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Corporation's Attorney-Client Privilege Extends to Counsel's Communications With "Functional Employees" Outside the Company

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Counsel conducting an internal investigation immediately face two related and important tasks: identifying the "client" group whose communications with counsel are within the attorney-client privilege exclusively held by the corporation and avoiding, through corporate Miranda warnings and other techniques, a subsequent claim by any of the interviewee-employees that they jointly hold the privilege because counsel represented them personally at the same time as representing the corporation. A corporation's ability to fully and exclusively control the privilege is critical, whether to restrict and prevent discovery of employee statements by a civil adversary in order to limit exposure to liability and damages or conversely to be enabled to provide discovery and disclosure of employee statements to curry favor with law enforcement in an effort to avoid prosecution of the entity.

But identifying the "client" group of employees is complicated in organizations, such as sales-driven companies, with many 1099'd "independent contractors" who performed roles critical to the matter under investigation. Are they employees whose statements to counsel are within the corporation's exclusively-held privilege or not? And, if they are employees, do they hold a cognizable claim to the privilege because they reasonably believed that the interviewing attorneys represented them as individuals?

The first question – when is an employee an employee for privilege purposes – was addressed in a recent Ninth Circuit opinion. United States v. Graf, 610 F.3d 1148 (9th Cir. 2010). The defendant in Graf was an outside consultant to a health insurance provider used to commit fraud against its insureds. Although not listed anywhere as an officer, director or employee of Employers Mutual, Graf was heavily involved in the company's affairs.

When the company hired counsel to deal with federal regulators, Graf made false statements to counsel, all while directing other employees to conceal documents from investigators. (The opinion did not address the applicability of the crime-fraud exception to any privilege). Following Graf's indictment, the government called those attorneys as witnesses to testify to Graf's statements to them, and the court-appointed fiduciary then operating the company agreed to waive its privilege and allow them to testify as to the statements. Graf objected, claiming that since he was not an employee, but an outside consultant, his statements were outside the corporate zone of privilege and, further, that he jointly held the privilege with the company and he would not waive it.

A two part analysis was employed, to determine first if Graf was an employee within the "client" group of Employers Mutual and, second, to decide if he held his own privilege as to discussions with counsel. The Eighth Circuit case of In re Bieter Co., 16 F.3d 929 (8th Cir. 1994) supplied the first answer. Under Bieter, communications between company counsel and outside consultants fall within the company's exclusively-held privilege if the consultant is "the functional equivalent of an employee," looking to factors such as the extent of daily involvement with the company's activities and the role in managing and directing employees. See also Trustees of Elec. Workers Local No. 26 v. Trust Fund Advisors, Inc., 266 F.R.D. 1 (D.D.C. 2010). Graf was, under Bieter and its progeny, a functional employee of Employers Mutual.

Having found presumptively, then, that the privilege attaching to Graf's statements to counsel belonged to and was able to be waived by the company, the Ninth Circuit then dismissed his claim to a jointly-held privilege. Adopting for the first time the multi-part standard of In re Bevill, Bresler & Schulman Asset. Mgmt. Corp., 805 F.2d 120 (3d Cir. 1986) (already the law in the First, Second, and Tenth Circuits), the Graf court held that he failed to carry his burden as to several indicia of a separate, personal attorney-client relationship with corporate counsel, including

failing to show that he made clear he was seeking individual legal advice, that the attorneys indicated they were representing him individually, and that the substance of the communications did not concern the affairs of Employers Mutual. As a result, there was no error in admitting the attorneys' testimony against him and Graf's conviction was affirmed.

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