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# The Attorney-Client Privilege in Shareholder Litigation: The Need For A Predictable Standard

## INTRODUCTION

The attorney-client privilege<sup>1</sup> has long been an effective means of protecting the confidential communications between a client and his attorney from discovery by adverse parties. However, when the party asserting the privilege owes a fiduciary duty<sup>2</sup> to the party seeking discovery, the latter may defeat the privilege if certain requirements are met. This article focuses on this issue as it arises in the corporate area. In the corporate context the number of people involved and the variety of interests competing for recognition make the interrelationship between the attorney-client privilege and fiduciary duties unusually complex.<sup>3</sup> This article will briefly discuss the

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1. Rule 503(b) and (c) of the Uniform Rules of Evidence provides a succinct definition of this privilege and who may assert it:

(b) General rule of privilege. A client has a privilege to refuse to disclose and to prevent any other person from disclosing confidential communications made for the purpose of facilitating the rendition of professional legal services to the client (1) between himself or his representative and his lawyer or his lawyer's representative, (2) between his lawyer and the lawyer's representative, (3) by him or his representative or his lawyer or a representative of the lawyer to a lawyer or a representative of a lawyer representing another party in a pending action and concerning a matter of common interest therein, (4) between representatives of the client or between the client and a representative of the client, or (5) among lawyers and their representatives representing the same client.

(c) Who may claim the privilege. The privilege may be claimed by the client, his guardian or conservator, the personal representative of a deceased client, or the successor, trustee, or similar representative of a corporation, association, or other organization, whether or not in existence. The person who was the lawyer or the lawyer's representative at the time of the communication is presumed to have authority to claim the privilege but only on behalf of the client.

The related "work product" privilege is defined and discussed in notes 10-19 *infra* and accompanying text. Traditional exceptions to the privilege are examined at notes 20-30 *infra* and accompanying text.

2. A fiduciary relationship generally arises in situations where one party holds a position of superiority and influence over another such that the second party is forced to rely on the first party's continuing good faith. See *Small v. Nelson*, 137 Me. 178, 182, 16 A.2d 473, 475 (1940); *Schweickhardt v. Chessen*, 329 Ill. 637, 649, 161 N.E. 118, 123 (1928); Note, *The Attorney-Client Privilege and the Corporation in Shareholder Litigation*, 50 S. CAL. L. REV. 303, 318 (1977).

3. In a corporation, the board of directors, officers and individual shareholders all have diverse interests. Generally, those who control corporate affairs or formulate policy owe a fiduciary duty to both the corporate entity and the stockholders. See *Pepper v. Litton*, 308 U.S. 295, 306 (1939) (directors); *Woodson v. McAllister*, 121 F.2d 126, 129 (5th Cir. 1941) (officers). A similar duty is owed to minority shareholders by majority shareholders. See *Mount v. Seagrave Corp.*, 112 F. Supp. 330, 333 (S.D. Ohio 1953), *aff'd* 212 F.2d 389 (6th Cir. 1954).

historical background of those aspects of the attorney-client privilege relevant in corporate litigation. It then will examine the parameters of the privilege as asserted by corporate fiduciaries in shareholder litigation.

### HISTORICAL BACKGROUND

In the modern corporate setting, the elements of control and ownership are separate.<sup>4</sup> Since stock is easily alienable on the exchange system, the stockholders tend to change frequently.<sup>5</sup> Thus, despite their "ownership" position, stockholders almost always take a passive role in the corporation's daily decisions and affairs. Nevertheless a fiduciary duty is owed to them, as "management is not managing for itself."<sup>6</sup>

Although a corporation is not a natural person, it is entitled to assert the attorney-client privilege when it is sued either directly or derivatively by its own shareholders.<sup>7</sup> To invoke the privilege, however, there must be a professional relationship between the corporation and its attorney.<sup>8</sup> Moreover, the communications must have been kept confidential by the corporation from their inception; it would be unnecessary to prevent the plaintiff from obtaining information which previously had been available.<sup>9</sup>

The fiduciary relationship between stockholders and management imposes an obvious strain on the attorney-client privilege; since shareholders necessarily rely on management's good faith, they must have access to management's communications if they are to question that good faith effectively. To ensure shareholders an adequate forum for their grievances, the attorney-client privilege should be applied conservatively and the competing interests of the parties should be weighed carefully.

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4. The officers and managers conduct the day-to-day business affairs and decisions of the corporation; the stockholders are the actual owners. A. BERLE AND G. MEANS, *THE MODERN CORPORATION AND PRIVATE PROPERTY* 119-25 (1932).

5. One difficulty stemming from this transience is the allocation of damages after successful shareholder suits. It may be difficult to determine which shareholders are entitled to damages, as those who are shareholders at the time suit is filed may have sold their stock by the time the litigation is completed. Thus, a new shareholder at the termination of a lawsuit could receive damages even though personally incurring no loss from the wrongdoing.

6. *Garner v. Wolfinbarger*, 430 F.2d 1093, 1101 (5th Cir.), *cert. denied*, 401 U.S. 974 (1971).

7. *Radiant Burners, Inc. v. American Gas Ass'n*, 320 F.2d 314, 323 (7th Cir. 1963).

8. The privilege cannot be invoked by a corporation to avoid disclosure when documents funnelled into a lawyer's hands were not previously covered by the privilege. *Id.* at 324.

9. *Id.*

*The Work Product Doctrine*

A related privilege often invoked in shareholder litigation is the attorney "work product" doctrine.<sup>10</sup> Two types of materials are considered work product: (1) the attorney's tangible work; and (2) the attorney's mental impressions formed as a result of that work.<sup>11</sup> These materials, when used by counsel in the course of preparation for litigation,<sup>12</sup> are immune from discovery.<sup>13</sup>

To overcome the work product privilege, the discovering party must show "good cause," *e.g.*, non-availability of witnesses,<sup>14</sup> the contesting party's superior opportunity for knowledge<sup>15</sup> or access to on-the-spot statements,<sup>16</sup> conflicts of interest or lapse of time.<sup>17</sup> With

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10. The work product doctrine was established by the United States Supreme Court in *Hickman v. Taylor*, 329 U.S. 495 (1947). In *Hickman*, prior to litigation, owners of a tugboat which sank for unknown reasons had retained a law firm to protect them against potential lawsuits by the families of 5 drowned crew members. The respondent, a member of the law firm, had privately interviewed the surviving crew members. The family of one of the drowned crew members subsequently filed suit against the tugboat owners and requested discovery of the attorney's memoranda, which included statements made by the survivors. The respondent denied the request on the basis that records of the statements were his work product materials compiled on behalf of his client for use in litigation. The Supreme Court, agreeing with the respondent, held that the materials sought were the attorney's work product and therefore were immune from discovery. The Court noted that the information collected from the witnesses was not protected by the attorney-client privilege because it was collected in anticipation of litigation. *Id.* at 508. In this case, statements of the survivors had been taken a second time at a public hearing and the hearing transcripts were available to the petitioner. Nevertheless, the Court characterized the petitioner's demand for the initial statements taken by the respondent as

an attempt to secure the production of written statements and mental impressions contained in the files and the mind of the attorney . . . without any showing of necessity or any indication or claim that denial of such production would unduly prejudice the preparation of petitioner's case or cause him any injustice.

*Id.* at 509. This doctrine has now been codified. FED. R. Civ. P. 26(b)(3).

11. A lawyer is entitled to a certain degree of privacy in his or her work; organizing information, preparing theories and planning strategies must be done "without undue and needless interference." 329 U.S. at 509.

12. Substantial likelihood of trial is enough to show anticipation of litigation. See Note, *Discovery of Attorney's Work Product*, 12 GONZ. L. REV. 284, 287 (1977).

13. This protection, however, is not absolute. For example, the party seeking discovery must prove that discovery of the evidence is a "necessity" or that undue prejudice, hardship, or injustice will result if discovery is denied. 329 U.S. at 509. The burden can be satisfied by demonstrating "substantial need" or "lack of other available sources." *Advisory Committee's Explanatory Statement Concerning Amendments of the Discovery Rules*, 48 F.R.D. 487, 500 (1969). In contrast, discovery of non-privileged materials is allowed upon a mere showing of relevance. FED. R. Civ. P. 26 (b)(1).

14. See, *e.g.*, *Williams v. Northern Pac. Ry. Co.*, 30 F.R.D. 26, 28 (D.C. Mont. 1962).

15. See, *e.g.*, *State of California v. United States*, 27 F.R.D. 261, 262 (N.D. Cal. 1961).

16. See, *e.g.*, *Brown v. New York, New Haven & Hartford R.R. Co.*, 17 F.R.D. 324, 325 (S.D.N.Y. 1955). On-the-spot statements possibly overlap the category of superior knowledge. See note 14 *supra*. For example, the government may at times know of the existence and content of on-the-spot statements because of its superior opportunity for knowledge. See *Commonwealth Edison Co. v. Allis-Chalmers Mfg. Co.*, 211 F. Supp. 736, 742 (N.D. Ill. 1962).

17. See *Southern Ry. Co. v. Lanham*, 403 F.2d 119 (5th Cir. 1968). In *Lanham*, 3 members

tangible documentary evidence,<sup>18</sup> a party must show that the documents were "essential" to the preparation of its case.<sup>19</sup> Thus, courts must balance the attorney's privacy against the opposing party's "substantial need" and potential hardship. The discretion of the courts in defining "good cause" can result in inconsistent application of the work product doctrine. Therefore, attorneys and their clients often are unable to determine what information will be discoverable by an adverse party.

#### EXCEPTIONS TO AND WAIVER OF THE PRIVILEGE

One traditional exception to the attorney-client privilege particularly relevant in shareholder litigation is the joint attorney exception. This arises when one attorney acts for two parties who have a common interest. In shareholder litigation both shareholders and management have a common interest in the welfare of the corporation. As a result, the same attorney may be consulted by both management and shareholders prior to litigation. An attorney has an obvious conflict of interest when he or she advises parties who later oppose each other in court. The joint attorney situation also occurs where the two parties are separate corporations with interlocking directorates, and a director serving both has communications with a single attorney regarding each of the corporations. The purpose of the joint attorney exception is to alleviate the problems caused by conflicts of interest by making available to both sides those communications which relate to the other party.<sup>20</sup>

A more complex but equally germane inroad into the attorney-client privilege is the crime/fraud exception.<sup>21</sup> Communications

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of a family were killed when their automobile collided with one of the defendant's trains. Following the accident, the railroad's claims agent took statements at the scene from the train's crew and recorded his mental impressions. In the subsequent wrongful death suit, the decedents' family requested production of the results of the agent's investigation. The Fifth Circuit held that the agent's on-the-spot reports were discoverable, but that his mental impressions were not. *Id.* at 131.

18. Tangible documentary evidence is defined as "documents and tangible things, prepared in anticipation of litigation or for trial, by or for a party . . ." *Hickman v. Taylor*, 329 U.S. 495, 509 (1947).

19. *Commonwealth Edison Co. v. Allis-Chalmers Mfg. Co.*, 211 F. Supp. 736 (N.D. Ill. 1962).

20. *Simpson v. Motorists Mut. Ins. Co.*, 494 F.2d 850 (7th Cir. 1974); *La Rocca v. State Farm Mut. Auto Ins. Co.*, 47 F.R.D. 278 (W.D. Pa. 1969).

21. *See, e.g., United States v. Bob*, 106 F.2d 37 (2d Cir.), *cert. denied*, 308 U.S. 589 (1939), involving a prosecution for using the mails to defraud purchasers of stock in gold mines. The court held that before the attorney-client privilege could be overcome, the plaintiff must establish *prima facie* that a crime or fraud has been committed; "mere assertion" of a crime or fraud is not sufficient. Once the plaintiff meets this burden, the attorney is released from

made by a client to an attorney before or during the commission of a crime or fraud are not privileged, while information concerning crimes that have already been committed *are* privileged. When strictly construed, this exception is too limited in scope to be of significant value in shareholder litigation. Many corporate acts which may violate shareholder rights do not constitute a "crime" or "fraud" within the meaning of the exception.<sup>22</sup> Furthermore, although shareholders are afforded liberal opportunities to seek redress for corporate wrongs by virtue of expanded securities laws which provide remedies for "subtle and complex violations of the law,"<sup>23</sup> the prerequisite of showing a crime or fraud before the attorney-client privilege can be defeated diminishes the liberal benefits of the securities laws. Thus, shareholders are not adequately assisted in obtaining information essential to their case. Moreover, when a crime or fraud is alleged, the plaintiff must first make a *prima facie* showing that such violations exist.<sup>24</sup> The burden of proof is difficult for shareholders to meet, since the quantum of evidence sufficient to constitute *prima facie* is unclear.

Several courts, however, have attempted to broaden this exception. Some construe it to include torts in addition to crimes and fraud<sup>25</sup> "where there are other substantial abuses of the attorney-

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his duty to maintain confidentiality unless the communications occurred *after* the commission of the crime or fraud. *Id.* at 40. In *Bob*, a *prima facie* case was established against the defendant through the testimony of a co-conspirator. Since the defendant had consulted with his attorney during the commission of the crime charged, the communications were not privileged. *Id.* The court therefore required the defendant's attorney to testify to conversations and written communications which evidenced the defendant's control of the fraudulent activities. See also *Union Camp Corp. v. Lewis*, 385 F.2d 143, 144 (4th Cir. 1967), in which the court stated that the attorney-client privilege is "withdrawn upon a *prima facie* showing that the lawyer's advice was designed to serve his client in commission of a fraud or crime."

22. See Note, *The Attorney-Client Privilege and the Corporation in Shareholder Litigation*, 50 S. CAL. L. REV. 303, 327 (1977). Fraud also can be a tort. *United States v. Aldridge*, 484 F.2d 655 (7th Cir. 1973); *United States v. Shewfelt*, 455 F.2d 836, 840 (9th Cir. 1972).

23. *The Attorney-Client Privilege and the Corporation in Shareholder Litigation*, *supra* note 22, at 327. Shareholders may sue, for example, under section 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. § 78j(b) (1970) and rule 10b-5 thereunder, 17 C.F.R. § 240.10b-5 (1977). Those provisions prohibit corporations and their officers and directors from making any material misstatements. A discussion of the wide range of activities prohibited by these sections is beyond the scope of this article. For extensive, though slightly dated, treatment of those issues, see generally 1-6 L. LOSS, *SECURITIES REGULATION* (1961 and Supp. 1969). For a recent Supreme Court discussion of the scope of rule 10b-5, see *Ernst & Ernst v. Hochfelder*, 425 U.S. 185 (1976).

24. *Union Camp v. Lewis*, 385 F.2d 143, 144 (4th Cir. 1967); *United States v. Bob*, 106 F.2d 37, 40 (2d Cir. 1939).

25. See, e.g., *Pfizer, Inc. v. Lord*, 456 F.2d 545, 549 (8th Cir. 1972); *Int'l Tel. & Tel. v. United Tel. Co. of Fla.*, 60 F.R.D. 177 (M.D. Fla. 1973); *United States v. United Shoe Mach. Corp.*, 89 F. Supp. 357 (D. Mass. 1950). *Contra*, *Burlington Indus. v. Exxon Corp.*, 65 F.R.D. 26, 40 (D. Md. 1974).

client relationship."<sup>26</sup> These courts have inherently recognized that limiting shareholder protection to situations where the corporation has committed a crime or fraud is too restrictive. The difference between crime and action that is of questionable legality is a difference of "degree, not of principle."<sup>27</sup>

Allegations of waiver can also circumvent the attorney-client privilege and place additional information in the hands of the shareholders. There are a variety of ways to waive the privilege, but only the client, or one acting on the client's behalf, may do so.<sup>28</sup> In the corporate sphere, for example, the privilege is waived when documents are filed in a corporation's general files, for such filing destroys their confidentiality.<sup>29</sup> A corporate client also may waive the privilege by allowing inspection of private files containing communications between the corporation and its counsel.<sup>30</sup> From the shareholder's viewpoint, however, waiver alone is usually of limited utility, since it only applies when corporate management has failed to maintain the confidentiality of its communications. With the aid of competent counsel, management will rarely allow such information to become discoverable.

#### RECENT DECISIONS

##### *Garner v. Wolfinbarger*

In *Garner v. Wolfinbarger*,<sup>31</sup> the Fifth Circuit Court of Appeals attempted to clarify the status of the attorney-client privilege in the corporate setting. Rejecting the traditional theory that the privilege could be challenged only by means of an exception or claim of waiver, the *Garner* court added a new form of attack that permitted shareholders to "show cause" why the privilege should not apply in a particular case.<sup>32</sup>

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26. *Int'l Tel. & Tel. v. United Tel. Co. of Fla.*, 60 F.R.D. 177, 184 (M.D. Fla. 1973).

27. *Garner v. Wolfinbarger*, 430 F.2d 1093, 1103 (5th Cir. 1970). The court explained that past criminal acts are not discoverable by this exception. If a person has already committed a wrong and is now seeking advice, he is entitled to more confidentiality than one who is advised beforehand not to act, and then, having acted, seeks to maintain the confidence. *Id.* at 1103 n.20.

28. 8 J. WIGMORE, EVIDENCE § 2292 (McNaughton Rev. 1961)[hereinafter cited as WIGMORE]. A corporate attorney usually has implied authority to disclose confidential information or otherwise waive the privilege. O'Neal & Thompson, *Vulnerability of Professional-Client Privilege in Shareholder Litigation*, 31 BUS. LAW. 1775, 1792 (1976).

29. *United States v. Kelsey-Hayes Wheel Co.*, 15 F.R.D. 461, 465 (E.D. Mich. 1954).

30. *Id.* at 464. Once litigation is commenced, the privilege is waived if privileged information is voluntarily disclosed pursuant to negotiation; the remaining contents of the opened file, however, are still privileged. *American Optical Corp. v. Medtronic, Inc.*, 56 F.R.D. 426, 431 (D. Mass. 1972).

31. 430 F.2d 1093 (5th Cir. 1970).

32. The terminology used in *Garner* is similar to that used to explain the "good cause"

In *Garner*, stockholders of the First American Life Insurance Company of Alabama (FAL) brought a class action suit directly against the corporation and derivatively against its officers, alleging common law fraud and specific statutory violations relative to the corporation's issuance of stock.<sup>33</sup> The man who served as the corporation's attorney during the period of the challenged stock issuance later became the corporation's president, and held the latter position at the time the litigation ensued. The plaintiffs asked him about the challenged transactions, limiting their questions to his role as an attorney for the corporation. He refused disclosure on the ground that the attorney-client privilege protected his communications to and from the corporation during the time in question. The Fifth Circuit held that the privilege was neither totally unavailable, as the district court had ruled,<sup>34</sup> nor absolutely applicable, as the corporation contended;<sup>35</sup> rather, the correct rule was between these two positions.<sup>36</sup> The court recognized Professor Wigmore's contention that the social benefits that result from the unimpeded flow of information between attorney and client may outweigh the detrimental effect of withholding the substance of that information from the trier of fact.<sup>37</sup> Applying that balancing test, the court acknowledged the presumption that the court is entitled to hear all evidence, and, therefore, a privilege that prevents discovery must be strictly construed.<sup>38</sup>

The *Garner* court carefully analyzed the privilege because the corporate defendants purportedly were acting in the plaintiff shareholders' best interests at all times. Management urged its need for the protection of the privilege by noting the practical impossibility of satisfying all of the shareholders of a sizeable corporation. The obvious irony was that the shareholders representing ninety percent of the ownership of the corporate stock were the parties seeking the information. The court believed that management should not be

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requirements which can defeat the work product privilege. See text accompanying notes 14-19 *supra*.

33. Those statutes invoked included the following: Securities Act of 1933, 15 U.S.C. §§ 77a-77aa (1970); Securities Exchange Act of 1934, 15 U.S.C. §§ 78a-78hh-1 (1970); Investment Company Act of 1940, 15 U.S.C. §§ 80a-1-80a-52 (1970); SEC Rule 10b-5, 17 C.F.R. § 240.10b-5 (1977); Alabama Securities Act, ALA. CODE tit. 53, §§ 28-65 (Supp. 1969).

34. The district court held that the corporation could not assert the privilege against its stockholders. 280 F. Supp. 1018 (N.D. Ala. 1968).

35. 430 F.2d at 1097. Not surprisingly, the American Bar Association appeared as *amicus curiae* and supported the corporation's view of absolute privilege. It feared that without the privilege, counsel might "hedge or soften their opinions." *Id.* at 1102.

36. *Id.*

37. WIGMORE, *supra* note 28, at § 2285(4).

38. 430 F.2d at 1101.

entitled to withhold communications. "Management judgment must stand on its merits, not behind an ironclad veil of secrecy which under all circumstances preserves it from being questioned by those for whom it is, at least in part, exercised."<sup>39</sup>

Thus, the court held that the application of the privilege is not absolute.<sup>40</sup> It concluded that when a corporation is charged with acting adversely to shareholder interests, its attorney-client privilege should be subject to the right of the shareholders to show "good cause" why it should not be available under particular circumstances.<sup>41</sup>

The court listed nine factors to be considered in determining whether or not the shareholders have "good cause" for compelling disclosure of certain documents, despite assertion of the privilege: (1) the number of shareholders and the percentage of stock represented by each; (2) the presence or absence of shareholder good faith; (3) the nature of the shareholders' claim and whether or not it is obviously colorable; (4) the apparent necessity or desirability of the shareholders obtaining the information and whether or not the information is available from other sources; (5) the nature of the claim, *i.e.*, if wrongful corporate action is alleged, whether the action is criminal, illegal but not criminal, or of doubtful legality; (6) the relation of the communications to either past or prospective actions; (7) the relation of the communications to the litigation itself; (8) the extent to which the communication is identified, contrasted with the extent to which the shareholders are blindly fishing; and (9) the risk of revelation of trade secrets or other information which the corporation would desire to keep confidential for reasons independent of the litigation.<sup>42</sup>

The *Garner* court's use of general, rather than specific, indicia for measuring good cause probably was necessary to render the criteria applicable to a variety of unforeseen situations. However, that flexi-

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39. *Id.* The court stated that the attorney's advice or actions should not be altered by the existence of either a potential privilege or possible discovery. The court added that if the privilege were absolute, a corporation could disregard its attorney's advice to abandon a contemplated course of action which the attorney felt was potentially illegal or fraudulent. If the corporation then proceeded with its plan, it could not be found guilty of disregarding the warning because it could invoke the privilege and thereby guarantee secrecy in subsequent litigation.

40. In fact, the court was more inclined to refuse the corporation any invocation of the privilege. The court cited *Pattie Lea, Inc. v. District Court of City and County of Denver*, 161 Colo. 493, 423 P.2d 27 (1967), and held that communications between the corporation and its accountant were not privileged against the shareholders because the initial employment of the accountants was for the benefit of all the shareholders.

41. 430 F.2d at 1103-04.

42. *Id.* at 1104.

bility generates a serious problem: when individual courts are vested with wide discretion, there is a strong possibility that they will reach inconsistent conclusions. Attorneys and their clients are still uncertain as to what information they will have to disclose in subsequent shareholder litigation. Rather than risk possible disclosure of material they would prefer to keep confidential, they may choose to be less than candid with each other. To effectuate the underlying policy of promoting open communication between attorney and client, the availability of the privilege must be assured. Before that assurance is possible, however, workable standards must be created to enable courts to apply the privilege in a predictable, uniform fashion.<sup>43</sup> Although the *Garner* court recognized that this deficiency existed in prior case law, the standards it established fail to provide an adequate solution to the problem. Specifically, the court did not clarify the quantum of proof necessary under any of its factors to destroy the privilege. It did not state the number of shareholders or the percentage of stock ownership necessary to show "good cause." In addition, the court made no attempt either to define "good faith," or to consider the possibility that some of the shareholders may act in good faith while others may not.<sup>44</sup>

#### *Post-Garner Developments*

Despite the vagueness of the Fifth Circuit's opinion in *Garner*, it did represent an ambitious judicial attempt to alleviate the problems peculiar to the attorney-client privilege in shareholder litigation. Nevertheless, after *Garner*, courts that have considered these issues have tended to pay only lip service to the *Garner* rationale and have rested their decisions on more traditional attorney-client grounds where possible. Thus, instead of elaborating upon and perhaps lending strength to the *Garner* indicia, the courts have been reluctant to take affirmative steps to clarify the posture of the attorney-client privilege with regard to shareholder litigation.

Even the Alabama District Court, considering *Garner* on remand,<sup>45</sup> declined to elaborate on the nine factors mentioned in the

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43. The Supreme Court mentioned this problem in *United States v. Topco Assoc., Inc.*, 405 U.S. 596 (1972), an antitrust case. In discussing whether a *per se* rule applied, Justice Marshall said that without *per se* rules "businessmen would be left with little to aid them in predicting in any particular case what courts will find to be legal and illegal under the Sherman Act." *Id.* at 609-10 n.10. *Per se* rules allow no room for the balancing of interests or the reasonableness of behavior. If an act, such as price fixing, were shown, the defendant would automatically be in violation of the Sherman Act.

44. Several issues were not raised in *Garner* at all; *e.g.*, the significance of shareholder "good faith" if the corporation is in fact guilty as alleged; the reason why the nature of the claim is relevant; and what is meant by "apparent" necessity.

45. *Garner v. Wolfinbarger*, 56 F.R.D. 499 (S.D. Ala. 1972).

Fifth Circuit's opinion. Instead, the court relied on facts adduced at a hearing held after the appellate opinion was rendered, most of which evidenced corporate wrongdoing.<sup>46</sup> Only the factor of "wrongful corporate action" was specifically mentioned in finding the attorney-client privilege inapplicable.<sup>47</sup> The court held that the transactions involved were indicative of corporate wrongdoing;<sup>48</sup> however, since this was sufficient to overcome the privilege under the crime/fraud exception,<sup>49</sup> no reference to the appellate court decision was necessary.

In *Bailey v. Meister Brau*,<sup>50</sup> an Illinois district court had an ideal opportunity to clarify *Garner's* "good cause" factors. The plaintiff was a shareholder of Black Company, which had been acquired by Meister Brau. In an attempt to secure information relating to the acquisition, Bailey sought information from Cappadocia, a named defendant who, while an officer of Meister Brau, had become president and chairman of the board of Black shortly before it was purchased by Meister Brau. The communications the plaintiff desired were conversations Cappadocia had had with Meister Brau's counsel in the month preceding the acquisition. Cappadocia denied the plaintiff's request, contending that although he was a director and officer of Black prior to the acquisition, he was also an officer of Meister Brau, and that his conversations with Meister Brau's attorney therefore were protected by the attorney-client privilege.<sup>51</sup>

Instead of applying *Garner*, the court granted the plaintiff a right to see the communications on the ground that Cappadocia, as an officer and director of Black, had a fiduciary duty to inform Black's shareholders of the acquisition plans.<sup>52</sup> The court did use Wigmore's

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46. Oral testimony established that various people had been paid sums of money or granted stock options in order to secure the registration of FAL securities without compliance with SEC regulations. The plaintiffs also showed that FAL had made a public offering of its stock, intentionally failing to register it with the SEC. See Securities Act of 1933, 15 U.S.C. §§ 77a-aa (1970). Asserting the privilege, the attorney for the corporation avoided answering whether or not he had known of these events.

47. 56 F.R.D. at 504.

48. *Id.*

49. The attorney-client communications occurred before and during the commission of these acts. See notes 21-27 *supra* and accompanying text.

50. 55 F.R.D. 211 (N.D. Ill. 1972).

51. *Id.* at 212.

52. *Id.* at 214. In such a situation, Cappadocia, as an officer of Black, could avail himself of the attorney-client privilege only if he were communicating with Black's attorney. Similarly, in his role as a Meister Brau officer, he could hold privileged conversations only with counsel for Meister Brau. As an officer of Black, however, he could not communicate with Meister Brau's counsel and then invoke the privilege against Black's shareholders because, in those roles, the parties would not be in an attorney-client relationship with each other.

balancing test,<sup>53</sup> stating that management's fiduciary duties gave the plaintiff an interest in the communications sufficient to outweigh the interests served by confidentiality.<sup>54</sup> Thus, the only effect *Bailey* had on *Garner* was to extend "good cause" to situations involving two different corporations.<sup>55</sup>

In *Valente v. PepsiCo., Inc.*,<sup>56</sup> a suit was brought by the minority shareholders of Wilson Sporting Goods, Inc. seeking damages from PepsiCo for an allegedly illegal merger with Wilson. The plaintiffs claimed that PepsiCo had made certain untrue representations to them in violation of rule 10b-5<sup>57</sup> and the Securities Exchange Act of 1934,<sup>58</sup> and had committed other acts of fraud.

In the time period immediately preceding the merger, PepsiCo owned a seventy-four percent interest in Wilson which enabled it to elect several of its own officials, including its general counsel, to sit on Wilson's board. The court therefore found that PepsiCo, as a controlling shareholder, owed a fiduciary duty to Wilson's minority shareholders to "protect the interests of the minority from domination and overreaching by the controlling shareholder."<sup>59</sup>

When the plaintiffs requested certain information relating to the fairness of the merger, PepsiCo invoked the attorney-client privilege and denied the request. The plaintiffs responded that the *Garner* ruling rendered the privilege unavailable to a corporation as against those to whom it owed a fiduciary duty.<sup>60</sup>

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53. Plaintiff noted, among other contentions, that the injury to the relationship because of the disclosure must outweigh the benefit gained before the privilege would apply. *Id.* at 213.

54. The factors mentioned were that the plaintiff had alleged wrongful corporate action, and that the disclosures had been clearly identified and were not available elsewhere. 55 F.R.D. at 214.

55. See Note, *The Corporate Attorney-Client Privilege in the Federal Courts*, 22 CATH. LAW. 138, 166 (1976). This distinction arguably is insignificant because one corporation was acquiring the other, and because the opinion was based primarily on the fiduciary relationships that existed. Since the privilege and exceptions are based on fiduciary obligations, it does not matter how many corporations are involved. See also *Duplan Corp. v. Deering Milliken, Inc.*, 397 F. Supp. 1145, 1184-85 (D.S.C. 1975), where the court said that "the fact that the communications are among formally different corporate entities which are under common ownership or control leads this court to treat such interrelated corporate communications in the same manner as intra-corporate communications."

56. 68 F.R.D. 361 (D. Del. 1975).

57. 17 C.F.R. § 240.10b-5 (1977).

58. 15 U.S.C. §§ 78a-78hh-1 (1970).

59. 68 F.R.D. at 364. The issues in this case arose specifically from tax problems. PepsiCo wanted to minimize its tax liability and simultaneously maintain tax benefits already possessed by Wilson. PepsiCo made studies which apparently resulted in a method for PepsiCo to achieve the tax benefits it desired. It was these studies that the plaintiffs were attempting to discover.

60. *Id.* at 366.

Although the *Valente* court noted that the existence of the fiduciary duty was not in itself conclusive, it recognized that the existence of the obligation added weight to the plaintiffs' request. As in *Garner* and *Bailey*, the court found the information discoverable and ordered PepsiCo to make two documents available to the plaintiffs.<sup>61</sup> However, it based its decision on the joint attorney exception, not on the *Garner* indicia. Moreover, it broadened this traditional exception by holding that communications between two attorneys retained by PepsiCo were discoverable. The traditional exception covered communications between an attorney and a client. PepsiCo, the client whose interests were being discussed by the attorneys, had a fiduciary obligation to the minority shareholders of Wilson, and the court would not allow the attorney for PepsiCo to disregard that duty.

The court distinguished *Garner* on the ground that it involved a minority shareholder seeking information from his own corporation, whereas the plaintiff in *Valente* was seeking information from a separate corporation which was a controlling shareholder in Wilson. Thus, the court's conclusion was consistent with *Garner*; however, it was based on the imposition of a fiduciary duty upon the majority shareholder.

The court did mention some of the *Garner* factors, stating that if the plaintiff shareholders were not acting in good faith, if the majority of the shareholders would be better served by the privilege, or if there were trade secrets involved, the privilege might have been allowed.<sup>62</sup> These elements, however, were available to invoke the privilege before *Garner* was decided. Although the *Valente* court made that brief reference to *Garner*, it refused to apply *Garner* expressly.

A more recent opportunity to clarify *Garner* arose in the Northern District of Texas in the case of *Broad v. Rockwell International Corp.*<sup>63</sup> Plaintiffs, debenture holders of the bonds of the defendant corporation (Rockwell), were seeking disclosure of certain attorney-client communications. They were unable to establish a *prima facie* allegation of fraud regarding a securities transaction. Rockwell as-

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61. *Id.* at 368. General counsel to PepsiCo sat on Wilson's board. He owed two separate fiduciary obligations and could not subordinate one to the other. The court said that the fact that his relationship with Wilson was not one of attorney to client was not important. Although it is true that one's knowledge in one capacity carries over to the other capacity and cannot be isolated, the court nonetheless extended the traditional joint attorney exception. Previously both parties were required to have a professional attorney-client relationship with the same attorney.

62. The court did not elaborate further on these factors.

63. [1976-1977 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 95,894 (N.D. Tex. 1977).

serted that *Garner* did not alter the requirement that a party seeking access to privileged documents must make a *prima facie* showing of fraud before the items can be discovered. In holding the information discoverable, the court placed great emphasis on the fiduciary duty Rockwell owed to the plaintiffs. Referring to Wigmore's balancing approach,<sup>64</sup> the court interpreted *Garner* as establishing that when shareholders are involved, the scales may tip in favor of their interests, and that the existence of fiduciary duties to the shareholders alters the traditional justification for the privilege.

Although *Garner* granted shareholder plaintiffs additional opportunities to defeat the privilege, the underlying policy of promoting free communication between attorney and client arguably remained unchanged.<sup>65</sup> This policy persists even when the privilege is overcome by one of the exceptions. The "good cause" standards of *Garner* merely introduced alternative methods of favoring the shareholders' interest in full disclosure over the competing free communication policy.

The *Broad* court made greater use of the *Garner* criteria than previous cases; it noted that there were a "substantial number" of debenture holders suing, that the securities law violation was "obviously colorable," and that the plaintiffs were not "blindly fishing."<sup>66</sup> Nevertheless, this mere recitation of *Garner's* vague standards without amplification is of little predictive value to parties who may need to avail themselves of the privilege or courts which may need to decide privilege issues in the future. In any given case, some of *Garner's* indicia no doubt would be applicable, but as yet, they have not been clarified sufficiently to be amenable to meaningful analysis.

#### CONCLUSION

The fiduciary relationship between the officers and directors of a corporation and the shareholders becomes a matter of serious concern to the corporate attorney when the parties become adversaries in shareholder litigation. The policies favoring the confidentiality of communications between the attorney and corporate representatives must be balanced against traditional concepts of fiduciary duty. These competing concerns have made the application of the

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64. See note 37 *supra* and accompanying text for discussion of this approach.

65. Before the privilege can be available, the harm resulting from the disclosure must be greater than the benefit gained from the correct disposal of the litigation. See WIGMORE, *supra* note 28, at § 2285.

66. [1976-1977 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 95,894 at 91,304.

attorney-client privilege in shareholder litigation particularly difficult.

The traditional arguments for and against the privilege are available to parties involved in this type of litigation. Directors and officers may argue that a corporation, like any other client, deserves the assurance that confidential communications to the corporation's attorney will not be discoverable; otherwise the corporation's representatives may be unwilling to speak freely, and the attorney may not be able to obtain the information necessary to represent his client effectively. Alternatively, shareholders may assert a "substantial need" for an attorney's work product, may rely on the joint attorney or crime/fraud exceptions, or may argue waiver to overcome the attorney-client privilege. The decision in *Garner v. Wolfenbarger* has given shareholders an additional method for challenging the privilege: they may attempt to show "good cause" why the privilege should not be upheld. They may rely on any of the nine factors enumerated in *Garner*, but the factors are so vague and overbroad that the likelihood of defeating the privilege is completely within the trial court's discretion.

The *Garner* court may have hoped to further the policy of disclosure by attempting to afford shareholders a broad opportunity to defeat an asserted attorney-client privilege. In practice, however, the *Garner* factors have not had the far-reaching impact that might have been expected. The few subsequent cases have mentioned *Garner* and occasionally have cited one or two of its factors in alleged support of their rulings; nevertheless, each of those courts actually resolved its privilege issues within the bounds of the traditional exceptions. Disclosure often has been ordered, but courts have declined to articulate what role, if any, the *Garner* factors would play in those determinations.

If *Garner* represented the start of a trend towards fuller disclosure in shareholder litigation, the holdings in *Bailey*, *Valente*, and *Broad* are consistent with that movement. It remains unclear, however, whether parties seeking disclosure are bound by traditional exceptions to the attorney-client privilege or whether they may rely successfully on the broader *Garner* "good cause" factors. Further, if the *Garner* criteria provide an acceptable justification for defeating the privilege, it remains uncertain how broadly or narrowly they should be construed. Given the complexity of modern corporations and their need for regular and extensive contact with their own counsel, the confusion over the scope of the attorney-client privilege is of vital importance. The degree to which confidential communications later may be discoverable may well affect the degree of openness between a corporate client and its attorney. Yet, as the law stands

currently, parties to shareholder litigation are completely unable to predict with any certainty what a court will evaluate when the privilege is asserted and challenged. If corporate clients are to receive any viable protection from the attorney-client privilege, the courts must either clarify *Garner* so that its standards can be applied uniformly, or overtly abandon it.

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