DIRECTORS' AND OFFICERS' LIABILITY
PRESERVING CONFIDENTIALITY OF INTERNAL INVESTIGATIONS

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In the current legal and regulatory environment, allegations of corporate wrongdoing that give rise to civil litigation frequently spawn parallel regulatory or other government investigations or proceedings. In response to such allegations, the board may wish to retain independent counsel to conduct an internal corporate investigation into the allegations for one or more of a variety of reasons. These may include preparation for civil litigation, a desire to reassure shareholders that the company is committed to ferreting out any potential corporate misconduct, and to cooperate with government entities such as the SEC or U.S. Attorney's Office that have commenced or may commence formal or informal investigatory proceedings.

As numerous recent cases demonstrate, an internal investigation and its results will be of enormous interest not only to government entities and shareholders, but also to the company's auditors and other outside advisers, and actual or potential civil litigation adversaries. In order to make an informed decision about whether to authorize an internal investigation and, if so, how to maximize the chance of maintaining the confidentiality of the fruits of the investigation in subsequent proceedings after they are voluntarily shared with the government, it is essential to understand the substantial body of law addressing these issues. While courts have candidly acknowledged that "unfortunately, 'the case law addressing the issue of limited waiver is in a state of 'hopeless' confusion,'"[1] recent decisions from the Sixth Circuit Court of Appeals and the Delaware Court of Chancery reaching contrary conclusions about the validity of confidentiality assertions after disclosures to the government made pursuant to a confidentiality and non-waiver agreement illustrate the two approaches competing for primacy in the courts.

Effects of Disclosure

The circumstances surrounding a particular corporate problem may favor sharing with the government privileged information or material that is subject to work product immunity. For example, because of the obvious law enforcement benefits from the cooperation of an entity under investigation, the SEC has expressly adopted a policy, when deciding to pursue, increase or decrease enforcement penalties, of considering favorably "self-policing, self-reporting, remediation and cooperation."[2]

Determination of whether complete waiver of (a) privileged status and (b) work product immunity arises from disclosure of confidential information to a third party outside the privileged relationship entails separate inquiries. As a general rule, voluntary disclosure of a privileged communication to a third party outside the privileged relationship waives the privilege attaching to such communication and, depending on the circumstances, communications related to the subject matter of the disclosed communication.[3] Courts have been reluctant to embrace the notion of "selective waiver," so that disclosure to any third party ordinarily constitutes waiver as to the world at large.

If materials qualify for work product protection, however, the universe of parties with whom the work product may be shared without resultant waiver is larger than that in the privilege context. Because the work product doctrine serves to protect the fruits of an attorney's analysis, research and other labors from disclosure to an adversary, disclosure to a non-adversarial third party does not waive the protection of the work product doctrine as to other third parties.[4] Most courts have held a company forfeits work product protection when it provides an internal investigation report or other litigation-driven material to a government entity that is investigating or considering investigating the company because government investigators are deemed adversaries of the company.[5]

The potential application of these waiver principles after the voluntary disclosure to governmental entities or other third parties of reports presenting factual and legal conclusions reached after internal corporate investigations, and materials underlying such reports, raises several issues. First, the party seeking to maintain the confidentiality of the results of an internal investigation and materials underlying the results, such as summaries of witness interviews, must demonstrate that such information is privileged in the first place. Courts have widely accepted that information gathered in the course of a confidential internal corporate investigation conducted by independent counsel, including counsel's report, is privileged.

The Sixth Circuit recently observed in *In re Columbia/HCA Healthcare Corp.* that "[t]he decision to enter into settlement negotiations [with governmental entities], and to disclose otherwise confidential information in the process, is a tactical one made by the client and his or her attorney. All litigation-related tactical decisions have an upside and a downside."[6] Case law is sharply divided as to whether the downside of waiver for all time follows the decision to voluntarily disclose privileged information such as an internal investigation report in order to cooperate with a government agency, thereby subjecting the information to discovery in litigation between the discloser and a third party. The cases may be grouped broadly into three categories: (a) selective waiver is permissible; (b) selective waiver is impermissible in all circumstances; and (c) selective waiver may be invoked where confidential information was disclosed pursuant to a signed confidentiality and non-waiver agreement. Because very few courts outside of the Eighth Circuit have adopted selective waiver in the absence of a confidentiality agreement, the current debate has centered on the efficacy of confidentiality agreements in which the disclosing party and the recipient of the information, typically the

government, agree that no waiver of any applicable privilege or work product immunity will arise from the voluntary disclosure.

Bright-Line Waiver

The Sixth Circuit's recent decision in *In re Columbia/HCA Healthcare Corp.*[7] illustrates the bright-line rule of absolute waiver applied by certain courts even when the disclosure was made pursuant to a specific confidentiality and non-waiver agreement in which the disclosing party and the government agreed that disclosure would not constitute a waiver of any privilege. There, either in response to or in anticipation of a Justice Department investigation into possible Medicare fraud, Columbia/HCA conducted several confidential, internal audits of its Medicare patient records. In the course of negotiations with the Justice Department to resolve the criminal fraud investigation, the company agreed to share the results of the internal audits with the government. In exchange for this cooperation, the Justice Department signed a confidentiality agreement governing its obtaining of the documents, which specified that the disclosure of the confidential information did not constitute a waiver of any privilege or work product immunity.

The Sixth Circuit flatly rejected the efficacy of such agreements, questioning "whether the Government should assist in obfuscating the 'truth-finding process' by entering into such confidentiality agreements at all."[8] As to the privilege, the court concluded that "attorney-client privilege was never designed to protect conversations between a client and the Government -- *i.e.*, an adverse party -- rather, it pertains only to conversations between the client and his or her attorney." It acknowledged that recognizing a selective waiver for disclosures to governmental authorities would promote numerous salutary ends, including encouraging full cooperation with government investigations and saving considerable time and expense associated with the investigation of potential civil and criminal violations. The court concluded, however, that these objectives are outweighed, by countervailing considerations. Asserting that a "plaintiff in a shareholder derivative action or a qui tam action who exposes accounting and tax fraud provides as much service to the 'truth finding process' as an SEC investigator," the court declined to make judgments about which litigation adversaries served sufficiently important public roles to permit disclosure of privileged information without waiver and which did not. The court also expressed discomfort at enforcing any agreement that may make the government party to non-disclosure of information regarding potentially actionable misconduct.

The Sixth Circuit acknowledged that the work product doctrine is distinct from and broader than the attorney-client privilege, and extends beyond confidential communications between the attorney and client to any document prepared in anticipation of litigation by or for the attorney. It concluded, however, that during the fraud investigation the Justice Department was an adversary of the company, and that total waiver followed the decision to share work product with the government because "[t]he ability to prepare one's case in confidence, which is

the chief reason articulated in *Hickman* for the work product protections, has little to do with talking to the Government."

Selective Waiver

A growing body of case law is retreating from the bright line waiver position exemplified by decisions like *In re Columbia/HCA Healthcare Corp.*, and hold that a company does not forfeit work product protection as to other third parties when it produces an internal investigation report or other submission to the government pursuant to a signed confidentiality agreement expressly stating that the disclosing party does not waive, *inter alia*, work product protection. The Delaware Court of Chancery's recent decision in *Saito v. McKesson HBOC, Inc.*,[9] offered a thoroughly reasoned analysis of decisions addressing the issue and concluded that "the more prudent policy would be to recognize . . . expectations of privacy and hold that [a disclosing company] can therefore assert its work product privilege over . . . documents disclosed [to a government entity] under a confidentiality agreement."[10]

Saito arose out of an internal investigation conducted by outside counsel at the direction of the company's audit committee after revelations of possible misconduct that allegedly resulted in the filing of materially false or misleading financial statements. The investigation culminated in a written report by outside counsel for the audit committee, summarizing the relevant facts and legal principles involved in various pending actions and governmental investigations that followed the first of several downward revisions of revenues. The company informed the SEC and the Justice Department of the internal investigation and agreed to disclose the work product generated from the internal investigation after both governmental entities signed a confidentiality agreement affirming that no waiver would result from the disclosures. In a subsequent private civil action, plaintiff asserted waiver and sought production of the work product provided to the government. Significantly, the SEC appeared as an *amicus* to support the company's effort to resist production in the civil action.

The court surveyed the case law and noted that some federal courts had already sustained work product protection when a confidentiality agreement was in place prior to disclosure to a government entity. In addition, several courts withholding work product protection based on a particular set of facts involving disclosures to governmental authorities had acknowledged that a contrary conclusion might have been reached had a confidentiality agreement been signed before disclosure. The Court of Chancery adopted this principle, reasoning that leaving work product status intact after disclosure of material to a government entity would promote "cooperation with the law enforcement agencies without any negative cost to society or private plaintiffs." It emphatically rejected the notion that allowing a company to preserve work product protection after making a disclosure to the government permits disclosing parties "to have their cake and eat it too," observing that "[d]isclosures made to the SEC when the corporation is under investigation are not really akin to enjoying a dessert." Rather, the court took the view that "litigating shareholders want to have their cake

and eat it too: they want disclosing parties to continue disclosing to the SEC so they are better protected, while at the same time they want access to these disclosures for their own tactical advantage." Finally, the court noted that recognizing the doctrine of selective waiver of work product protection to government entities does not undermine the integrity of the work product doctrine because private plaintiffs are in the same position they would have been had no disclosure been made. "Because a confidentiality agreement would prevent the law enforcement agency from passing along privileged information to other private adversaries, the adversarial system is still protected."

Conclusion

Counsel should endeavor at every stage of an internal investigation to prevent waiver of privileged communications and work product material. Inadvertent disclosure to third parties outside the privileged relationship, partial disclosure of a privileged communication or reference to one in a press release or public statement, placing a privileged communication at issue in litigation and, as discussed herein, voluntarily disclosing privileged communications or work product to the government all may result in waiver as to all actual or potential adversaries. Informed evaluation of the consequences of waiver requires particular consideration of the possibility of subject matter waiver, in which disclosure of part of a privileged communication, or fewer than all privileged communications concerning a subject, may topple the privilege for related privileged communications.

If the company decides that is in its best interest to voluntarily disclose privileged or work product information to a government entity, the disclosure should be made pursuant to a confidentiality agreement which provides, *inter alia*, that the disclosure of any report, document or information to the government does not constitute a waiver of any applicable privilege or the work product doctrine. If possible, the company should secure the commitment of the government entity to appear in any subsequent proceeding in which production of disclosed information is sought and join the company in seeking to maintain the privileged status of such information. The efficacy of the agreement may depend on the jurisdiction in which a subsequent assertion of waiver is made, but the important policy concerns expressed in decisions like *Saito* furnish convincing grounds for a court to reject waiver in such circumstances.

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[1] *In re Columbia/HCA Healthcare Corp. Billing Practices Litig.*, 293 F.3d 289, 294-95 (6th Cir. 2002) (citation omitted); *see also Saito v. McKesson HBOC, Inc.*, 2002 WL 31657622, *7 (Del. Ch. Nov. 13, 2002) ("The vigorousness of this clashing of swords suggests that the matter is far from settled" in federal or state courts).

[2] Report of Investigation Pursuant to Section 21(a) of the Securities and Exchange Act of 1934 and Commission Statement on the Relationship of Cooperation to Agency Enforcement Decisions, SEC Release No. 44969 (Oct. 23, 2001), at 2.

[3] *See In re Columbia/HCA Healthcare Corp.*, 293 F.3d at 294; *Westinghouse Elec. Corp. v. Republic of the Philippines*, 951 F.2d 1414, 1424 (3d Cir. 1991); *In re Subpoena Duces Tecum*, 738 F.2d 1367, 1369 (D.C. Cir. 1984); *U.S. v. Melvin*, 650 F.2d 641, 645 (5th Cir. 1981).

[4] *See, e.g.*, *Falise v. American Tobacco Co.*, 193 F.R.D. 73, 80 (E.D.N.Y. 2000); ("Unlike the attorney-client privilege, the work- product privilege is not necessarily waived by disclosure to any third party; rather, 'the courts generally find a waiver of the work product privilege only if the disclosure "substantially increases the opportunity for potential adversaries to obtain the information."'") (citing *In re Pfizer Inc. Sec. Litig.*, 1993 WL 561125, *6 (S.D.N.Y. Dec. 23, 1993)).

[5] *Columbia/HCA Healthcare Corp.*, 293 F.3d at 306-07 ("The ability to prepare one's case in confidence, which is the chief reason . . . for the work product protections, has little to do with talking to the Government. Even more than attorney-client waiver, waiver of the protections afforded by the work product doctrine is a tactical litigation decision."); *see also In re Steinhardt Partners, L.P.*, 9 F.3d 230, 235 (2d Cir. 1993); *Westinghouse*, 951 F.2d at 1430-31; *In re Subpoena Duces Tecum*, 738 F.2d at 1371-72; *Bank of Amer., N.A., v. Terra Nova Ins. Co.*, 2002 WL 31842119, *6 (S.D.N.Y. Dec. 19, 2002).

[6] 293 F.3d at 294.

[7] 293 F.3d 289 (6th Cir. 2002).

[8] *In re Columbia/HCA Healthcare Corp.*, 293 F.3d at 303; *see also Westinghouse*, 951 F.2d at 1428 (holding that confidentiality and non-waiver agreement with Justice Department did not prevent waiver because "[e]ven though the DOJ apparently agreed not to disclose the information, under traditional waiver doctrine a voluntary disclosure to a third party waives the attorney-client privilege even if the third party agrees not to disclose the communications to anyone else").

[9] 2002 WL 31657622 (Del. Ch. Nov. 13, 2002).

[10] *Id.*, 2002 WL 31657622 at *7.