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**A PRIMER ON ATTORNEY-CLIENT PRIVILEGE AND TIPS FOR PROTECTING AN INSURER'S CRITICAL SELF-ANALYSIS,**

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*Introduction*

"Critical self-analysis," "internal compliance audit," "self-evaluation" — all are phrases now commonly used by insurers. Spurred over the last several years by a desire to assure compliance with state and federal laws, as a hedge against class action litigants, and to meet standards set by the Federal Sentencing Guidelines, many insurers have established or are planning to establish compliance departments that assist the company in completing self-critical analyses of the company's operations. One of the major issues that arise in a self-critical analysis is the discoverability of the analysis report itself and of documents relating to the analysis. Is the company merely providing a road map for plaintiffs' class action suits, for example? What can the insurer do to strengthen its claim that such documents are confidential and not discoverable?

Some courts have recognized a critical self-analysis privilege.<sup>1</sup> However, the critical self-analysis privilege is relatively new, few courts have considered it, and even fewer have adopted it.<sup>2</sup> Insurers therefore cannot rely on the availability of this privilege to protect their compliance audit documents from disclosure to third parties. And, while legislation creating a critical self-analysis privilege for insurers' compliance audit documents is being considered in several states, to date such legislation has been adopted only in Illinois. For the time being, at least, insurers must rely on the attorney-client privilege or the attorney work product doctrine to protect their compliance audit documents. This article is a primer on the attorney-client privilege and provides tips on preserving the confidentiality of an insurer's critical self-analysis documents through that privilege.

*Primer on Attorney-Client Privilege*

The attorney-client privilege originated in common law and is the oldest of the privileges that protect confidential communications. Its purpose "is to encourage full and frank communication between attorneys and their clients."<sup>3</sup> The privilege is intended to encourage clients' communication with their lawyers, recognizing that full disclosure will further observance of the law and the administration of justice. The Federal Rules of Evidence and the rules of evidence in each state codify the privilege.<sup>4</sup>

**Establishing the existence of the privilege.** Five elements are necessary to establish the existence of the attorney-client privilege:

the attorney-client privilege:

1. The person or entity asserting the privilege is or seeks to become a client.
2. The person to whom the communication was made is an attorney acting in his or her capacity as attorney for the client at the time of the communication.
3. The communication is made by the client.
4. The communication is made in confidence.
5. The communication is made to obtain legal advice or assistance.<sup>5</sup>

The attorney-client privilege is available to companies in the same way that it is available to individuals.<sup>6</sup> The party asserting a claim of attorney-client privilege bears the burden of proof in establishing that the privilege exists.<sup>7</sup>

**Communications entitled to the privilege.** The attorney-client privilege belongs to the client. Although the company is the client and the privilege attaches to the company,<sup>8</sup> a company can communicate only through its directors, officers, employees and shareholders, and it is these communications that may be protected by the privilege. It is important to note, however, that not all communications made by a director, officer, employee or shareholder fall within the privilege. Courts currently use two tests to determine whose communications may be protected by the privilege: the subject matter test and the control group test.

Under the subject matter test currently applied by the U.S. Supreme Court, only communications made to counsel by management and by employees at the direction of management on matters within the scope of the employees' duties for the company are privileged.<sup>9</sup> To fall within the subject matter test, the employee must make the communication at the direction of a superior in order to obtain legal advice for the company, the subject matter of the communication must be within the scope of the employee's employment duties, and the communication must be limited to those persons who need to know.<sup>10</sup> The persons giving the information should be told that the purpose is to assist the company in obtaining legal advice and that the information is confidential.

Although the subject matter test is currently used by federal courts, state courts may use either the control group test or the subject matter test. Under the control group test, only those persons in the company who are in control or who will take a substantial role in determining the company's course of action based on the legal advice sought are protected by the privilege.<sup>11</sup> The control group is usually top management and those mid-level managers who make the decisions based on the legal advice given to the company.

Communications to an in-house lawyer will only be shielded under the attorney-client privilege if they are given to the lawyer so that the lawyer can provide legal advice to the company.<sup>12</sup> Communication between corporate departments or corporate officers may not be protected, even if discussing the need or decision to seek legal advice.<sup>13</sup> Remember that the attorney-client privilege attaches only when the lawyer is acting in the capacity of a legal advisor. Communications made so that the lawyer can give

lawyer is acting in the capacity of a legal advisor. Communications made so that the lawyer can give business or technical advice do not fall within the privilege.<sup>14</sup> Although the attorney-client privilege applies equally to in-house counsel as to outside counsel, merely using in-house counsel as a conduit through which corporate documents are run is not sufficient for the privilege to attach.<sup>15</sup>

The law of attorney-client privilege distinguishes between communication and fact. While communication may be protected by the attorney-client privilege, underlying facts that are the subject of the communication may not be protected.<sup>16</sup> However, courts have recognized that communications from lawyers rendering legal advice often must contain references to non-legal matters and such references generally will not destroy the privilege.<sup>17</sup>

The privilege protects the client's communication to the lawyer. The lawyer's communication to the client containing privileged information that the client has communicated to the lawyer also is privileged. However, not all courts have found that the lawyer's communication to the client giving legal advice is protected under the attorney-client privilege.<sup>18</sup>

Communications between co-counsel are protected even though they are not communications with the client because they contain information that would be privileged if made to the client. Therefore, communications between in-house and outside counsel are privileged.<sup>19</sup> Communications between attorneys also are protected if the clients of those attorneys enjoy a "community of interest," for example, potential or actual joint defendants.<sup>20</sup>

Moreover, to be privileged, communications must be made in confidence, the client must intend that the communications remain confidential, and the expectation of confidence must be reasonable.<sup>21</sup> Disclosure must be to as few internal persons as possible and to no outsiders except outside counsel, co-counsel, or counsel whose client shares a community of interest.

**Waiver of Privilege.** The attorney-client privilege can be waived if any part of the communication is disclosed to a third party, if the company produces privileged documents, or if the company through deposition testimony discloses privileged communications.

Courts are split on whether the privilege is lost if confidential documents are turned over to the government on a confidential basis or in answer to a subpoena; however, the privilege is lost if the company voluntarily releases the documents to the government.<sup>22</sup> At least some courts recognize a limited waiver if the documents are turned over to a government agency under a protective order, stipulation or other express reservation of the attorney-client privilege.<sup>23</sup> Courts appear to be in agreement, however, that companies waive the privilege when they reveal documents to outside investment bankers and auditors.<sup>24</sup>

Once the company voluntarily waives the privilege, it generally cannot thereafter be asserted for any documents relating to the same matter.<sup>25</sup> Additionally, waiver by the company may also waive the privilege as to any employee communications.<sup>26</sup>

**Exception to Privilege.** Communications relating to legal advice requested or given for the purpose of committing, covering up or furthering a crime or fraud are not protected.<sup>27</sup> However, a mere allegation or suspicion of a crime or fraud is not sufficient to defeat the privilege.<sup>28</sup> Rather, the party seeking discovery must show a factual basis "adequate to support a good faith belief by a reasonable person" that the materials for which disclosure is sought may reveal evidence to establish the claim of crime or

that the materials for which disclosure is sought may reveal evidence to establish the claim of crime or fraud. The court may then hold an in camera review of the communication to determine whether it supports the claim.<sup>29</sup> In addition, the party seeking discovery must show that the communications were intended to facilitate or conceal the crime or fraud.<sup>30</sup> The crime-fraud exception does not apply to communications on past or completed crimes or fraud.<sup>31</sup>

### *Preserving the Attorney-Client Privilege*

While the attorney-client privilege cannot be guaranteed, a company can take actions that will increase the likelihood of attaining the privilege:

1. The company should establish and document the purpose and scope of the critical self-analysis project. If the directive comes from the board of directors, it should be memorialized in the minutes. If the directive comes from top management, it should be documented in a memorandum to the file.
2. The company's top management should issue a written directive to counsel to undertake the analysis for the purpose of providing legal advice to management.
3. In-house and outside attorneys should be an integral part of the project from the beginning. Prior to beginning the project, counsel should establish a protocol for gathering the information needed for the analysis and for providing the legal analysis that will maximize the likelihood that confidential communications will remain protected from discovery.
4. If the company expects to hire outside consultants, other than an outside lawyer, it should consider doing so through counsel to increase the likelihood that communications with the consultants will be subject to either the attorney-client or attorney work product privileges. If the company retains outside counsel, he or she should retain the consultants. Consultants and experts must clearly be working under the guidance of counsel.
5. Counsel should assume the primary responsibility for file maintenance and documentation of privileged communications, since counsel is likely to have the greatest knowledge of the application of the attorney-client privilege.
6. Because both the control group and subject matter tests are used depending on jurisdiction and the facts of the case, the company should attempt to meet both tests if possible. The company representative chosen to communicate with counsel should be top management or someone who clearly has the responsibility for making corporate decisions. In addition, only employees who have knowledge because of their duties in the company should be contacted for background or factual information.

company should be contacted for background or factual information.

7. The company's top management should issue a written directive advising company employees that they will be expected to cooperate with in-house and outside counsel so that the company can receive legal advice. Company employees should communicate directly with counsel to minimize the risk of an inadvertent waiver.

8. Conferences and meetings on legal matters should involve only the minimum number of participants necessary. If possible, the company should limit such meetings to top management and other control personnel involved in the matter and those employees who have necessary factual knowledge because of their employment duties. The company should keep written reports or minutes of meetings identifying the participants, describing the legal issue discussed, and stating the company's intent to keep the discussion confidential.

9. To maintain confidentiality, communications with counsel should be disclosed only on a "need to know" basis and to as few persons as possible. Counsel should make as few copies as possible of privileged information. Counsel should address his or her legal advice to a specific person or persons and not to a department. Counsel should obtain information from corporate employees as directly as possible.

10. All corporate employees who have fact-gathering or other roles in the internal audit should be cautioned to coordinate all activities with counsel and not to communicate with anyone else, especially attorneys representing adverse parties, without prior clearance from the insurer's in-house or outside counsel.<sup>32</sup>

11. Written communications should be identified as either being directed to or coming from counsel. Legal titles on such correspondence should be used to help identify the person as legal counsel.

12. All communications should clearly state that they are for the purpose of obtaining legal and not business advice, since business advice is not covered by the privilege. Legal opinion language should be used wherever possible. The communications should state the request for legal advice, the facts and questions submitted to the attorney, and the attorney's analysis and legal conclusions. Legal and business advice should not be given in the same document.

13. Counsel or experts acting on behalf of counsel should review all relevant corporate materials. Clearly mark documents "confidential - attorney-client privileged." While a "confidential" label in and of itself will not assure that the document is covered by the attorney-client privilege, labeling it confidential will help establish a confidential intent, and it will alert those who receive the document that it should be kept in

and it will alert those who receive the document that it should be kept in the strictest confidence. However, companies should not mark documents indiscriminately, since indiscriminate or inappropriate use of the label can harm a privilege claim.

14. To be on the safe side, mark all documents that you wish to keep privileged as "attorney work product" as well as "attorney-client privileged information." In application, the attorney-client privilege and the attorney work product doctrine often overlap and it often is not clear which protection applies. Again, do not mark documents indiscriminately.

15. Since there is no guarantee, despite precautions taken to preserve confidentiality, that documents will be protected from discovery, consider avoiding the creation of inculpatory documents unless necessary to perform the analysis effectively.

16. When interviewing company employees, counsel should tell them that counsel represents the company and not the employees. Employees do not have a claim of attorney-client privilege with respect to communications between the employee and counsel; that claim belongs to the company.

17. If the company's board of directors will discuss or act on the analysis, counsel should attend the board meeting and the agenda should indicate that counsel will be present to render legal advice. Minutes should be drafted in a manner that will avoid waiving the privilege.

18. The company should establish a formal policy on who has the authority to waive the attorney-client privilege. Generally, only top management should have such authority. The policy should include procedures for identifying and segregating privileged materials.

19. The company should not announce publicly that it is undertaking a compliance audit or investigation. A public announcement may intimate that a report will be published in the future and risk jeopardizing the attorney-client privilege.

20. Disclosure to government agencies should be resisted if at all possible. If the company makes voluntary disclosure, it should be under a grant of confidentiality by the government agency. All documents submitted should be identified on their face as confidential. In addition, the company should inform the agency through a cover letter that the documents are confidential and are not to be given to third parties. Failure to seek a protective order from the agency prior to producing the documents may waive the right thereafter to assert the privilege.

## *Conclusion*

Insurers considering critical self-analyses should understand that the attorney-client privilege is unlikely to be adequate to protect all information collected in the analysis from discovery. However, if the critical self-analysis is planned with the privilege in mind, the attorney-client privilege can be used to limit discovery substantially. Insurers should not undertake a critical self-analysis without studying the application of the attorney-client privilege and establishing procedures for the analysis to obtain optimum protection.

### *Endnotes*

1. *See, e.g., Wesley Medical Center v. Clark*, 669 P.2d 209 (Kan. 1983) (privilege for hospital peer review committee records); *Coburn v. Seda*, 677 P.2d 173 (Wash. 1984) (privilege for records of hospital quality review committee).

2. For courts denying the privilege *see, e.g., CPC International, Inc. and Brodson Properties, Inc. v. Hartford Accident and Indemnity Co.*, 620 A.2d 462 (N.J. Ct. App. 1992); *State ex rel. Celebrezze v. CECOS Int'l, Inc.*, 583 N.E.2d 1118 (Ohio App.1990); *Scroggins v. Uniden Corp. of America*, 506 N.E.2d 83 (Ind. Ct. App. 1987).

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

4. *See, e.g., Fed. R. Evid. 501*, which reads in part:

[T]he privilege of a witness . . . shall be governed by the principals of the common law as they may be interpreted by the courts of the United States in light of reason and experience.

As an example of a state provision, *see sec. 905.03, Wis. Stats.*, which reads in part:

GENERAL RULE OF PRIVILEGE. A client has a privilege to refuse to disclose and to prevent any other person from disclosing confidential communications made for the purpose of facilitating the rendition of professional legal services to the client; between the client or the client's representative and the client's lawyer or the lawyer's representative; or between the client's lawyer and the lawyer's representative; or by the client or the client's lawyer to a lawyer representing another in a matter of common interest; or between representatives of the client or between the client and a representative of the client; or between lawyers representing the client.

5. *See United States v. United Shoe Mach. Corp.*, 89 F. Supp. 357, 358 (D. Mass. 1950).

6. *Radiant Burners, Inc. v. American Gas Ass'n.*, 320 F.2d 314 (7th Cir.), *cert. denied*, 375 U.S. 929 (1963).

7. See, e.g., *Motley v. Marathon Oil Co.*, 71 F.3d 1547, 1550 (10th Cir. 1995).

8. See Model Rules of Professional Conduct Rule 1.13.

9. *Upjohn*, 449 U.S. at 394-95. In *Upjohn*, both in-house and outside counsel were directed by the company to do an internal investigation of payments that were made to foreign governments to secure business. Interviews were conducted and the lawyers sent questionnaires to company personnel. The Internal Revenue Service sought access to the interviews and questionnaires, and the company refused claiming attorney-client privilege and work product doctrine. Lower courts applied the control group test, holding that the employees who were interviewed or received questionnaires were too low in the corporate hierarchy to be protected by the privilege. The U.S. Supreme Court rejected the control group test in favor of the subject matter test. However, the control group test is still used in some states.

10. See, e.g., *Harper & Row Publishers v. Decker*, 423 F.2d 487, 491 (7th Cir. 1970), *aff'd*, *Decker v. Harper & Row Publishers, Inc.*, 400 U.S. 348 (1971).

11. See, e.g., *Philadelphia v. Westinghouse Electric Corp.*, 210 F. Supp. 483 (E.D. Pa. 1962).

12. See, e.g., *Teltron Inc. v. Alexander*, 132 F.R.D. 394 (E.D. Pa. 1990).

13. See, e.g., *Duttle v. Bandler & Kass*, 127 F.R.D. 46 (S.D.N.Y. 1989).

14. See, e.g., *United States v. Davis*, 636 F.2d 1028, 1039-40 (5th Cir.), *cert. denied*, 454 U.S. 862 (1981).

15. *United States v. Davis*, 131 F.R.D. 391 (S.D.N.Y. 1990).

16. See, e.g., *Upjohn v. U.S.*, 449 U.S. at 395.

17. See, e.g., *Spectrum Systems International Corp. v. Chemical Bank*, 581 N.E.2d 1055 (N.Y. 1991).

18. See, e.g., *Burlington Industries v. Exxon Corp.*, 65 F.R.D. 26, 37 (D. Md. 1974); *but see*, e.g., *United States v. International Business Machines Corp.*, 66 F.R.D. 206, 211-12 (S.D.N.Y. 1974). However, it is possible that the lawyer's communication to the client giving legal advice will be privileged under the attorney work product doctrine if it is prepared in anticipation of litigation.

19. See, e.g., *Natta v. Zletz*, 418 F.2d 633, 637 n.3 (7th Cir. 1969).

20. See, e.g., *Duplan Corp. v. Deering Milliken, Inc.*, 397 F. Supp. 1146, 1172 (D.S.C. 1974).

21. See, e.g. *Wylie v. Marley Co.*, 891 F.2d 1463, 1551 (10th Cir. 1989).
22. See, e.g., *Permian Corp. v. United States*, 665 F.2d 1214 (D.C. Cir. 1981).
23. See, e.g., *Teachers Insurance & Annuity Association v. Shamrock Broadcasting Co.*, 521 F. Supp. 638 (S.D.N.Y. 1981).
24. See, e.g., *Eastman Kodak Co. v. International Harvester Co.*, 14 Fed. R. Serv. 2d 1272, 1273 (S.D.N.Y. 1970) (prohibition against disclosure includes a company's financial auditors and investment bankers); *United States v. Arthur Young & Co.*, 465 U.S. 805 (1984) (prohibition against disclosure includes company's financial auditors).
25. See, e.g., *In re Bevill, Bresler & Schulman Asset Management Corp.*, 805 F.2d 120 (3d Cir. 1986).
26. See, e.g., *In re Grand Jury Investigation No. 83-30557*, 575 F. Supp. 777 (N.D. Ga. 1983).
27. See, e.g., *In re International Sys. & Controls Corp. Sec. Litig.*, 693 F.2d 1235, 1242 (5th Cir. 1982).
28. See, e.g., *Burlington Industries v. Exxon Corp.*, 65 F.R.D. 26, 40-41 (D. Md. 1974).
29. *United States v. Zolin*, 491 U.S. 554 (1989).
30. See, e.g., *Pritchard-Keang Nam Corp. v. Jaworski*, 751 F.2d. 277 (8th Cir. 1984), cert. denied, 472 U.S. 1022 (1985).
31. See, e.g., *In re Sealed Case*, 754 F.2d 395 (D.C. Cir. 1985).
32. At least one court permitted opposing counsel to have ex parte communications with employees for the purpose of obtaining factual information holding that corporate employees are not parties to a lawsuit against the employer company. *Niesig v. Team I*, 558 N.E. 2d 1030 (N.Y. 1990), aff'd as modified, 545 N.Y.S.2d 153 (App. Div. 2d Dep't 1989). But see *Public Service Electric and Gas Co. v. Associated Electric and Gas Insurance Services, Ltd.* 745 F. Supp. 1037 (D. N.J. 1990).

This article is necessarily a brief treatment of a very complex subject. Companies are urged to consult their counsel prior to beginning a critical self-analysis. For a bibliography of sources consulted for this article, please contact the writer.

