Sharing Privileged Information During Due Diligence

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2013-12-06 11:50:57.0

Consider this scenario: During routine due diligence for an impending transaction, the acquiring company learns that the business it is trying to buy has received a grand jury subpoena and is now conducting an internal investigation. Before the buyer will proceed further, it requests detailed follow up due diligence. The seller would like to provide the requested information so that it can sell the business. But some of what the buyer wants to know and the seller wants to share is protected by the attorney-client privilege. Concerns about waiving the privilege by sharing that information are creating an obstacle to closing the deal.

This is a familiar scenario in corporate transactions, especially in heavily regulated industries where government investigations are commonplace. The ultimate owner of the business will want to ensure that attorney-client communications remain privileged if litigation ensues. But sharing such materials during due diligence could result in waiver of the privilege and, ultimately, to the materials being used against the business in subsequent litigation.

Do the parties have any option, short of waiving privilege or walking away from the deal? One solution may be to share the privileged information in a way that allows the parties to successfully assert the common interest doctrine.

The Common Interest Doctrine

The common interest doctrine is sometimes referred to as a privilege, but it is really an exception to the rule that sharing privileged communications with a third party results in waiver of the privilege. For the doctrine to apply, the parties must have common interests that are legal, not just commercial, and most courts require that the interests be identical, not just similar. The doctrine typically applies to co-parties in litigation. It has also been applied in the context of a commercial transaction—where the parties sharing the privileged information are on opposite sides of the negotiating table—although application in that context is not guaranteed. Whether a court would apply it in the transactional context depends on a number of factors, including the timing of the communications, the nature of the transaction, the jurisdiction in which the waiver issue is litigated and the steps taken to maintain the confidentiality of the information.

There are strong policy reasons for applying the common interest doctrine in this context. As one federal court explained, “courts should not create procedural doctrine that restricts communications between buyers and sellers, erects barriers to business deals, and increases the risk that prospective buyers will not have access to important information that could play key roles in assessing the value of the business or product that they are considering buying. Legal doctrine that impedes frank communication between buyers and sellers also sets the stage for more lawsuits, as buyers and sellers are more likely to be unpleasantly surprised by what they receive.” *Hewlett-Packard Co. v. Bausch & Lomb, Inc.* (N.D. Cal. 1987). However, most courts do not take such an expansive view, cautioning that because the attorney-

client privilege is an obstacle to the search for the truth, it should be narrowly construed consistent with the purpose of the privilege: securing confidential legal advice.

When Does The Common Interest Doctrine Apply To M&A Transactions?

Courts are most likely to apply the common interest doctrine to privileged information shared during due diligence where the acquirer will succeed to the liabilities of the target or where the parties to the transaction may face litigation covering both the pre- and post-closing periods. In contrast, courts have refused to apply the common interest doctrine where disclosures of privileged information were intended to further a commercial venture, even if that venture involves some legal risk. Unfortunately, the line between pursuit of common "business" and "legal" interests is not clearly delineated, and existing court decisions often do not reveal the specific circumstances that distinguish between them.

The timing of the disclosures and other considerations, such as restrictions placed on the privileged materials prior to sharing, are also factors that courts consider. For example, privileged information contained in offering documents provided to multiple potential investors was not protected by the common interest doctrine in *Santella v. Grizzly Indus. Inc.* (D. Ore. 2012). The court noted that "companies can wait until they have entered into a more formal negotiating relationship and confidentiality agreement . . . which would further assist in demonstrating the existence of a common interest." In contrast, where a deal was "largely locked up" and was subject to a confidentiality agreement providing for control over access to the privileged information, the court in *Tenneco v. S.C. Johnson* (N.D. Ill. 1999) applied the common interest doctrine to an attorney opinion that had been shared with the buyer.

How To Minimize The Risk Of Waiver

When deciding whether the potential consequences of a privilege waiver are worth the risk of sharing privileged information, a company must assess the prospect that a court will apply the common interest doctrine. There are a number of steps that the parties can take reduce the risk of waiver:

- **Execute a common interest agreement:** Do not rely on an existing nondisclosure agreement pursuant to which confidential business information is exchanged. The existence of a separate common interest agreement will signal that the holder of the privilege considers the information to be privileged, not just proprietary, and intends to try to preserve the privilege.
- **Identify the common interest:** The common interest agreement should state with specificity the litigation or legal issue about which the parties share a common interest. For example, if there is an internal investigation or government investigation pending or anticipated, the agreement should refer to the nature of the investigation and how the parties' interests align post-closing. Including such details in a common interest agreement may help persuade a court that the disclosures of privileged information were made for legal rather than commercial purposes, and that the existence of common legal interests is not a position that was developed after the fact.
- **Wait until the transaction is far enough along:** Disclosing privileged information to multiple suitors will significantly increase the risk that a court finds that a waiver has occurred. In contrast, disclosure to a single party after the transaction appears likely to close minimizes that risk.
- **Limit access to any privileged information:** Only counsel and key members of the deal team with an interest in the common legal issue should be allowed access. In some instances, the parties may be able to negotiate an "attorneys' eyes only" agreement. Such limits will strengthen the argument that the disclosures were made for legal rather than commercial purposes.

- **Transfer any privileged information through counsel:** The involvement of counsel in the sharing of privileged information will bolster the position that the parties needed the information so they could obtain legal advice. If the information flows directly to/from company executives, there is a greater risk that the communication will be seen as furthering commercial, rather than legal, interests.
- **Limit the amount of privileged information shared:** A significant amount of information that the buyer needs can be obtained from non-privileged sources, including materials received from regulators, presentations made to prosecutors and summaries of meetings. Indeed, if enough non-privileged information is available, sharing privileged information can sometimes be avoided altogether. Assess what privileged information really needs to be shared, and then share only the information that is necessary to advancing the identified common legal interests.
- **Clearly mark all privileged documents:** Privileged communications remain privileged only if the holder of the privilege takes care to maintain the confidentiality of the communications. Accordingly, clearly marking any privileged documents that are shared with a legend such as "Subject to Common Interest Agreement" will help demonstrate that the holder exercised due care and guard against downstream disclosures that otherwise could constitute waiver.

The Bottom Line

Reliance on the common interest doctrine is not advisable in many transactions, and even where it appears to fit the situation, there is no guarantee that a court will apply it. But in appropriate situations, careful planning and thoughtful legal advice can help ensure the continued privilege status of shared information and facilitate closing the deal.

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