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Renewed Respect for Attorney Confidentiality
in Internal Corporate Investigations and Audit Inquiries

I thought you might be interested in a series of recent statutory, judicial and policy pronouncements that show renewed respect for the confidentiality of attorneys' work-product in internal corporate investigations and reports to auditors. These may be useful in evaluating how to respond to a demand for such work-product made by the Government or a litigant in a private civil action.

Listed in chronological order, the recent authorities supporting confidentiality are:

1. Merrill Lynch & Co., Inc. v. Allegheny Energy Inc., 229 F.R.D. 441, 448 (S.D.N.Y. 2004). The court denied Allegheny's motion to compel Merrill Lynch to turn over two internal investigation reports prepared under the guidance of its counsel. The court held that the reports were confidential work-product immune from disclosure. The immunity was not waived by Merrill Lynch having provided copies of the reports to the outside auditors. The auditors were not adverse to Merrill Lynch, nor were they a conduit to a potential adversary. Rather, Merrill Lynch and its auditors had a common interest; they were "aligned insofar as they both seek to prevent, detect and root out corporate fraud. Indeed, this is precisely the type of limited alliance that courts should encourage."

This is not the earliest decision holding that disclosure of an attorney's work-product to the client's independent auditor does not waive immunity from disclosure to an adversary. See, e.g., Southern Scrap Material Co. v. Fleming, No. Civ. A. 01-2554, 2003 WL 21474516, at *9 (E.D.La. Jun. 18, 2003); In re Pfizer, Inc. Sec. Litig., No. 90 Civ. 1260, 1993 WL 561125 (S.D.N.Y. Dec. 23, 1993); Gramm v. Horsehead Indus., Inc., No. 87 Civ. 5122 (MJL), 1990 WL 142404 (S.D.N.Y. Jan. 25, 1990); Tronitech, Inc. v. NCR Corp. 108 F.R.D. 655 (S.D. Ind. 1985). Although decided more than two years ago, I include Merrill Lynch among the recent developments because it is often cited and relied upon in the more recent decisions.

2. American S.S. Owners Mut. Protection and Indem. Ass'n, Inc. v. Alcoa S.S. Co., Inc., No. 04 Civ. 4309 LAKJAF, 2006 WL 278131 (S.D.N.Y. Feb. 2, 2006). The court denied defendants' discovery of two opinion letters prepared by plaintiff's attorneys apparently estimating the likelihood of success in litigation and analyzing plaintiff's legal strategies and options. The opinion letters were provided to plaintiff's actuary to assist it

in estimating litigation loss reserves in connection with the actuary's preparation of its own report to the New York Insurance Department concerning loss and loss adjusted expense reserves. Quoting United States v. Adlman, 134 F. 3d 1194, 1195 (2d Cir. 1990), the court held that the opinion letters' work-product immunity from disclosure to an adversary is not lost " 'merely because [they are] intended to assist in the making of a business decision influenced by the likely outcome of anticipated litigation.' "

3. Int'l Design Concepts, Inc. v. Saks, Inc., No. 05 Civ. 4754 (PKC), 2006 WL 1564684 (S.D.N.Y. Jun. 6, 2006). Relying on Merrill Lynch, the court held that work-product immunity for a report prepared by defendant's counsel concerning a possible fraud at defendant was not waived by disclosing the report to defendant's outside auditor.

4. Lawrence E. Jaffe Pension Plan v. Household Int'l, Inc., 237 F.R.D. 176 (N.D.Ill. 2006). The court held that opinion letters of defendant's general counsel summarizing pending and threatened litigation, other draft and final letters written variously by and to defendant's counsel concerning such opinion letters, audit letters based on such opinion letters and defendant's litigation database did not lose their attorney-client privilege protection or work-product immunity because they were provided to defendant's outside auditors. Similarly, the auditors' memoranda based on the contents of such letters and discussions with defendant's counsel were immune from disclosure to the class-action plaintiffs. The court noted that disclosure to the auditors did not substantially increase the opportunity for potential adversaries to obtain the information.

5. In re: JDS Uniphase Corp. Sec. Litig., No. C-02-1486 CW (EDL), 2006 U.S. Dist. LEXIS 76169 (N.D.Cal. Oct. 5, 2006). Relying on Merrill Lynch and Samuels v. Mitchell, 155 F.R.D. 195 (N.D.Cal. 1994), the court held that work-product immunity was not lost for minutes of eight meetings of the defendant corporation's board because the minutes had been disclosed to defendant's outside auditors. Accordingly, the minutes were not required to be turned over to the class action lead plaintiff.

6. Section 607 of the Financial Services Regulatory Relief Act of 2006 ("FSRRA") provides that disclosure to a federal, state or foreign banking regulator of "any information" in the course of any supervisory or regulatory process shall not waive or otherwise affect any privilege under federal or state law that might otherwise be claimed "as to any person" other than the banking regulator. In other words, disclosure to a bank regulator does not waive either the attorney-client privilege or the attorney's work-product immunity from disclosure to anyone else. Section 607 was enacted into law effective October 13, 2006 as Public Law 109-351, and is codified at 12 U.S.C. §§ 1785(j) and 1828(x).

7. Memorandum of U.S. Deputy Attorney General Paul J. McNulty on Principles of Federal Prosecution of Business Organizations, Dec. 12, 2006 (www.usdoj.gov). The McNulty memorandum significantly modifies the previous Justice Department policy concerning the demand for corporate waivers of attorney-client privilege and work-product protection.

> Waiver of attorney-client and work product protections is not a prerequisite to a finding that a company has cooperated in the government's investigation.
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> Prosecutors may only request waiver of attorney-client or work product protections when there is a legitimate need for the privileged information to fulfill their law enforcement obligations.
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> If a legitimate need exists, prosecutors should seek the least intrusive waiver necessary to conduct a complete and thorough investigation, and should follow a step-by-step approach to requesting information.

Mem. at 8,9. If a legitimate need exists, prosecutors may request first "purely factual information" (Category I information), but only with written authorization of the U. S. Attorney who must provide a copy of the request to, and consult with, the Assistant Attorney General of the Criminal Division before granting or denying the request. If attorney-client communications or non-factual attorney work product (Category II information) is sought, the U.S. Attorney must obtain written authorization from the Deputy Attorney General. "If a corporation declines to provide a waiver for Category II information after a written request from the United State Attorney, prosecutors must not consider this declination against the corporation in making a charging decision." Mem. at 10.

8. In re Vecco Instruments, Inc. Sec. Litig., No. 05 MD 1695 (CM) (GAY), 2007 WL 210110, at *2 (S.D.N.Y. Jan. 25, 2007). The court denied plaintiffs' motion to compel production of investigative reports concerning the restatement of the defendant corporation's financial statements. The reports were prepared by outside counsel and the forensic accountants assisting it. Work-product immunity for the reports was not waived by the defendant corporation's press release nor by a letter from its counsel to the SEC, both of which "merely summarized the findings and conclusions of the internal investigation and did not quote, paraphrase or reference any of the specific documents at issue in support of its conclusion." Citing Merrill Lynch, the court held that generally work-product immunity is not waived if the disclosure does not substantially increase the opportunity for potential adversaries to obtain the information.

9. Allied Irish Banks, p.l.c. v. Bank of America, N.A., No. 03 Civ. 3748 (DAB) (GWG), 2007 WL 177870 (S.D.N.Y. Jan. 25, 2007). This case is an exception to the others discussed in this memorandum. In Allied Irish, the court held that there was no work-product immunity for an internal investigative report. But this exception proves the

rule; in order for an investigative report to have work-product immunity from discovery in litigation it must be an *attorney's* work-product prepared in anticipation of litigation. Allied Irish Bank engaged a well-respected consultant Eugene A. Ludwig, former Comptroller of the Currency, to conduct an investigation of its foreign currency trading. The consultant was assisted by a law firm. The court held that the investigation was done for a business purpose, not because of anticipated litigation. According to the court, this was evident by the bank having engaged Ludwig to conduct the investigation and then publicized Ludwig's lead role in order to restore the market's confidence. This is complimentary of Ludwig, but unfortunately compromised the confidentiality of the investigation.

10. In re Cardinal Health, Inc. Sec. Litig., No. C2 04 575 ALM, 2007 WL 495150 (S.D.N.Y. Jan. 26, 2007). The court quashed plaintiffs' subpoena to produce, among other things, interview memoranda, presentation binders and documents reviewed by counsel who conducted an internal investigation for the audit committee of the defendant corporation's board of directors. These materials had been disclosed to the SEC and to the U.S. Attorney's Office. Nevertheless, the court held that neither the attorney-client privilege nor work-product immunity had been waived because the defendant corporation and the Government shared a common interest in assuring that the defendant's financial and accounting practices be as "clean as a hounds tooth." Accord, In re Natural Gas Commodities Litig., 232 F.R.D. 208 (S.D.N.Y. 2005) (disclosure to government agencies of privileged and work-product documents generated in the course of the defendant corporation's internal investigation did not waive the right to withhold the documents from plaintiffs). But see, e.g., In re Qwest Communications Int'l Inc., 450 F.3d 1179 (10th Cir. 2006) (both privileged and work-product immunity from disclosure in private civil litigation were waived by disclosure of documents to government agencies notwithstanding written confidentiality agreements with each agency).

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A few words of caution. First, there remain many decisions holding that disclosure of privileged material or attorney work-product to the Government or to the client's accountants waives the protection from discovery in litigation. Various of those decisions are discussed in the above cases and are either distinguished or criticized (e.g., Medinol, Ltd. v. Boston Scientific Corp., 214 F.R.D. 113 (S.D.N.Y. 2002)).

Second, FSRRA § 607 described above may result in requiring disclosures of attorney-client privileged or work-product material that would otherwise be protected from disclosure to bank regulators. And once the material is in the hands of a bank regulator, what is the protection against that regulator sharing it with another regulator or a congressional or state legislature's oversight committee?

Third, the intellectual underpinnings of the "common interest" rationale in a number of the above opinions could use some shoring up. It is somewhat paradoxical to treat independent public accountants, regulators and prosecutors as having a common interest with the company to ferret out fraud and corruption, but not plaintiffs who sue derivatively on behalf of the company or class-action plaintiffs (particularly those representing the company's owners) whom courts typically call private attorneys general.

The point of this memorandum, however, is not so much to critique, but to collect these recent decisions and other materials and bring them to your attention with the hope that they may be helpful.

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