Samaritan Foundation v. Goodfarb*, the Arizona Supreme Court faced this issue head-on and formulated its own test because of a concern that the broad subject-matter approach of *Upjohn* would privilege statements of employees who were only witnesses to the conduct at issue, even where their connection to the liability-causing events was not close enough to fit the "classical" model of a client. 862 P.2d 870 (Ariz. 1993). In that case, communications to hospital counsel by nurses who had observed, but not participated in, an operation in which a child's heart had stopped were held not privileged. *Id.* Although the nurses had watched the operation in the course of their employment, the court noted, they were only "witnesses to the event" and their statements thus not afforded the privilege. *Id.* at 880. The Arizona court's test would apply differently depending on who initiated the communication. See *id.* Communications initiated by an employee and made to counsel in confidence will be privileged if the employee is seeking legal

Upjohn furnishes binding precedent only in federal court cases other than diversity claims. State courts have adopted varied approaches to the issue of who speaks for the corporation. As of 1997, fourteen states adopted *Upjohn* or a similar subject-matter approach; eight adopted some version of the control group test; the remaining twenty-eight, including North Carolina, had taken no position by statute, rule, or state court case.⁷³

B. Work Product Immunity for the Corporation

In *Hickman v. Taylor*, the Supreme Court questioned the availability of work product protection to corporations because of the concern that the doctrine would permit a corporation, especially one with a large legal staff, to “pull a dark veil of secrecy over all the pertinent facts it can collect after the claim arises.”⁷⁴ The Court, however, determined that these concerns did not override the policy considerations that support work product protection in the corporate context,⁷⁵ and explicitly applied the work product doctrine to corporate counsel.

IV. IN-HOUSE COUNSEL COMMUNICATIONS AND WORK PRODUCT

“Theoretically, for purposes of the attorney-client privilege, there is no distinction between an attorney who is employed in-house and one who is outside the corporate organization.”⁷⁶ Like the theoretical underpinnings of the privilege and work product immunity for corporations generally, however, the equivalence in

advice. *See id.* If, however, the investigation is initiated by the corporation, factual communications from corporate employees will be privileged only if they concern the employee's own conduct within the scope of employment and are made to aid counsel in assessing or responding to the legal consequences of that conduct. *Id.* at 872-73; Hamilton, *supra* note 25, at 641. The Arizona legislature has approved legislation that would reject the *Goodfarb* court approach in favor of an interpretation that is closer to *Upjohn*. Hamilton, *supra* note 25, at 642.

73. Hamilton, *supra* note 25, at 633-46.

74. *Hickman v. Taylor*, 329 U.S. 495, 506 (1947).

75. *See id.* at 507.

76. Allan D. Ullberg & George A. Kuhlman, *Legal Ethics: Current Trends Concerning In-House Attorney-Client Privilege*, SC40 ALI-ABA Course Study Materials (March 1998), LEXIS, Secondary Legal Library, Combined ALIABA Course of Study Materials File. *See Upjohn Co. v. United States*, 449 U.S. 383 (1981); *United States v. United Shoe Machinery Corp.*, 89 F. Supp. 357, 360 (D. Mass. 1950); RESTATEMENT (THIRD) OF THE LAW GOVERNING LAWYERS § 73 cmt. i (1998).

treatment of in-house and outside counsel has proven difficult to maintain in specific circumstances. During the past thirty years, corporations have made dramatic changes in how they obtain legal services. Both the number and the importance of in-house counsel increased strikingly over this period, although the growth in numbers of in-house lawyers appears to have slowed in recent years.⁷⁷ With this growth in numbers has come an increase in the sophistication and complexity of matters that are dealt with routinely by in-house counsel.⁷⁸ These changes have given rise to new questions regarding the unique role of the in-house lawyer within the corporate structure, especially in relation to the fundamental principle of confidentiality of client information.⁷⁹ As in-house counsel take on more and more prominence—or notoriety⁸⁰—courts are called on to articulate their understanding of the special status and role that the in-house lawyer fills for an employer-client.

Courts have sometimes applied stricter standards to in-house counsel than to outside counsel in determining whether to protect confidential information, both through attorney-client privilege and work product immunity.⁸¹ The stricter standards frequently reflect one or both of two fundamental concerns. The first is a suspicion that, because they are employees of their client, and their livelihood depends on that single corporate client, in-house counsel are not as independent as outside counsel.⁸² The

77. John H. Tinney, *Partnering and Strategic Trading Alliances Between In-House and Outside Counsel*, PLI Order No. H4-5185 (Mar./Apr. 1994), WL 497 PLI/Lit 525; Abram Chayes & Antonia H. Chayes, *Corporate Counsel and the Elite Law Firm*, 37 STANFORD L. REV. 277, 277 (1985); Geoffrey C. Hazard, Jr., *Ethical Dilemmas of Corporate Counsel*, 46 EMORY L. J. 1011, 1011-12 (1997).

78. Nancy J. Moore, *Conflicts of Interest for In-House Counsel: Issues Emerging from the Expanding Role of the Attorney-Employee*, 39 S. TEX. L. REV. 497, 498 (1998); see Chayes & Chayes, *supra* note 77, at 278.

79. See Samuel R. Miller & Irwin H. Warren, *Conflicts of Interest and Ethical Issues for the Inside and Outside Counsel*, 40 BUS. LAW. 631, 631-32 (1985).

80. The recent financial failure and bankruptcy filing of Enron Corporation have drawn unwelcome attention to the roles played by its in-house general counsel and some of its large legal staff. See, e.g., Miriam Rozen, "An Unenviable Position," TEX. LAW., Feb. 1, 2002, at 1; David Hechler, "Enron's Legal Staff Battered, Confused," NAT'L L.J., Feb. 4, 2002, at A1.

81. VILLA, *supra* note 23, § 1.05 at 1-41 ("There is no question that communications with in-house counsel receive special scrutiny.").

82. See 1 GEOFFREY C. HAZARD, JR. & WILLIAM HODES, THE LAW OF LAWYERING § 17.7 at 17-21 (3d ed. 2002); *infra* notes 85-98 and accompanying text.

second derives from the fact that in-house counsel are much more likely than outside counsel to perform a role that mixes legal with business or other functions,⁸³ leading courts to resist the extension of disclosure protections to roles played by counsel outside the traditional lawyer function. Underlying these concerns is the foundational worry, discussed above,⁸⁴ that the very nature of the corporate entity creates opportunities in which in-house counsel may help their corporation clients create a very large "zone of silence" by taking advantage of confidentiality protections crafted originally for the benefit of individual clients. The special questions regarding in-house counsel have emerged in the contexts of both attorney-client privilege and attorney work product, and this section will examine courts' treatment of in-house counsel in both areas.

A. *Independence of In-House Counsel*

In upholding the application of the attorney-client privilege to in-house counsel communications in *Upjohn Co. v. United States*, the Supreme Court took significant comfort in the independence required of all lawyers:

The first step in the resolution of any legal problem is ascertaining the factual background and sifting through the facts with an eye to the legally relevant. . . . "It is for the lawyer in the exercise of his *independent professional judgment* to separate the relevant and important from the irrelevant and unimportant. The observance of the *ethical obligation* of a lawyer to hold inviolate the confidences and secrets of his client not only facilitates the full development of facts essential to proper representation of the client but also encourages laymen to seek early legal assistance."⁸⁵

83. See *Sec. & Exch. Comm'n v. Gulf & W. Indus., Inc.*, 518 F. Supp. 675, 678; *infra* notes 99-178 and accompanying text; *supra* notes 7-8 and accompanying text.

84. See *supra* notes 30-44 and accompanying text.

85. *Upjohn Co. v. United States*, 449 U.S. 383, 391 (1980) (citation omitted) (emphasis added). In addition, the court placed special reliance on in-house counsel's role of helping corporations to comply with the law in an age of increasing complex regulation. *Id.* at 392; see 24 CHARLES ALLEN WRIGHT & KENNETH W.

The court thus recognized the ethical duty of independence that a lawyer, whether in-house or outside, must fulfill in the performance of his or her services as a lawyer.⁸⁶ The duty is set

GRAHAM, JR., FEDERAL PRACTICE AND PROCEDURE § 5480, at 245 n.37 (1986). See Amy L. Weiss, Note, *In-house Counsel Beware: Wearing the Business Hat Could Mean Losing the Privilege*, 11 GEO. J. LEGAL ETHICS 393, 402 (citing Alison M. Hill, Note, *A Problem of Privilege; In-House Counsel and the Attorney-Client Privilege in the U.S. and the European Community*, 27 CASE W. RES. J. INT'L L. 145, 186 (1995)) ("In-house attorneys are in a better position than outside counsel to encourage corporations to comply with the law because they are associated intimately with day-to-day corporate affairs.").

86. Other courts have found support for limiting the privilege to practicing attorneys in: (1) the courts' supervisory authority over lawyers, RICE, *supra* note 20, § 3.2; (2) the fact that lawyers are trained in the law and skilled in practice, *Upjohn*, 449 U.S. at 389 (quoting *Hunt v. Blackburn*, 128 U.S. 464, 470 (1888) ("[the attorney-client privilege] is founded upon the necessity, in the interest and administration of justice, of the aid of persons having knowledge of the law and skilled in its practice, which assistance can only be safely and readily availed of when free from the consequences or the apprehension of disclosure")); and (3) the requirement that lawyers abide by the ethics rules to which licensed attorneys must adhere. *Vernitron Med. Products, Inc. v. Baxter Labs., Inc.*, 1975 U.S. Dist. LEXIS 12613, *325 (D.N.J. Apr. 29, 1975) (noting that both patent attorneys and patent agents must conform to the standards of ethical and professional conduct set forth in the Code of Professional Responsibility adopted by the American Bar Association); *Woods v. N.J. Dep't of Educ.*, 858 F. Supp. 51, 55 (D.N.J. 1993). Every formulation of the requirements for application of the privilege includes the presence of a lawyer. In North Carolina, for example, application of the privilege is available only "if the relation of attorney and client existed at the time the communication was made." *State v. McIntosh*, 336 N.C. 517, 523-24, 444 S.E.2d 438, 442 (1994) (quoting *State v. Murvin*, 304 N.C. 523, 531, 284 S.E.2d 289, 294 (1981)); *Evans v. United Servs. Auto. Ass'n*, 142 N.C. App. 18, 32, 541 S.E.2d 782, 791 (2001) (quoting *McIntosh*, 304 N.C. at 531, 284 S.E.2d 294); see *State v. Jennings*, 333 N.C. 579, 611-12, 430 S.E.2d 188, 204 (1993) (concluding that a judge is not an attorney for purposes of the application of the attorney-client privilege, since a judge cannot engage in private practice in North Carolina); *State v. Van Landingham*, 283 N.C. 589, 601, 197 S.E.2d 539, 547 (1973) (noting that the attorney-client privilege cannot attach to communications with an advisor who had no right to appear on behalf of a prisoner in court); *State v. Smith*, 138 N.C. 700, 702, 50 S.E. 859, 860 (1905) (finding the attorney client privilege would not attach if the advisor could not appear as the prisoner's attorney in court); see also *Nemecek v. Bd. of Governors of the Univ. of N.C.*, 48 Fed. R. Serv. 3d (West) 254, 2000 WL 33672978 (E.D.N.C. Sept. 27, 2000) (holding that communications with "lay representative" of professor in university tenure dispute not protected by attorney-client privilege because representative was not an attorney). The Fourth Circuit Court of Appeals requires that "[t]he person to whom the communication is made is a member of a bar of a court, or his subordinate, and in connection with this communication is acting as a lawyer . . ." *Better Gov't Bureau, Inc. v. McGraw (In re Allen)*, 106 F.3d 582, 600 (4th Cir. 1997). In-house counsel normally are not required to maintain bar membership in every state in which counsel performs services. Paper Converting

forth in Rule 2.1 of the ABA Model Rules of Professional Conduct: "In representing a client, a lawyer shall exercise independent professional judgment and render candid advice."⁸⁷

In the context of corporate legal representation, the requirement of independence can perhaps best be seen in the application of Rule 1.13 of the ABA Model Rules of Professional Conduct.⁸⁸ The rule sets out the ethical principles that apply to a lawyer for an organization, such as a corporation,⁸⁹ and spells out that a lawyer for a corporation who learns that a corporate officer is acting in a manner that would violate a legal obligation to the corporation, or result in a violation of law that might be imputed to the organization, should consider a number of possible actions including, "going up the ladder" within the organization, ultimately to the company's board of directors, in an effort to rectify the situation.⁹⁰ If this "internal whistle-blowing"⁹¹ does not

Mach. Co. v. FMC Corp., 215 F. Supp. 249, 251 (E.D. Wis. 1963); see RICE, *supra* note 20, §§ 3.2, 3.14; VILLA, *supra* note 23, § 1.05. They are, however, generally required to be admitted to the bar of at least one state. See United States v. United Shoe Machinery Corp., 89 F. Supp. 357, 360 (D.Mass. 1950); RICE, *supra* note 20, § 3.2 at 9 n.13; VILLA, *supra* note 23, § 1.05.

87. ABA MODEL RULES OF PROF'L CONDUCT R. 2.1; see also N.C. REVISED RULES OF PROF'L CONDUCT R. 2.1 (similarly stated as the analogous ABA rule).

88. ABA MODEL RULES OF PROF'L CONDUCT R. 1.13; see 1 HAZARD & HODES, *supra* note 82, § 17.1.

89. ABA MODEL RULES OF PROF'L CONDUCT R. 1.13.

90. ABA MODEL RULES OF PROF'L CONDUCT R. 1.13; 1 HAZARD & HODES, *supra* note 82, § 17.11-17.12. Rule 1.13(b) provides as follows:

If a lawyer for an organization knows that an officer, employee, or other person associated with the organization is engaged in action, intends to act, or refused 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 which reasonably might be imputed to the organization and is likely to result in substantial injury to the organization, the lawyer shall proceed as is reasonably necessary in the best interest of the organization. In determining how to proceed, the lawyer shall give due consideration to the seriousness of the violation and its consequences, the scope and nature of the lawyer's representation, the responsibility in the organization and the apparent motivation of the person involved, the policies of the organization concerning such matters, and any other relevant considerations. Any measures taken shall be designed to minimize disruption of the organization and the risk of revealing information relating to the representation to persons outside the organization. Such measures may include among others:

remedy the problem, the rule leaves only one practical alternative for the attorney—to resign:

If, despite the lawyer's efforts in accordance with paragraph (b), the highest authority that can act on behalf of the organization insists upon action, or a refusal to act, that is clearly a violation of law and is likely to result in substantial injury to the organization, the lawyer may resign or withdraw in accordance with Rule 1.16.⁹²

Somewhat ironically, the same ethical requirement of independence for corporate lawyers may result in a perceived lack of independence of in-house counsel, as opposed to outside practitioners.⁹³ Resignation from representation of the in-house counsel's one and only client likely will be an event of substantially greater magnitude for the in-house lawyer than it would be to a private practitioner who does work for numerous clients.⁹⁴ As one commentator noted: "To sacrifice the fruits (both present and

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- (1) asking reconsideration of the matter;
 - (2) advising that a separate legal opinion on the matter be sought for presentation to appropriate authority in the organization; and
 - (3) referring the matter to higher authority in the organization, including, if warranted by the seriousness of the matter, referral to the highest authority that can act on behalf of the organization as determined by applicable law.

ABA MODEL RULES OF PROF'L CONDUCT R. 1.13(b).

91. 1 HAZARD & HODES, *supra* note 82, § 17.12 at 17-40.

92. N.C. REVISED RULES OF PROF'L CONDUCT R. 1.13(b).

93. Brian D. Farrow, *The Corporate Department Lawyer: Counsel to the Entity*, 34 BUS. LAW. 1797, 1802 (1979).

94. Susanna M. Kim, *Dual Identities and Dueling Obligations: Preserving Independence in Corporate Representation*, 68 TENN. L. REV. 179, 204 (2001) ("One of the most salient distinguishing features between inside and outside counsel for the corporation is the economic dependence of inside counsel on a single client."); see Rachel S. Arnov Richman, *A Cause Worth Quitting For? The Conflict Between Professional Ethics and Individual Rights in Discriminatory Treatment of Corporate Counsel*, 75 IND. L.J. 963, 989-91 (2000); Sally R. Weaver, *Ethical Dilemmas of Corporate Counsel: A Structural and Contextual Analysis*, 46 EMORY L. J. 1023, 1027 (1997).

future) of a career devoted singlemindedly to the affairs of a single client has perhaps even the flavor of Greek tragedy."⁹⁵

In addition to economic dependence on their corporation clients for their paychecks, in-house lawyers also may find opportunities for great financial reward tied to the success of their employer. This linkage can undermine the perception of lawyer independence that has undergirded availability of privilege and work product protection. For example, James Derrick, the general counsel of Enron Corporation, found significant fortune through his stock ownership and compensation programs benchmarked to the performance of the corporation.⁹⁶ While good arguments can be made that there is little difference between in-house counsel and partners in law firms that have large corporate clients,⁹⁷ questions continue to be raised regarding the policy of applying the privilege to in-house counsel.⁹⁸

95. Forrow, *supra* note 93, at 1802; see also 24 WRIGHT & GRAHAM, *supra* note 85, § 5480 at 244-45 and n.37.

96. Prior to the bankruptcy filing of Enron Corporation, Derrick sold more than \$12.5 million in Enron stock that he received as part of his compensation package, according to information reported to the SEC. Rozen, *supra* note 80, at 1.

97. 24 WRIGHT & GRAHAM, *supra* note 85, § 5480 at 245 n.37. Note in this regard the questions recently raised in connection with representation of Enron Corporation by the Houston firm of Vinson & Elkins, Enron's primary outside counsel. Riva D. Atlas, *Enron's Many Strands: The Law Firm; A Law Firm's 2 Roles Risk: Suit by Enron, Experts Say*, N.Y. TIMES, Jan. 29, 2002, at C1.

98. *Ryall v. Appleton Electric Co.*, 153 F.R.D. 660, 662 n.1 (D. Col. 1994) ("For reasons grounded in the historical foundation underlying the attorney-client privilege, . . . I question the fairly recent expansion of the privilege to encompass corporate in-house counsel. Nevertheless, applying the law as it is and not as I think it should be . . ."); see VILLA, *supra* note 23, § 1.05. The European Court of Justice, for example, has ruled that in-house counsel in the European Community are not entitled to protection of the attorney-client privilege, "based on the assumption that once attorneys are employed by a corporation they can no longer be independent." Alison M. Hill, Note, *A Problem of Privilege: In-House Counsel and the Attorney-Client Privilege in the United States and the European Community*, 27 CASE W. RES. J. INT'L L. 145, 145-46 (1995). See generally Joseph Pratt, Comment, *The Parameters of the Attorney-Client Privilege for In-House Counsel at the International Level: Protecting the Company's Confidential Information*, 20 Nw. J. INT'L L. & BUS. 145 (1999); Maurits Dolmans, *Attorney-Client Privilege For In-House Counsel: A European Proposal*, 4 COLUM. J. EUR. L. 125 (1998).

B. *Function of In-House Counsel: Lawyer or Businessman*

Notwithstanding the lingering concerns regarding in-house counsel independence, the courts in the United States have in principle settled the issue in favor of applying the attorney-client privilege to communications to and from in-house lawyers.⁹⁹ They sometimes apply the privilege and work product doctrine differently, though, to in-house attorneys.

Although he served as “outside” counsel, Joel Dolkart played multiple roles for Gulf & Western, much like an in-house counsel in a typical organization.¹⁰⁰ His case illustrates the examination of these concerns by looking at the functions actually performed by in-house lawyers.¹⁰¹ Courts may apply special scrutiny to the functions performed by in-house counsel in determining whether the relevant communications were sufficiently tied to the lawyer’s legal, as opposed to business, financial, or other services and advice.

1. Attorney-Client Privilege and “Legal Advice”

In the *Gulf & Western* case,¹⁰² the district court was troubled that Dolkart “wore several hats”: lawyer, director, corporate secretary, and a member of the company’s pension advisory committee.¹⁰³ The court was unable to assume that his “discussions with corporate officials involved legal advice,” one of the foundational elements of attorney-client privilege.¹⁰⁴ The problem illustrated by his multi-faceted work for Gulf & Western is even more serious for in-house counsel.

There has never been any question that privileged communications must have been made “for the purpose of

99. *Upjohn Co. v. United States*, 449 U.S. 383 (1981); *United States v. United Shoe Machinery Corp.*, 89 F. Supp. 357, 360 (D. Mass. 1950); see RICE, *supra* note 20, § 3.14; VILLA, *supra* note 23, § 1.05.

100. *Sec. & Exch. Comm’n v. Gulf & W. Indus., Inc.*, 518 F. Supp. 675, 678 (D.D.C. 1981).

101. See generally 518 F. Supp. 675.

102. See *supra* notes 1-9 and accompanying text.

103. 518 F. Supp at 678.

104. *Id.* at 683.

obtaining legal assistance."¹⁰⁵ The problem is how to determine when a communication is for the purpose of legal assistance where there may be more than one reason for the communication. The difficulty is perhaps most easily seen when in-house counsel also serves as a member of the board of directors of the corporation client.¹⁰⁶ As one corporate lawyer lamented:

[T]he conversation is always muddled: there's a legal answer and then there's ten minutes of business answers and then there's five minutes of legal answers and then there's seven minutes of business answers, and so on. You can't try to sit there with two hats, taking them off and putting them on and taking them off and figuring out how you are going to document [the distinction].¹⁰⁷

This problem also extends to in-house counsel who are not board members. In-house counsel are "expected to be immersed in the corporation" functioning as "members of the 'team' responsible for running the business."¹⁰⁸ As valuable team members, employee-lawyers are inevitably involved in inseparable business and legal roles.

Courts have formulated various approaches in attempting to divine the purpose of counsel communications in connection with applying attorney-client privilege. The Restatement Third of the Law Governing Lawyers requires that "[a] client must consult the lawyer for the purpose of obtaining legal assistance and *not predominantly for another purpose*."¹⁰⁹ The Restatement ventures that determining whether the test is met "depends upon the circumstances," and looks to the extent the lawyer performs legal and non-legal work, the nature of the communication, and whether or not the lawyer previously provided legal assistance relating to

105. RESTATEMENT (THIRD) OF THE LAW GOVERNING LAWYERS § 72 (1993); *see* State v. McInstosh, 336 N.C. 517, 444 S.E.2d 438 (1994).

106. Kim, *supra* note 94, at 239-42.

107. *Id.* at 19 (quoting Conflict of Interest and Corporate Counsel: Choosing the Best Path, ACCA Docket, Fall 1993, at 42 (remarks of Norman Krishova)).

108. Richman, *supra* note 94, at 991.

109. RESTATEMENT (THIRD) OF THE LAW GOVERNING LAWYERS § 72 cmt. c (1993) (emphasis added).

the same matter.¹¹⁰ In general, though, the Restatement characterizes American decisions as applying the privilege if “one of the significant purposes of a client in communicating with a lawyer is that of obtaining legal assistance.”¹¹¹ Some courts have applied a “but-for” test in the determination, holding a communication privileged if it would not have been made but for the legal advice purpose.¹¹²

Other courts have applied a more stringent analysis, at least where in-house counsel communications are at issue. In *Rossi v. Blue Cross and Blue Shield of Greater New York*,¹¹³ the New York Court of Appeals examined an internal memorandum from in-house counsel regarding a defamation claim against Blue Cross. The potential claimant had challenged language in Blue Cross’s coverage rejection form that labeled certain medical procedures “experimental” or “not generally recognized by an appropriate governmental agency.”¹¹⁴ The memorandum was prepared on the day the defamation suit was served on Blue Cross¹¹⁵ and was sent to the Blue Cross medical director and copied to the company’s general counsel. It covered conversations between the staff attorney and plaintiff’s counsel, conversations between the staff counsel and the Food & Drug Administration regarding the

110. *Id.*

111. *Id.* § 122 cmt. c reporter’s note.

112. *Reich v Hercules, Inc.*, 857 F. Supp. 367, 373 (D.N.J. 1994) (using a “but for” test, instead of a predominant purpose, in finding that reviews made in the ordinary course of business for at least two years prior to an accident for the employer’s own internal safety reasons did not qualify for the privilege); *see also* *S. Bell Tel. & Tel. Co. v. Deason*, 632 So.2d 1377, 1383 (Fla. 1994) (establishing a five-pronged test to determine what communications are privileged); *First Chicago Int’l v. United Exch. Co. Ltd.*, 125 F.R.D. 55, 57 (S.D.N.Y. 1989) (finding that the fraud investigation documents were created only because counsel asked for them to use in providing legal advice, and therefore entitled to the privilege).

113. *Rossi v. Blue Cross and Blue Shield of Greater N.Y.*, 540 N.E.2d 703 (N.Y. 1989).

114. *Id.* at 704. The plaintiff was a radiologist who performed nuclear magnetic resonance imaging. *Id.* Blue Cross allegedly rejected more than 2000 claims from the plaintiff’s patients who were Blue Cross subscribers, by sending them a form that stated: “Your contract does not cover procedures which are experimental or whose effectiveness is not generally recognized by an appropriate governmental agency.” *Id.* The new procedure apparently had been approved by the FDA, but Blue Cross continued its rejection policy even after the plaintiff notified it of the government approval. *Id.*

115. *Id.*

plaintiff's medical procedure, the staff lawyer's understanding of Blue Cross's reimbursement policy and the rejection language, and the staff lawyer's opinion and advice regarding the rejection language.¹¹⁶ The court held that the memorandum was covered by the attorney-client privilege, but in so doing held that a privileged communication must be "primarily or predominantly of a legal character" to qualify for protection.¹¹⁷ The court noted that the Blue Cross staff attorney functioned only as a lawyer for the company and did not perform any other role, and found persuasive the fact that the memorandum was prepared on the very day the lawsuit was received.¹¹⁸ In analyzing the applicable law, however, the court observed:

[U]nlike the situation where a client individually engages a lawyer in a particular matter, staff attorneys may serve as company officers, with mixed business-legal responsibility; whether or not officers, their day-to-day involvement in their employers' affairs may blur the line between legal and nonlegal communications; and their advice may originate not in response to the client's consultation about a particular problem but with them, as part of an ongoing, permanent relationship with the organization. In that the privilege obstructs the truth-finding process and its scope is limited to that which is necessary to achieve its purpose, the need to apply it cautiously and narrowly is heightened in the case of corporate staff counsel, lest the mere participation of an attorney be used to seal off disclosure.¹¹⁹

116. *Id.*

117. *Id.* at 706. The "predominant purpose" requirement follows the English view. RESTATEMENT (THIRD) OF THE LAW GOVERNING LAWYERS § 122 cmt. c reporter's note (1998) (citing *Waugh v. British Rys. Bd.*, [1980] A.C. 521 (H.L.)).

118. *Rossi*, 540 N.E.2d at 706.

119. *Id.* at 705 (internal citations omitted) (quoted in *Georgia-Pacific Corp. v. GAF Roofing Manufacturing Corp.*, 1996 WL 29392, at *3-4 (S.D.N.Y. Jan. 25, 1996)).

In a much discussed 1996 case, *Georgia-Pacific Corp. v. GAF Roofing Manufacturing Corp.*,¹²⁰ the United States District Court for the Southern District of New York applied perhaps the most stringent test in finding the attorney-client privilege unavailable to protect communications between in-house environmental counsel and corporate officers in connection with the negotiation of an asset purchase agreement. The court found that counsel's role as a negotiator fell outside the "traditional function" of a lawyer and that his conversations as part of the negotiation process "involved business judgments of environmental risks."¹²¹

The case involved a breach of contract claim by Georgia-Pacific against GAF, which had undertaken to acquire certain assets related to Georgia-Pacific's roofing business.¹²² GAF refused to close on the properties after a dispute arose with respect to Georgia-Pacific's responsibility to complete environmental remediation of one of the properties.¹²³ Michael Scott, an in-house environmental lawyer for GAF, had reviewed the environmental representations and covenants in the proposed asset purchase agreement.¹²⁴ He had expressed concerns to management about indemnification coverage and other matters and suggested to senior management ways to negotiate the agreement.¹²⁵ Scott later personally took part in the negotiations with respect to environmental provisions of the asset purchase agreement, including the same provisions that GAF relied on in refusing to close on the purchase.¹²⁶

In the ensuing litigation, Georgia-Pacific sought to ask Scott three questions in a deposition: (1) what recommendations had he made to GAF's negotiators as to how the proposed agreement should be changed and what the impact of the changes would be; (2) whether he recommended to GAF senior management that GAF should consider certain options other than an indemnification; and (3) whether a senior GAF executive had

120. *Georgia-Pacific Corp. v. GAF Roofing Mfg. Corp.*, 1996 WL 29392 (S.D.N.Y. Jan. 25, 1996).

121. *Id.* at *4-*5.

122. *Id.* at *1.

123. *Id.* at *2.

124. *Id.* at *1.

125. *Georgia-Pacific Corp.*, 1996 WL 29392, at *1.

126. *See id.* at *1-*2.

asked him to cancel a meeting that had been scheduled with Georgia-Pacific lawyers.¹²⁷

The district court ruled that none of these communications were protected by the attorney-client privilege because of Scott's role as a negotiator rather than a legal advisor:

[I]t is clear that Mr. Scott was not "exercising a lawyer's traditional function." The record indicates that Mr. Scott was asked to review GP's proposed agreement with respect to the environmental provisions. He then negotiated the environmental provisions of the agreement, and after execution of the agreement, he served as negotiator of the matters to be included in Schedule 1. *As a negotiator on behalf of management, Mr. Scott was acting in a business capacity . . .* Mr. Scott's averment that he rendered legal advice to management, although considered, does not overcome the nature of his role in the transaction as revealed by his deposition.¹²⁸

127. *Id.* at *2-*3.

128. *Id.* at *4-*5 (internal citations omitted) (emphasis added). The decision has spawned blistering criticism from the ABA and numerous commentators. See, e.g., Mark C. Van Deusen, *The Attorney-Client Privilege for In-House Counsel When Negotiating Contracts: A Response to Georgia-Pacific Corp. v. GAF Roofing Manufacturing Corp.*, 39 WM. & MARY L. REV. 1397 (1998); Weiss, *supra* note 85; Jerome J. Shestack, *ABA Speaks Out for Corporate Counsel and "The Rule of Law"*, 5 METROPOLITAN CORP. COUNS. 1 (Dec. 1997), WL 12/97 Metro. Corp. Couns. 1; McNeil, 1997 ABA Sec. of Litig. Rep. 120 (on file with author). In a case based on what one commentator has labeled "'an almost identical fact situation,' the United States District Court for the Northern District of Illinois, in *Diversey U.S. Holdings, Inc. v. Sara Lee Corp.*, had no difficulty finding that [the] privilege covered information gathering and negotiation services provided by in-house counsel." ROBERT L. HAIG, *SUCCESSFUL PARTNERING BETWEEN INSIDE AND OUTSIDE COUNSEL* 33-49 (citing *Diversey U.S. Holdings, Inc. v. Sara Lee Corp.*, No. 91 C 6234, 1994 WL 71462 (N.D. Ill. Mar. 3, 1994)). In that case, Sara Lee's in-house counsel participated in negotiating the language to be used in the contract in question and circulated draft language to various employees to get comments. *Diversey*, 1994 WL 71462, at *1 (N.D. Ill. Mar. 3, 1994). The court concluded that:

[t]his strikes us as the gathering of information by an attorney from the client to enable the attorney to provide competent legal services—in this case, the drafting of a contract. Drafting legal documents is a core activity of lawyers, and obtaining

Georgia Pacific and related cases highlight a difficult problem for in-house lawyers: most courts will honor a presumption that outside counsel's communications are for legal advice, but the same is not true for in-house counsel.¹²⁹ In-house counsel must be particularly aware of the legal advice requirement.¹³⁰ Those who hold multiple offices in the corporate structure may be especially vulnerable, even in contexts other than negotiation.¹³¹ In the final

information and feedback from clients is a necessary part of the process. Thus, we find that Sara Lee's attorneys were acting in a legal, not business capacity.

Id. at *1.

129. *Compare* *Diversified Indus., Inc. v. Merideth*, 572 F.2d 596, 610 (8th Cir. 1977), with *United States v. Chevron Corp.*, 1996 U.S. Dist. LEXIS 8646, at *4 (N.D. Cal. May 29, 1996); see *VILLA*, *supra* note 23, § 1.16.

130. See EDNA SELAN EPSTEIN, *THE ATTORNEY-CLIENT PRIVILEGE AND THE WORK-PRODUCT DOCTRINE* 136, 233 (4th ed. 2001).

Nothing is harder to disentangle in the modern business world than in-house counsel who gives legal advice but is also intimately involved with the business operations of the client. . . . Corporations and in-house counsel need to be aware that not every communication that they believe will necessarily be privileged will indeed be safe from compelled disclosure.

Id.

131. At board and other meetings, an in-house counsel who is also a board member or corporate officer may wish to be cautious not to intermingle his or her notes regarding legal problems and advice with notes regarding the business matters discussed at the meeting. See *Boca Investerings P'ship v. United States*, 31 F. Supp. 2d 9, 12 (D.D.C. 1998) (explaining, in a case in which an attorney was a corporation's vice president for taxes, that "[w]hen a lawyer acts merely to implement a business transaction or provides accounting services, the lawyer is like any other agent of the corporation whose communications are not privileged"); *Borase v. M/A Com, Inc.*, 171 F.R.D. 10, 14 (D. Mass. 1997) (observing in case in which attorney was corporation's general counsel, former senior vice-president, and corporate secretary that "[t]he attorney-client privilege attaches only when the attorney acts in that capacity. . . . It does not apply when in-house counsel is engaged in nonlegal work." (citations and internal quotations omitted)). In *Kramer v. Raymond Corporation*, the defendant sought to protect as privileged the minutes for its Corporate Product Liability Management Team. 1992 WL 122856, at *1 (E.D. Pa. May 29, 1992). The defendant provided an affidavit from its former general counsel summarizing the function of the liability management team as "gathering and sharing of information concerning (a) pending product liability claims, (b) reported accidents which might lead to product liability claims, and (c) possible actions which might be taken to minimize or avoid potential product liability claims." *Id.* at *2. Additionally, former counsel's affidavit described his role to include providing legal advice to the team and using information gathered by the team to provide "legal advice to the Corporation and to assist outside counsel in defending litigation." *Id.* The court did not find that

analysis, the legal/business overlap inherent in the job of in-house counsel makes it extremely difficult for in-house lawyers, and for those corporate officers and employees who must communicate with in-house counsel, to know whether their words may later become part of compelled testimony.

2. Work Product Immunity and “Anticipation of Litigation”

While *Georgia Pacific* and similar cases have narrowed the attorney-client privilege that many in-house counsel had relied upon, the courts have also been careful to examine the function played by counsel, and particularly in-house counsel, in applying the work product doctrine.¹³² In particular, courts have sought to distinguish between documents prepared “in anticipation of litigation” and those prepared in the ordinary course of business¹³³ and, in so doing, have been willing to find a business—as opposed to a litigation—purpose in many contexts.¹³⁴

The Supreme Court in *Hickman v. Taylor* initially questioned the availability of work product protection to corporations because of concerns that corporations could unfairly use their lawyers to keep important “facts” from litigants.¹³⁵ The Court determined that these concerns did not override the policy considerations that support work product protection in the corporate context,¹³⁶ and the work product doctrine has consistently been applied to corporate counsel.¹³⁷ Application of the doctrine in the corporate context, and particularly in situations

all the communications “were made primarily for the purpose of securing legal advice” and did not allow the privilege for the minutes. *Id.*

132. See VILLA, *supra* note 23, § 2.07.

133. See, e.g., *Willis v. Duke Power Co.*, 291 N.C. 19, 35, 229 S.E.2d 191, 201 (1976); *Evans v. United Servs. Auto. Ass’n*, 142 N.C. App. 18, 28, 541 S.E.2d 782, 789 (2001).

134. VILLA, *supra* note 23, §2.07. See Thomas Wilson, Note, *The Work Product Doctrine: Why Have an Ordinary Course of Business Exception?*, 1988 COLUM. BUS. REV. 587 (1988).

135. 329 U.S. at 506.

136. *Id.* at 507.

137. *Radiant Burners, Inc. v. Am. Gas Ass’n*, 207 F. Supp. 771, 776 (N.D. Ill. 1962), *rev’d on other grounds*, 320 F.2d 314 (7th Cir. 1963), *cert. denied*, 375 U.S. 929 (1963); see *Sandberg v. Va. Bankshares, Inc.*, 979 F.2d 332, 355 n.22 (4th Cir. 1992) vacated, 1993 WL 524680 (4th Cir. 1993) (on appellee’s unopposed motion to vacate and remand to district court for dismissal); VILLA, *supra* note 23, § 2.01.

involving in-house counsel, though, continues to pose problems for courts, which remain concerned with the potential for abuse by corporate litigants and their counsel.¹³⁸

Thus, while the work product doctrine does protect documents prepared by other corporate employees acting under the direction of counsel in an appropriate context, courts have expressed a concern that in-house counsel's office not be used to create a screen against discovery:

[S]ince Rule 26 clearly protects party, and not just attorney, preparation, the fact that a particular communication may not go to an attorney does not prevent its being work product. At the same time, if an attorney is simply a "mail drop" for the purposes of trying to create a screen against discovery, and the content of the document indicates it is neither work product nor a communication subject to the attorney-client privilege, the fact that a document is sent through an attorney cannot prevent its having to be produced.¹³⁹

Courts often require an especially strong showing that documents prepared by in-house counsel were prepared in anticipation of litigation. Meeting notes taken by in-house counsel are examined very closely. The court in *Redvanly v. NYNEX Corp.* denied work product protection to extensive notes taken by in-house counsel during a meeting in which a disgruntled employee was confronted with allegations of wrongdoing and terminated.¹⁴⁰ Notwithstanding specific testimony from counsel that his notes were prepared in anticipation of litigation both by the disgruntled employee and another employee, and that they recorded his mental impressions and opinions, the court found the work product doctrine inapplicable: "[C]ontrary to defendant's counsel's representations, the notes are hardly [counsel's] 'mental impressions and thoughts.' They are, in essence, a running

138. See VILLA, *supra* note 23, § 2.01.

139. *In re Air Crash Disaster at Sioux City, Iowa*, 133 F.R.D. 515, 520 (N.D. Ill. 1990); see VILLA, *supra* note 23, § 2.04.

140. 152 F.R.D. 460, 465 (S.D.N.Y. 1993).

transcript of the meeting in abbreviated form."¹⁴¹ After characterizing testimony by the attorney as "dishonest," the court ordered production of the notes since "the 'anticipation of litigation' requirement is not met simply because a document is prepared in the course of business that a party knows may be useful in the event litigation should ensue."¹⁴²

The Fourth Circuit Court of Appeals addressed the application of work product protection to in-house counsel's meeting notes in *Sandberg v. Virginia Bankshares, Inc.*,¹⁴³ a 1992 case involving a claim for breach of directors' fiduciary duties in connection with a merger. When a group of shareholders filed a state court action seeking to enjoin the proposed merger, the general counsel of a bank that proposed to merge with a holding company subsidiary attended a meeting with officials of the bank, its proposed merger partner and outside counsel for both parties.¹⁴⁴ The meeting was called both to review litigation strategy with respect to the injunction lawsuit and to conduct a "final review" of the proposed merger prior to a shareholder meeting scheduled shortly thereafter.¹⁴⁵ At the meeting, the bank's CEO considered postponing the meeting and obtaining an independent valuation because of concerns raised regarding the purchase price; however, counsel for the holding company persuaded him to go forward without a separate valuation.¹⁴⁶ The plaintiff shareholders in a subsequent case sought to obtain the bank general counsel's notes of this meeting, which concededly focused in part at least on the pending litigation.¹⁴⁷ The court ordered production of the notes:

[The defendant] has not shown that the Bank's general counsel prepared the notes in anticipation of litigation rather than in the 'ordinary course of business.' Although the general counsel's affidavit indicates the purposes of the April 20 meeting, *it*

141. *Id.* at 466.

142. *Id.* at 467.

143. 979 F.2d 332 (4th Cir. 1992), *vacated*, 1993 WL 524680 (4th Cir. 1993) (on appellee's unopposed motion to vacate and remand to district court for dismissal).

144. *Id.* at 348-49.

145. *Id.* at 349.

146. *Id.*

147. *Id.*

does not indicate her purpose in making the notes. The mere fact that a lawsuit was pending does not transform an attorney's notes into material prepared in anticipation of litigation. Moreover, while a general counsel may be involved in litigation strategy and oversight, *it is also possible that her involvement in the litigation is no different from that of other corporate officers.* In either case, her purpose in taking the notes is not self-evident and we find that [defendant] has failed to satisfy its burden of proof on this issue.¹⁴⁸

Courts have also addressed the "anticipation of litigation" requirement in the context of internal corporate investigations, where they have been very careful to scrutinize the claim for protection where the corporate client has a high public profile or may have other business reasons for the investigation.¹⁴⁹ In *In re Kidder Peabody Securities Litigation*,¹⁵⁰ the federal district court denied work product protection to a report of an internal investigation performed by counsel. Because of "Kidder's unique public profile and its vulnerability to the ebb and flow of market opinion and the predations of its competitors,"¹⁵¹ the court concluded that Kidder would have hired counsel to perform the inquiry "even if no litigation had been threatened at the time."¹⁵² The court in *In re Leslie Fay Companies, Inc. Securities Litigation*¹⁵³ similarly denied protection to an internal investigation report because the report would have been prepared even absent litigation in connection with decisions on firing personnel, determining the magnitude of the suspected fraud, implementing new internal control procedures, and reassuring creditors that the company was vigorously addressing the matters at issue.¹⁵⁴

Although some courts have thus confined work product protection to documents created "primarily," "principally," or

148. *Id.* at 356 (emphasis added).

149. VILLA, *supra* note 23, § 2.07.

150. *In re Kidder Peabody Sec. Litig.*, 168 F.R.D. 459 (S.D.N.Y. 1996).

151. *Id.* at 466.

152. *Id.* at 465.

153. *In re Leslie Fay Cos., Inc. Sec. Litig.*, 161 F.R.D. 274 (S.D.N.Y. 1995).

154. *Id.* at 280-81.

“exclusively” to assist in litigation,¹⁵⁵ a recent decision by the Second Circuit Court of Appeals, *United States v. Adlman*,¹⁵⁶ modified this test in a way that could become important for corporations that claim work product protection. The *Adlman* court held that a document need not be prepared primarily or exclusively to assist in litigation in order to meet the anticipation-of-litigation test. Rather, the test is whether “the document can fairly be said to have been prepared or obtained *because of* the prospect of litigation.”¹⁵⁷ Documents prepared for both litigation and business purposes will be protected unless such documents “would have been created in essentially similar form irrespective of the litigation.”¹⁵⁸

Adlman involved a legal analysis prepared at the request of Sequa Corporation by an attorney-accountant with Arthur Andersen & Co.¹⁵⁹ In 1989, Sequa was considering a merger of two of its wholly owned subsidiaries.¹⁶⁰ Sequa hired Andersen to evaluate the tax implications of the proposed transaction, and Andersen’s attorney-accountant prepared a detailed memorandum that considered likely IRS challenges to the transaction, analyzed possible legal theories and strategies that Sequa could adopt in response, recommended means of structuring the transaction, and made predictions regarding the likely outcome of litigation.¹⁶¹ Sequa proceeded with the transaction.¹⁶² On audit, the IRS requested the Andersen analysis and Sequa cited the work product doctrine in refusing to turn it over.¹⁶³ The district court twice denied Sequa’s claim of work product protection: first on the basis that the document “was prepared for litigation based on actions or events that had not yet occurred at the time of its creation” and, after the Court of Appeals rejected this rationale,¹⁶⁴ on the ground

155. See VILLA, *supra* note 23, § 2.07, n.97 (citing several cases).

156. *United States v. Adlman*, 134 F.3d 1194 (2d Cir. 1998).

157. *Id.* at 1202.

158. *Id.* at 1202; see *Mount Vernon Fire Ins. Co. v. Try 3 Bldg. Services, Inc.*, 1998 WL 729735, at *3 (S.D.N.Y. Oct. 16, 1998) (discussing both the 1995 and the 1993 Second Circuit *Adlman* cases).

159. *Adlman*, 134 F.3d at 1195.

160. *Id.*

161. *Id.* at 1195.

162. *Id.*

163. *Id.* at 1196.

164. *United States v. Adlman*, 68 F.3d 1495, 1501 (2d Cir. 1995).

that the analysis was not prepared “in anticipation of litigation.”¹⁶⁵ On appeal, the Second Circuit ruled in *Sequa*’s favor, rejecting the “primarily or exclusively to assist in litigation” test in favor of its “because of” test in determining whether a document is prepared in anticipation of litigation.¹⁶⁶

The court identified as a question of first impression in the Second Circuit, “whether [the work product doctrine] is inapplicable to a litigation analysis prepared by a party or its representative in order to *inform a business decision which turns on the party’s assessment of the likely outcome of litigation expected to result from the transaction.*”¹⁶⁷ Applying the doctrine only to documents prepared primarily to assist in litigation, the court said, would exclude any analysis prepared to aid the business decision with respect to a proposed transaction.¹⁶⁸ The court thus preferred the “because of” approach articulated in the Wright & Miller federal procedure treatise:

The Wright & Miller “because of” formulation accords with the plain language of Rule 26(b)(3) and the purposes underlying the work product doctrine. Where a document is created because of the prospect of litigation, analyzing the likely outcome of that litigation, it does not lose protection under this formulation merely because it is created in order to assist with a business decision.¹⁶⁹

The *Adlman* decision has been described as a significant expansion of the applicability of the work product doctrine.¹⁷⁰ Still, the issue of when documents are prepared in anticipation of litigation will continue to be particularly vexing for in-house

165. *United States v. Adlman*, 134 F.3d 1194, 1196 (2d Cir. 1998).

166. *Adlman*, 134 F.3d at 1197-98.

167. *Id.* at 1197 (emphasis added).

168. *Id.* at 1198-99.

169. *Id.* at 1202.

170. *See, e.g.*, Harvey Kurzweil, Paul J. Bschorr, & Daniel S. Goldsmith, *Second Circuit Interprets and Potentially Expands Work Product Protection*, WL 12 No. 7 INSIGHTS 27 (1998); Charles M. Yablon & Steven S. Sparling, *United States v. Adlman: Protection for Corporate Work Product?*, 64 BROOKLYN L. REV. 627 (1998).

counsel.¹⁷¹ In a case decided six years before *Adlman*, the Fourth Circuit Court of Appeals advanced an apparently more limited “because of” test, holding that the “driving force” behind preparation of a document is the key inquiry:

The document must be prepared *because* of the prospect of litigation when the preparer faces an actual claim or a potential claim following an actual event or series of events that reasonably could result in litigation. Thus, we have held that materials prepared in the ordinary course of business or pursuant to regulatory requirements or for other non-litigation purposes are not documents prepared in anticipation of litigation within the meaning of Rule 26(b)(3). . . . Following any industrial accident, it can be expected that designated personnel will

171. *Mount Vernon*, 1998 WL 729735, at *5. See *Granite Partners v. Bear, Stearns & Co., Inc.*, 184 F.R.D. 49 (S.D.N.Y. 1999). The court in *Granite Partners* ordered production of notes of witness interviews, valuation analyses, and other documents prepared by agents and consultants of a bankruptcy trustee even though they were prepared “because of” litigation, since the trustee had published a report that relied on the documentation and thereby waived the protection by placing the documents “at issue,” and because the plaintiff had overcome the presumption of protection by showing substantial need for the documents. 184 F.R.D. at 55-56. The court relied on the reasoning of the *In re Kidder Peabody Securities Litigation*, 168 F.R.D. 459 (S.D.N.Y. 1996), and *In re Leslie Fay Companies, Inc. Securities Litigation*, 161 F.R.D. 274 (S.D.N.Y. 1995), cases to deny the protection, and explained application of the *Adlman* precedent as follows:

It may well be said that the effect of *Adlman* is to enforce the work product privilege even if there is a dual purpose for the creation of the materials. However, even if the documents at issue were to fall within *Adlman*'s interpretation of Rule 26(b)(3), that would not end the inquiry. Indeed, the *Adlman* court confirmed that: although a finding under this test that a document is prepared because of the prospect of litigation warrants application of Rule 26(b)(3), this does not necessarily mean that the document will be protected against discovery. Rather, it means that a document is eligible for work-product privilege. The district court can then assess whether the party seeking discovery has made an adequate showing of substantial need for the document and an inability to obtain its contents elsewhere without undue hardship. . . . Furthermore, *Adlman* does not deal with the waiver issue presented here.

Granite Partners, 184 F.R.D. at 53.

conduct investigations, not only out of a concern for future litigation, but also to prevent reoccurrences, to improve safety and efficiency in the facility, and to respond to regulatory obligations. *Determining the driving force behind the preparation of each requested document* is therefore required in resolving a work product immunity question.¹⁷²

The courts of North Carolina also have applied a “because of” test to this question, albeit one that takes into account the “purpose” for creation of the document. In *Cook v. Wake County Hospital System, Inc.*,¹⁷³ the North Carolina Court of Appeals ordered production of a form accident report prepared by a hospital employee following a doctor’s serious slip-and-fall near the hospital’s intensive care unit. The court denied work product protection for the accident report:

Here defendant’s accident reporting policy exists to serve a number of *nonlitigation, business purposes*. These business purposes impose a continuing duty on hospital employees to report any extraordinary occurrences within the hospital to risk management. These duties exist whether or not the hospital chooses to consult its attorney in anticipation of litigation. Here, absent any other salient facts, it cannot be fairly said that the employee prepared the accident report *because of* the prospect of litigation. In short, the accident report would have been compiled, pursuant to the hospital’s policy, regardless of whether [plaintiff] intimated a desire to sue the hospital or whether litigation was ever anticipated by the hospital.¹⁷⁴

A very recent North Carolina case relied primarily on *Cook* to address the issue in the context of insurance company investigative reports. In *Evans v. United Services Automobile*

172. Nat’l Union Fire Ins. Co. v. Murray Sheet Metal, 967 F.2d 980, 984 (4th Cir. 1992); see Yablon & Sparling, *supra* note 170, at 644-45.

173. 125 N.C. App. 618, 482 S.E.2d 546 (1997).

174. *Cook*, 125 N.C. App at 625, 482 S.E.2d at 551-52 (emphasis added).

Association,¹⁷⁵ the North Carolina Court of Appeals held that an insurance company's entries in a "claims diary" and other investigative reports and materials are not entitled to work product immunity unless they were prepared after a decision by the insurer to deny coverage.¹⁷⁶ The court did not discuss *Adlman*, relying instead on the "ordinary course of business exception" to work product protection:

Here, defendants carried out the investigative process and ultimately denied plaintiff's claim. It appears that the investigation stage of the claims process is one carried out in the ordinary course of an insurer's business Until defendants determined that their homeowners' policy did not provide coverage to plaintiff, we cannot say as a matter of law that defendants "reasonably" anticipated litigation. Consequently, we do not believe that material prepared in the course of the investigatory process is normally entitled to the Rule 26 qualified work product immunity.¹⁷⁷

Thus, in spite of the expansion of work product immunity apparently heralded by *Adlman*, the availability of the protection remains far from certain in the corporate context, especially as it may apply to documents and reports prepared by in-house attorneys as part of their normal business "routine."¹⁷³

175. *Evans v. United Servs. Auto. Ass'n*, 142 N.C. App. 18, 541 S.E.2d 782 (2001).

176. *Id.* at 30-31, 541 S.E.2d at 790.

177. *Id.* at 30, 541 S.E.2d at 790; see *Mount Vernon Fire Ins. Co. v. Try 3 Bldg. Servs., Inc.*, 1998 WL 729735 (S.D.N.Y. Oct. 16, 1998). The court in *Mount Vernon* similarly held that investigative reports prepared for an insurance company were not protected by the work product doctrine in a coverage dispute where the investigation was carried out before the claim was referred to the insurer's counsel and before the company issued a reservation of rights as to the coverage issue. 1998 WL 729735 (S.D.N.Y. Oct. 16, 1998). The court noted the holding in *Adlman*, but found application of the doctrine to investigative reports prepared for insurance companies "particularly troublesome because it is the routine business of insurance companies to investigate and evaluate claims and to defend their insureds against third-party claims." *Id.* at *5.

178. In-house counsel should also consider the following cases: *Guy v. United Healthcare Corp.*, 154 F.R.D. 172, 181 (S.D. Ohio 1993) (noting that an attorney's draft of the minutes of a board meeting may not be protected by the work product doctrine if the draft and the subject matter of the meeting are not connected to the

V. PRIVILEGE AND THE REGULATED FINANCIAL INSTITUTION

If it is available, the attorney-client privilege is an absolute privilege.¹⁷⁹ The rationale is that qualifications to the privilege would make its application unpredictable. Without predictability, clients would lose confidence in the privilege, thus defeating the purpose of encouraging full and frank disclosure.¹⁸⁰ In the *Gulf & Western* decision discussed above, however, the District Court made clear its view that the SEC, in its role as “protector of the public interest,” may be able to show “good cause” that would justify requiring disclosure even if the privilege were deemed to apply.¹⁸¹ Not surprisingly, other regulatory agencies share the *Gulf & Western* court’s view of the importance of the public interest they are attempting to serve. For example, in the Comptroller’s Handbook used by the Office of the Comptroller of the Currency, the agency instructs its examiners to request privileged materials when a regulated bank’s “capital and earnings are exposed to material risk, or when the bank’s exposure is otherwise considered significant.”¹⁸² The Handbook also confirms the Comptroller’s view that “a bank that discloses privileged information to an examiner during an examination does not waive its privileges.”¹⁸³

threat of anticipated litigation); *Shipes v. BIC Corp.*, 154 F.R.D. 301, 308-09 (M.D. Ga. 1994) (stating that work product of “in-house experts” likely to be afforded less protection and that legal department databases that manage and track the status of claims against the corporation are protectable work product); *Carey-Canada, Inc. v. Cal. Union Ins. Co.*, 118 F.R.D. 242, 246 (noting that preliminary drafts of litigation footnotes prepared by in-house counsel that appear in a corporation’s annual report are usually drafted with the pending litigation in mind, and thus are protected under the work product doctrine); *Johnston v. Dillard Dept. Stores, Inc.*, 152 F.R.D. 89, 92-93 (E.D. La. 1993) (holding in-house attorney’s participation on a corporate committee, such as an ERISA plan committee, does not render the deliberations and minutes of the committee’s meetings protected work product).

179. *Willis v. Duke Power Co.*, 291 N.C. 19, 35, 229 S.E.2d 191, 201 (1976) (“The trial court should take care in its supervision of further discovery to protect fully defendant’s attorney-client privilege. This protection is absolute under Rule 26”); see *supra* notes 18-26 and accompanying text.

180. See RICE, *supra* note 20, § 2.2; VILLA, *supra* note 23, § 1.03 [B].

181. *Sec. & Exch. Comm’n v. Gulf & W. Indus., Inc.*, 518 F. Supp. 675, 686 (1981).

182. OFFICE OF THE COMPTROLLER OF THE CURRENCY, *Evaluating Other Legal Matters*, COMPTROLLER’S HANDBOOK, 2000 WL 226429 (O.C.C.).

183. OFFICE OF THE COMPTROLLER OF THE CURRENCY, *Access to Privileged Materials*, COMPTROLLER’S HANDBOOK, 2000 WL 226431 (O.C.C.); see also In the Matter of David Paul, Former Chairman of the Board, Chief Executive Officer and

It then sets forth certain steps for the examiner and counsel to take in order to preserve the privilege, which include exchanging written communications identifying the materials being provided and explaining that the materials are being provided pursuant to the Comptroller's examination authority.¹⁸⁴ Responding to the concern that disclosure to the Comptroller would constitute a waiver of the privilege, thus opening the door for required disclosure to other parties, the Comptroller assures counsel that the disclosure is not voluntary and thus does not constitute a waiver.¹⁸⁵

It is not clear, however, that the agency, simply by its own pronouncement, has the power or authority to determine whether the disclosure will constitute a waiver.¹⁸⁶ In *In re Leslie Fay Companies, Inc. Securities Litigation*,¹⁸⁷ the Federal District Court for the Southern District of New York refused to apply the

Controlling Shareholder of Centrust Bank, a State Savings Bank, No. OTS AP92-66 (O.T.S.) (July 8, 1992), 1992 WL 560965 (refusing to stay depositions on basis of alleged violation of attorney-client privilege, noting that specific objections can be raised during course of depositions and that the ALJ involved has ordered that information from depositions will be disclosed only to OTS enforcement personnel and will not be shared with the DOJ).

184. OFFICE OF THE COMPTROLLER OF THE CURRENCY, *supra* note 183.

185. See *Bank Examiners: Examination Authority*, OCC Interpretive Letter (Dec. 3, 1991), 1991 WL 338409 (suggesting that banks place an "appropriate legend" on documents furnished to the OCC in order to clarify involuntary disclosure and refute waiver claim).

186. See, e.g., *Westinghouse Elec. Corp. v. Republic of the Philippines*, 951 F.2d 1414 (3d Cir. 1991) (finding that voluntary disclosure to the SEC and DOJ in course of investigation waived privilege even though SEC regulations said that information would be kept confidential and noting circuit split with regard to whether disclosure to government waives privilege); see also Anne C. Flannery & Jennifer S. Milano, *The Confusion Continues: Protection of Internal Corporate Investigation Materials Under the Attorney-Client Privilege and Work Product Doctrine, Revisited*, PLI Order No. B4-7206 (Nov. 1997), WL 1023 PLI/Corp 519, 527-38 (discussing the unsettled case law regarding internal investigations and privileges). Exemption 8 of the federal Freedom of Information Act (FOIA) exempts from disclosure information "contained in or related to examination, operating, or condition reports prepared by, on behalf of, or for the use of an agency responsible for the regulation or supervision of financial institutions. 5 U.S.C. § 552(b)(8) (2000); see also *McCullough v. FDIC*, 1 Gov't Disclosure Service (Prentice-Hall) ¶ 80,194 at 80,495 (D.D.C. 1980) (holding that all records, regardless of source, in the possession of the regulating agency and related to a bank's financial condition and operations are exempt from disclosure under the FOIA). Therefore, financial institutions cannot convincingly assert that disclosure to a regulatory agency will automatically make the information available to the general public, which again weakens the claim of attorney-client privilege.

187. *In re Leslie Fay Cos., Inc. Sec. Litig.*, 161 F.R.D. 274 (S.D.N.Y. 1995).

attorney-client privilege to an internal audit report prepared by counsel because the report had been produced to the SEC and the United States Attorney's Office.¹⁸⁸ Similarly, in *In re Kidder Peabody Securities Litigation*,¹⁸⁹ the same court ruled that production of an internal report to the SEC waived the privilege.¹⁹⁰

Apparently in response to the inconsistent and unpredictable court approach to the question of waiver, a bill was introduced in the U.S. House of Representatives that would have codified that disclosure to a regulatory agency does not constitute a waiver.¹⁹¹ In 1999, the Federal Reserve Board wrote in support of the proposed Bank Examination Report Privilege Act that the legislation would "overcome the present reluctance of many institutions to disclose information."¹⁹² As a practical matter, the fact that heavily regulated entities, such as financial institutions, have frequent contact and interactions with their governing agencies may result in practical pressure to disclose "privileged materials." The Office of Thrift Supervision (OTS) was not hesitant about flexing its muscles to obtain materials, some of which were alleged to be protected by privilege, from the law firm of Kaye, Scholer, Fierman, Hays & Handler and several of its individual partners in the context of the failure of Lincoln Savings

188. *Id.* at 283-84.

189. *In re Kidder Peabody Sec. Litig.*, 168 F.R.D. 459 (S.D.N.Y. 1996).

190. *Id.* at 472-73. In *In re Subpoena Duces Tecum Served on Willkie, Farr & Gallagher*, the court found a waiver when an internal investigation report prepared by an outside law firm was turned over to the client's accountants in order to obtain an unqualified audit opinion. 1997 WL 118369, at *4 (S.D.N.Y. March 14, 1997). In *In re Woolworth Corp. Securities Class Action Litigation*, however, the court reached a different result, finding no waiver of the privilege even though an internal investigation report was produced to the SEC, because the plaintiff had equal access to the materials and witnesses used to prepare the report. 1996 WL 306576, at *2-*3 (S.D.N.Y. June 7, 1996). There is also authority to the effect that no waiver would result where production of a communication to a third party is protected by a confidentiality agreement. *Salomon Bros. Treasury Litigation v. Steinhardt Partners (In re Steinhardt Partners, L.P.)*, 9 F.3d 230 (2d Cir. 1993); see Gary G. Lynch, *Internal Investigations*, PLI Order No. B4-7239 (Nov. 1998), WL 1085 PLI/Corp 369, 397.

191. Depository Institution Regulatory Streamlining Act of 1999, H.R. 1585, 106th Cong. (1999) (introduced April 27, 1999).

192. *Depository Institution Regulatory Streamlining Act of 1999: Hearing on H.R. 1585 Before the House Subcomm. on Finl. Inst. and Consumer Credit of the Comm. on Banking and Fin. Serv.*, 106th Cong. 58 (1999) (prepared statement of Laurence H. Meyer, Member, Bd. Of Governors, Fed. Reserve Sys.). The bill did not pass.

and Loan Association.¹⁹³ In March 1991, the OTS initiated a \$275 million enforcement action against Kaye Scholer, freezing the law firm's assets for six days until the firm agreed to pay the government \$41 million in fines.¹⁹⁴ In this and similar cases against other law firms, the OTS and other agencies argued that "public policy" demands that different standards apply to federally regulated institutions and their legal counsel.¹⁹⁵ With such history in mind, federally regulated institutions and their counsel may be reluctant to assert the privilege in circumstances where it otherwise would bar disclosure.

Courts have occasionally examined such agency efforts to qualify the attorney-client privilege. In *Texas Utilities Electric Co. v. Marshall*,¹⁹⁶ the Texas Court of Appeals addressed an appeal by Texas Utilities of a trial court order that compelled production of certain documents related to the construction of the Comanche Peak Steam Electric Station, a two-unit nuclear power plant.¹⁹⁷ Texas Utilities was the majority owner of the nuclear plant and was embroiled in litigation with the minority owners, including the Texas Municipal Power Agency.¹⁹⁸ In denying application of the attorney-client privilege, the trial court had stated:

The fact that we are engaged in the construction of a nuclear power plant creates . . . such a trusteeship and such a fiduciary relationship, not merely *inter se*, but as between all the owners as a group and *the public whose interest is vital and is at stake in this matter*. That the failure to disclose this information would be a violation of the trust that the public must

193. LISSA L. BROOME & JERRY W. MARKHAM, REGULATION OF BANK FINANCIAL SERVICE ACTIVITIES 558-66 (2001).

194. *Id.* at 558 (quoting James O. Johnston, Jr. & Daniel Schott Schechter, *Introduction: Kaye, Scholer and the OTS—Did Anyone Go Too Far?*, 66 S. CAL. L. REV. 977 (1993)).

195. See generally Charles W. Wolfram, *Mapping the Minefield: The Applicable Ethics Rules and Conflicting Duties*, PLI Order No. B4-7009 (June 15, 1992), WL 779 PLI/Corp. 53; Ed Hendricks & Mary Berkheiser, *Where Were the Lawyers?*, 18 LITIGATION 30 (Summer 1992). The Kaye Scholer order likely rested on the OTS's view of the law firm's duty to volunteer information to the agency, as if the agency were a court under Model Rule 3.9. See VILLA, *supra* note 23, § 3.9.

196. *Texas Utils. Elec. Co. v. Marshall*, 739 S.W.2d 665 (Tex. App. 1987).

197. *Id.* at 666.

198. *Id.*

have in those entities that are licensed to carry on nuclear power generating operations. The Court will not permit that.¹⁹⁹

The court of appeals reversed, finding that “[n]o ‘public interest’ exception exists” under the Texas law of attorney-client privilege.²⁰⁰

Also illustrative is *Southern Bell Telephone and Telegraph Company v. Deason*,²⁰¹ a 1994 case decided by the Florida Supreme Court. In *Southern Bell*, the Florida Office of Public Counsel asked the Florida Public Service Commission to investigate allegations that Southern Bell had falsified information regarding its compliance with certain provisions of the Florida Administrative Code.²⁰² The investigation was subsequently consolidated with a pending rate case, and the Office of Public Counsel filed various motions to compel the production of documents from Southern Bell.²⁰³ When the Commission ordered Southern Bell to produce all requested documents, Southern Bell asked the Florida Supreme Court to quash the Commission orders on the ground that the documents were protected by the attorney-client privilege.²⁰⁴

The court held that Southern Bell employees’ statements to in-house counsel were protected by the attorney-client privilege, rejecting the Commission’s argument that Southern Bell, as a regulated entity, did not have the full attorney-client privilege that was recognized in the *Upjohn* case.²⁰⁵ The court stated that “[the Commission] cannot exercise its regulatory power at the expense of destroying the corporate attorney-client privilege.”²⁰⁶ Citing two previous cases involving the Federal Energy Regulatory Commission and the Federal Communications Commission, the Public Service Commission had asserted that regulated entities have an obligation to comply with governing rules and regulations, and that, as a statutorily created regulatory agency, the

199. *Id.* (emphasis added).

200. *Id.* at 667.

201. *S. Bell Tel. & Tel. Co. v. Deason*, 632 So. 2d 1377 (Fla. 1994).

202. *Id.* at 1380.

203. *Id.*

204. *Id.*

205. *Id.* at 1381-82 & n.9.

206. *Id.* at 1382.

Commission has the duty to ensure Southern Bell's compliance with the law.²⁰⁷ The *Southern Bell* court acknowledged the policy interests at stake, but noted that all companies operating in the United States are regulated by one or more government agencies, including the IRS and, often, the SEC.²⁰⁸ Recognizing a "regulated entity" exception to the attorney-client privilege could ultimately lead to elimination of the attorney-client privilege in the corporate context, and thus the court concluded that a company's regulated status does not entitle its regulating body to full access to its confidential communications.²⁰⁹

In at least one context, though, the privilege has been "qualified." While a governmental attorney-client privilege has generally been recognized,²¹⁰ the absolute nature of the attorney-client privilege has become far less certain in that context. In *In re Lindsey*,²¹¹ the D.C. Circuit Court of Appeals refused to permit Bruce Lindsey, as Deputy White House Counsel, to assert government attorney-client privilege to avoid responding to a federal grand jury involved in a federal criminal investigation regarding the Whitewater and Lewinsky matters that ultimately led to impeachment hearings for President Clinton.²¹² In refusing to prevent disclosure, the court emphasized that federal evidentiary privileges should be narrowly construed and that their application to government lawyers requires the existence of a "public good transcending the normally predominant principle of

207. See *S. Bell Tel. & Tel. Co.*, 632 So. 2d 1377, 1381-82 (Fla. 1994). 1381-82 (citing *Consol. Gas Supply Corp.*, 17 Fed. Energy Reg. Comm'n Rep (CCH) ¶ 63,048 (Dec. 2, 1981) and *In re Notification to Columbia Broad. Sys., Inc.* Concerning Investigation by CBS of Incidents of "Staging" by Its Employees of Television News Programs, 45 F.C.C.2d 119 (1973) (noting that the regulating agency has a duty to protect the public interest and ensure compliance with the Natural Gas Act)); see also *Texas Utils. Elec. Co. v. Marshall*, 739 S.W.2d 665 (Tex. App. 1987) (rejecting argument that the attorney-client privilege should be "set aside" because of public interest when party was seeking disclosure from a regulated nuclear power plant).

208. *S. Bell Tel. & Tel. Co.*, 632 So. 2d at 1382 & n.9.

209. *Id.*

210. See *In re Bruce R. Lindsey* (Grand Jury Testimony), 158 F.3d 1263, 1269 (D.C. Cir. 1998) (citing PROPOSED FED. R. EVID. 503(a)(1); RESTATEMENT (THIRD) OF THE LAW GOVERNING LAWYERS § 124 (Proposed Final Draft No. 1, 1996)).

211. *Id.*; see also *In re Grand Jury Subpoena Duces Tecum*, 112 F.3d 910 (8th Cir. 1997) (holding that the White House could not invoke any form of government attorney-client privilege to withhold information from federal grand jury).

212. *In re Lindsey*, 158 F.3d at 1278.

utilizing all rational means for ascertaining the truth.”²¹³ Lindsey was purportedly acting in the role of attorney, with the Office of the President as his client.²¹⁴ The court distinguished government attorneys from members of the private bar,²¹⁵ particularly in the context of investigations of federal criminal offenses, and especially as they relate to offenses committed by those in the government. Unlike private attorneys, who are charged only with representing their clients to the best of their ability, the government lawyer has an additional and overriding duty:

With respect to investigations of federal criminal offenses, and especially offenses committed by those in government, government attorneys stand in a far different position from members of the private bar. Their duty is not to defend clients against criminal charges and it is not to protect wrongdoers from public exposure. The constitutional responsibility of . . . all members of the Executive Branch, is to “take Care that the Laws be faithfully executed.”²¹⁶

It is difficult to predict whether courts would sanction further qualifications of the attorney-client privilege in the regulated industry context. Whether or not this occurs, in-house lawyers must face a huge practical problem: denying to the regulators, with whom they are required to deal virtually on a daily basis, access to materials that may be helpful and important to those regulators in carrying out their duties. The result is another very significant complication for the in-house lawyer and his or her client in predicting what communications will remain confidential.

213. *Id.* at 1268 (quoting *Elkins v. United States*, 364 U.S. 206, 234 (1960) (Frankfurter J., dissenting)).

214. *See id.*

215. *Id.* at 1271-72. Note that President Clinton’s conversations with his personal counsel, the same conversations that were had with Lindsey, remained fully protected by the attorney-client privilege. *Id.* at 1282.

216. *Id.* at 1272 (quoting U.S. CONST. art. II, § 3).

VI. SPECIAL SITUATIONS

This section highlights a few special circumstances in which in-house counsel should take special care to consider whether their communications and reports are protected.

A. *Internal Investigations*

The *Upjohn* case considered a voluntary internal investigation conducted by a corporation's general counsel, and the Supreme Court utilized the encouragement of such voluntary compliance efforts as the primary rationale for its decision to uphold the application of the attorney-client privilege.²¹⁷ Companies are using internal investigations more and more frequently to deal with allegations of corporate misconduct.²¹⁸ Not only does the *Upjohn* rationale support such steps, but there are other strong incentives for corporations to conduct their own investigations. The Federal Sentencing Guidelines offer the hope of a reduced sentence for the organization if offenses are promptly self-reported before they are discovered by third parties.²¹⁹ Government agencies, such as the SEC, have effectively used a "carrot and stick" approach to encourage such voluntary compliance efforts.²²⁰ The Delaware Chancery Court's 1996 decision in *In re Caremark International, Inc. Derivative Litigation*²²¹ clarified that directors have a duty to monitor corporate operations and take steps to see that the corporation is in compliance with applicable laws.

217. Cohn, *supra* note 27, at 746-47.

218. Flannery & Milano, *supra* note 186, at 523.

219. U.S. SENTENCING GUIDELINES MANUAL §§ 8C2.5(g)(1), 8C2.5(f) (2001), available at <http://www.ussc.gov/2001guid/CHAP8.pdf> (last visited Feb. 20, 2002).

220. See, e.g., In the Matter of Daiwa Securities America, Inc., and William M. Brachfeld, Exchange Act Release No. 34-31924 (Feb. 25, 1993), WL 53 SEC Docket 1517; see Anne C. Flannery & Katherine M. Polk, *Between a Rock and a Hard Place: Internal Corporate Investigations and the Attorney-Client Privilege*, PLI Order No. B4-7141 (Oct./Nov. 1996), WL 963 PLI/Corp 585; Joseph T. McLaughlin & J. Kevin McCarthy, *Corporate Internal Investigations—Legal Privileges and Ethical Issues in the Employment Law Context*, SD06 ALI-ABA Course of Study Materials 991, 993-94 (1998), LEXIS, Secondary Legal Library, Combined ALIABA Course of Study Materials File; Lynch, *supra* note 190, at 373-74.

221. 698 A.2d 959 (Del. Ch. 1996).

While *Upjohn* confirms that the attorney-client privilege applies to communications made in the course of an internal investigation, the actual application of the privilege in that setting remains problematic. For instance, in *In re Allen*,²²² the Fourth Circuit Court of Appeals overturned a district court finding that the privilege was not available to protect communications in an investigation conducted by an attorney because the attorney's duties were merely "investigative."²²³ The lower court apparently believed that if a client retains an attorney to perform the 'rudimentary' task of conducting an investigation, that assignment can never constitute legal work and so the attorney-client privilege does not protect communications between the client and the investigating attorney.²²⁴

In addition to the questioning of the legal advice requirement illustrated by the district court in *In re Allen*,²²⁵ and the potential for waiver when internal investigation reports are disclosed to third parties,²²⁶ in-house counsel may confront difficult issues when former employees of the corporation have information that could be important in connection with a matter under investigation. The Supreme Court in *Upjohn* declined to decide whether communications with former employees are covered by the privilege.²²⁷ Most courts since *Upjohn* have held that the privilege does apply in the case of former employees.²²⁸ Language in a concurring opinion in *Upjohn*, however, supports the proposition that the privilege should be limited to situations in which the former employee is communicating with counsel at the direction of management, concerning matters within the scope of his or her employment, so that the corporation can obtain legal advice.²²⁹ Other courts have gone even further and required a

222. *Better Gov't Bureau, Inc. v. McGraw (In re Allen)*, 106 F.3d 582 (4th Cir. 1997).

223. *Id.* at 603.

224. *Id.* at 601.

225. *See supra* notes 222-24 and accompanying text.

226. *See supra* notes 175-190 and accompanying text.

227. *Upjohn Co. v. United States*, 449 U.S. 383, 394 n.3 (1980); *see VILLA, supra* note 23, § 1.03[C].

228. *See, e.g., In re Allen*, 106 F.3d at 605-06; *see VILLA, supra* note 23, § 1.03[C].

229. *Upjohn*, 449 U.S. at 402-03 (Burger, C.J., concurring); *see VILLA, supra* note 23, § 1.03[C] & n.31; *see also Nakajima v. Gen. Motors Corp.*, 857 F. Supp. 100, 104 (D.D.C. 1994) (refusing to apply the privilege where former employee's communication with counsel was three years after employee left defendant's

showing that the corporation had the legal authority to direct the former employee to cooperate in counsel's investigation, thus making it advisable to include in employment contracts and severance agreements a contractual undertaking by each employee to cooperate with the company's counsel in any internal investigation.²³⁰ Also, in order to prevent a waiver of the privilege by a former employee, the corporation should instruct employees and former employees not to communicate with other attorneys regarding corporate business without the corporation's consent.²³¹

B. Subsidiaries

Another special circumstance arises in the context of communications between parents and subsidiaries. Often, the same in-house counsel acts as attorney for the parent and for the subsidiary, or counsel for a subsidiary reports both to the CEO of the subsidiary and to the general counsel of the parent.²³² The general rule that applies in this situation tends to avoid these complications. The sharing of communications between a corporate parent and its subsidiary does not, in and of itself, compromise the availability of the privilege, because the parent and the subsidiary have a common interest in the protection of such information.²³³ "The universal rule of law, expressed in a variety of contexts, is that the parent and subsidiary share a community of interest, such that the parent (as well as the subsidiary) is the 'client' for purposes of the attorney-client

employment, and where defendant had not alleged employee was questioned in order for defendant to obtain legal advice).

230. See *Clark Equip. Co. v. Lift Parts Mfg. Co.*, 1985 WL 2917, at *5-*8 (N.D. Ill. Oct. 1, 1985); *Connolly Data Sys., Inc. v. Victor Tech., Inc.*, 114 F.R.D. 89, 93-95 (S.D. Cal. 1987); RESTATEMENT (THIRD) OF THE LAW GOVERNING LAWYERS § 73 cmt. e (1998); VILLA, *supra* note 23, § 1.03 [C] & n.4.

231. See Thomas W. Hyland & Molly Hood Craig, *Attorney-Client Privilege and Work Product Doctrine in the Corporate Setting*, 62 DEF. COUNS. J. 553, 557 (1995).

232. See John T. Hundley, *White Knights, Pre-Nuptial Confidences, and the Morning After: The Effect of Transaction-Related Disclosures on the Attorney-Client and Related Privileges*, 5 DEPAUL BUS. L.J. 59, 63-64 (1992) (providing a hypothetical example of such a problem).

233. See, e.g., *Duplan Corp. v. Deering Milliken, Inc.*, 397 F. Supp. 1146, 1172 (D.S.C. 1974); see VILLA, *supra* note 23, § 1.03[D]; Hundley, *supra* note 232, at 82-83; Andrew R. Taggart, Comment, *Parent-Subsidiary Communications and the Attorney-Client Privilege*, 65 U. CHI. L. REV. 315, 319-22 (1998).

privilege.”²³⁴ When a subsidiary is sold, however, or when control of a corporate subsidiary passes to new management, the issue of who controls the privilege becomes more complicated. Generally, control over the privilege is held to pass to new management of the subsidiary in a sale context; the new managers can waive or assert the privilege, even as to communications by former officers and directors, without the consent of the former parent.²³⁵

A 1988 case decided in Illinois illustrates the problems that can arise from this rule. In *Medcom Holding Co. v. Baxter Travenol Labs, Inc.*, a corporate parent sold the stock of its subsidiary.²³⁶ Following the sale, the purchaser sued the selling parent for securities fraud under Section 10(b) of the Securities Exchange Act of 1934, alleging that the selling parent had concealed the existence of a lawsuit against the parent and the subsidiary by a former officer of the subsidiary.²³⁷ In that action, which had been settled and dismissed—with the court file placed under seal upon request of all parties—the selling parent had made allegations that raised serious questions about the business of the subsidiary and other matters.²³⁸ The purchaser of the subsidiary sought to compel production of sixteen documents, primarily memoranda between the subsidiary’s officers and in-house attorneys in the selling parent’s legal department, which had represented both the parent and the subsidiary prior to the sale.²³⁹ The purchaser caused the subsidiary, which it controlled after the sale, to waive the privilege with respect to these communications,

234. *Glidden Co. v. Jandernoa*, 173 F.R.D. 459, 472 (W.D. Mich. 1997); see RESTATEMENT (THIRD) OF THE LAW GOVERNING LAWYERS § 73 cmt. d (1998).

235. *Commodity Futures Trading Comm’n v. Weintraub*, 471 U.S. 343, 349 (1985); *Bass Public Ltd. Co. v. Promus Cos.*, 868 F. Supp. 615, 619 (S.D.N.Y. 1994); *Medcom Holding Co. v. Baxter Travenol Labs., Inc.*, 689 F. Supp. 841, 844 (N.D. Ill. 1988). “When ownership of a corporation . . . passes to successors, the transaction carries with it authority concerning or waiving the privilege. . . . [C]ommunications from directors, officers, or employees of the acquired organization to lawyers who represent only the predecessor organization . . . may no longer be covered by the privilege.” RESTATEMENT (THIRD) OF THE LAW GOVERNING LAWYERS § 73 cmt. k (1998).

236. 689 F. Supp. 841, 842 (N.D. Ill. 1988)

237. *Id.* at 842 & n.3.

238. *Id.*

239. *Id.*

and the selling parent sought to invoke the privilege.²⁴⁰ The court held that the privilege had been waived:

“[W]hen control of a corporation passes to new management, the authority to assert and waive the corporation’s attorney client privilege passes as well. New managers installed as a result of a takeover, merger, loss of confidence by shareholders, or simply normal succession, may waive the attorney client privilege with respect to communications made by former officers and directors. Displaced managers may not assert the privilege over the wishes of current managers”²⁴¹

The result in *Medcom* has been criticized as overly formalistic.²⁴² In *Medcom*, the new managers of the assets of the sold subsidiary inherited control of the privilege even though, prior to the stock sale, the subsidiary had transferred the great majority of its assets to third parties, including its parent.²⁴³ Had the transaction been effected as a sale of assets, rather than a sale of stock in the subsidiary, the selling parent would normally have retained control over the privilege and the right to decide whether to waive it.²⁴⁴ Additionally, it may be possible for the selling parent to retain at least shared control over the waiver of the privilege by contract.²⁴⁵ Thus, counsel should consider whether to

240. *Id.* at 842.

241. *Id.* at 842-43 (quoting *Commodity Futures Trading Comm’n*, 471 U.S. 343, 349 (1985)).

242. Taggart, *supra* note 233, at 331-33.

243. See Hundley, *supra* note 232, at 94.

244. See, e.g., *Cheeves v. S. Clays, Inc.*, 128 F.R.D. 128, 130 (M.D. Ga. 1989). Even in an asset sale, the privilege may be deemed waived if documents evidencing the privileged communication are transferred to the purchaser of the assets as part of the selling subsidiary’s files. Hundley, *supra* note 232, at 94-95. And where, as in *Medcom*, the privilege issue arises where the purchased subsidiary’s new management alleges fraud by the selling parent, the general crime/fraud exception to the attorney-client privilege may prevent assertion of the privilege by the seller in any event. See MCCORMICK, *supra* note 15, § 95; VILLA, *supra* note 23, §§ 1.22[C], 1.2b.

245. See *Bass Public Ltd. Co. v. Promus Cos.*, 868 F. Supp 615, 621; VILLA, *supra* note 23, § 1.22[C]; Taggart, *supra* note 232, at 333-34 & n.95.

include in a stock sale agreement a provision reserving the attorney-client privilege for the selling parent.²⁴⁶

VII. CONCLUSION

The managers and officers of Gulf & Western who conversed day-in-day-out with Joel Dolkart, their general counsel, likely believed that all of their conversations would always remain confidential. They were disappointed, at least in part, for reasons that are increasingly relevant in in-house legal practice. The expanding role of in-house lawyers for corporations generally, and for regulated financial institutions in particular, has given rise to numerous complications in relation to the application of both the attorney-client privilege and work product immunity. Courts continue to harbor suspicions regarding possibly inappropriate efforts by corporations to use their lawyers, especially their employee-lawyers, to shield from disclosure communications and reports that will be important in providing just decisions. These suspicions have led to numerous restrictions and qualifications on the privilege and the immunity that would not otherwise apply to private practitioners. In-house counsel must be especially wary of these complications as they seek to understand the rules under which they work and to balance the need for full and frank disclosure with their corporate clients against the possibility that unfairly damaging information may come to light in unexpected ways.

246. VILLA, *supra* note 23, § 1.22[C].