

Court Highlights Risks Associated with Attorney-Client Privilege in Parent-Subsidiary Joint Representations

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Lawyers regularly represent multiple entities within a corporate family without considering that in undertaking what is technically a joint representation there is any risk that the attorney-client privilege of each of the clients could be compromised. What could be a more congruent joint representation than that of parent and wholly-owned subsidiary? But in a wake-up call to the profession, the Third Circuit, in *Teleglobe USA Inc. v. BCE Inc.*, reminded all lawyers that the privilege in this situation is hardly an impregnable fortress. All it takes is for the interests of the parent and subsidiary to diverge, the lawyers for both to ignore the developing conflict, or new individuals to be in control of the subsidiary's privilege through acquisition, bankruptcy or an assertion of rights by disgruntled creditors of the subsidiary, to create a situation in which the parent's privileged information is shared with those whose interests might be quite hostile to the interests of the parent. And the real risk is that those asserting a divergence of interest will have the benefit of 20/20 hindsight, leading to the possibility of a finding that there was a divergence of interest at a time long before the lawyers or clients, acting in good faith, recognized a need to take special steps to protect the corporate privilege.

Key Holdings of *In re Teleglobe*

- The Third Circuit ruled that privileged documents are discoverable if a parent company and its subsidiary were jointly represented by the same lawyer on matters of common interest at a time when their interests diverged.
- The Third Circuit held that, in the context of a joint representation, privileged communications between a lawyer and the parent and/or the subsidiary may be particularly susceptible to discovery if a dispute arises between the parent and its subsidiary, for example in the context of a spin-off or sale of a subsidiary or where a subsidiary becomes insolvent.
- The Third Circuit suggested Delaware courts would likely require a parent company to produce privileged

information when the parent owes a fiduciary duty to creditors of an insolvent subsidiary.

- The Third Circuit held that Delaware courts would impose sanctions against any party that abuses the discovery process, including preventing such party from asserting its right to assert the attorney-client privilege, if the courts found that the party had acted in bad faith, willfully, or was at fault.

Practice Pointers Set Forth by the Third Circuit

- The Third Circuit recommended that parent companies limit their disclosures of privileged information to subsidiaries.
- The Third Circuit encouraged lawyers for parent companies to limit the scope of joint representations with their client's subsidiaries.
- The Third Circuit stated that a subsidiary should obtain separate counsel for matters in which the interests of the parent are (or are likely to become) adverse to those of the subsidiary.

What Information Is Subject to Discovery?

All privileged communications relating to matters for which the parent company and its subsidiary are jointly represented by the same lawyer are subject to discovery in a dispute between them. In situations where the same lawyers are involved in all legal matters of a parent and its subsidiaries, all of a company's and its subsidiaries' privileged communications could be subject to discovery.

Who Can Discover Such Information?

In the event of a dispute between a parent company and its subsidiary, each party could discover privileged information of the other. In addition, creditors of a subsidiary could also discover privileged information of the parent company if the subsidiary is insolvent.

LESSONS FOR IN-HOUSE AND OUTSIDE COUNSEL

The *In re Teleglobe* court made the following recommendations to parent and subsidiary companies that share legal services:

Limit the Disclosure of Confidential Information

To avoid inadvertently creating a joint representation (or expanding the scope of an existing joint representation), lawyers should limit disclosures of privileged information among affiliated companies. Where privileged information is disclosed to directors or officers who share positions on multiple affiliated companies, *In re Teleglobe* concluded that no joint representation would be deemed created or expanded as long as the disclosure of privileged information *does not occur* while such directors or officers are working in their capacity as directors and officers of an affiliated company.

Define and Limit the Scope of Joint Representations

Lawyers for parents and subsidiaries should “limit the scope of a joint representation in a sophisticated manner.” For example, where a lawyer representing a parent company seeks confidential information from the parent’s subsidiaries in order to complete necessary SEC or other governmental filings, the lawyer should (i) limit the scope of his or her joint representation to the filing and (ii) make clear that the representation is limited to assisting the parent company with making an accurate filing. In the event that the lawyer is provided with privileged information from a subsidiary, the substance of which raises legal issues not related to the filing, the lawyer should consider advising the subsidiary to obtain its own legal representation relating to such issues.

Take Action When Interests Begin to Diverge

Whenever the interests of a parent company and one of its subsidiaries begin to diverge, such as in a spin-off, sale or insolvency situation, the parent company should either seg-

regate the responsibilities of its lawyers between the parent and the subsidiary or direct the subsidiary to secure its own representation. In such situations, lawyers for the parent could continue to represent a subsidiary on matters that are unrelated to the issues on which the parties’ interests have diverged; however, lawyers should clearly set forth the scope of such representation to avoid future attacks on privilege. Independent representation of a subsidiary should be secured “once the parties’ interests become sufficiently adverse that the parent does not want future controllers of the subsidiary to be able to invade the parent’s privilege.”

Be Aware of Fiduciary Duties Owed to Creditors and of Discovery Sanctions

Lawyers should be aware that courts may compel the discovery of privileged material, regardless of the steps taken to avoid the application of the joint representation rules discussed above, if:

- the court finds that a corporation may have violated its fiduciary duties to its creditors while the corporation was insolvent; or
- the court finds that the corporation abused the discovery process and, in doing so, acted in bad faith, willfully, or was at fault.

* * *

Our concern is that the Third Circuit’s decision in *In re Teleglobe* seems to ignore certain practical realities of today’s corporate world. Nonetheless, unless and until that decision is reversed or overruled, the legal principles it sets forth represent the current status of Delaware law with respect to the attorney-client privilege in the corporate context. Lawyers should be aware of the risks that exist when a parent company and its subsidiary are jointly represented and, when faced with that situation, should conduct themselves with great care.

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