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A Tale of Two States: Access to Attorney-Client Privilege Materials in Intra-Corporate Disputes Involving Close Corporations

In this Issue:

Most people communicating with their lawyer rightfully believe their discussions are privileged and cannot be disclosed to others without permission. However, when litigation ensues, because the attorney-client privilege interferes with full discovery and testimony, the privilege is strictly construed. Particularly in the context of disputes between shareholders, directors, officers and corporations, the lines have become blurred whether, and to what extent, otherwise privileged communications may be discovered in litigation. Two courts recently reached opposite results in deciding whether privileged communications should be produced to the parties' adversaries in litigation. While both courts were careful to note that they were basing their decisions upon the peculiar facts in the case, the differing results are remarkable.

In *Chambers v. Gold Medal Bakery, Inc.*, 983 N.E.2d 683 (Mass. 2013), the Massachusetts Supreme Court held that directors/shareholders of a closely-held company who were adverse to the corporation did not have the right to obtain privileged corporate communications. The Court recognized that, although directors may generally have a right to access the company's books and records, and have fiduciary duties to manage the corporation, those principles are premised on the notion that the interests are not adverse to those of the corporation. Based upon the facts presented there—multiple lawsuits over time,

efforts to gain control of the corporation, and a desire to drive up the stock price—the Court found that the interests were sufficiently adverse to deny the directors access to the company's privileged communications. The significant factor in the decision was the directors' adversity reflected in the desire to sell shares at the highest possible price which was adverse to the corporation's interests. "The idea that a director whose interests are adverse to those of a corporation on a given issue is not automatically entitled to access the corporation's confidential communications with counsel furthers the policy rationale underlying the attorney-client privilege: it promotes candid communications between attorneys and organizational clients." *Id.* at 693 (citing *Upjohn Co.v. United States*, 449 U.S. 383 1981)). The court precluded the directors' discovery of and access to the privileged materials. Id. at 698 (also noting that the directors' status as shareholders did not change the result).

More recently, the Delaware Chancery Court in *In re Information Management Servs., Inc. Derivative Litig.*, 2013 WL 4772670 (Del. Ch., Sept. 5, 2013) found that e mail communications involving two board members and their personal outside counsel were not privileged. In the case, the corporation was 50% owned by two families' trusts, each of which had two members appointed to the corporation's board. Due to differences over how the company should be operated and whether one of the families' board members were breaching their fiduciary duties, litigation ensued. During the course of the litigation, it was discovered that the two adverse board members had used their work e mail accounts both before and after the filing of the lawsuit to communicate with their personal attorneys. The company had collected the e mails and the board members asserted the attorney-client privilege. The principal issue was whether the board members had a reasonable expectation of confidentiality under the circumstances of the case. In particular, whether, as employees of the corporation, the directors reasonably could expect that e mails sent to their lawyers from the company's e -mail system would remain confidential. Finding the emails were not confidential under the circumstances, the court relied upon four factors:

- whether the corporation had a policy banning personal use of the company's e mail system,
- whether the company monitors the employees' computers or e mails,
- whether third parties have a right of access to the computer or e mails, and
- whether the corporation notified the employees or whether the employees were aware of use and monitoring policies.

Here, the two defendant board members clearly were aware that the corporation had a policy concerning personal use of the company's e mail system. The company did monitor the system and the directors clearly knew that their e mails would not remain confidential due to the company's policies. As a result, the court ordered that the information be produced.

The Delaware Chancery Court limited its findings in the case to an intra-corporate dispute involving a close corporation. Its discussion centered around privacy issues and whether, even if the personal e-mails between client and attorney were privileged communications, the clients reasonably could expect confidentiality when using the company's e-mail system. But the court went further to discuss and pose questions whether the privilege analysis may be different in a more traditional derivative action

involving a stockholder plaintiff with a relatively nominal stake and a board comprising individuals without any affiliation to the suing stockholder. If circumstances were different, such as where the party trying to overcome the privilege was not the corporation, its analysis would not necessarily translate.

These two recent cases highlight the vexing privilege issues that can arise in intra-corporate disputes between shareholders, officers and directors of small and closely-held organizations. As Chambers recognizes, persons with interests adverse to the corporate entity can be denied access to privileged materials which they otherwise might be entitled to absent the dispute. And Information Management holds that the privilege can be lost when adverse directors use the company's e-mail system to communicate with counsel. Communicating policies on personal e-mail use and clearly distinguishing communications as privileged may serve to avoid potentially troublesome controversies should litigation arise.

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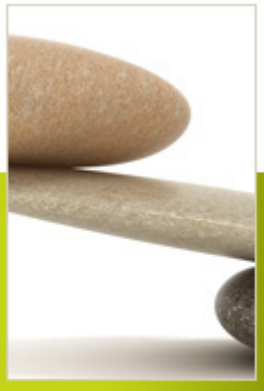

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