Commercial & Business Litigation
FROM THE SECTION OF LITIGATION COMMERCIAL & BUSINESS LITIGATION COMMITTEE

Spring 2012, Vol. 13 No. 3 – Privilege and E-Discovery

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Are Clawback Agreements Being Used to Their Full Extent?

By Jennifer F. Beltrami – April 30, 2012

In its infancy, electronic discovery was heralded as being potentially much more cost effective than discovery by the old-fashioned method of review and production of boxes of hard-copy documents. We now know that to be far from true. The universe of documents potentially relevant to a case and the cost to review and produce such documents have exploded, caused in part by the specter of sanctions for failure to preserve and by complicated, often unwieldy search methodology. Electronic document review can escalate litigation costs by the hundreds of thousands of dollars.

Litigants have responded to such prohibitive costs by entering into “clawback” or “quick-peek” agreements and, in some cases, seeking to memorialize such agreements in a court order. A clawback agreement or order provides that a party producing materials in discovery may “claw back” inadvertently produced privileged materials, while a quick-peek agreement or order allows litigants to produce documents before conducting a privilege review, instead reviewing a smaller set of documents once the party to whom the documents are produced selects those documents it wishes to copy. New Federal Rule of Evidence 502, which went into effect in 2008, explicitly codifies and encourages the use of such agreements and orders. And Federal Rule of Civil Procedure 26(b)(5)(B) now provides a uniform procedure for dealing with inadvertently produced privileged documents. However, clawback arrangements have by no means become universal; many litigants fail to take full advantage of the protections potentially afforded by such agreements.

The Rules Seek to Contain Costs
Federal Rule of Evidence 502 was enacted in 2008 with the stated purpose of reducing the rapidly escalating cost of electronic discovery. One simple provision of the new rule provides a mechanism to safeguard parties to a proceeding against the perils and expense of a huge privilege review as well as the consequences of inadvertent production of privileged material—in that proceeding and others. Rule 502(d) reads:

> **Controlling Effect of a Court Order.** A Federal court may order that the privilege or protection is not waived by disclosure connected with the litigation pending before the court—in which event the disclosure is also not a waiver in any other Federal or State proceeding.

This level of protection is available only if memorialized in a court order, but a party agreement also provides a level of protection. Fed. R. Evid. 502(e) (“An agreement on the effect of disclosure in a Federal proceeding is binding only on the parties to the agreement, unless it is incorporated into a court order.”). Litigants should be mindful that, even if an opposing party will not agree to a clawback provision, they should consider seeking the entry of a clawback order. Some courts will enter such an order sua sponte. *See Radian Asset Assurance, Inc. v. Coll. of the Christian Bros. of N.M.*, No. CIV 09-0885 JB/DJS, 2010 WL 4928866 (D.N.M. Oct. 22, 2010) (court suggested and entered protective order with clawback provision).

The “major purpose” of Rule 502(d) is to cut costs, as the advisory committee notes specify:

> [Rule 502] responds to the widespread complaint that litigation costs necessary to protect against waiver of attorney-client privilege or work product have become prohibitive due to the concern that any disclosure (however innocent or minimal) will operate as a subject matter waiver of all protected communications or information. This concern is especially troubling in cases involving electronic discovery.

The notes further specify that the goal of the rule is to reassure parties that court orders protecting against waiver of privilege will be enforced:

> The rule seeks to provide a predictable, uniform set of standards under which parties can determine the consequences of a disclosure of a communication or information covered by the attorney-client privilege or work-product protection. Parties to litigation need to know, for example, that if they exchange privileged information pursuant to a confidentiality order, the court’s order will be enforceable.
>
> . . . .
>
> [T]he court order may provide for return of documents without waiver *irrespective of the care taken by the disclosing party*; the rule contemplates enforcement of “claw-back” and “quick peek” arrangements as a way to avoid the excessive costs of pre-production review for privilege and work product. *See Zubulake v. UBS Warburg LLC,* 216 F.R.D. 280, 290 (S.D.N.Y. 2003) (noting that parties may enter into “so-called ‘claw-back’ agreements that allow the parties to forego privilege review altogether in favor of an agreement to return inadvertently produced privilege documents”). The rule provides a party with a predictable protection from a court order—predictability that is needed to allow the party to plan in advance to limit the prohibitive costs of privilege and work product review and retention.

Fed. R. Evid. 502 advisory committee’s notes (emphasis added).

Thus, Rule 502(d) is an essential tool in achieving one of the main purposes of Rule 502: reducing the cost of electronic discovery.

In the absence of a clawback order, the court will fall back on Rule 502(b), which, even without a court order or agreement between the parties, protects against inadvertent disclosure:

> **Inadvertent Disclosure.** When made in a Federal proceeding or to a Federal office or agency, the disclosure does not operate as a waiver in a Federal or State proceeding if:
>
> (1) the disclosure is inadvertent;
> (2) the holder of the privilege or protection took reasonable steps to prevent disclosure; and
> (3) the holder promptly took reasonable steps to rectify the error, including (if applicable) following Federal Rule of Civil Procedure 26(b)(5)(B).

Many Courts Encourage, Uphold, and Enforce Clawback Provisions
Courts have relied on Rule 502(d) to enforce party agreements and orders containing clawback and quick-peek provisions, in some cases without regard to the level of review the parties engaged in. *See, e.g.*, *Degeer v. Gillis*, No. 09 C 6974, 2010 WL 3732132, at *8 (N.D. Ill. Sept. 17, 2010) (following clawback agreement to find no waiver; no application of Rule 502(b)); *Rodriguez-Monguio v. Ohio State Univ.*, No. 2:08-cv-00139, 2009 WL 1575277, at *3 (S.D. Ohio June 3, 2009) (relying on clawback provision in protective order to find no waiver); *Alcon Mfg. Ltd. v. Apotex, Inc.*, No. 1:06-cv-1642-RLY-TAB, 2008 WL 5070465, at *6 (S.D. Ind. Nov. 26, 2008) (enforcing clawback provision of protective order to find no waiver and observing that "expensive, painstaking review" such as "double or triple-check[ing] all disclosures" . . . "is precisely what new Evidence Rule 502" was "designed to avoid"); *Morris v. Scenera Research, LLC*, No. 09 CVS 19678, 2011 WL 3808544 (N.C. Super. Ct. Aug. 26, 2011) (finding no need to examine whether review and recall was reasonable under Rule 502(b), as the parties had entered into a clawback agreement).

Some Courts Don't Give Clawback Provisions the Power Rule 502 Intended
Somewhat perplexingly, some courts, even since the adoption of Rule 502(d), have engaged in an analysis under Rule 502(b) even though a clawback or non-waiver agreement is in place. *See Mt. Hawley Ins. Co. v. Felman Prod., Inc.*, 271 F.R.D. 125 (S.D. W.Va. 2010) (despite clawback agreement, steps to prevent disclosure of privileged materials in the first instance must be reasonable; finding waiver because producing party failed to conduct sampling to determine efficacy of search terms); *Relion, Inc. v. Hydra Fuel Cell Corp.*, No. CV06-607HU, 2008 WL 5122828 (D. Or. Dec. 4, 2008) (finding waiver where two emails slipped through review of documents spanning 40 feet of shelf space, despite protective order with clawback provision). Such decisions are potentially quite destructive to the efficacy of Rule 502, which, as the advisory committee notes indicate, was intended to encourage entry and enforcement of clawback orders to reduce the need for parties to concern themselves over whether their conduct would pass scrutiny under a Rule 502(b) reasonableness analysis.

Other decisions are ambiguous as to whether the court's analysis relied on the existence of a clawback agreement or order, or on the weighing of Rule 502(b) factors. *See, e.g.*, *Bd. of Trs., Sheet Metal Workers' Nat'l Pension Fund v. Palladium Equity Partners, LLC*, 722 F. Supp. 2d 845 (E.D. Mich. 2010) (upholding clawback provision in protective order but also enumerating factors demonstrating that Rule 502(b) factors were met by producing party; finding no waiver);

Kandel v. Brother Int'l Corp., 683 F. Supp. 2d 1076 (C.D. Cal. 2010) (enforcing clawback provision in protective order but also making specific determination as to whether producing party's review and recall were reasonable). The reason for the ambiguity may lie in the wording of the clawback provision itself. Without a sufficiently broad provision, the court may feel constrained to engage in the exercise of weighing reasonableness pursuant to Rule 502(b).

Crafting a Strong Claw to Avoid Costs

Parties can increase the cost-avoidance efficacy of a clawback provision and decrease the likelihood that the court will examine the parties' conduct under Rule 502(b) by crafting a clawback agreement that contains more protective language. If crafted broadly enough, a clawback provision can obviate the need for a privilege review entirely. The simple provisions used by the parties in the *Degeer* and *Morris* cases were deemed sufficiently clear that the court need not analyze the parties' conduct pursuant to Rule 502(b). In *Degeer*, 2010 WL 3732132, the provision read simply as follows:

> [I]nadvertent production of any confidential, privileged, or work product documents shall be without prejudice to any claims that the document is confidential or privileged, and shall constitute neither a waiver of any claim of privilege that may otherwise attach thereto nor a general waiver of such claim or privilege.

In *Morris*, 2011 WL 3808544, the provision read as follows:

> The production of attorney-client privilege materials, work product protected materials, or trial preparation materials shall not constitute a waiver of those protections. In the event of such protected information, the Parties will follow the procedure set out in Rule 26(b)(5).

However, given decisions such as *Palladium*, *Kandel*, *Mt. Hawley*, and *Relion*, in which the clawback provisions were arguably no less clear than those in *Degeer* and *Morris*, it might behoove a party to include in the clawback provision language specifying that the review undertaken by producing parties is deemed to satisfy the reasonableness requirement of Rule 502. The provision at issue in *Mt. Hawley* contained such language as to parties' conduct upon discovery of the inadvertent production but not as to the initial review.

Other language may be included at least to cut off inquiry as to whether the disclosure is inadvertent. For example: "Production of materials as to which a claim of privilege is later asserted pursuant to this provision shall be deemed inadvertent." Even language requiring "that the producing party promptly makes a good-faith representation that such production was inadvertent or mistaken" may be sufficient. *See Alcon*, 2008 WL 5070465. In *Degeer*, 2010 WL 3732132, for example, the court enforced the clawback provision, but it did engage in a determination as to whether the disclosure was inadvertent. Language such as the foregoing may render such inquiry unnecessary.

Lessons from the Case Law
Thus, although the advisory committee notes suggest it, litigants are unlikely to take the drastic step of forgoing a privilege review altogether, because there is no absolute guarantee the clawback provision in the confidentiality order will be enforced. Also, at least one court has indicated that a "document dump" without "[any] effort whatsoever to review for privilege or protected documents" may not be permissible even under an enforceable clawback provision. *See Rajala v. McGuire Woods, LLP*, No. 08-2638-CM-DJW, 2010 WL 2949582, at *7 (D. Kan. July 22, 2010) (entering clawback order on showing of good cause by party seeking the order, over opposing party's objection). However, even if it does not eliminate the need for review altogether, the entry of a Rule 502(d) clawback order containing the right provisions can at least drastically reduce the cost of such review.

A further reason parties may be reluctant to rely too heavily on clawback provisions is that once a party is on notice of an inadvertent production, the safeguards of Rule 502 may be lost altogether. *See United States v. Sensient Colors, Inc.*, No. 07-1275 (JHR/JS), 2009 WL 2905474, at *22–23 (D.N.J. Sept. 9, 2009), *and* Fed. R. Evid. 502(b) advisory committee's note ("The rule does not require the producing party to engage in post-production review to determine whether any protected communication or information has been produced by mistake. But the rule does require the producing party to follow up on obvious indications that a protected communication or information has been produced inadvertently."); *see also Brookdale Univ. Hosp. v. Health Ins. Plan of Greater N.Y.*, No. 07 CV 1471(RRM)(LB), 2009 WL 393644 (E.D.N.Y. Feb. 13, 2009) (enforcing clawback agreement but finding privilege preserved only as to those documents initially recalled; producing party not excused from reexamination of entire production). Thus, one mistake in a huge document production could require re-review of the entire production.

But there certainly does not seem to be much downside, if any, in seeking the entry of a protective order with a clawback provision. It would seem that one of the only advantages to not entering into a clawback agreement or seeking a clawback order from the court may be that, should one's adversary slip up and inadvertently produce a privileged document, one may argue that the privilege has been waived (although, for such a waiver argument to succeed, one would still need to show that the producing party had failed to satisfy the standard of Rule 502(b)). Engaging in such tactics on the slim chance of gaining a litigation advantage would seem to be clearly outweighed by the potential peril that can be avoided with a clawback agreement or order. *See Rajala*, 2010 WL 2949582, at *7 ("To deny entry of such a clawback provision merely because Plaintiff would be deprived of the opportunity to demonstrate that the producing party had not taken reasonable care to prevent disclosure would defeat the purpose behind rule 502(d) and (e). The goal is not to encourage disputes regarding waiver and inadvertent production, but to prevent such disputes from arising in the first place.").

The disadvantages of proceeding without a clawback provision include exposure to malpractice claims arising from the inadvertent production of privileged material and a higher cost of privilege review. Although a party may fall back on Rule 502(b), without a clawback agreement or order, that party faces the risk that the court will not deem the efforts made to protect the information sufficient to satisfy Rule 502(b). Most courts do favor the producing party and find that no waiver results from inadvertent production of privileged material, but not all do, and the determination is within the discretion of the court. How much simpler to reach an agreement, "so ordered" by the court, at the outset of the case, that any materials inadvertently produced will not effect a waiver of the privilege. As Judge Shira Scheindlin, author of the *Zubulake* decision quoted in the advisory committee notes to Rule 502, reminded attendees at a recent New York State Bar Association meeting, remember to seek a clawback order—especially in cases where high electronic discovery costs loom.

Keywords: litigation, commercial, business, clawback provisions, Federal Rule of Evidence 502, containing costs

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The Rule 26 Amendments: One Year Later

By Louis E. Kempinsky and John C. Keith – April 30, 2012

On December 1, 2010, several amendments to Federal Rule of Civil Procedure 26 took effect. The primary thrust of the 2010 amendments was to address the "undesirable effects" of the 1993 amendments to Rule 26, which had provided for "routine discovery into attorney-expert communications and draft reports." 2010 amends., advisory committee's notes. The four main changes were

- generally narrowing the subject-matter of a testifying expert's disclosure, Fed. R. Civ. P. 26(a)(2)(B);
- extending work-product protection to draft expert reports, Fed. R. Civ. P. 26(b)(4)(B);
- providing new work-product protection to attorney-expert communications, Fed. R. Civ. P. 26(b)(4)(C); and
- clarifying which testifying experts are required to provide written reports, Fed. R. Civ. P. 26(a)(2)(B) and (C).

The 2010 amendments have been in effect for just over a year, and they have not been applied in all cases. The 2010 amendments apply to cases pending as of December 1, 2010, only "when just and practicable." Order Amending Federal Rules of Civil Procedure, Apr. 28, 2010. As is not surprising in light of the standard, cases examining whether it would be "just and practicable" to apply the new version of the rule are highly fact-driven and have come down on both sides. Case law interpreting the amendments is still in an early stage of development. Nonetheless, a number of potentially significant issues have already emerged.

Are Experts' Notes Protected from Disclosure?

One such issue is whether an expert's notes are protected from disclosure. The 2010 amendments narrowed Rule 26(a)(2)(B)(ii) "to provide that disclosure include all 'facts or data considered by the witness in forming' the opinions to be offered, rather than the 'data or other information' disclosure prescribed in 1993." 2010 amends., advisory committee's notes. Rule 26(b)(4)(B) was also amended to provide work-product protection for draft expert reports. Together, these amendments could fairly be read to protect an expert's notes. Like a draft report, notes arguably are in the nature of work product (albeit at a more elemental level than the draft report itself) and consist of more than the raw "facts or data considered by the witness."

At least one court has found an expert's notes to be protected under the new version of Rule 26. *See D.G. ex rel. G. v. Henry*, 08-CV-74-GKF-FHM, 2011 WL 1344200 (N.D. Okla. Apr. 8, 2011) ("The court finds that notations or highlights on the case files do not constitute facts or data and do not need to be provided under Fed. R. Civ. P. 26(a)(2)(B)(ii)."). However, at least two other courts have reached the opposite conclusion. Both rejected the argument that notes qualify as draft reports and relied instead on a statement in the advisory committee notes that, under the amended Rule 26(b)(4), "the expert's testing of material involved in litigation, and notes of any such testing, would not be exempted from discovery." 2010 amends., advisory committee's notes. *See Dongguk Univ. v. Yale Univ.*, 3:08-CV-00441 TLM, 2011 WL 1935865 (D. Conn. May 19, 2011) ("As for Kim's hand-written notes, as a general matter, an expert's notes are not protected by 26(b)(4)(B) or (C), as they are neither drafts of an expert report nor communications between the party's attorney and the expert witness."); *In re Asbestos Prods. Liab. Litig. (No. VI)*, MDL 875, 2011 WL 6181334 (E.D. Pa. Dec. 13, 2011) ("We note with respect to Dr. Anderson, that he has in his possession copies of his hand-written notes. These do not fall under the draft report provision of Rule 26(b)(4)(B). These notes were not 'draft reports,' but rather reflect his own interpretations of the B-read results he was retained to analyze for CVLO.").

Are Experts Who Do Not Write a Report Deprived of Protection?

Perhaps an even more interesting, and significant, issue arising from the 2010 amendments is the tension created between two of the amended provisions in the treatment of experts who do not write a formal report. On the one hand, the amendments clarify that many types of experts, including employees who do not typically provide expert testimony, are not required to provide written reports under Rule 26(a)(2)(B). On the other hand, the new protections for attorney-expert communications in Rule 26(b)(4)(C) appear to be limited to those experts who are in fact required to provide Rule 26(a)(2)(B) reports. Taken together, the two amendments are arguably a case of "one hand giveth, and the other taketh away."

Many Experts Need Not Prepare a Long-Form Report

As part of the 2010 amendments, section (a)(2)(C) was added to Rule 26 "to mandate summary disclosures of the opinions to be offered by expert witnesses who are not required to provide reports under Rule 26(a)(2)(B) and of the facts supporting those opinions." 2010 amends., advisory committee's notes. By its plain text, Rule 26(a)(2)(B) requires a report only from an expert "retained or specially employed to provide expert testimony in the case or one whose duties as the party's employee regularly involve giving expert testimony." However, many courts were uncomfortable with numerous categories of experts being wholly exempt from any reporting requirement, and the amendment, by requiring at least a short-form disclosure from all experts, "resolves a tension that has sometimes prompted courts to require reports under Rule 26(a)(2)(B) even from witnesses exempted from the report requirement." 2010 amends., advisory committee's notes.

By helping to clarify that courts should not require a long-form report from any type of expert except the two specifically described in section (a)(2)(B)—specially retained experts and employees who regularly give expert testimony—section (a)(2)(C) gives parties an incentive to look elsewhere for their expert opinions, including to their own employees who do not regularly give expert testimony. *Allstate Insurance Co. v. Nassiri*, 2:08-CV-00369-JCM, 2011 WL 2975461 (D. Nev. July 21, 2011), illustrates the implications of applying the amended rule as it apparently was intended to be. That case involved claims by an insurance company (Allstate) to recover the inflated portions of dozens of insurance claim settlements, arising from the defendant's allegedly improper and unnecessary medical services and billings. Allstate sought to introduce expert testimony on damages from an employee (Patterson), who reviewed the claim files and the underlying expert opinion of Allstate's retained medical expert and then calculated the reasonable settlement value of the claims, using a formula created by Allstate.

The court engaged in an extended discussion of two lines of authority that had developed prior to the 2010 amendments, addressing whether Rule 26 required a report from a party employee expert who had no percipient knowledge of the events in dispute but developed his opinions solely in preparation for trial. The court held that, while the amendment did not explicitly reject the prior majority interpretation that a report is required, the fact that the rule was not amended to adopt that position, but instead to require at least a short-form disclosure from all experts, supported the prior minority interpretation that no report is required. Accordingly, the court held that no long-form report was required from Patterson, notwithstanding the following findings: (1) "Patterson was not involved in evaluating and determining the settlement value of the underlying claims during the time that they were being adjusted or litigated;" (2) "[r]ather, he was assigned the task of reviewing the settlements and determining the amount of Allstate's alleged damages for purposes of testifying in this case;" and (3) "Patterson functioned exactly as an expert witness normally does, providing a technical evaluation of evidence he has reviewed in preparation for trial." *Nassiri*, 2011 WL 2975461, at *9.

Privilege and Work-Product Protections May Be Waived

While cases like *Nassiri* might give organizational parties a strong incentive to use their own employees as experts and thereby avoid preparing a long-form report, cases like *United States v. Sierra Pacific Industries*, CIV S-09-2445 KJM EF, 2011 WL 2119078 (E.D. Cal. May 26, 2011), illustrate the potential drawbacks of that approach. The case concerned damages caused by the Moonlight Fire in 2007, for which the government brought suit. Two government employees investigated the fire and prepared an Origin and Cause Report documenting their findings. The parties and the court agreed that these employees were non-retained, "non-reporting" expert witnesses subject only to the short-form disclosure requirements of Rule 26(a)(2)(C).

Based in large part on that finding, the court held that the witnesses' communications with the government's attorneys were not protected under Rule 26's newly added section (b)(4)(C), providing new work-product protections for attorney-expert communications (subject to certain enumerated subject-matter carve-outs). Because the new section limits its protections to attorney communications with "reporting experts" under Rule 26(a)(2)(B), by its terms it "does not itself protect communications between counsel and other expert witnesses, such as those for whom disclosure is required under Rule 26(a)(2)(C)." 2010 amends., advisory committee's notes.

The *Sierra Pacific* court acknowledged that "the advisory committee notes explain that the new rule does not provide protection for communications between non-reporting experts and counsel, *but does not disturb any existing protections*," such as privilege or independent development of the work-product doctrine. *Sierra Pacific*, 2011 WL 2119078, at *5 (emphasis added). Nonetheless, the court held that any existing protections were waived when the employees were designated as experts. The court discussed at length the state of the law on this issue as it existed in the Ninth Circuit prior to the 2010 amendments, as well as the advisory committee's deliberations. The court noted that the advisory committee had explicitly discussed this issue and, finding that there were certain circumstances under which broad discovery should be allowed into an attorney's communications with a non-reporting employee expert, had refused to protect such communications in all cases. Ultimately, the *Sierra Pacific* court declined to hold that designating an individual as a non-reporting expert waives privilege and work-product protections in all cases, or even in all cases involving non-reporting employee experts. Nonetheless, the court held that, in this particular case, the government had waived any otherwise applicable protections.

Although the *Sierra Pacific* court's holding was thus limited, it still demonstrates the risk parties run in designating their own employees as non-reporting experts. This risk is particularly acute where the employee is also a fact witness and has had otherwise privileged communications with counsel concerning percipient aspects of his or her testimony. Notably, the *Sierra Pacific* court ordered the disclosure of all of the witnesses' communications with counsel, even though it expressly acknowledged the witnesses' hybrid fact/expert role. The court reasoned as follows: "While it is desirable that any testifying expert's opinion be untainted by attorneys' opinions and theories, it is even more important that a witness who is testifying regarding his own personal knowledge of facts be unbiased. Therefore, at least in some cases, discovery should be permitted into such witnesses' communications with attorneys, in order to prevent, or at any rate expose, attorney-caused bias." *Sierra Pacific*, 2011 WL 2119078,*10. Thus, it was the witnesses' status as *fact* witnesses that caused the court to find a waiver, an illogical result. The testimony of all fact witnesses, not just hybrid fact/expert witnesses, can be tainted by attorney bias. However, allowing a client representative to testify as a fact witness does not generally waive the attorney-client privilege.

While the court's reasoning was suspect, it could nonetheless serve as a template for other courts. The holding thus gives organizational parties good cause to be wary of designating their own employees as non-reporting experts, even if the 2010 amendments clarify that such experts need not provide a long-form written report.

Keywords: litigation, commercial, business, Federal Rule of Civil Procedure 26, expert witnesses, work-product privilege, attorney-client privilege

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The Benefits of a *Miranda*-Type Approach to *Upjohn* Warnings

By Sehyung Daniel Lee – April 30, 2012

Prosecutors have begun to charge corporate employees with obstruction of justice when an employee lies or tampers with evidence during an internal corporate investigation, even if no government investigation of the company is pending at the time. Because employees can now be charged with a crime that carries penalties including up to 20 years in prison, investigating attorneys may want to consider expanding the *Upjohn* warnings provided to corporate employees to include a warning derived from the criminal *Miranda* warning context, notifying them that lying or providing false documents in an internal investigation can lead to criminal punishment.

Following the seminal decision in *Upjohn Co. v. United States*, 449 U.S. 383 (1981), attorneys conducting internal corporate investigations typically provide certain warnings to corporate employees they interview, including that counsel is working for the employer, not the employee; the attorney-client privilege is in effect; and the privilege is held by the employer, and the employer alone can decide to waive it. In light of increasing prosecutions of employees, there are two good reasons why investigating counsel should now include a criminal *Miranda*-type warning to its *Upjohn* warnings: first, as matter of fairness to inform employees that they could be committing a crime; and, second, to prevent employees from muddying investigations by providing misinformation.

Although an investigating attorney would prefer candor when interviewing employees, if given the choice of hearing a lie or hearing nothing, most investigating attorneys will choose an employee's silence. Silence tells the investigating attorney that the employee thinks that he or she did something wrong, whereas a lie will waste time until the investigating attorney discovers that the employee is lying. Unfortunately, to prevent lying, investigating attorneys do not have a magic pen that will write the words "I must not tell lies" on an employee's hand. However, in light of these new prosecutions, investigating attorneys can warn employees of the criminal consequences of lying and prevent the introduction of misinformation into their investigation.

The Criminal Statute

The new prosecutions stem from 18 U.S.C. § 1519, which provides as follows:

> Whoever knowingly alters, destroys, mutilates, conceals, covers up, falsifies, or makes a false entry in any record, document, or tangible object with the intent to impede, obstruct, or influence the investigation or proper administration of any matter within the jurisdiction of any department or agency of the United States or any case filed under title 11, or in relation to or contemplation of any such matter or case, shall be fined under this title, imprisoned not more than 20 years, or both.

Courts have found that section 1519 applies in three scenarios: when there is a federal investigation, when the defendant anticipates there will be a pending federal investigation, or when there is no pending federal investigation. Therefore, whether there is a federal investigation pending is irrelevant to a section 1519 violation. Even where there is only an internal corporate investigation, a violation may arise where a defendant tampers with documents with the "intent to impede, obstruct, or influence" the investigation. *United States v. Yielding*, 657 F.3d 688 (8th Cir. 2011).

Although the statute was originally considered an anti-shredding statute, courts have recently interpreted section 1519 to include a wide range of conduct, including falsifying documents provided to the government during a kick-back investigation, *id.*; destroying computer records from a personal computer before the Federal Bureau of Investigation started its investigation, *United States v. Kernell*, No. 10-cr-6450, 2012 WL 255765, at *1 (6th Cir. Jan. 30, 2012); and throwing undersized fish overboard before the Coast Guard could inspect the fish, *United States v. Yates*, No. 2:10-cr-66, 2011 WL 344093, at *1 (M.D. Fla. Aug. 8, 2011).

A Second Circuit case illustrates how section 1519 could apply in the context of internal corporate investigations. In *United States v. Gray*, 642 F.3d 371 (2d Cir. 2011), one of the guards at a privately owned prison assaulted a prisoner, who was hospitalized for treatment of injuries in the assault. During an internal prison investigation, the other guards who witnessed the incident submitted false reports, stating that no force had been used on the prisoner. However, some of the guards had a change of heart and submitted new reports stating that force had been used. Several months later, Office of the Inspector General of the Department of Justice (DOJ) commenced a federal investigation of the incident. The guards who submitted false reports were eventually convicted of violating section 1519. The guards appealed, arguing that the statements they submitted did not violate section 1519 because they were employed by a private entity, not the government, and because there was no evidence that the guards knew or contemplated that their false reports would be submitted to the government during its investigation. The Second Circuit found that because the DOJ is charged with addressing allegations of excessive force, and the guards were aware of the DOJ policy of investigating charges of excessive force, the false reports were made in a matter "within the jurisdiction" of the federal department, and the court thus upheld the section 1519 convictions.

Prosecutors have also recently used section 1519 in a corporate setting to prosecute employees who destroyed records or lied to corporate counsel during an internal investigation before the government investigation began. In *United States v. Ray*, No. 2:08-cr-01443 (C.D. Cal. 2008), the defendant, a vice president (VP) of human resources, and the chief executive officer (CEO) lied and provided false reports to in-house counsel concerning the back-dating of stock options. Based on that information, the in-house counsel submitted reports to the Securities and Exchange Commission (SEC), which then conducted an investigation and discovered the two corporate officers' misrepresentations. The VP, who agreed to help the government and testify against the

CEO, was charged with and pled guilty to conspiracy to violate section 1519. The CEO, on the other hand, was not charged with any counts related to section 1519.

As in the *Gray* matter, no federal investigation had begun when the VP in *Ray* made his false statements. In-house counsel was investigating because of the recent SEC practice of scrutinizing companies' stock option back-dating practices, as opposed to the company having been alerted to any suspected wrongdoing. To clearly implicate section 1519, the plea agreement specifically noted that the VP was aware that the SEC was investigating corporate stock option back-dating practices, thus placing the issue within the jurisdiction of a federal agency. However, the prosecutors also expanded section 1519 to apply to the VP's false statements to in-house counsel, in addition to his submission of false reports. The VP received three years of probation and a $10,000 fine.

In another recent prosecution, *United States v. Carson*, No. 8:09-cr-00077 (C.D. Cal. 2009), the defendant was accused of violating section 1519 by tearing up documents and flushing them down the toilet before her meeting with in-house counsel concerning a bribery investigation. However, the government later filed an ex parte application to dismiss the count, the sole reason being that the dismissal would be "in the interests of justice."

Although the defendant in *Ray* pleaded guilty to conspiracy to violate section 1519 and although the section 1519 charge in *Carson* was dismissed, employees should be aware that lying to in-house counsel during the course of an internal investigation could result in criminal prosecution. Inevitably, this will place some employees between a rock and a hard place. Assuming that an employee did something wrong, if he or she keeps quiet or refuses to cooperate, the employee could be fired by the company for impeding an internal investigation. However, if the employee lies to the investigating attorney to save his or her job, he or she can now face criminal punishment, including jail time. Therefore, the best time to warn an employee of the consequences of lying would be before the employee has an opportunity to lie—namely, at the beginning of the employee interview.

The Limitations of an *Upjohn* Warning

When a company suspects that it might have committed wrongdoing, it will usually ask its in-house counsel, or hire outside counsel, to conduct an internal investigation of the matter. During the course of an internal investigation, employees are interviewed to determine whether the company committed wrongdoing and, if so, the potential ramifications. If a company determines that it is in its own best interest to release the employee interviews to the government, companies can and will release the interviews, even if it will be to the detriment of the employee.

In order for the company to release employee interviews to the government, the company must have the right to do so. In other words, if the conversations between an employee and counsel are protected by attorney-client privilege but the company is the client, the company can release the employee's interview to the government. However, if the employee is the attorney's client, counsel must not release the interview to the government without the employee's consent.

Under *Upjohn*, investigating counsel will give warnings to employees so that the company will have the right to release its employees' interviews. According to the American Bar Association, it is recommended that counsel give the *Upjohn* warnings at the outset of the employee interview, with the minimum warnings that (1) counsel is retained by the company, not the employee; (2) the attorney-client privilege is in effect; and (3) the privilege is held by the company, which alone can decide to waive it. *See* ABA WCCC Working Group, *Upjohn Warnings: Recommended Best Practices When Corporate Counsel Interacts with Corporate Employees* [PDF] (July 17, 2009). These warnings do not address potential criminal liability.

The Proposed Solution: A *Miranda*-Type Warning

Notably absent in the ABA-suggested *Upjohn* warnings is the *Miranda*-type warning of the right to remain silent and that anything the person says or does can and will be used against that person in a court of law. In the past, a *Miranda*-type warning in corporate investigations was usually unnecessary because the purpose of the *Upjohn* warnings was to inform an employee that although the employee interview would be protected under attorney-client privilege, the investigating attorney did not represent the employee. In fairness, the *Upjohn* warnings also made sure that an employee would understand the reason for the warning, that the company held the attorney-client privilege, and that it was the company's choice whether to disclose the employee's interview. In this way, the employee can make an informed decision on what to disclose to the investigating attorney.

In light of recent prosecutions under section 1519 for lying to an investigating attorney, a natural extension of the *Upjohn* warnings would be to include a *Miranda*-type warning that would inform the employee of the potential criminal consequences for lying to the internal investigator, and allow the employee to make an informed decision on the nature and accuracy of information he or she will provide to the investigating attorney.

However, repeating the entire criminal *Miranda* warning verbatim to give the employee notice would be counterproductive. The stigma of a complete *Miranda* warning is more likely to instill unnecessary fear and suspicion, both of which would hamper an internal investigation. Rather, a mere instruction that making false statements during the interview or producing falsified documents could result in criminal prosecution should suffice.

Obviously, adding a *Miranda*-type warning to the *Upjohn* warnings might cause employees to be less candid. However, an employee who has nothing to fear will probably tell the truth (as do most innocent people when given the *Miranda* warning), and employees who have done something wrong might be less willing to lie to cover up their tracks. By being placed on notice that lying to the investigating attorney could result in criminal prosecution, the employee now has more reason to remain silent than to lie. If an employee chooses to remain silent, the investigating attorney can infer that the employee believes he or she has done something wrong, rather than having to come to this conclusion weeks or months later after following up on bad information.

Conclusion
Although there is not yet a plethora of prosecutions against employees under section 1519 for lying during an internal investigation prior to government involvement, employees should be made aware that their lies during an internal investigation could result in criminal penalties. This will allow employees to make informed decisions on what to disclose. Although this additional warning may cause employees to be less forthcoming during an interview with investigating counsel, it may also ensure that the information provided by employees to investigating counsel is truthful and accurate.

Keywords: litigation, commercial, business, *Miranda* rights, *Upjohn* warnings, attorney-client privilege

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Reviewing Privilege Issues During Transaction Negotiations

By Scott B. Murray – April 30, 2012

Almost every litigator has been asked at some point to handle a business litigation case involving operative documents that neither the litigator nor his or her firm was involved in drafting. In such situations, the litigator often finds that the client's case could have been stronger if certain contract provisions or transactional documents had been drafted with a keener eye toward future litigation that might develop. Because of this common experience, many litigators work with their firms' transactional teams during the negotiation of transactions to assist with drafting contract and other transactional language that might benefit their clients in future litigation.

However, how often are litigators or attorneys well-versed in privilege issues asked to assist transaction teams for the express purpose of limiting the disclosure or exchange of privileged information during due diligence and the extensive negotiations that often occur between the parties, especially in complex transactions? Given that the parties to a proposed transaction are often more concerned with obtaining and reviewing the information necessary to analyze and structure the deal than they are with thinking about how the disclosure of privileged information might be used against them in a future lawsuit, it is often difficult to convince the businesspeople that such privilege issues are a significant concern. This is especially true when counsel is preventing the exchange or disclosure of information that the parties believe is needed to overcome a negotiating hurdle. Even if your answer to the question of involving a litigator or other attorney to manage and supervise privilege issues is "Often" or "Always," a recent Illinois Appellate Court decision highlights why parties to a transaction should rigorously analyze the need to disclose or exchange privileged information during due diligence and negotiations to avoid or limit the unintentional waiver of privilege protections. Although the case has been appealed to the Illinois Supreme Court, which may have already issued a decision by the date this article is published, the Illinois Appellate Court's ruling nonetheless highlights the need for transacting parties to consider carefully the disclosure and exchange of privileged information.

Center Partners, Ltd. v. Growth Head GP, LLC

In *Center Partners, Ltd. v. Growth Head GP, LLC*, 957 N.E.2d 496 (Ill. App. Ct. 2011), the Illinois Appellate Court upheld a lower court's order requiring the production of documents that had been withheld as privileged by the defendants. The underlying facts can be summarized relatively briefly. Three separate groups of entities were negotiating together to purchase the various assets of a fourth entity. The three groups were also communicating and negotiating among themselves regarding the acquisition, and during these communications and negotiations, they shared with one another legal advice regarding the acquisition that they each had received from their respective legal counsel. Moreover, in addition to the purchase agreement that the three groups entered into with the fourth entity, the three groups entered into a separate joint purchase agreement among themselves, regarding the allocation of the various assets and the purchase price each would pay, and, simultaneously with the closing of the purchase, another agreement regarding control of one of the entities among the assets they had purchased. Subsequently, minority limited partners of a sub-entity that was subject to the control agreement brought suit against the three acquiring groups, alleging breach of fiduciary duty and other contractual duties arising from the purchase.

The plaintiffs won a motion to compel the production of attorney-client communications that had been disclosed between the three groups during negotiations. They subsequently filed a motion to compel the production of all attorney-client communications between each of the acquiring groups and their respective counsel—even those not disclosed to another group—based on a subject-matter waiver argument. This would entail the production of over 1,500 documents identified on the defendants' privilege logs. The lower court granted the motion following an in camera review of some of the documents, and after the lower court denied a motion for reconsideration, certain of the defendants appealed.

The Illinois Appellate Court Ruling

The appellate decision, affirming the lower court ruling requiring the production of the privileged documents, includes several sweeping statements regarding subject-matter waiver under Illinois law:

- "Notwithstanding the application of the privilege, the privilege can be waived by the client when the client voluntarily discloses the privileged information to a third party. The scope of the waiver extends to all communications relating to the same subject."
- "Defendants disclosed among one another their attorneys' position on specific terms of the transaction and the structure for allocating control . . . as well as various written documents containing privileged attorney-client communications. These disclosed communications and documents are clearly waived, and the scope of the waiver extends to all communications relating to the same subject matter, *i.e.*, the purchase . . . ."
- "[W]e find no reason to distinguish between a waiver occurring during the course of litigation or during a business negotiation. Once the privileged communication is disclosed to a third party, the privilege is waived, and the scope of the waiver extends to all communications relating to the same subject matter."
- "Further, to clarify, we do not hold that disclosure of certain privileged communication during negotiations nullifies *all* privileged communication and information as related to a particular business transaction, but, rather and specifically, as related *only* to the subject matter of the privilege that is already waived."

957 N.E.2d at 501–3 (emphasis in original).

In reaching its decision, the court stated that the attorney-client privilege is to be "construed 'within its narrowest possible limits[,]'" based on Illinois's "'strong policy of encouraging disclosure, with an eye toward ascertaining that truth which is essential to the proper disposition of a lawsuit.'" *Id.* at 501 (quoting *Waste Mgmt., Inc. v. Int'l Surplus Lines Ins. Co.*, 144 Ill. 2d 178, 190, 579 N.E.2d 322 (1991)).

These broad statements are the focus of an amicus brief—filed by the Illinois State Bar Association, Association of Corporate Counsel, and Association of Corporate Counsel Chicago Chapter—arguing that the court's decision is incorrect. However, regardless of the outcome of the case before the Illinois Supreme Court, and even granted that courts in other states may be more protective of privileged information than the Illinois Appellate Court was in its decision, transacting parties and their counsel should take certain practical guidance from the Appellate Court ruling.

Negotiation, Like Litigation, Raises Privilege Concerns
Companies involved in negotiating transactions are often very cautious about disclosing or exchanging privileged information with the party on the other side of the table. This is only natural because the other party is often considered an adversary in connection with the negotiation of the terms and conditions of the deal. Even when the transaction is a friendly one, each company is still attempting to negotiate the best terms and conditions for its interests and is usually careful to safeguard privileged communications with its counsel, which might reveal its business objectives and goals for the transaction. Therefore, it is not often a challenge to convince companies to avoid disclosure of privileged information to the party across the negotiating table.

However, when companies are working together in a transaction on the same side of the table, their joint interests in the structure and terms of the deal may alter their normal inclination to be guarded with privileged information. In such situations, the businesspeople may consider themselves to be jointly negotiating the deal and may feel that because their companies' interests are aligned, there is less concern about exchanging privileged information. Moreover, regardless of the alignment of the parties, if the issues are complex and the financial stakes substantial, there is often even more pressure for the parties to disclose and exchange information, including privileged information, that will assist the businesspeople in understanding any roadblocks or hurdles that have developed during the negotiations. Counsel is often called upon in such situations to find solutions to help the businesspeople obtain and review the information deemed necessary to resolve the issue, especially if the problematic issue is a legal one raised by counsel.

In such situations, it may be important to have a litigator or other attorney who is tasked with spotting and analyzing privilege issues as part of the transaction team. One reasonable interpretation of *Center Partners* is that companies should avoid viewing the negotiation of a transaction differently than litigation. During litigation, clients and their counsel are especially focused on privilege issues to avoid disclosing their litigation strategy or facts about the case that have been disclosed in confidence, as both are considered integral to the outcome of the litigation. However, in negotiating a transaction, such concerns regarding protecting privileges recede. The terms and the conditions of the deal are the parties' primary focus, and the discussion of various legal considerations and how they effect the terms and conditions being negotiated are considered means to consummating the deal that should not (and often must not) stand in the way of negotiations.

The Privilege Manager
Therefore, the appointment of a litigator or other attorney focused on privilege issues as "privilege manager" may be useful to avoid or limit the disclosure and exchange of privileged

information to reduce the risk of a waiver argument being asserted by future litigants seeking to obtain the privileged information and use it against the disclosing party. This privilege manager should be well versed in privilege issues, especially any state-specific privilege case law that might apply to the transaction. The privilege manager should be part of the transaction team from the start of negotiations and made aware of any potential issues that may be the focus of legal advice or opinions communicated to the client or the subject of attorney work product.

The privilege manager should be asked to consider the potential risks of disclosing or exchanging a variety of privileged information and, as necessary, to develop alternative means for the parties to negotiate the terms and conditions of the transaction without disclosing or exchanging privileged information or drafting an agreement between the transacting parties governing the protection of privileged information to be disclosed between the parties. Such agreements, sometimes labeled "common interest agreements," state the parties' reasons for the disclosure of privileged information and their agreement that such disclosure either does not evidence the disclosing party's waiver of any applicable privilege (i.e., in anticipation of future litigation) or represents only a limited waiver of any applicable privilege for the communications or documents exchanged and not a subject-matter waiver. Of course, the effectiveness of such agreements to defeat any future waiver arguments will depend on the governing law applied to the agreement by the court ultimately reviewing the agreement.

Before any privileged information is shared with third parties, including parties on the same side of the negotiating table, the privilege manager should be asked to consider ways to limit or eliminate the need to disclose or exchange such privileged information, or limit the disclosure or exchange so as to reduce the scope of any potential subject-matter waiver arguments. The privilege manager will therefore be asked to balance the immediate interest in assisting the parties' negotiations with the long-term concern of exposing privileged information to production in future litigation. The balance may often fall on the side of disclosure or exchange, but the analysis will help the parties craft the best solution for the disclosure or exchange.

Conclusion
You never know with any certainty when a deal or business relationship is going to lead to litigation. From the outset of negotiations, parties should consider how to best position themselves for any foreseeable future litigation. The *Center Partners* case reminds us that the protection of privileged information during due diligence and negotiations is also a significant consideration for the parties. Litigation counsel are often looking for ways to obtain access to privileged communications in the search for evidence to support their clients' claims or defenses. Therefore, transacting parties should carefully consider being as vigilant in protecting privileged information during negotiations as they otherwise might be during litigation.

Keywords: litigation, commercial, business, transaction negotiations, privilege, Illinois

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Negotiating Effective Search Terms Will Save Expense Later

By Angela M. Scafuri – April 30, 2012

Lack of attention to the requirements of electronic discovery is a black hole in which many litigators may find themselves, leading to extra discovery expense and, sometimes, sanctions by the court. How many cases have we seen regarding a party's failure to issue a litigation hold, a seemingly simple task? Or cases detailing the failure of parties to engage in a substantive Rule 26(f) conference, failing to discuss the form and manner of production of electronically stored information (ESI) until the last minute, when discovery requests are actually served?

Similarly, parties routinely fail to give proper attention to search terms for ESI. In a rush to comply with a court-ordered deadline, parties often fail to craft detailed search parameters. When it comes to negotiating search terms, why do parties seem to ignore the critical importance of this not so simple task? Taking the time to craft effective search terms now can save you from a huge headache later. Indeed, the opinion in a recent decision from the District of New Jersey, *I-Med Pharma, Inc. v. Biomatrix Inc.*, No. 03-3677 (DRD), 2011 U.S. Dist. LEXIS 141614, at *1 (D.N.J. Dec. 9, 2011), begins with the following thought: "This case highlights the dangers of carelessness and inattention in e-discovery." Therein lies a cautionary tale on the importance of negotiating effective search parameters.

The *Biomatrix* Decision

In *Biomatrix*, I-Med filed suit alleging that Biomatrix had failed to provide its products to I-Med in breach of contracts granting I-Med exclusive distribution rights. The parties entered into a stipulation to resolve discovery disputes. As part of the stipulation, I-Med permitted Biomatrix, through its expert, to conduct a forensic search of I-Med's computer network, including servers and related storage devices. The search parameters negotiated between the parties included more than 50 specified keywords, including some in French. The search parameters were extremely broad. They were not narrowed to a particular time period or to specific custodians. Nor were the search parameters limited to active files; they included a search of unallocated space, which held deleted files, partially deleted files, and other temporary files. The expert was charged not only with the task of culling these data but also with determining how and when documents and files containing keywords were deleted, modified, or both.

Biomatrix's expert ultimately provided I-Med with a ZIP file of the records retrieved from its systems. Pursuant to the stipulation, I-Med had agreed to review the material, determine which documents were responsive and which were confidential, and create a privilege log as to any privileged documents. The non-privileged documents, as well as the log, were to be turned over to Biomatrix within 60 days of I-Med's receipt of the documents from the expert. After receipt of the ZIP file, however, I-Med complained that just to open each file would take more than 10,000 hours of time: The expert's work had returned 187,796 active files and more than 251 gigabytes of data in the deleted files—consisting of 64,382,929 hits (documents) in unallocated space alone, representing some 95 million pages of data. I-Med asked for, and was granted, more time for its privilege review.

Prior to the deadline for production, I-Med sought to further tailor the ESI search parameters, asking for an agreement that it need provide only the deleted files of a single custodian. Biomatrix objected, stating that the parties had negotiated the process and parameters for the ESI search, and that the resulting search had confirmed that substantial deletions were made system-wide. After a telephone conference, the magistrate judge entered an order permitting I-Med to withhold data found in the unallocated space, thereby avoiding the expense of a costly privilege review, but also allowing Biomatrix to seek reimbursement for the costs incurred by its expert in extracting and searching for the data. The order was based, in part, on findings that the burden of the privilege review by I-Med would outweigh any potential benefit and that the likelihood of finding relevant, admissible evidence was "minimal."

Biomatrix appealed the magistrate judge's decision. On appeal, the district court upheld the order, determining that the benefit of the review of material from the unallocated space was unlikely to justify the burden and expense that would be required to complete it. In addition to the expenditure of resources that would be required of I-Med to accomplish the review, the court considered the expenditure of resources by Biomatrix in obtaining the data, but the court determined that it "pale[d] in comparison to the millions of dollars" that would be spent by I-Med to review the material adequately. *Id.* at *16. As the court noted, "[a] privilege review of 65 million documents is no small undertaking," adding that, "[e]ven if junior attorneys are engaged, heavily discounted rates are negotiated, and all parties work diligently and efficiently, even a cursory review of that many documents will consume large amounts of attorney time and cost millions of dollars." *Id.* at *15.

Critically, the court noted that I-Med "should have exercised more diligence before stipulating to such broad search terms." *Id.* at *17. The court went on to state:

> In evaluating whether a set of search terms are reasonable, a party should consider a variety of factors, including: (1) the scope of documents searched and whether the search is restricted to specific computers, file systems, or document custodians; (2) any date restrictions imposed on the search; (3) whether the search terms contain proper names, uncommon abbreviations, or other terms unlikely to occur in irrelevant documents; (4) whether operators such as "and", "not", or "near" are used to restrict the universe of possible results; (5) whether the number of results obtained could be practically reviewed given the economics of the case and the amount of money at issue.

Id.

The court also addressed Biomatrix's complaint that the magistrate judge had improperly modified the agreement between the parties relating to the ESI search parameters. In this regard, the court counseled that "[w]hile courts should not casually discard agreements between the parties, nor should they abrogate their duty to balance both burden and the likelihood of uncovering relevant evidence merely because a party made an improvident agreement." *Id.* at *14.

Perhaps the most telling line of the district court's opinion is the following: "While [I-Med] should have known better than to agree to the search terms used here, the interests of justice and basic fairness are little served by forcing [I-Med] to undertake an enormously expensive privilege review of material that is unlikely to contain non-duplicative evidence." *Id.* at *17–18. In *Biomatrix*, I-Med, the plaintiff, was thus fortunate that the court did not force it to review an estimated 95 million pages of records found in unallocated space, notwithstanding I-Med's initial agreement to broad search terms and unlimited parameters. Indeed, the court realized that the search terms originally agreed upon were *too* broad, making the costs associated with performing a full privilege review burdensome. Further, the likelihood of any of the data being responsive was especially low because searches of data from the unallocated space of I-Med's computer systems would cause the projected costs to be disproportionate to any potential gain.

Tailoring Reasonable ESI Search Parameters

Biomatrix reminds us why it is critical to negotiate effective search parameters. Continued failure to adhere to basic concepts, like attention to detail, undeniably leads to escalated litigation costs when addressing issues related to ESI. So, what can you do to avoid the type of situation in which the plaintiff found itself in *Biomatrix*?

First, pay attention. Do not enter into ESI stipulations haphazardly or without some preliminary evaluation and preparation. Do not think you can go back later and try to tailor the search request more narrowly. There is something to be said for getting it right the first time. Take time at the outset of the case to interview key custodians and discuss potential search terms. Your client's information technology (IT) department will be an invaluable resource during the course of the litigation. Make the effort to learn about your client's IT department early on, and determine who may be able to provide assistance with regard to the anticipated ESI search and collection process. The IT department may be able to run a preliminary search of certain keywords to get an initial idea of the amount of data the search may retrieve.

Second, make sure your stipulation includes the basics. In *Biomatrix*, we learned that the ESI stipulation between the parties did not contain a limit on the most basic of search parameters like time frame and custodians. These two factors alone can make all the difference between a 95-million-page result and a 950-page result. Search parameters should not just detail keywords. They should include a date range, identify key custodians, identify file types, and identify the systems to be searched. When negotiating which systems will be searched, it is best to get input from your client regarding active files and unallocated space.

Third, carefully consider whether there is a need to search unallocated space—the space on a custodian's drive that is not used for storing active files. It may contain only segments of files that were previously deleted from the drive. More times than not, the data collected from unallocated space are not useful, and the cost to search it far exceeds the potential benefit. If intentional deletion of ESI is not an issue in the case, there is no compelling reason to review data in the unallocated space of a custodian's drive. Of course, there may be occasions when the information in unallocated space may be critical to your case. The key is to make your inquiries with your client *before* negotiating the ESI search parameters.

Finally, consider testing the search terms. If you are struggling with keyword selection, it may benefit your client to expend the resources to test those search terms. Enlist your client's IT department to assist you with this process. The key here is to strike a balance between responsive documents and extraneous and irrelevant files. In addition, if you do receive a particularly large set of ESI documents from your keyword search, it may be beneficial to perform a sampling. By sampling, you can create a sample set from your search result to determine whether you are retrieving false hits or relevant data.

The Concepts of Cooperation and Proportionality
Remember the concepts of cooperation and proportionality. Both the courts and counsel have an equal responsibility to remain proactive in their efforts to curb electronic discovery abuses and the exploding costs of litigation associated with abusive discovery practices, like overbroad requests for ESI and document dumps.

The guiding principles of proportionality are referenced in both Rule 26 of the Federal Rules of Civil Procedure and The Sedona Conference. The Rule 26 proportionality test allows the court to "limit discovery if it determines that the burden of the discovery outweighs its benefit." *In re IKB Deutsche Undustriebank AG*, 2010 WL 1526070, at *5 (N.D. Ill. 2010); *see also* Fed. R. Civ. P. 26(b)(2)(C)(iii).

The Sedona Conference explains the importance of the Rule 26 proportionality test:

> The metrics test set forth in Rule 26(b)(2)(C)(iii) provides courts significant flexibility and discretion to assess the circumstances of the case and limit discovery accordingly to ensure that the scope and duration of discovery is reasonably proportional to the value of the requested information, the needs of the case, and the parties' resources.

The Sedona Conference, "The Sedona Conference Commentary on Proportionality in Electronic Discovery," 11 *Sedona Conf. J.* 289, 294 (2010) (footnote omitted).

"If courts and litigants approach discovery with the mindset of proportionality, there is the potential for real savings in both dollars and time to resolution." John L. Carroll, "Proportionality in Discovery: A Cautionary Tale," 32 *Campbell L. Rev.* 455, 460 (2010).

Conclusion
Well-crafted ESI search parameters, including a focus on keywords, are critical to promote speedy resolution of cases as well as to reduce litigation costs and avoid protracted litigation and

unnecessary expense. Cooperation and communication are equally critical to expeditious and cost-effective electronic discovery in litigation.

Keywords: litigation, commercial, business, electronic discovery, electronically stored information, search parameters

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Privilege-Waiver Issues in Bankruptcy after MF Global

By Meryl B. Vinocur and Catherine G. Pappas – April 30, 2012

In late October 2011, it was discovered that MF Global, Inc., a major commodities broker-dealer, had transferred $700 million from customer accounts to the broker-dealer and made a loan of $175 million in customer funds to its U.K. subsidiary to cover massive liquidity shortfalls. Customer accounts were frozen, and the parent company, MF Global Holdings, Ltd., with certain of its subsidiaries, including the broker-dealer, filed for bankruptcy on October 31, 2011. These events have led to a teaching moment concerning waiver of the corporate attorney-client privilege by the debtor's trustee and the effect of waiver on the debtor's officers and directors and those of the debtor's subsidiaries.

Countless questions have been raised regarding the mismanagement of client funds at MF Global, and investigations have been launched by, among others, the Commodity Futures Trading Commission, the Securities and Exchange Commission, and James Giddens, the trustee appointed by the Securities Investor Protection Corporation (SIPC) to liquidate MF Global under the Securities Investor Protection Act (SIPA). As part of the investigations, these entities have requested from parent MF Global Holdings, now a debtor in bankruptcy, communications relating to customer accounts and other business operations. Louis Freeh, former Federal Bureau of Investigation director and the Chapter 11 trustee appointed to manage MF Global Holdings' assets in bankruptcy, initially denied these requests, claiming that such communications were protected by the attorney-client privilege. Freeh's refusal to provide such communications was not well received by the various constituencies clamoring to marshal MF Global's assets in the wake of its rapid collapse. Yet, Freeh was within his rights to do so, even if it conflicted with the interests of the SIPC trustee of the subsidiary broker-dealer.

Whereas management's fiduciary duty prior to a bankruptcy filing is to the corporation's shareholders, the duty after a bankruptcy filing runs to general creditors as well as equity holders. The trustee's role in bankruptcy, generally, is to administer the estate for the benefit of all creditors. By contrast, the role of a SIPC trustee in a SIPA liquidation generally consists of recovering funds for wronged customers of the brokerage firm. For that reason, the sometimes competing interests of the respective trustees can invite tension in delicate situations like MF Global, where communications are shielded and privilege is asserted by one trustee to the frustration of the other. Nonetheless, the privilege was Freeh's to assert (or waive) on behalf of MF Global Holdings, the debtor in bankruptcy.

The Impact of *Weintraub*

In *Commodity Futures Trading Commission v. Weintraub*, 471 U.S. 343, 358 (1985), the U.S. Supreme Court ruled that a debtor corporation's bankruptcy trustee controls the debtor's attorney-client privilege and thus can waive that privilege. In *Weintraub*, the Commodity Futures Trading Commission (CFTC) subpoenaed a bankrupt corporation's former counsel, seeking evidence of suspected misappropriation of funds by company insiders. Although the attorney asserted the corporation's attorney-client privilege, the CFTC was able to obtain a waiver of that privilege from the bankruptcy trustee, and the Supreme Court held that such a waiver was valid. Because corporate directors fail to retain any managerial power in a bankruptcy reorganization where a trustee has been installed, the Supreme Court held that management also should not retain control over the attorney-client privilege. Therefore, a trustee in bankruptcy may waive the attorney-client privilege of a corporate debtor for communications made prior to the declaration of bankruptcy. Communications between corporate officers and in-house or outside counsel, which would generally remain protected and confidential outside of bankruptcy, are likewise subject to waiver and disclosure by the trustee.

Notably, the *Weintraub* Court also rejected the idea that the interest against self-incrimination of former officers and directors trumps the trustee's capacity to waive the privilege, holding that the goal of uncovering insider fraud "would be substantially defeated if the debtor's directors were to retain the one management power that might effectively thwart an investigation into their own conduct." *Id.*, 471 U.S. at 353–54.

Bankruptcy courts across the United States, following the Supreme Court's ruling in *Weintraub*, have permitted trustees to waive the attorney-client privilege and disclose relevant communications that, at the time they were made, were protected. In the case of MF Global Holdings, Chapter 11 trustee Freeh followed suit and, on February 14, 2012, agreed to turn over thousands of emails and documents to the federal authorities and to the SIPC trustee, which will likely provide a far more detailed look at what went wrong in the days leading up to MF Global's collapse and bankruptcy filing. Significantly, the disclosure of these documents could lead investigators to those within MF Global who committed wrongdoing and consulted with MF Global's attorneys, despite their likely understanding at the time that such communications would be protected by privilege and would never be revealed to outside parties.

As the current economic crisis continually spawns civil and criminal investigations into failing companies, corporate officers must be mindful that the waiver of privilege may ultimately be decided not by those in power at the time those communications were made, but by a trustee or receiver appointed at a later time. Attorneys representing individuals targeted in federal criminal investigations should be aware that, after bankruptcy or the initiation of a receivership proceeding, their clients' prior communications with company counsel (in-house or outside counsel), even communications involving the legal implications of the conduct at issue in the investigation, may be disclosed to government investigators.

The attorney-client privilege exists to facilitate free and open communication between the client and the attorney and is vital to our legal system. The privilege is designed to protect the vulnerable party from producing documents that are otherwise damaging to its case. Courts may refuse to apply the privilege in circumstances that perpetuate a criminal act, such as fraud. Lifting the privilege, however, can also expose the debtor to harm by chilling communication between attorney and client.

The Supreme Court was careful not to extend its holding in *Weintraub* to cases involving individual debtors, which has led to a split of authority on the question of whether a trustee can unilaterally waive the attorney-client privilege in an individual bankruptcy case. The absence of guidance from the Supreme Court on that point has led lower courts to three different outcomes on the privilege issue in the individual context. Some courts have held that the attorney-client privilege of an individual debtor passes to the bankruptcy trustee by operation of law. *In re Smith*, 24 B.R. 3, 5 (Bankr. S.D. Fla. 1982). Others have held that a trustee may not waive an individual debtor's attorney-client privilege. *In re Hunt*, 153 B.R. 445, 454 (Bankr. N.D. Tex. 1992). Finally, some courts have taken a functional approach that balances the equities and weighs the trustee's need for the information against the harm the disclosure would cause to the debtor. *In re Miller*, 247 B.R. 704, 710 (Bankr. N.D. Ohio 2000).

In MF Global Holdings' corporate bankruptcy, however, the privilege was squarely Freeh's to waive. In doing so, Freeh presumably had to consider not only the threat that the bankruptcy estate would be depleted by the claims of government authorities if certain wrongdoings were uncovered but also the possibility that exposure of wrongdoing may also reveal avoidance action claims that Freeh may later pursue to bring assets back into the bankruptcy estate. Freeh likely also sought sufficient time to review the communications with his own professionals on behalf of the bankruptcy estate before making those communications available to those with similar and possibly competing interests.

Important Considerations

Concerns of privilege are paramount in any bankruptcy case, particularly in those where a trustee is appointed. These concerns should be carefully considered prior to a company filing for bankruptcy protection. After *Weintraub*, and in light of the current financial crisis, it is important for attorneys to be aware of the possible implications for their clients. In cases where companies have already filed for bankruptcy, counsel representing individuals must be mindful that their clients' prior communications—both factual information disseminated to company counsel and company counsel's legal advice on the conduct under investigation—may be turned over to the government. For companies on the precipice of bankruptcy or receivership, counsel for individuals must be aware that current communications with corporate counsel may be subject to waiver upon the filing of the bankruptcy petition or receivership proceeding. Therefore, while counseling corporate clients prior to the bankruptcy or receivership filing, attorneys should remind their clients that any communications between individuals in management and corporate counsel may later be used against them in their personal capacity or, at a minimum, may be subject to review by third parties.

Recent news reports have indicated that criminal prosecution of MF Global's management may not be likely, based on preliminary reviews of communications and documentation provided by the debtor. Nevertheless, the issues of privilege and waiver that have figured so prominently in the case are important to remember for effective representation of corporate clients and corporate debtors in similar situations.

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NEWS & DEVELOPMENTS

Possibility of Theft Is Not Enough for Injury

In *Katz v. Pershing, LLC*, No. 11-1983 (1st Cir. Feb. 28, 2012), the First Circuit explored the limits imposed by Article III standing requirements on a private claim that alleges a failure to protect sensitive, nonpublic, personal information in the absence of an actual data-security breach.

Katz's allegation that Pershing's conduct increased the "risk that someone might access her data and that this unauthorized access (if it occurs) will increase the risk of identity theft and other inauspicious consequences" was, for the First Circuit, too remote to meet Article III's requirement of actual or impending injury in fact. The court also rejected Katz's argument that she had suffered injury in fact when she purchased identity theft insurance and a credit-monitoring service in response to the inadequacies of Pershing's data security. The possibility that her nonpublic personal information "might someday be pilfered" was "remote at best," the court decided, and it "simply did not rise to the level of a reasonably impending threat." Without the threat of "actual or imminent, not speculative" injury, there was no injury for purposes of Article III standing.

Keywords: litigation, commercial, business, First Circuit, identity theft

—Paula Bagger, Cooke Clancy & Gruenthal LLP, Boston, Massachusetts

Discovery for Use in Foreign Litigations Gets a Boost

In *Brandi-Dohrn v. IKB Deutsche Industriebank AG*, No. 11-4851 (2d Cir. Mar. 6, 2012), the U.S. Court of Appeals for the Second Circuit held that a litigant in a foreign lawsuit can obtain discovery in the United States without having to show that the discovery would be admissible in the foreign action. With this ruling, the Second Circuit joins other circuits that have previously addressed the issue. This case also highlights that discovery in the United States can be a powerful tool that may be used in disputes in other countries.

Keywords: litigation, commercial, business, Second Circuit, Germany, discovery

—Stuart M. Riback, partner, Wilk Auslander LLP, New York, New York

Contra Proferentem Doesn't Apply if Drafter Is Unknown

In *Shaw Hofstra & Associates v. Ladco Development, Inc.*,No. 11-2368 (8th Cir. Mar. 12, 2012), the Eighth Circuit affirmed the district court's refusal to give a *contra proferentem* instruction to the jury in a breach-of-contract case where there was insufficient evidence in the record as to which party drafted the contract language at issue.

Keywords: litigation, commercial, business, Eighth Circuit, *contra proferentem*, contracts

—Stephen R. Clark and Kristin E. Weinberg, Clark Law Firm, LLC

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