PRESERVING PRIVILEGE: THE CAREFUL AND LIMITED PUBLIC USE AND DISCLOSURE OF THE RESULTS OF AN INTERNAL INVESTIGATION

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In this extraordinary business environment, more and more companies are encountering situations in which they should, or must, conduct internal investigations into allegations or suspicions of wrongdoing by their employees or executives. As reported in a recent *Wall Street Journal* article, it seems that "[p]lenty of companies have gotten into plenty of trouble lately."[1] Indeed, the financial press has reported recently of numerous instances of alleged corporate wrongdoing and significant, ongoing internal investigations at public companies.[2]

Many of these internal investigations involve mismanagement at the highest levels of companies and on a massive scale. Others involve malfeasance by mid-level managers or lower-level employees. Some misconduct is isolated while other wrongdoing is significantly more severe or widespread. Wherever it occurs and whatever the circumstances, an internal investigation is an increasingly common, and often crucially necessary, means by which companies seek to ferret out

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[1] Joann S. Lublin, "As Their Companies Crumbled, Some CEOs Got Big-Money Payouts," *The Wall Street Journal*, February 26, 2002 (discussing allegations of wrongdoing by executives at Global Crossing, Kmart, Enron, Lucent Technologies and WorldCom) (available on WESTLAW at 2002 WL-WSJ 3387044).

[2] *E.g.*, Scot J. Paltrow et al., "Peregrine Audit Raises Questions About KPMG's Internal Controls," *The Wall Street Journal*, May 31, 2002; Chip Cummins, "Seitel Cites Possible Misuse of Funds," *The Wall Street Journal*, June 26, 2002; Simon Romero et al., "WorldCom Says It Hid Expenses, Inflating Cash Flow," *New York Times*, June 26, 2002, at A1; *see also* John R. Wilke et al., "Two Key Figures in Enron Debacle Offer Cooperation for Immunity," *The Wall Street Journal*, February 27, 2002; Dow Jones Newswires, "Service Corp. International Comments on Recent Litigation," February 28, 2002 (available online at wsj.com); Connie Ling, "Asia Global Crossing Is Now Seen As 'Distressed Asset,' Banker Says," *The Wall Street Journal*, March 1, 2002; Dow Jones Newswires, "Bank Probe Not Expected to Pinpoint Trader's Help," March 12, 2002 (available online at wsj.com); Dow Jones Newswires, "Homestore Completes Internal Inquiry," March 12, 2002 (available online at wsj.com).

wrongdoing and, at the same time, protect their investors, the corporate welfare and their public images.

In many ways, then, internal investigations are more high-profile than ever and have taken on a recognized importance by companies and government regulators alike. Notably, in one on-going case, government regulators reportedly sought to delay or curtail a company's internal probe in deference to the government's own investigation.[3]

Especially in this atmosphere of continued revelations of corporate fraud, the preliminary and ultimate findings of the investigation raise significant issues for a company about the appropriate measures to take when wrongdoing is discovered. Such steps may include terminating or disciplining responsible employees or managers, implementing new compliance measures to avoid or detect similar problems in the future, and notifying appropriate regulators. These steps require sophisticated and complex considerations by a company's senior management and its counsel.

Frequently, there also exists the need for the company to take proactive steps beyond finding out what happened and why, disciplining its personnel and taking corrective steps. From the company's viewpoint, "[t]he battles to avoid liability and to protect the brand must both be won."[4] With good reason, management may want to publicly release information about the findings of the investigation to calm investors' concerns, protect (or restore) the company's image, assure customers and employees, and demonstrate that it is serious about punishing those responsible. Or, it may want to voluntarily disclose the findings to the government to head off an investigation or convince regulators not to sanction the company or to limit the scope and severity of remedial or punitive

[3] *See* Deborah Solomon et al., "U.S. Wants WorldCom to Halt Probe," *The Wall Street Journal*, July 5, 2002; Simon Romero, "Inside Inquiry By WorldCom is Continuing," *New York Times*, July 6, 2002, at C2.
[4] Mark Herrman & Kim Kumiega, "On Trial in the Courts of Law and Public Opinion: The Tension Between Legal and Public Relations Advice," *Litigation*, Vol. 28, No. 4 at 29 (Summer 2002).

measures. Companies may even need to decide whether executives or employees should testify before grand juries and regulatory or legislative bodies, and the attendant risks and concerns that entails.[5]

The public use and disclosure to regulators of the results of an internal investigation raise important additional issues that companies and their counsel should consider, particularly because companies will be under intense scrutiny following the wave of corporate reforms and regulations enacted in the Sarbanes-Oxley Act of 2002 signed into law by President Bush on July 30, 2002. In this climate of corporate scandal, it is almost impossible for a significant public company or other regulated organization to keep private all findings of an internal investigation.

Two of a company's most important audiences at such times of crisis will often be the general public and regulators. However, the public release of the findings of the investigative report or the disclosure to regulators is risky because such uses potentially jeopardize the company's attorney-client and work product privileges. Private plaintiffs, interested prosecutors and government regulators will often be watching closely for a chink in the corporation's privilege armor to assert a claim of waiver and gain access to the underlying factual materials at the heart of the company's internal investigation.

A. Public Use of the Results of the Internal Investigation

Understandably, companies hope to protect the core results of their internal investigations (*e.g.*, notes and summaries of interviews with employees and memoranda identifying and analyzing critical documents and other evidence), while simultaneously making public use of the results to defend themselves.[6] There is thus an inherent tension between some degree of disclosure to the public about the investigation's findings and protecting against an unwanted disclosure due to waiver.

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[5] *See* Susan Pulliam et al., "WorldCom Is Denounced at Hearing," *The Wall Street Journal*, July 9, 2002 at A3 (describing possible waiver of Fifth Amendment privilege by former WorldCom CEO Bernard Ebbers); Judith Burns, "House Asks Whether Former WorldCom CEO Waived Protection," *The Wall Street Journal*, July 8, 2002; Colleen DeBaise et al., "Workers Invoking Fifth May Clash With Employers," *The Wall Street Journal*, August 7, 2002 (discussing how company policies requiring cooperation with regulatory inquiries conflict with employees' right to plead the Fifth Amendment).

[6] Lawrence Byrne, "When the Bell Tolls," *Corporate Counsel*, August 26, 2002 (noting that "[t]he business must speak publicly with one voice, and in a manner that is approved by counsel.").

Recently, the Court of Appeals for the Second Circuit observed that "where a corporation has disseminated information to the public that reveals parts of privileged communications or relies on part of privileged reports, courts have found the privilege waived." *In re Grand Jury Proceedings*, 219 F.3d 175, 184 (2d Cir. 2000) (discussing waiver of the attorney-client privilege). Clearly, any public statements create a risk that a court will find waiver. A line of cases in this area is instructive in how to lessen that risk. As the cases suggest, there are ways for companies to report publicly on the results of an internal investigation without necessarily causing a waiver of the attorney-client or work product privileges.

One case where no waiver was found is *In re Dayco Corp. Derivative Securities Litigation*, 99 F.R.D. 616 (S.D. Oh. 1983). In that case, a law firm was hired by a Special Review Committee of Dayco's Board of Directors to investigate allegations of fraud by the company, its Board and employees. The company later issued a two-page press release that summarized the "findings and conclusions" of the investigation and its report, but did not contain either the underlying facts or counsel's report. The plaintiffs in securities litigation sought production of the report (and related documents) prepared by the law firm during its investigation. *Id.* at 619. The court held that the company did not waive any privilege or immunity[7] by issuing the press release because it did not release the substance or any "significant part" of the report of the internal investigation, nor did it summarize evidence found in the report or combine the findings of counsel with those of the Board of Directors. Instead, the company merely released the findings of counsel's report. *Id.* The court reasoned that there was nothing unfair about allowing the company to claim privilege in the litigation. *Id.*

[7] The decision mentions both the attorney client privilege and work production protection, but it did not distinguish between the two for purposes of its waiver analysis.

Similarly, in *In re Woolworth Corp. Securities Class Action Litigation*, 1996 WL 306576 (S.D.N.Y., June 7, 1996), the careful use of the results of an internal investigation also led a court to reject claims of waiver on separate policy grounds. There, Woolworth's Treasurer made allegations about intentional accounting irregularities at the company and securities litigation ensued. A committee of Woolworth's Board hired a law firm to investigate. The firm publicly issued a lengthy report of the findings of its investigation, which plaintiffs used as a "roadmap" in their pleadings. *Id.* at *1.

Plaintiffs then moved to compel the law firm to produce its internal notes and memoranda created in the investigation. The court found as a threshold matter that the law firm's materials were covered by the attorney-client privilege because the firm was retained to provide legal advice, as well as perhaps some business advice. *Id.* at *1-2. Noting that the privilege protects from disclosure only the communications between client and counsel and not the underlying facts, the court then held that Woolworth had not waived the attorney-client privilege by publishing a report on its internal investigation because plaintiffs had long had access to the facts in the report and had previously deposed many of the employees interviewed. Significantly, the court stated that public policy concerns weighed against a finding of waiver because "[a] finding that publication of an internal investigative report constitutes waiver might well discourage corporations from taking the responsible step of employing outside counsel to conduct an investigation when wrongdoing is suspected . . . . For shareholders to obtain the benefits of investigative reports of the type at issue here, these corporate decision makers must know that the integrity of communications made to independent counsel will be preserved." *Id.* at *2.

And, in a pre-cursor to the Second Circuit's decision in *U.S. v. Adlman*, 134 F.3d 1194 (2d Cir. 1998), the court held that the notes and memos were subject to work product protection as well. It

found that, under the circumstances, there was no meaningful distinction between documents prepared purely in anticipation of litigation and those prepared also for "business purposes," as plaintiffs had argued to claim that there was no work product protection. *Id.* at *3.

In contrast is *Granite Partners, L.P. v. Bear Stearns & Co. Inc.*, 184 F.R.D. 49 (S.D.N.Y. 1999), where the defendants sought production of notes of witness interviews, analyses and other key documents obtained and created by the plaintiffs' bankruptcy trustee and his counsel during an investigation into the collapse of three hedge funds run by plaintiffs. From the outset of the investigation, the trustee had the purpose of publishing a report, both to the Bankruptcy Court and the general public, on the causes of the collapse of the funds. *Id.* at 51. Once completed, the report itself was, in fact, widely distributed. *Id.* The report contained direct quotations from witness interviews, excerpts and descriptions of information from collected documents and conclusions of an expert's analysis. Also attached to the report was a selection of key documents collected by the trustee in his investigation. *Id.* at 51, 55. The court held that plaintiffs had waived the work product privilege as to the underlying notes and memos of the investigation. It stated that the "use of selected quotes from the Trustee's interview notes waives any privilege claimed on the unquoted portions of those notes." *Id.* at 55. By affirmatively using the very portions of the internal investigation as to which he later sought the court's protection, the Trustee had created a situation where the policy considerations made the court's waiver decision almost inescapable.[8]

Perhaps better known on the issue of public disclosure of a report of an internal investigation is *In re Kidder Peabody Securities Litigation*, 168 F.R.D. 459 (S.D.N.Y. 1996). After discovering huge

[8] *Granite Partners* was decided under the Second Circuit's holding in *U.S. v. Adlman*, 134 F.3d 1194 (2d Cir. 1998). In construing the "in anticipation of litigation" language of Rule 26(b)(3), in *Adlman*, the Second Circuit held that a document created "because of" anticipated litigation does not lose work production protection simply because it is intended to aid in making a business decision that is influenced by the probable outcome of anticipated litigation. 134 F.3d at 1195. The Court noted that "the fact that a document's purpose is business-related appears irrelevant to the question whether it should be protected under Rule 26(b)(3)." *Id.* at 1200. Thus, it does not have to be prepared primarily in anticipation of litigation

trading losses in government securities by trader Joseph Jett, Kidder Peabody hired a law firm to conduct an internal investigation and recommend steps for reform at the company. From the start, Kidder and its then parent company, General Electric, engaged in an extensive and concerted public relations campaign to minimize the perception of wrongdoing. *Id.* at 462-66. General Electric publicly released the investigative report, which summarized the firm's factual findings and suggestions for corrective action at Kidder. *Id.* at 464. The report contained factual summaries of documents used in interviews of employees, "explicit paraphrases from the interviews," and "a series of allusions to witnesses' statements." Civil lawsuits ensued, and plaintiffs sought production of the law firm's summaries and notes.

The court found that Kidder had waived the attorney-client privilege in two ways. First, Kidder's publication of the report required production of the interview documents that were specifically referred to in the report. The court rejected Kidder's argument that no waiver should be found because witnesses were not quoted in the report. It further noted that the report "offers a very specific paraphrase of statements made by witnesses in the course of arguably privileged communications . . . . Disclosure of the substance of a privileged communication is as effective a waiver as a direct quotation since it reveals the 'substance' of the statement." *Id.* at 469-70. Interestingly, the court did not find that Kidder's use of paraphrases caused a wholesale waiver of its attorney-client privilege, but the court did not tarry long on that question in light of its next finding. Second, the court ordered the release of the balance of the factual portions of the interview documents because of Kidder's "repeated injection of the substance of the report into this and other litigations and into related litigative contexts." *Id.* at 470. Here, as in *Granite Partners*, the court based its decision on fairness, noting that a party cannot "use the substance of the documents as a sword while at the

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to have work product protection; it can have a dual business and litigation purpose. The Second Circuit's holding is consistent with decisions from several other circuits. *Id.* at 1202.

same time invoking the privilege as a shield to prevent disclosure of the very materials that it has repeatedly invited the courts to rely upon." *Id.* at 472.[9]

In light of this precedent, is there a constructive way for a company to shield the heart of an internal investigation while still making public statements? While there are no roadmaps to a safe way to proceed and competing interests need to be balanced, corporate counsel can take certain steps to address their clients' competing business and legal interests.

First, at the outset, the company should consider what will be disclosed or released to the public and whether there is or likely will be a need to publicly report on the investigation. Counsel should consider memorializing its intention to preserve interview notes and memoranda, while contemplating publication or release of a summary report or statement that does not quote from or paraphrase those materials.

Second, in drafting a summary for public consumption, counsel should make statements based on publicly available or non-privileged information. Counsel must take great care in its use of interviews conducted under privilege pursuant to *Upjohn Co. v. United States*, 449 U.S. 383 (1981). Accordingly, counsel should maximize its use of facts that can be derived from non-privileged sources, including documents.

Third, companies should limit their use of reports or summaries of internal investigations. Limited company statements about the existence of an internal investigation, which are issued to reassure investors and the public, are common. But having released such a statement, if a company

[9] In *Kidder*, a pre-*Adlman* decision, the court also found no work product protection for the notes and factual summaries of interviews because pressing business concerns were the prime reason for Davis Polk's retention and work, not litigation. *Id.* at 462-67. *See also In re Leslie Fay Cos., Inc. Securities Litigation*, 161 F.R.D. 274 (S.D.N.Y. 1995) (where Leslie Fay's board was informed of accounting irregularities in its financial statements; its Audit Committee hired Weil Gotshal & Manges to conduct an internal investigation and prepare a report into the causes of the alleged wrongdoing; the investigation and its results were made public to relieve concerns of creditors, customers and shareholders of the company; the report contained summaries of interviews during the investigation; the court held that there was no work product protection because there was no on-going or anticipated litigation and Leslie Fay conducted the investigation mainly for

then makes repeated substantive and affirmative use of its report or summaries, especially in the litigation context, courts will be quick to find waiver based on the unfairness of allowing the company to use the results of its investigation as both a sword and a shield.

B. Disclosure to Government Regulators

Another way in which companies seek to use the results of their internal investigations is by sharing the results or report of their internal investigation with regulators to persuade them not to take action against the company, to enhance settlement prospects,[10] or to induce them to investigate or sue an adversary.[11] The potential benefits to the company from such disclosure are great, but so are the risks of waiver as to third parties. In general, courts have not accepted the notion of "selective" or "limited" waiver and have held that a company waives the attorney client privilege as to third parties by disclosing investigative materials to the government.[12]

Agencies such as the SEC and Department of Justice have, at times, entered into confidentiality agreements with companies that disclose the results of their internal investigation. Two recent cases, with different results, are illustrative of how the issues arise.

In *McKesson HBOC, Inc. v. Adler*, 254 Ga. App. 500 (Ga. Ct. App. 2002), the investor in a suit over false financial statements sought legal memoranda, summaries of employee interviews and the Audit Committee's report generated by McKesson in the investigation by its Audit Committee. The SEC investigated, and McKesson cooperated by providing the investigative materials, under a written confidentiality agreement, to the SEC for use in its investigation of some former managers and

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business reasons and that the company waived the attorney-client privilege as to interview notes and documents because it earlier produced the report to the SEC). *Id* .at 283.

[10] *See, e.g., In re Columbia/HCA Healthcare Corp. Billing Practices Litigation*, 293 F.3d 289 (6th Cir. 2002).

[11] *See Information Resources, Inc. v. Dun & Bradstreet Corp.*, 999 F. Supp. 591 (S.D.N.Y. 1998).

[12] *Columbia/HCA Healthcare, supra* (cataloguing the different approaches taken by courts). However, the Eighth Circuit in *Diversified Industries Inc. v. Meredith*, 572 F.2d 596 (8th Cir. 1978) upheld a claim of attorney client privilege for an investigative report and documents prepared by outside counsel that were disclosed to the SEC in response to a subpoena in non-public investigation (and later sought in civil litigation), primarily on the ground that a contrary holding might thwart

employees (McKesson was not the target of the inquiry). The trial court decided there was a waiver of the attorney client privilege and, without addressing McKesson's claim of work product, ordered production of the documents.

On appeal, the Georgia Court of Appeals affirmed as to the waiver of the attorney client privilege because McKesson contemplated disclosure of the documents to the SEC almost from the start of the investigation. *Id.* at 504. As to possible work production protection, however, the court observed that work product is "not necessarily waived by disclosure to a third party" and there was significant evidence of cooperation between the company and the SEC (such as the voluntary disclosure, confidentiality agreement and the SEC's *amicus* brief detailing how helpful the disclosure was to its investigation), that indicated that they were not adversaries and instead shared a "common interest." *Id.* at 502-03. The court thus recognized the possibility of work product protection despite disclosure to the SEC.[13]

In the recent case of *In re Columbia/HCA Healthcare Corp. Billing Practices Litigation*, 293 F.3d 289 (6th Cir. 2002), the court affirmed a finding of waiver of both the attorney client and work product privileges. There, the government sought "internal audits" prepared by Columbia/HCA in response to or in anticipation of a government fraud investigation. The company initially refused the request, but changed course when new management took over and opened settlement discussions. As part of those talks, the company produced some of the audits and related documents to the government under a confidentiality agreement. *Id.* at 292. Extensive civil litigation ensued in which the plaintiffs also sought the documents.

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the ability of corporations to use outside counsel to investigate and advise them in order to protect shareholders and customers. *Id.* at 611.

[13] Ultimately, the court remanded the case for factual findings on the company's claim of work product. *Id.* at 500; *see also In re Steinhardt Partners, L.P.*, 9 F.3d 230 (2d Cir. 1993) (where the court stated that it was not adopting a *per se* rule that all voluntary disclosures to the government waive work product protection and that the issue should be dealt with on a case by case basis).

After surveying the conflicting case law in this area, the Sixth Circuit Court of Appeals rejected all concept of selective waiver, noting that predictability and certainty weighed in favor of a clear-cut rule of waiver. *Id.* at 302. The court reached the same conclusion as to work product protection where it concluded that there was no compelling reason to differentiate between the two privileges. *Id.* at 307.[14]

Where does this precedent leave companies that are contemplating disclosure of the results of an internal investigation to regulators? *First*, recognize the significant risk of waiver that exists in this context. Most courts have simply not been willing to accept the notion of selective waiver, and the circumstances of the cases vary widely. At the outset of the investigation, consider whether the company will attempt to use the investigation to seek favorable treatment from government regulators. Counsel should also consider whether, and how, disclosure of the results of the investigation may fit into a strategy of self-reporting of wrongdoing to regulators.

Second, counsel should memorialize as much as possible the non-adversarial relationship with the subject government agency.

Third, where possible, counsel should enter into a written confidentiality agreement with the government because several courts have suggested that an explicit confidentiality agreement with the relevant government regulator weighs in favor of allowing the company to shield the disclosed reports with claims of privilege.

Fourth, corporate counsel should expressly reserve, at the time of disclosure, the right to assert or maintain the attorney client privilege or work product immunity in a later proceeding where the privilege or immunity may be at issue.

[14] One judge dissented on policy grounds, stating that the court's decision would chill companies' cooperation with the government. *Id.* at 307 *et seq.*

Fifth, where possible, counsel should limit its disclosures to the government to non-privileged materials.

Preserving the attorney client and work product privileges is a crucial aspect of internal investigations. Recent events and case law dictate that corporations and their counsel should anticipate and address the issue of waiver as to third parties before making public use of the report or findings of an internal investigation or disclosing them to regulators.

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