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PROTECTING CONFIDENTIALITY OF INTERNAL REVIEWS BY FINANCIAL SERVICES PROVIDERS

Internal Investigations by Financial Institutions May Be Protected from Disclosure by the Attorney-Client Privilege or the Attorney Work-Product Doctrine. The Protections May Be Lost or Waived, However, without Procedures and Documentation Specifically Addressed to the Requirements of Confidentiality.

By Benjamin B. Klubes*

Consumer financial services companies, including banks and other lenders, are facing rapidly growing risk management and litigation issues involving compliance with laws and regulations prohibiting protected class discrimination, unfair and deceptive trade practices, invasion of privacy through sale or provision of customer data to third parties, and other consumer issues. Addressing customer and employee complaints, compliance program development and monitoring, and litigation in these areas requires that inside and outside counsel for companies have the necessary facts to properly advise their clients. The gathering of those facts, and the provision of legal advice, is best done within the protections of the attorney-client privilege and work-product doctrine. The preservation of such protections requires an understanding of the basic elements of each, as well as their practical application

THE ATTORNEY-CLIENT PRIVILEGE

The attorney-client privilege protects the confidentiality of certain oral and written communications made between an attorney and his or her client.[1] The classic formulation of the privilege holds that communications are privileged when:

(1) the asserted holder of the privilege is or sought to become a client;

(2) the person to whom the communication was made is a lawyer;

(3) the communication relates to a fact of which the attorney was informed (a) by his client, (b) in confidence, (c) for the purpose of securing or receiving a legal service; and

(4) the privilege has been asserted and not been waived by the client.[2]

1. *See Upjohn Co. v. United States*, 449 U.S. 383 (1981).
2. *See United States v. United Shoe Mach. Corp*, 89 F. Supp. 357, 358-59 (D. Mass. 1950).

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The rationale that undergirds this privilege is the encouragement of candid disclosures and advice between attorneys and their clients.[3]

The necessity for the maintenance of confidentiality is highlighted by the fact that the protections described below are waived if a confidential communication or a substantial portion thereof, is voluntarily or involuntarily disclosed to a third party outside the corporation.[4] This includes communication disclosed to the government pursuant to an investigation — even an effort to persuade the government not to pursue an action against the client — a regulatory record-keeping requirement, or other governmental requirement.[5]

THE ATTORNEY WORK-PRODUCT DOCTRINE

The work-product doctrine derives from *Hickman v. Taylor*, 329 U.S. 495 (1947), and has since been incorporated into Rule 26 of the Federal Rules of Civil Procedure.[6] In 1981, the Supreme Court's *Upjohn* decision reaffirmed the work-product doctrine and clarified that it applies to corporate as well as individual clients.[7] The policy behind the work-product doctrine is that a litigant should not be able to discover and benefit from an opposing attorney's research and litigation strategy.

The work-product doctrine provides a qualified privilege: materials prepared in anticipation of litigation or in preparation for trial are protected absent a showing of substantial need or undue hardship by an opposing party.[8] The protection applies not only to work done by counsel, but to work and documents generated pursuant to their direction and supervision.[9] Opinion work-product receives greater, sometimes even absolute, protection. Rule 26(b)(3) of the Federal Rules of Civil Procedure defines opinion work-product as "mental impressions, conclusions, opinions, or legal theories of an attorney or other representative of a party concerning the litigation."

PRESERVING THE PRIVILEGE

Obviously, an essential element in assertion of confidentiality is the involvement of counsel. Because in-house corporate counsel often serves a dual role as both a business and a legal advisor, the corporation must first establish that such counsel was providing a *legal* service or *legal* advice when the corporation seeks to invoke the privilege. To preserve the privilege, a legal department should establish separate procedures for handling legal versus business matters so that communications with in-house counsel acting in his legal capacity will be clearly distinguishable from those in which in-house counsel was acting in a business capacity.

As a related matter, the corporations cannot shield information merely by having the legal department review documents or attend meetings. Instead, the attorney's receipt of any document or attendance at any meet-

3. *See Upjohn Co.*, 449 U.S. at 389.
4. *United States v. Dakota*, 188 F.3d 663, 667 (6th Cir. 1999) (voluntary disclosures waive the privilege); *Georgetown Manor, Inc. v. Ethan Allen, Inc.*, 753 F. Supp. 936, 937-938 (S.D. Fla. 1991) (involuntary disclosures waive the privilege).
5. *United States v. Billmyer*, 57 F.3d 31, 37 (5th Cir. 1995).
6. Rule 26(b)(3) provides, in relevant part:
   [A] party may obtain discovery of documents and tangible things otherwise discoverable under subdivision (b)(1) of this rule and prepared in anticipation of litigation or for trial or for another party or by or for that other party's representative (including the other party's attorney, consultant, surety, indemnitor, insurer, or agent) only upon a showing that the party seeking discovery has substantial need of the materials in the preparation of the party's case and that the party is unable without undue hardship to obtain the substantial equivalent of the materials by other means. In ordering discovery of such materials when the required showing has been made, the court shall protect against disclosure of the mental impressions, conclusions, opinions, or legal theories of an attorney or other representative of a party concerning the litigation.
7. *See Upjohn*, 449 U.S. at 397-401.
8. *See* FRCP 26(b)(3); *FTC v. Grolier, Inc.*, 462 U.S. 19, 20 (1983); *Upjohn*, 449 U.S. at 385.
9. *In re Grand Jury (Impounded)*, 138 F.3d 978, 981 (3d Cir. 1998).

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ing must be for the purpose of obtaining information or giving legal advice to render such communications privileged. Similarly, the underlying or preexisting facts contained in a communication are not privileged merely because they were disclosed to the attorney for the purpose of obtaining legal advice. Essentially, an underlying fact must be disclosed but the communication incorporating such fact is privileged.[10]

Because the privilege applies only to *confidential* communications, in-house counsel should limit the dissemination of privileged communications. A wide dissemination could suggest a lack of intent to keep the communication confidential. In-house counsel may want to transmit such communications only to employees covered under a "control group" test. Those are the employees who are in a position to substantially influence how to act upon legal advice or who are parts of a group with such authority.

INVOKING PROTECTION

Counsel and compliance personnel at financial services companies, particularly lenders, are subject to an increasing barrage of issues raised internally or by customers or government agencies regarding discrimination, unfair and deceptive trade practices, and privacy violations. Issues could be raised by a customer complaint that he or she was the subject of discrimination by a company employee; an inquiry from a government enforcement or regulatory agency about the company's sales, underwriting, marketing, or other practice that either might discriminate against protected classes or constitute an unfair and deceptive trade practice; or consumer groups or class action lawyers attacking company practices with respect to sharing data about its customers with third parties. In each of these situations, it is essential for counsel to gather the facts relating to the issues in order to best advise and defend the client. How does one do so and still preserve the attorney-client privilege and work-product doctrine protection?

The effort to begin the fact-gathering and factual and legal analysis with the proper privilege protections should involve a documented request from inside counsel to outside counsel or, if outside counsel is not involved, a memorandum to the file, indicating that the company seeks legal advice of counsel with respect to a matter, and that there is the possibility of litigation arising from this matter.

To begin the fact-gathering step in providing advice on a consumer complaint, or responding to a government inquiry, counsel generally must communicate with company employees. Under the *Upjohn* standard, an employee's communication with counsel will be subject to the company's privilege when the communication (i) is about matters within the scope of the employee's corporate duties, and (ii) is made for the purpose of obtaining legal advice.[11] When speaking with company employees, counsel should inform the employee at the outset of their discussion that the counsel is acting on behalf of the corporation and not the employee. This prevents an employee from asserting the privilege on his or her personal behalf with respect to that communication at a later date. The *Upjohn* standard suggests some additional guidelines:

(1) all communications to employees should state that information is needed for the purpose of providing legal advice to the company;

(2) the communication should also state that the request is pursuant to an executive directive asking corporate employees to provide counsel with the information;

(3) the communication should concern matters within employee's corporate duties; and

(4) the employee should be requested to keep the communication confidential.

The generation of written materials documenting interviews with employees, or providing analyses of the facts or law, must be done with care. As described above, the work-product doctrine covers documents generated in the course of an internal corporate investigation, such as work papers, notes, memoranda, and reports gathered or prepared by counsel and their agents in anticipation of litigation. Documents covered by the attorney-client privilege or attorney work-product protection should be marked accordingly.

Two particular areas of concern are analyses of lending data and self-testing or "mystery shopping." In responding to customer complaints or government inquiries, or in proactive compliance strategies, many financial service companies conduct increasingly sophisticated data analyses, and have instituted self-testing efforts. It is important to take all reasonable steps to protect such materials.

10. *Upjohn*, 449 U.S. at 395.

11. *Upjohn*, 449 U.S. at 394.

A first protective step is to have such efforts directed and reviewed by the company's general counsel, or by outside counsel. Moreover, to the extent it is reasonable, work that is in anticipation of litigation should be so designated to bolster the claim of attorney work-product doctrine protection. As noted above, work done at the direction or under the supervision of an attorney still falls within the attorney work-product doctrine.

With respect to self-testing or "mystery shopping," work-product protection may be a useful compliance tool. If a decision is made to undertake such an effort, and there are a variety of factors beyond the scope of this article to consider in making such a decision, it is important to have attorney supervision of such self-testing to maximize the ability to preserve the privilege with respect to the tests and their results. In particular, inside or outside counsel should be involved in the decision to undertake such an effort, and the selection of the vendor to perform the testing. Test results should be reported to counsel in writing, and marked as privileged. Distribution of the results should be limited.

Recent legislation and related new regulations under both the Equal Credit Opportunity Act and the Fair Housing Act provide a privilege for self-testing by lenders to assure compliance with these fair lending statutes.[12] The newly minted privilege applies to self-testing conducted by a lender, or an independent third party at the request of a lender, that has identified a possible violation of the fair lending law, and the lender has taken, or is taking, appropriate corrective action to address a violation.[13]

The privilege, however, is subject to a number of limitations that significantly curtail its potential value. For the privilege to apply, the lender must take appropriate corrective action when the self-test shows it is "more likely than not" that a violation occurred.[14] In addition, the lender may not refer to or describe the report as a defense to charges of fair lending violations without surrendering the privilege.[15] However, for the sole purpose of determining an appropriate penalty or remedy, disclosure of the report or results may be compelled in conjunction with an adjudication or admission of a violation of the fair lending statutes.[16] These provisions may discourage institutions from openly discussing with their examiners the nature and scope of their self-testing programs — out of concern for the loss of privilege. Moreover, allowing plaintiffs and government regulatory and enforcement agencies to compel disclosure of self-test information, even for the limited enforcement purpose of determining damages, will have the effect of discouraging institutions from incorporating self-testing into their regular compliance programs.[17]

One potential additional protection for internal investigative efforts is the self-evaluation privilege. The basic rationale for the privilege is the "overwhelming public interest," in encouraging certain critical internal evaluations and discussions which might be deterred were confidentiality not assured.[18] Disclosure of "candid self-examination [would] deter or suppress socially useful investigations and evaluations."[19] The self-evaluative privilege ultimately "fosters the compelling public interest in observance of the law."[20] The elements of the self-evaluative privilege: (i) the information in question results from a self-critical analysis; (ii) the information was intended to be and has been kept confidential; (iii) the public has a strong interest in preserving the free flow of the type of information sought; and (iv) the free flow of that information would be curtailed if the information were discoverable.[21]

The privilege extends to evaluative materials only, not the facts underlying an evaluation. Like other privileges, dissemination of the material sought to be protected waives the privilege. Further, the privilege is qualified and can be overcome "by a showing of particularized need . . . outweigh[ing] the public interest in confidentiality."[22] The privilege is not uniformally recognized and its reach has been circumscribed even where recognized: "Whatever may be the status of the 'self-evaluative' privilege in the context of private litigation, courts with

12. 15 U.S.C. § 1691c-1 (1999); 42 U.S.C. § 3614-1 (1999); 12 C.F.R. § 202.15 (1999); 24 C.F.R. § 100.140 (1999).
13. 15 U.S.C. § 1691c-1. According to Official Staff Commentary on the regulations issued in July 1998, appropriate corrective action is determined on a case-by-case basis. Self-tests designed for purposes unrelated to the statutes at hand, such as assessments of customer service, are not privileged even if they reveal discrimination covered by the statutes.
14. 12 C.F.R. § 202.15(c)(1999); 24 C.F.R. ' 100.143.
15. 15 U.S.C. § 1691c-1(b)(1)(A).
16. 15 U.S.C. § 1691c-1(b)(1)(B).
17. Lenders embarking on self-testing should also ascertain whether there is relevant state law providing a self-evaluative protection to the testing.
18. *Bredice v. Doctors Hospital, Inc.*, 50 F.R.D. 249, 251 (D.D.C. 1970).
19. *Hardy v. New York News, Inc.*, 114 F.R.D. 633, 640 (S.D.N.Y. 1987).
20. *Id.*
21. *Grimes v. DSC Communications Corp.*, 724 A.2d 561, 570 (Del. Ch. 1998) (citation omitted).
22. *Todd v. South Jersey Hospital System*, 152 F.R.D. 676, 683 (D.N.J. 1993) (internal quotation marks and citation omitted).

apparent uniformity have refused its application where, as here, the documents in question have been sought by a governmental agency."[23]

CONCLUSION

The risk management environment financial services companies are facing today necessitates taking care to protect the availability of the attorney-client privilege and work-product doctrine. To do so, inside and outside counsel must be familiar with the essential elements and limits of those protections, and take consistent affirmative steps to best position factual investigation, legal analysis, and advice to preserve those elements and stay within those limits. ■

23. *Federal Trade Comm'n v. TRW, Inc.*, 628 F.2d 207, 210 (1980) (the privilege does not shield company's internal fair credit compliance auditing reports and internal responses to those reports from FTC subpoena). Only one of the three cases cited by the DC Circuit for that proposition, however, actually supports it. *Compare United States v. Noall*, 587 F.2d 123, 126 (2d Cir. 1978) (the privilege does not shield company's internal audit reports and related work papers from IRS summons) *with Emerson Elec. Co. v. Schlesinger*, 609 F.2d 898, 906-07 (8th Cir. 1979) (rejecting challenge based on self-evaluation privilege to information sharing between EEOC and contract compliance office within the Department of Labor based on Memorandum of Understanding) *and Reynolds Metals Co. v. Rumsfeld*, 564 F.2d 663, 667 (4th Cir. 1977) (same).