SHEPPARD MULLIN
SHEPPARD MULLIN RICHTER & HAMPTON LLP
ATTORNEYS AT LAW

September 2003

"Just Between You and Me": Practical Tips for Sharing Privileged Information with a Prospective Buyer without Waiving the Attorney-Client Privilege*

By Brette S. Simon and Lawrence M. Braun[1]

Introduction

A company is contemplating whether to enter into a sale transaction to sell one or more of its lines of business, or is currently in the midst of a business sale transaction. As is common for any operating business, the company has ongoing litigation, investigations or legal issues where it has involved its attorneys. In some cases, the company may have recently discovered information which requires that same attention from its legal counsel. The company discusses these issues in detail with its attorneys, which brings such conversations under the protective umbrella of the attorney-client privilege.[2]

Should the company decide to proceed with the sale transaction, it faces the following dilemma: On one hand, it is incumbent on the company, as the seller, to disclose to the buyer all material information relating to the business it is purchasing.[3] On the other hand, should the company share this confidential information with the potential buyer, it jeopardizes waiving the attorney-client privilege with respect to the particular information, and, potentially, any other privileged information relating to the same subject matter.[4] This means that if litigation is pending or is later filed against the seller by a third party claimant (other than the buyer)[5] regarding the problem, and the opposing party requests this confidential information, the seller will be unable to assert that it is privileged, and will have to provide potentially damaging information to the claimant.

Proper handling of this potential Catch-22 is critical to a successful transaction and to avoiding ongoing exposure. With gun-shy buyers already pre-disposed to finding reasons to back out of transactions, the least desirable outcome for the seller is to disclose the information to the buyer in a manner that waives the privilege, only to watch the buyer walk away from the deal. This leaves the seller with the worst of both worlds–a busted deal, and a waiver of the privilege.

*This article was first published in ACCA-SoCal's Focus, third quarter 2003.

A seller faced with the facts outlined above can potentially lessen its risk of waiving the attorney-client privilege by invoking the "common interest"[6] exception to the attorney-client privilege, as explained below.

Attorney-Client Privilege

Generally speaking, the attorney-client privilege protects confidential communications between a client and its attorney, and any disclosure of a confidential communication outside this privileged relationship will waive the privilege.[7] Thus, in the fact pattern above, absent a valid exception, the seller will have waived the attorney-client privilege with respect to the confidential information upon its disclosure of such information to the buyer. This can have particularly damaging consequences. Not only is the privilege waived with respect to the specific information shared with the buyer; in addition, the waiver extends to the entire subject matter of the disclosure.[8] Thus, the seller has now effected an implied waiver as to all other undisclosed communications relating to the same subject.

Common Interest Doctrine–An Extension of the Attorney-Client Privilege

The common interest doctrine expands the application of the attorney-client privilege, and is an exception to the general rule that the attorney-client privilege is waived upon disclosure of privileged information to a third party. Courts have held that privileged communications can retain a protective shield under the attorney-client privilege if the disclosing party and the receiving party have a common legal interest, such as where they are "involved in or anticipate joint litigation…the key consideration is that the nature of the legal interest be identical, not similar, and be legal, not solely commercial."[9]

The facts of Hewlett-Packard Co. v. Bausch & Lomb Inc.[10] are particularly illustrative. In that case, Bausch & Lomb disclosed an attorney's opinion letter to GEC, the prospective buyer of one of Bausch & Lomb's divisions. The letter concerned the validity and possible infringement of a third party's patent. The court agreed with Bausch & Lomb's position that it had a common legal interest with GEC. Specifically, at the time Bausch & Lomb disclosed the opinion letter, there was a real possibility that GEC would purchase the division, and if it did, the odds were strong that both Bausch & Lomb and GEC would end up defending the same product against the same patent in a single lawsuit that Hewlett-Packard could be expected to bring. Thus, at the time Bausch & Lomb and GEC were negotiating, it seemed likely that both of them would be sued by Hewlett-Packard, and in that litigation Bausch & Lomb and GEC would be identically aligned, fighting to protect interests distinguished only by the time frame in which they sold allegedly infringing product.[11]

In holding that the common interest exception applied, the court in Hewlett-Packard placed considerable emphasis on the fact that Bausch & Lomb had taken "substantial steps" to assure that GEC maintained the confidentiality of the letter. Specifically, only two copies of the opinion letter were transmitted to GEC; GEC was instructed that

no further copies were to be made; both copies were returned to Bausch & Lomb's counsel; and the letter was not disclosed to others.[12]

Conversely, the fact that "no steps appear to have been taken by [the defendant]'s lawyers and its employees, to ensure that the privileged communications, though shared, would remain confidential," was a key factor in the court's rejection of the application of the common interest exception in Libbey Glass, Inc. v. Oneida, Ltd. [13] The court in Libbey noted that the parties took "no steps to safeguard the privilege" and "on that basis alone," the court found the attorney-client privilege was waived.[14]

Practical Suggestions for Sellers (and Buyers)

There is no black letter law in this area.[15] Thus, with any disclosure to a potential buyer, there is always the risk that a court will decide that the seller has waived the attorney-client privilege upon its disclosure of privileged information to a prospective buyer. However, based on the holdings in Hewlett-Packard and Libbey, there are a number of steps that a seller (as well as the prospective buyer) can take, which, at a minimum, will increase the likelihood that the parties can invoke the common interest exception and preserve the privilege:

1. **Execute a Confidentiality Agreement.**

Evidence that the parties made an effort to keep the privileged information confidential is essential to satisfying the requirements of the common interest doctrine. While most sellers require a prospective buyer to sign a confidentiality or non-disclosure agreement upon commencement of due diligence in a M&A transaction, it behooves the seller to re-read carefully the provisions of that agreement. For example, does the confidentiality period terminate after a certain number of years? How does it address disclosures required by law? The parties should consider a provision which keeps privileged information confidential in perpetuity, with no expiration date. In addition, the seller should insist that, in the event a buyer is required by law (e.g., pursuant to a subpoena, under SEC disclosure rules, etc.) to disclose such confidential information, the buyer must notify the seller immediately. In the event that applicable law mandates disclosure, the agreement should obligate the buyer to assert the attorney-client privilege, and to cooperate with the seller in attempting to seek a protective order or other forms of confidential treatment for such information.

2. **Limit Access to the Privileged Information.**

The parties should agree in writing as to the nature and number of people who will be allowed to have access to the privileged information. Obviously, the fewer the better. Further, disclosure should be restricted to key, senior executives of the buyer. The seller should limit the number of copies of the confidential documents provided to the buyer, should not provide them electronically, and should clearly and conspicuously stamp them "confidential,"

"attorney-client privileged" and "joint defense privileged." In the event that the deal is not consummated or the matter is resolved, the seller should require that the documents be returned to the seller.

3. **Unfortunately, You Have to Leave the Accountants and Investment Bankers Out of It.**

As discussed above, disclosure of privileged information outside of a privileged relationship will, absent a permitted exception, result in a waiver of the attorney-client privilege. While there is no guarantee that the seller will be able to fall within the four corners of the common interest exception with respect to information shared with a potential buyer, the seller clearly waives the attorney-client privilege if it widens the pool of people "in the know" to include accountants and/or investment bankers. While the buyer may or may not be ultimately considered to have a "common legal interest" with the seller, the seller's and buyer's business advisors certainly do not. Thus, these advisors should not participate in any conference calls or meetings during which the privileged information is discussed.

4. **Require the Buyer to Provide Post-Closing Access to Information and Employees.**

In the event that a purchase and sale agreement is entered into between the parties, the seller should require that the agreement allow the seller to have access to the transferred employees of the sold business, as well as the books, records, and other documents relating to the business. In the event that a lawsuit is filed relating to the potential liability, the seller will need to call upon its former employees as witnesses, and will need access to the books and records of the business it sold to respond to discovery requests, etc.

5. **Consider Entering into a Joint Defense Agreement.**

Entering into a joint defense agreement can provide evidence that the disclosures were made between the parties in the course of formulating a common legal strategy, thus bolstering their argument that the common interest exception should apply to the shared information. However, determining whether or not to enter into a joint defense agreement requires careful analysis. While the subject of joint defense agreements is beyond the scope of this article, as a general matter, each party and its attorney should consider, among other issues: whether the joint defense agreement could itself wind up the subject of a future disclosure request if, for example, either party becomes the subject of a government investigation; the nature of the duties of each party set forth in the joint defense agreement and the potential for breach-ing such duties; which party will be responsible for the relevant issue and indemnification after the closing; and how much information the seller should share under the terms of the joint defense

agreement (and whether the failure to disclose certain items could constitute a material omission).

6. **Use Caution in Discussing the "Issue."** In the event that a court holds that the common interest exception was not satisfied and the seller waived the attorney-client privilege, the Miranda rule will be applied: Everything that has been said can and will be used against you. Thus, the parties should be sensitive to the way in which the situation is characterized. Avoid referring to the matter in conversations or correspondence as a "problem," or using other words with negative connotations.

Conclusion

Which of the suggestions outlined above will be the best course of action will naturally depend on the facts and circumstances of the particular case. However, the above provides an overview of the issues faced in such a situation, and a general guide as to how the parties can best achieve their mutual goal of shared information and doing a deal, while lessening the likelihood that they will waive the attorney-client privilege.

---

[1]© Brette S. Simon 2003.

[2]For purposes of this hypothetical, the reader should assume that all of the requirements necessary to invoke the attorney-client privilege have been met.

[3]Engaging in willful blindness and adopting a "don't ask, don't tell" policy with the buyer risks a fraud claim, should the company sell the business without informing the buyer of the problem, and the other alternative–telling the buyer "I just found out about something bad, but I can't tell you about it"–doesn't tend to go over well at the negotiating table.

[4]Generally, voluntary disclosure of privileged attorney-client communications to a third party waives the privilege as to all other communications on the same subject.

[5]The subject of this article addresses ways to preserve the attorney-client privilege with respect to a claim brought by a third party other than the prospective buyer. Confidential information shared with a potential buyer would not be privileged should a dispute arise between the seller and the buyer.

[6]The "common interest" doctrine is also often referred to as the "community of interest" rule or the "common defense" doctrine.

[7]Specifically, the privilege applies only if (1) the asserted holder of the privilege is or sought to become a client; (2) the person to whom the communication was made (a) is a member of the bar of a court, or his subordinate and (b) in connection with this communication is acting as a lawyer; (3) the communication relates to a fact of which the attorney was informed (a) by his client (b) without the presence of strangers (c) for the purpose of securing primarily either (i) an opinion on law or (ii) legal services or (iii) assistance in some legal proceeding, and not (d) for the purpose of committing a crime or tort and (4) the privilege has been (a) claimed and (b) not waived by the client. *United States v. United Shoe Machinery Corp.*, 89 F.Supp. 357, 358-59 (D.Mass.1950); *Union Carbide v. Dow Chemical*, 619 F.Supp. 1036, 1046 (D.Del.1985); *Advanced Technology Associates Inc., v. Herley Industries, Inc.* 1996 WL 711018 (E.D.Pa.1996).

[8]*Katz v. AT&T Corporation*, 191 F.R.D. 433,439 (E.D.Pa.2000); *Helman v. Murry's Steaks, Inc.* 728 F.Supp. 1099, 1103 (D.Del.1990).

[9]*Union Carbide v. Dow Chemical*, 619 F.Supp. 1036 (D.Del.1985) (emphasis added); *Hewlett-Packard Co. v. Bausch & Lomb Inc.,* 115 F.R.D. 308, 309 (1987); *Duplan Corp. v. Deering Milliken, Inc.,* 397 F.Supp. 1146, 1172 (D.S.C.1974).

[10]115 F.R.D. 308 (1987). See also *Rayman v. American Charter Federal Savings & Loan Association*, 148 F.R.D. 647 (D.Neb.1993); *B.E.Meyers & Co., Inc. v. United States*, 41 Fed.Cl. 729 (1998).

[11]Notably, the court reached its conclusion despite the fact that Bausch & Lomb and GEC did not complete the sale and did not have to litigate the same issues in fact, reasoning that the common interest exception only required that joint litigation be anticipated. *Hewlett-Packard* at 310.

[12]*Id* at 309.

[13]197 F.R.D. 342 (1999).

[14]*Id* at 349.

[15]Other courts have handed down rulings contrary to the decision in *Hewlett-Packard and Rayman*. See, e.g., *Bank Brussels Lambert v. Credit Lyonnais*, 160 F.R.D. 437 (S.D.N.Y.1995); *Walsh v. Northrop Grumman Corp.*, 165 F.R.D. 16 (E.D.N.Y.1996); *Oak Industries v. Zenith Industries*, No. 86C4302, 1988 WL79614 (N.D.Ill. July 27, 1988); *SCM v.Xerox Corp*. 70 F.R.D. 508 (D.Conn.1976).

[16]See, e.g., *Walsh v. Northrop Grumman Corp.*, 165 F.R.D. 16, 19 (E.D.N.Y.1996) ("The common enterprise upon which Salomon [Brothers, Inc.] and Northrop were embarked was a business, not a legal, enterprise.").

NOTES

About the Authors

Brette S. Simon

Brette S. Simon is Special Counsel in the Los Angeles office of Sheppard, Mullin, Richter & Hampton LLP. Ms. Simon specializes in mergers and acquisitions, corporate finance, emerging company/venture capital and joint venture transactions. She also advises clients on a wide range of business issues.

Ms. Simon may be reached at 213.617.5414 (Phone), 213.620.1398 (Fax) or bsimon@sheppardmullin.com.

Lawrence M. Braun

Lawrence M. Braun is the Chairman of the Corporate Practice in the Los Angeles office of Sheppard, Mullin, Richter & Hampton LLP. Mr. Braun represents public and private companies in the areas of securities, mergers and acquisitions, corporate finance and general business.

Mr. Braun may be reached at 213.617.4184 (Phone), 213.620.1398 (Fax) or lbraun@sheppardmullin.com.

LOS ANGELES

Sheppard, Mullin, Richter & Hampton LLP
333 South Hope Street, 48th Floor
Los Angeles, California 90071
213.620.1780 | Fax: 213.620.1398

WEST LOS ANGELES

Sheppard, Mullin, Richter & Hampton LLP
10940 Wilshire Boulevard, Suite 2030
Los Angeles, California 90024
310.824.0097 | Fax: 310.824.9788

SAN FRANCISCO

Sheppard, Mullin, Richter & Hampton LLP
Four Embarcadero Center, 17th Floor
San Francisco, California 94111
415.434.9100 | Fax: 415.434.3947

SANTA BARBARA

Sheppard, Mullin, Richter & Hampton LLP
800 Anacapa Street
Santa Barbara, California 93101
805.568.1151 | Fax: 805.568.1955

ORANGE COUNTY

Sheppard, Mullin, Richter & Hampton LLP
650 Town Center Drive, 4th Floor
Costa Mesa, California 92626
714.513.5100 | Fax: 714.513.5130

DEL MAR HEIGHTS

Sheppard, Mullin, Richter & Hampton LLP
12544 High Bluff Drive, Suite 300
San Diego, California 92130
858.720.8900 | Fax: 858.509.3691

SAN DIEGO

Sheppard, Mullin, Richter & Hampton LLP
501 West Broadway, 19th Floor
San Diego, California 92101
619.338.6500 | Fax: 619.234.3815

WASHINGTON, D.C.

Sheppard, Mullin, Richter & Hampton LLP
1300 I Street, NW, 11th Floor East
Washington, DC 20005
202.218.0000 | Fax: 202.218.0020

www.sheppardmullin.com