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Quarterly State Compliance Review

By Sandra Feldman

This edition of the Quarterly State Compliance Review looks at some legislation of interest to corporate lawyers that went into effect between Nov. 1, 2012 and Jan. 1, 2013. It also reviews some recent decisions of interest, including two from the Delaware Supreme Court.

In The State Legislatures

Legislation affecting corporations, LLCs and other types of business organizations went into effect in a number of states during the last quarter. Highlights from around the country include the following:

In California, Assembly Bill 1680, effective Jan. 1, 2013, amended provisions of the corporation law governing dissenters' rights to modify the definition of dissenting shares, clarify when fair market value is to be determined, and eliminate a restriction on the eligibility of publicly held shares. In Louisiana, Senate Bill 746, effective Jan. 1, 2013, amended the LLC law to authorize and provide for the manner of converting the state of organization of domestic and foreign LLCs.

In Massachusetts, House Bill 4352, effective Dec. 1, 2012, and in Illinois, Senate Bill 2897, effective Jan. 1, 2013, enacted Benefit Corporation Acts, authorizing the incorporation and operation of a "benefit corporation," which is a

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An Analysis of the DOJ And SEC's Long-Awaited New FCPA Guidance

By H. David Kotz

On Nov. 14, the Department of Justice (DOJ) and Securities and Exchange Commission (SEC) jointly released the long-promised FCPA guidance, entitled "FCPA: A Resource Guide to the U.S. Foreign Corrupt Practices Act" (hereinafter, referred to as the Guide). While the Guide is lengthy and addresses many topics, it is also carefully written in such a manner as to not limit the DOJ and SEC's future ability to broadly interpret the FCPA. Furthermore, there are several areas where hoped-for clarification did not completely materialize.

There are, however, several useful examples and guidance points in the Guide that will assist practitioners and companies in understanding how the FCPA may be interpreted in the future. This article discusses some of the more significant issues that were addressed as well as the ones that were not addressed in as much detail as was hoped.

Definition of 'Foreign Official'

The term "foreign official" is defined as any officer or employee of a foreign government or any department, agency or instrumentality thereof. The phrase "foreign official" has been broadly construed by the United States government to include employees of state-owned entities or state-controlled entities under the theory that these entities are "instrumentalities" of a foreign government. The Guide allows for the expanded definition and explains that whether a particular entity constitutes an "instrumentality" under the FCPA requires a fact-specific analysis of an entity's ownership, control, status and function. The Guide then explains the limited circumstances in which DOJ or SEC enforcement actions have involved foreign officials employed by entities in which a foreign government has less than 50% ownership, *i.e.*, only where the foreign government has "substantial control" over the entity at issue.

The Guide also provides examples of the following relevant factors to be considered in determining whether a representative of a foreign government is a "foreign official":

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FCPA Guidance

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1. The degree or extent of ownership or control the foreign state exercises over the entity;
2. How the foreign state characterizes the entity and its employees;
3. The purposes of the entity's activities;
4. The level of financial support by the foreign state;
5. Whether the governmental end or purpose sought to be achieved is expressed in the policies of the foreign government; and
6. Whether there is a general perception that the entity is performing governmental functions.

Accordingly, although some guidance is added, those who were hoping for a "bright-line" rule for determining when a person is a "foreign official" under the FCPA were disappointed.

'Anything of Value'

While the FCPA's anti-bribery provisions prohibit individuals and businesses from bribing foreign government officials with the "payment of money or anything of value," the statute expressly permits "reasonable and bona fide" expenditures. There has been a great deal of angst in the business community regarding what payments constitute reasonable and bona fide expenditures in the context of travel, entertainment, and gifts.

H. David Kotz serves as a director at Berkeley Research Group, a global expert services and consulting firm where he focuses on internal investigations and matters relating to Foreign Corrupt Practices Act and Anti-Money Laundering regulations. He is also a compliance monitor for firms that have entered into deferred prosecution agreements and similar arrangements with government agencies. Kotz previously served as the Inspector General of the SEC, where he authored the landmark, widely publicized report investigating the failure of the SEC to uncover Bernard Madoff's $50 billion Ponzi scheme.

The Guide provides examples of the types of payments that are improper under the FCPA, such as:

- A $12,000 birthday trip for a government official that included visits to wineries and dinners;
- $10,000 worth of dinner, drinks, and entertainment for a government official;
- A trip to Italy for eight government officials, including $1,000 of pocket money for each official; and
- A trip to Paris for a government official and his wife that consisted primarily of touring activities with a chauffeur-driven vehicle.

Although the FCPA does not have a *de minimus* monetary threshold, the Guide explains that items of nominal value (such as cab fare or promotional items) are unlikely to trigger liability without an intent to influence a foreign official.

'Facilitating Payments'

The FCPA's bribery prohibition contains a narrow exception for "facilitating or expediting payments" made in furtherance of routine governmental action. The facilitating payments exception applies only when a payment is made to further "routine governmental action" that involves non-discretionary acts. Defining what exactly would constitute "routine government action" has been difficult in practice. The Guide provides a few examples, such as processing visas, providing police protection or mail service, and supplying utilities like phone service, power, and water. It also indicates that routine government action does not include a decision to award new business to, or to continue business with, a particular party.

The Guide explains that whether a payment falls within this exception is not necessarily dependent on the size of the payment, although it notes that size can be telling, as a large payment is more suggestive of corrupt intent to influence a non-routine governmental action. However, the Guide states that the facilitating payments exception focuses on the purpose of the payment rather than its value. An example given in the Guide is of an

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Privileges, Clawbacks, and Inadvertent Disclosures

Is Technology the Solution?

By Todd Presnell

Several issues and concerns populate corporate counsels' minds when confronted with e-discovery demands, but two rise to the top: 1) collection and production cost; and 2) inadvertently producing information protected by evidentiary privileges. And these two concerns overlap, producing a Catch-22 dilemma for in-house lawyers. On the one hand, a complete pre-production privilege review of documents constitutes the highest-cost item in the e-discovery process. On the other hand, producing documents with limited to no privilege review risks inadvertent disclosures and privilege waiver, which may result is disastrous ethical and strategy-related consequences.

Many thought that courts' approval of lenient inadvertent disclosure rules and nonwaiver, or clawback, agreements would solve this double-edged problem. But neither avenue proved acceptable in practice. Some courts still found privilege waiver when documents were mistakenly disclosed without acceptable safeguards; and other courts ruled that clawback agreements did not obviate a pre-production privilege review and were not enforceable against third parties in subsequent litigation. And in these situations, parties were neither saving production-associated costs nor protecting their privileged information from discovery.

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A byproduct of technology-assisted review (TAR) software may provide the cost-savings and privilege protections that have eluded corporate counsel during the e-discovery age. This software, designed to identify relevant discovery documents without extensive attorney review, will more readily identify privileged documents and narrow the universe of relevant documents, thereby reducing costs associated with attorneys' privilege review in a way that inadvertent disclosure rules or clawback agreements never could.

Technology-Assisted Review Is Judicially Approved

Technology–assisted review software goes by many names, including "computer assisted review," "predictive coding" and "machine learning." Whatever its moniker, the software, using coding input by humans (lawyers), reviews or scans the universe of potentially relevant documents and identifies those documents most likely to contain relevant information. The initial step calls for the company lawyer to review and code a seed set of relevant documents. The TAR software identifies properties of the seed documents and uses these properties to review the entire set of potentially relevant documents and identify only the most relevant. The software may categorize documents as relevant in a yes/no format or by a relevance range (*e.g.*, a score of 15 on a 100 scale is less relevant, while a score of 85 on a 100 scale is highly relevant).

TAR software has advantages over the traditional linear document review. Statistics show that one advantage is that TAR review identifies relevant documents more accurately than human review. Another advantage is that utilization of TAR software greatly reduces attorney time and fees associated with a human review of the entire document universe. Because of its greater accuracy at a significantly lower cost, many corporate counsel have clamored for greater use of this emerging technology.

But these same counsel were fearful that TAR-related efforts would prove futile unless understood and approved by trial judges. And in the February 2012 decision in *Da Silva Moore v. Publicis Groupe*, 2012 WL 607412 (S.D.N.Y. Feb. 24, 2012), Magistrate Judge Andrew J. Peck became the first to judicially approve, in a written opinion, the use of TAR in the e-discovery context. Judge Peck, a long-time proponent of TAR software, noted that statistics show that computerized searches are at least as accurate as manual review. The court also noted that TAR software yielded much more effective results than traditional keyword searches, which he equated with the children's game "Go Fish!" And noting that TAR reviews require only 1.9% of human review of documents, he said the savings associated with privilege review were too drastic to ignore.

TAR software is not useful in all instances, providing its greatest benefit in large document cases. But with Judge Peck's influence in the e-discovery world, many believe that his *Da Silva Moore* decision will serve as a catalyst for greater use of TAR software in appropriate situations. The question whether to utilize a TAR application should hinge not simply on the volume of documents, but also on how the software can solve corporate counsel's Catch-22 dilemma of controlling privilege review costs while ensuring that privileged documents are not inadvertently disclosed.

Protection of Evidentiary Privileges

Corporate counsel's concerns about releasing privileged information go hand-in-hand with the rise in the volume of electronically stored information. The greater the volume of documents produced, the greater the chance that privileged information is inadvertently released. Courts quickly realized that e-discovery costs were increasing at a prohibitive rate and that attorneys' fees associated with privilege review was a significant portion of those costs. To remedy the growing problem, courts sought to reduce privilege review through the use of lenient inadvertent disclosure rules and nonwaiver or clawback agreements, primary through Federal Rule of Evidence 502.

A clawback agreement is effectively an agreement between the parties

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that, if certain defined protocols are followed, the disclosure of privileged information within a document production will not automatically constitute a waiver of the privilege. Federal Rule of Evidence 502 approves of clawback agreements as a way to avoid privilege waiver, and seeks to extend the nonwaiver doctrine to subsequent litigation in both federal and state courts. Rule 502(e) permits clawback agreements to govern waiver between the parties, but also to nonparties if incorporated into a Protective Order. And, with little regard for the *Erie* doctrine or state automony, Rule 502(f) extends the nonwaiver protection to subsequent proceedings whether in federal or state court.

Rule 502, however, has not turned out to be the cost-saving answer that many thought. The rule only applies to nonwaiver of the attorney-client privilege and the work product doctrine. It completely ignores that companies maintain electronically stored information that may be protected by other evidentiary privileges. For example, a healthcare provider likely maintains information protected by a state-law peer-review privilege; and other businesses maintain information protected by the state-law accountant-client privilege. And whether a Rule 502 sanctioned clawback agreement is enforceable in subsequent state-court proceedings remains unclear, but a likely scenario is that state courts will find privilege waiver regardless of any federal clawback agreement. In short, Rule 502 has limited application and uncertain enforceability that should give corporate counsel pause before relying on clawback agreements as a cost-saving tool.

To be sure, courts' embrace of clawback agreements as an e-discovery cost-reduction method has some basis of support. Some statistics show that these agreements cut privilege-review costs by 50%. Yet, others argue that these costs are not reduced but simply shifted to the opposing party; the producing party's review time and associated costs decrease but the receiving party's review time and costs correspondingly increase. This phenomenon is especially true in commercial litigation where both parties maintain large volume of potentially relevant documents.

Beyond the questionable cost savings, clawback agreements have not proven to be attractive options in practice. Clawback agreements do not obviate lawyer's ethical duty, exemplified in Model Rule 1.6, to competently safeguard against the unauthorized disclosure of her client's confidential information. Even with a clawback agreement in place, many courts have found privilege waiver where the producing party did not act with at least some diligence to identify and withhold privileged documents. And even when enforced, there is no guarantee that a nonwaiver finding in one proceeding results in similar nonwaiver finding in a subsequent proceeding. Consequently, clawback agreements do not necessarily safeguard a client's confidential information, and lawyers relying on them to do so run the risk of breaching state ethical obligations.

A more practical concern with clawback agreements is that a less than thorough privilege review will inevitably result in the production of privileged information. And even when a clawback agreement works perfectly, it is difficult to assess the damage done by permitting opposing counsel to review privileged information. Using whatever cliché you prefer, once privileged information is disclosed, you cannot "unring the bell," "put the toothpaste back in the tube," or "put the genie back in the bottle." In short, you cannot erase privileged information from your adversary's mind, and even when the privileged documents are returned, you can rarely assess how your adversary's review of the information will alter his litigation strategy. Will the information cause your adversary to depose new witnesses, research new legal theories not previously considered, or send discovery into a new subject area? So, while a clawback agreement may, in theory, reduce your client's e-discovery costs, it is difficult to quantify the added costs — including an adverse verdict — that may result from the disclosure of privileged information.

TAR to the Rescue?

So how can technology-assisted review software better solve corporate counsel's legitimate concerns over the issue of reducing costs associated with attorneys' privilege review while taking greater measures to prevent the disclosure of privileged information? There are two ways in which this new technology can alleviate corporate counsel's concerns.

First, TAR software should provide cost-savings that equal or exceed the cost-savings most associate with clawback agreements, but without the risks arising from inadvertent disclosure. Noting that the most significant portion of e-discovery costs come from attorneys' review for privileged information, clawback agreements seek to achieve savings in this area by encouraging less attorney review time. But TAR software will more accurately identify the scope of relevant documents for production and reduce the number of irrelevant documents. The result is that the scope of documents ultimately submitted for attorneys' privilege review is smaller which necessary means that attorney review time is correspondingly shorter. Thus, by using TAR to identify relevant documents, corporate counsel can afford to have a thorough privilege review, completed in less time, and achieve the same cost-savings as she would by using a clawback agreement and a less thorough review. And the cost-savings will be achieved without the ethical and strategy-related problems that arise from clawback agreements and inadvertent disclosures.

Second, while TAR software was designed to take coding and data entered by the client's lawyer and search for electronically stored information responsive to an adversary's discovery request, the same software can be used to identify and separate the privileged information within the company's electronic storage areas. For example, company counsel may identify keyword searches that would likely return privileged information. For attorney-client privileged information, the keywords may be the lawyers' names or words associated with the claim at issue; for peer-review privileged information the

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Success in Mediation

Counterintuitive Strategies

By Richard Shore

If your company or organization finds itself engaged in litigation, chances are that the dispute will be resolved in a conference room rather than a courtroom. Most lawsuits settle before judgment, and in-house counsel increasingly are turning to mediation — negotiation assisted by a third-party facilitator — to resolve their clients' disputes. They hope mediation will be faster and cheaper than litigation, and yield a better result.

But the potential benefits of mediation often are undermined because the participants enter the process with the very litigation-oriented, adversarial mindset they meant to leave behind. They focus on winning the argument rather than getting to yes. They try to game the system, glare across the table, argue about who is right, and just generally pour time and resources into activities that undermine the goal of settlement.

In-house counsel contemplating or involved in mediation should take a step back and consider whether the standard ways of doing things really serve their or their clients' needs. Do they promote your dispute resolution goals? Surprisingly often, the answer is no.

Based on a 20-year track record in ADR and litigation, and insights gleaned in helping clients resolve disputes worth billions of dollars, my emphatic advice to those involved in mediation is to stop doing what comes naturally. Following are four strategies that run counter to much conventional wisdom in the dispute resolution world. They may not be traditional, but properly employed, they work.

Richard Shore is a partner in Gilbert LLP, where he focuses his practice on the resolution of complex, multi-party insurance-coverage and other disputes through negotiation, alternative dispute resolution, and litigation.

1. Let the Other Side Pick The Mediator

Mediation should be speedy, economical, and conciliatory. But parties often kick things off with a mediator-selection process that is complex, expensive, time-consuming, and adversarial. There are some superb mediators with reputations for effectiveness that are well-deserved, and in-house or outside counsel may be familiar with other talented mediators who are less well known. If the other side will agree to one of these individuals, you are off to a good start. But often, due to skepticism, outright distrust, or for some other reason, the other side will not agree to someone you propose.

In that case, let the other side pick the mediator. This engenders cooperation, generates good will, speeds up the process, holds down costs, telegraphs confidence, and introduces you to new mediators you actually might like.

Have your opponent propose two or three names. This allows you to eliminate candidates who have a meaningful conflict or are otherwise unsuitable. But don't reject someone just because the other side views him or her favorably. That can be an advantage. Such a mediator will have more credibility with your opponent than someone who is viewed as completely neutral or as tilting in your favor. Your opponent will have a harder time resisting or discounting the mediator when he or she questions their arguments or pushes them to be more forthcoming in a settlement offer. And such a mediator, wanting to avoid any perception of bias, may bend over backwards to be fair to your side.

Remember that a mediator is not a decision maker and cannot force you to accept a settlement you do not like. So there is little downside risk to accepting a mediator proposed by the other side. And much to be gained.

2. Don't Argue About Who Is Right

Well, not as much as you or your outside counsel want to, anyway. The goal of mediation is not to win an argument; it is to reach a favorable settlement. Some amount of substantive back-and-forth is appropriate and even useful. But scoring substantive points is at most a tactic. Don't let it hijack the process.

The natural tendency of parties in mediation is to try to convince the other side and the mediator that their position is correct and will prevail in litigation. It is of course necessary to acquaint the mediator with the substance of the dispute and generally is useful to have the parties outline for each other their views of the merits. This can be conveyed through brief position statements or copies of briefs filed in litigation. It is a good idea for party representatives to briefly state their respective positions at the outset of the mediation, both to ensure that all of the participants have heard the key opposing viewpoints, and to fulfill the psychological need of each side to have its say. And it is crucial to address substance if there is reason to believe that a decision maker on the other side has been kept in the dark about (or does not understand) the litigation risks his or her side faces.

But usually, by the time mediation occurs, the parties are quite familiar with the factual and legal issues and have had ample opportunity to assess the case. An excessive focus on vindicating your side's arguments can harden positions, engender an antagonistic atmosphere, and divert attention from the goal of settlement. And it is expensive and time-consuming to boot.

Similarly, the practice of some mediators to question the parties about their positions in each others' presence is usually counterproductive. It violates the stricture to "first, do no harm." Where this technique is employed, each side will focus like a laser beam on implied critiques of the other side, while discounting challenges to its own position. Even talented mediators are unlikely to reveal significant issues the parties have overlooked, given the far greater time and resources the parties have devoted to analyzing the dispute, and the fact that they and their counsel often are experts in the subject matter involved.

Get to a negotiation over dollars or the other key settlement terms as quickly as possible. There will be plenty of time to argue over substance later if the mediation fails.

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3. Leave the Litigators at Home

Traditionally, litigators are tasked with both litigating a case and settling it. This generally occurs by default.

Often, it is more effective to create a separate settlement or mediation track led by a lawyer who is not the public face of the litigation. Just as generals wage war and diplomats negotiate peace, the litigators continue to focus their efforts on the adversary process and separate settlement counsel (from the same or a different firm) spearhead negotiation or mediation efforts. Although there may be some additional expense in getting another lawyer up to speed, the benefits of this dual-track approach can far outweigh the costs:

- Settlement counsel approach mediation with a clean slate, untainted by the adversarial atmosphere and even animosity that litigation creates. Once mediation is under way, settlement counsel can stay above the fray of litigation.
- Litigation and settlement require different mindsets. Having one person spearhead both may undercut his or her full engagement in either. Not everyone can switch gears so quickly.
- Settlement windows tend to open when litigation is at its most intense. Cases do often settle on the courthouse steps. Separating litigation and settlement functions allows litigators to charge ahead, maintaining pressure on the other side at crucial moments and ensuring that time and effort are not diverted from important litigation tasks, while settlement counsel can devote total effort to the mediation or other settlement process.
- Although many litigators are great at settlement, litigation and settlement are specialized skills, call on different abilities and personal qualities, and involve a different mindset. In-house counsel should spend at least as much time and effort selecting settlement counsel as they do selecting litigation counsel.

4. Deal with Hard Issues Last

I'm always amazed when a participant in mediation — sometimes even the mediator — says, "Let's get all the issues out on the table right up front." If the goal is to create as many impediments to settlement as possible, that is just the right approach. If the goal is to settle, it is generally far better to focus on a key issue — usually money — first, and leave the other, sometimes harder, issues for later.

From both a psychological and a process standpoint, if the parties have to juggle multiple hard issues all at the same time, the chances of a deal are remote. But if they can focus on a key term, it is easier to reach an agreement on that, and to use it as a foundation on which to build a comprehensive settlement. Once there is agreement on the key term, the parties will tend to feel that there is a deal and that the remaining terms will be worked out in due course. This approach creates momentum rather than impediments.

Indeed, it is often advantageous to leave key issues, or at least their final contours, to be worked out in the process of drafting a written agreement. Deals often fall apart over key substantive issues, but they generally don't fall apart over drafting issues. So consider leaving hard issues until the end, and call them drafting issues. A rose by another name might actually have fewer thorns.

Conclusion

These are some of the counterintuitive strategies that I have found useful in representing clients in innumerable mediations and other settlement efforts over the past two decades. Every dispute is unique, of course, and it is important that those involved in mediation tailor their approach to the particular dispute in question. Perhaps the most important advice for achieving success in mediation is to be creative and innovative and to adapt and readjust as the negotiation proceeds. Mediation and negotiation are fluid processes, and sometimes they benefit from being stirred up a bit.

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keywords may be associated with quality and assessment of care. Whatever the identifiers, the returned information will be used as a seed set for coding, and the TAR software will then scan the remaining universe of documents to locate those most likely to contain privileged information. Corporate counsel can save significant attorney-review costs by simply having the computer review the documents instead. And studies show that the software will actually be more accurate in identifying privileged information, thereby further reducing the possibility of inadvertent disclosure.

Summaries and Practical Tips

With reduction of e-discovery costs and privilege protection paramount considerations for corporate counsel, the following practical tips and summaries should provide focus and alleviate concerns.

- The *Da Silva Moore* decision approving the use of technology-assisted review software will likely increase corporate counsel's desire to utilize the software and achieve greater accuracy at lower costs. Corporate counsel should determine whether this technology is appropriate for her cases.
- Corporate counsel should be aware that inadvertent disclosure rules are not applied uniformly and do not always provide satisfactory safeguards against privilege waiver.
- Corporate counsel should be leery of using clawback agreements. Heralded by some as a protective umbrella, these agreements may create a conflict with counsel's ethical obligations and provide false assurances that nonwaiver

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The Sending and Receipt of Metadata

By Laura Clark Fey and Dylan L. Murray

Metadata is everywhere — in the overwhelming majority of electronically created documents and files. Distinct ethical and legal considerations and duties arise for in-house and for their company's outside counsel, both when sending and receiving electronic documents or files containing metadata. Further, those considerations and duties for in-house counsel and his/her company's outside counsel often differ and/or are dependent upon whether the transmission or receipt of metadata occurs in the context of: 1) discovery (*i.e.*, productions pursuant to a discovery request or subpoena); or 2) non-discovery communications. The sections that follow provide an overview of the ethical and legal considerations in both of those contexts with respect to both the sending and receipt of metadata by in-house counsel and the company's outside counsel.

What Is Metadata?

Metadata is frequently defined, simply, as "data about data." *See* Sedona Conference®, "Commentary on Ethics & Metadata," Public Comment Version (March 2012) (Sedona Commentary on Ethics & Metadata) at 1. Electronic documents and files "usually include[] not only the visible text but also hidden text, formatting codes, formulae, and other information associated with the file," with those various types of information frequently grouped together under the banner of "metadata." *See* The Sedona Principles (Second Edition): Best Practices, Recommendations & Principles for Addressing Electronic Document Production (June 2007), at 60. However, "metadata" can be broken down into many distinct categories, including application (or substantive) metadata, system metadata and embedded metadata.

Application Metadata

Application metadata is created by the application software that created the document or file, and it "reflects substantive changes made by the user." *Aguilar v. Immigration & Customs Enforcement Div. of U.S. Dep't of Homeland Sec.*, 255 F.R.D. 350, 354 (S.D.N.Y. 2008). As an example, types of metadata created by Microsoft Word include (but are not limited to) "track changes," "fast saves," inserting "comments," saving multiple "versions" of a document, and the making of any revisions to the original text of the document.

System Metadata

System metadata consists of information created by a user or an organization's information management system. Examples of types of system metadata include "data concerning 'the author, date and time of creation, and the date a document was modified.'" *Aguilar*, 255 F.R.D. at 354.

Embedded Metadata

Embedded metadata is comprised of data, such as numbers, text or other content, that is input into a file by a user, but which is not usually visible when the file's output display is viewed. Examples include "spreadsheet formulas, hidden columns, externally or internally linked files (such as sound files), hyperlinks, references and fields, and database information." *Aguilar*, 255 F.R.D. at 354-55.

Why Is Metadata Important?

The inclusion of metadata within documents and files can significantly implicate and impact ethical considerations and duties both in the non-discovery context (whenever in-house counsel or his/her company's outside counsel send and receive documents or files [often created by counsel] having metadata); and in the specific discovery context (when a company's electronically stored information ("ESI") is sent, produced or received by an attorney in connection with a discovery request or subpoena). *See* Sedona Commentary on Ethics & Metadata, at iii-iv. This can include ethical duties such as those of confidentiality, competence, and respect for the rights of third persons, as well as duties pertaining to discovery obligations under the applicable rules of civil procedure.

The Non-Discovery Context

Sending Metadata

The ethical duties of confidentiality and competence apply when in-house counsel or his/her company's outside counsel sends documents or files containing metadata to another attorney. The duty of competent representation of a client "requires the legal knowledge, skill, thoroughness, and preparation reasonably necessary for the representation." *See* ABA Model Rule of Professional Conduct, Rule 1.1, "Competence." New revisions to the ABA Model Rules of Professional Conduct (as proposed by the ABA Commission on Ethics 20/20 and approved by the ABA in August 2012) specify that the duty of competence (as set forth in Rule 1.1), and its attendant duty to keep abreast of changes in the law and its practice, includes "the benefit and risks associated with relevant technology." *See* ABA Commission on Ethics 20/20 Proposals (approved in August 2012), at www.americanbar.org, regarding Comment 6 to Rule 1.1. For an attorney, this should include an understanding "that metadata is stored within the majority of electronic files" and that appropriate action needs to be taken to protect it. *See* Crystal Thorpe, "Metadata: The Dangers of Metadata Compel Issuing Ethical Duties to 'Scrub' and Prohibit the 'Mining' of Metadata," 84 *N.D. L. Rev.* 257, 271 (2008).

The duty of confidentiality precludes an attorney from revealing "information relating to the representation of a client" absent informed consent, implied authorization or another applicable exception. *See* ABA Model Rule of Professional Conduct, Rule 1.6, "Confidentiality of Information." The ABA Commission on Ethics 20/20's new revisions impact the issue of the sending of metadata by specifically adding to Rule 1.6 a duty to "make reasonable efforts to prevent inadvertent or unauthorized disclosure of, or unauthorized access to, information relating to the representation of a client." *See* ABA Commission on Ethics 20/20 Approved

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Proposals regarding Rule 1.6 and new paragraph (c).

Additionally, some state ethical opinions have specifically found and stated a duty for attorneys to use reasonable care to prevent disclosure of confidential metadata, such as by "scrubbing" metadata from electronic documents before sending them. *See, e.g.*, New York State Bar Association Opinion 782 (Dec. 8, 2004). This duty would include both: 1) employing reasonable available technical means (such as "scrubbing") to remove confidential metadata prior to sending; and 2) upon discovery that confidential metadata has been sent, acting in a reasonably diligent fashion to notify recipients and to accomplish the return or destruction of such metadata. *See* Sedona Commentary on Ethics & Metadata, at 8.

Receiving Metadata

General Duty to Promptly Notify The Sender

Under ABA Model Rule of Professional Conduct 4.4(b), an attorney has a duty to promptly notify the sender when a document is received (*e.g.*, from outside counsel or in-house counsel at another company) that the recipient attorney knows or reasonably should know was inadvertently sent. *See* ABA Model Rule of Professional Conduct, Rule 4.4, "Respect for the Rights of Third Persons." The ABA Commission on Ethics 20/20's revisions to Rule 4.4(b) expressly apply that same duty to "electronically stored information" that has been inadvertently sent:

> (b) A lawyer who receives a document or electronically stored information relating to the representation of the lawyer's client and knows or reasonably should know that the document *or electronically stored information* was inadvertently sent shall promptly notify the sender.

See Commission on Ethics 20/20 Approved Proposals regarding Rule 4.4(b) (revisions in italics). The majority of state ethical opinions likewise agree that a receiving attorney has a duty to notify the sender of inadvertently sent metadata. *See* Tomas J. Garcia, "Jurisdictional Discord in Applying Ethics Guidelines to Inadvertently Transmitted Metadata," 23 *Geo. J. Legal Ethics* 585, 589 (2010).

In its new revisions, the Commission also clearly recognized situations where an electronic document or file is intentionally sent *but contains* ESI (such as metadata) that was not intended to be included in the transmission. The Commission's revisions to Comment [2] to Rule 4.4 state as follows (as reflected in italics):

> Paragraph (b) recognizes that lawyers sometimes receive a document *or Electronically Stored Information* that was mistakenly sent or produced by opposing parties or their lawyers. *A document or ESI is inadvertently sent when it is accidentally transmitted, such as when an email or letter is misaddressed or a document or ESI is accidentally included with information that was intentionally transmitted.*

See Commission on Ethics 20/20 Approved Proposals regarding Rule 4.4(b) and Comment [2] thereto (revisions in italics).

The Commission further makes clear that "ESI" includes metadata, revising Comment [2] to Rule 4.4 to define the phrase "document or ESI" as including, "in addition to paper documents, email and other forms of ESI, including embedded data (commonly referred to as 'metadata'), that is subject to being read or put into readable form." *Id*. The new revisions to Comment [2] also expressly apply the standard set forth in Rule 4.4(b) to metadata, stating that "[m]etadata in electronic documents creates an obligation under this Rule only if the receiving lawyer knows or reasonably should have known that the metadata was inadvertently sent to the receiving lawyer." *Id*.

The 'Mining' of Metadata

One unique issue in the area of receipt of metadata in the non-discovery context is whether a receiving attorney may ever even view a received file's metadata (often referred to as "mining") in the first place. The ABA and some states take the position that there is no prohibition against reading metadata received from another attorney so long as the duty imposed by Rule 4.4(b) is followed. *See, e.g.*, American Bar Association Formal Ethics Opinion 06-442 (Aug. 5, 2006). Some state jurisdictions also impose no such prohibition unless the receiving attorney has actual knowledge that the electronic document or file contains confidential metadata. *See, e.g.*, District of Columbia Bar Ethics Opinion 341, Review and Use of Metadata in Electronic Documents (September 2007).

However, a number of other jurisdictions impose a general prohibition on the ability of a receiving attorney to examine an electronic document or file for metadata. *See* Andrew W. Perlman, "The Legal Ethics of Metadata Mining," 43 *Akron L. Rev*. 785, 788-89 (2010) (citing seven jurisdictions that generally prohibit the viewing of a document's metadata). Still other state jurisdictions address the issue on a case-by-basis or have not yet addressed the issue at all. *See* Sedona Commentary on Ethics & Metadata, at 11. Given the wide disparity in state ethical rules and decisions on this issue, close examination of the rules and ethical opinions from the practitioner's local state of practice is essential. *See* Joshua Austin, "What to Do About Metadata: A Call to the Illinois State Bar Association for a Formal Ethics Opinion," 22 *DCBA Brief* 34, 35 (April 2010).

The Discovery Context

Producing Metadata in the Discovery Context

Unlike the non-discovery context, where in-house counsel and/or the company's outside counsel may typically freely withhold metadata from electronic documents and files that counsel chooses to send, an attorney in the discovery context, if requested to do so, will generally be required by most courts to produce relevant, responsive and non-confidential metadata included in electronic documents or files absent an assertion of privilege. *See, e.g.*, Fed. R. Civ. P. 26(b)(1) and 34(b)(2)(E)(i); *Williams v. Sprint/United Mgmt. Co.*, 230 F.R.D. 640 (D. Kan. 2005). In short, most courts find that metadata is fully discoverable if it is relevant to a claim or defense of any party. *See id.*

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Metadata

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As such (and also pursuant to an attorney's ethical duty of confidentiality), prior to production, "[a] lawyer has a duty to review metadata for confidential information, including information protected by the attorney-client privilege, in an otherwise non-confidential responsive file." *See* Sedona Commentary on Ethics & Metadata, at 16. Conversely, an act of simply "scrubbing" electronic documents of their metadata prior to a discovery production risks a subsequent finding of spoliation of evidence and/or violation of the ethical duty of fairness to the opposing party and counsel. *See* ABA Model Rule of Professional Conduct, Rule 3.4, "Fairness to Opposing Party and Counsel," paragraph (a).

If an attorney discovers that he has inadvertently produced confidential and/or privileged data (including metadata) in response to a discovery request, then the attorney has the same ethical duties discussed, *supra*, with respect to the non-discovery context. This would include "reasonable efforts" to prevent further authorized disclosure or access to such data, likely including use of reasonable diligence to promptly notify recipients and request the return or destruction of the data. *See, e.g.*, ABA Model Rule of Professional Conduct, Rule 1.6.

Receiving Metadata in the Discovery Context

If a company's outside counsel has served a discovery request that calls for the production of metadata along with responsive electronic documents and files, then the duty of diligence would demand that a review of such metadata be conducted after the production is received. *See* ABA Model Rule of Professional Conduct, Rule 1.3; *see also* Sedona Commentary on Ethics & Metadata, at 18. Proper and due diligence likely also requires reasonable efforts to ensure that the produced metadata is complete and has not been deleted or altered from the file's native format. *See id*. In the discovery context, the restrictions that some jurisdictions place upon metadata "mining" generally have no application and are limited to the receipt of metadata in non-discovery situations where: 1) a discovery request or subpoena is not involved; and 2) the sending of metadata (in contrast to the context of discovery) is typically inadvertent and unintended. *See id*. at 10-11, 19.

In contrast, where an attorney discovers that metadata has been inadvertently produced to her during the course of discovery, the receiving attorney's ethical duties with respect to that metadata should be same as in the non-discovery context. That would mean, for example, if the jurisdiction follows ABA Model Rule 4.4(b) or its substantial equivalent, then the receiving attorney would have a duty to promptly notify the sender. Further, if a receiving attorney is notified of the inadvertent production of a privileged document or data, then Fed. R. Civ. P. 26(b)(5)(B) would require its return or destruction. *See, e.g., Mt. Hawley Ins. Co. v. Felman Prod., Inc.*, No. 3:09-CV-00481, 2010 WL 1990555, at *3 (S.D. W.Va. May 5, 2010).

Ensuring That Metadata Is Not Sent or Produced Inadvertently

Scrubbing: A simple way to avoid the sending of confidential metadata is through the use of scrubbing software, such as Metadata Assistant. Scrubbing software scans and removes metadata from an electronic document or file prior to it being sent as an email attachment. Of course, in the context of discovery, a producing attorney (depending on the nature and scope of the discovery request) may have a duty to produce non-confidential, non-privileged metadata. In that event, the scrubbing of a document prior to production could be held to amount to spoliation of evidence. *See generally* Fed. R. Civ. P. 26(b)(1).

Conversion to Static Images: Metadata can also be eliminated by converting an electronic document or file to a static image, such as a .pdf (or a .tiff) file. However, printing and then scanning a document to .pdf, while eliminating metadata, also eliminates its searchability. Another option is electronically converting (rather than scanning) a document to .pdf, which permits the document to retain its searchability. An electronic document converted to .pdf loses its word processing software metadata, although it will have its own Adobe Acrobat-created metadata, such as the individual who created the .pdf and the date and time of the conversion to .pdf. *See* Sedona Commentary on Ethics & Metadata, at 23.

*Electronic Redaction*s: Although some word processing software offers electronic redaction tools, attorneys should be cautious in electronically producing any documents that have been redacted by such tools because of the danger that the redacted information may actually be retrievable from the document. *Id*. at 22-23. For example, what is thought to be an electronic redaction tool may simply be an overlay (*e.g.*, word processing software's border and shading options) that still permits the supposedly redacted text to be searched, copied and pasted in and from the document. *Id*.

Confidentiality and Other Agreements: In the litigation and discovery context, a company's outside counsel can pursue confidentiality or other agreements (such as non-disclosure and non-waiver agreements) and/or protective orders with opposing counsel concerning such issues as the inadvertent disclosure of metadata or the ability to search and use embedded information. *Id*. at 23. For example, at the start of litigation, counsel for each side can negotiate a confidentiality agreement that provides that any metadata disclosures in communications between them are unintentional and to be promptly deleted.

Conclusion

Although it may be invisible to the eye, metadata cannot be ignored — not when it is present in most documents or files created electronically. In-house counsel and their

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Oklahoma-based company that violated the FCPA when its subsidiary paid Argentine customs officials approximately $166,000 to secure customs clearance for equipment and materials that lacked required certifications or could not be imported under local law and pay a lower-than-applicable duty rate. Another example is where three subsidiaries of a global supplier of oil drilling products and services were criminally charged with authorizing an agent to make at least 378 corrupt payments (totaling approximately $2.1 million) to Nigerian Customs Service officials for preferential treatment during the customs process, including the reduction or elimination of customs duties.

The Guide also notes that labeling a bribe as a "facilitating payment" in a company's books and records does not make it one. It further warns that although true facilitating payments are not illegal under the FCPA, they may still violate local law in the countries where the company is operating.

However, as the Guide largely just reiterates the examples already set out in the statute and references cases that have already been adjudicated, it provides little additional guidance for companies and practitioners. Many commentators had hoped for more clarification in this area.

Due Diligence on Third Parties

The Guide reiterates that companies will be held liable for the conduct of their third parties, such as agents, consultants, and distributors. The Guide discusses how third parties, including agents, consultants, and distributors, are commonly used to conceal the payment of bribes to foreign officials in international business transactions. It notes that risk-based due diligence is particularly important with third parties and will also be considered by the government in assessing the effectiveness of a company's compliance program.

The Guide lists the following "guiding principles" it believes are applicable to all third-party due diligence:

- A third party's qualifications and associations should be understood, including its business reputation and relationships with foreign officials.
- Companies should have an understanding of the business rationale for including the third party in the transaction, including understanding the role of and need for the third party.
- Companies should undertake some form of ongoing monitoring of third-party relationships, including: 1) documenting that the third party is actually performing the work; 2) exercising audit rights; 3) providing periodic training; and 4) requesting annual compliance certifications.

Therefore, due diligence on third parties is critical for any M&A transaction and as part of a comprehensive compliance program and particular focus should be given to the guiding principles provided by the Guide.

Hallmarks of Effective Compliance Programs

The Guide notes that compliance programs that employ a "check-the-box" approach may be inefficient and, more importantly, ineffective. Although the Guide acknowledges that each compliance program should be tailored to a firm's specific needs, risks, and challenges, it also provides its own list of ten "hallmarks" of effective compliance programs, as follows:

1. Commitment from senior management and a clearly articulated policy against corruption, noting that compliance begins with the board of directors and senior executives setting the proper tone for the rest of the company.
2. A code of conduct and compliance policies and procedures, which it classifies as the foundation upon which an effective compliance program is built.
3. Oversight by a member of senior management with sufficient autonomy and resources to be effective, particularly looking at whether a company has assigned responsibility for the oversight and implementation of a company's compliance program to one or more specific senior executives within an organization.
4. Risk assessment and internal audit procedures, noting that one-size-fits-all compliance programs are generally ill-conceived and ineffective because resources inevitably are spread too thin, with too much focus on low risk markets and transactions to the detriment of high-risk areas.
5. Continuing advice and regular training for both new and current employees and third parties, referencing the fact that compliance policies cannot work unless effectively communicated throughout a company.
6. Enforced disciplinary measures for employees who violate the policy and incentives for employees who follow it, citing the fact that a compliance program should apply from the board room to the supply room — no one should be beyond its reach.
7. Comprehensive, risk-based due diligence on third parties and transactions.
8. Mechanisms for an organization's employees and others to report suspected or actual misconduct or violations of the company's policies on a confidential basis and without fear of retaliation, and for an effective, comprehensive internal investigation.
9. Updating the compliance policy through periodic testing and review in light of the constant evolution of a company's business changes over time, as well as changes in the environments in which it operates, the nature of its customers, the laws that govern its actions, and the standards of its industry.
10. Pre-acquisition due diligence and post-acquisition integration for mergers and acquisitions.

These "hallmarks" do not necessarily contain any new ideas, but it is helpful for companies to have a list of issues that it knows the government will certainly look for in their compliance programs.

Conclusion

The Guide does not provide much of the clarification that practitioners

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FCPA Guidance

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and firms were hoping for. Nevertheless, it does offer useful insight into which aspects of FCPA compliance and enforcement the DOJ and the SEC consider most significant, and should serve as somewhat of a minimum standard upon which compliance officers can rely. The Guide is clear that if a company has appropriately invested time and energy into creating and enforcing a comprehensive, effective, and tailored compliance program, the government will give that company credit when making its charging decisions. It also reiterates that the SEC and DOJ will continue to be aggressive in FCPA prosecutions against both companies and individuals.

While Assistant Attorney General Lanny Breuer's description of the Guide as "the most comprehensive effort ever undertaken by either the Justice Department or the SEC to explain [their] approach to enforcing a particular statute" may have been an exaggeration, companies should carefully scrutinize the Guide and consider reevaluating their current FCPA compliance programs in light of the new guidance from DOJ and the SEC.

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corporation formed to pursue a general public benefit. In Mississippi, House Bill 789, effective Jan. 1, 2013, amended provisions of the corporation law dealing with electronic communications, corporate names, shareholder meetings, director liability, mergers, administrative dissolution, and foreign corporations.

In Nebraska, Legislative Bill 854, effective Jan. 1, 2013, amended the LLC and corporation laws to provide that administratively dissolved or revoked LLCs and corporations must apply for reinstatement within five years after the effective date of dissolution or revocation. In New Hampshire, Senate Bill 1532 enacted the Revised LLC Act, which governs domestic LLCs formed on or after Jan. 1, 2013 and all foreign LLCs on Jan. 1, 2013. Domestic LLCs formed before that date will continue to be governed by the previous LLC law until Jan. 1, 2014, unless they elect to be governed by the Revised Act before then. In Oklahoma, Senate Bill 1279, effective Nov. 1, 2012, amended the Professional Entity Act to include, in the definition of "professional service," the services rendered by a licensed alcohol and drug counselor and a licensed behavioral practitioner. And in Tennessee, House Bill 3459, effective Jan. 1, 2013, revised provisions of the corporation law dealing with actions taken without a meeting, dissenters' rights, mergers, share exchanges, conversions, conflict of interest transactions, and inspections of books and records.

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IN THE STATE COURTS

DE Supreme Court Holds That LLC Manager Breached Contractual Fiduciary Duties

In *Gatz Properties, LLC v. Auriga Capital Corporation*, No. 148, 2012 (Del. Supr., Nov. 7, 2012), the minority members of a Delaware LLC sued the manager, who was also the majority member, after he bought out the plaintiffs for a price well below market value. The Delaware Chancery Court held that the managers of Delaware LLCs owe default fiduciary duties of loyalty and care as well as the contractual fiduciary duties imposed by the LLC agreement. The Chancery Court also held that the manager in this case breached both his default and contractual fiduciary duties.

The Delaware Supreme Court affirmed the ruling that the manager breached his contractual fiduciary duties. The court noted that the LLC agreement required a manager entering into a conflict of interest transaction to obtain a fair price. According to the court, this language imposed fiduciary duties even though it did not use the term. The court also agreed with the Chancery Court that the manager breached his duties by, among other things, ignoring a legitimate bid made by a third party, providing the plaintiffs with false information about their own and the third party's bids, and conducting a sham auction.

However, the court also held that the Chancery Court's holding that managers owe default fiduciary duties had no precedential value. The court stated that because the issue of fiduciary duties could be resolved by reference to the LLC agreement, and because no litigant asked the court to resolve the issue, it was unnecessary to decide whether default fiduciary duties exist.

DE Supreme Court Upholds Personal Jurisdiction Under Conspiracy Theory

In *Matthew v. Flakt Woods Group SA*, No. 150, 2012, (Del. Supr., November 20, 2012), a former member and manager of a Delaware LLC filed suit against a Swiss company, claiming that the company conspired with other members and managers to divest him of his interest in a lucrative joint venture between the company and the LLC. The Chancery Court dismissed for lack of personal jurisdiction after finding that the Swiss company did not know that the conspiracy had a nexus to Delaware as required under the conspiracy theory of jurisdiction. The plaintiff appealed.

The Delaware Supreme Court reversed. The court noted that the court must first determine whether Delaware's long-arm statute applied — an issue the Chancery Court did not address. The court then pointed out that as part of the alleged conspiracy the other members and managers filed a certificate of cancellation of the LLC, which, according to the court, constitutes the transaction of business in Delaware. Thus, because the alleged co-conspirators transacted business, the Swiss company transacted business and was subject to personal jurisdiction under the long arm-statute.

The court also held that the record showed that the Swiss company knew

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or should have known that the LLC was a Delaware entity and that therefore there was a Delaware nexus. The court stated that a sophisticated, global business like the Swiss company was likely to have conducted due diligence before entering into a long term venture with a startup, and likely to have investigated when its representative learned of the dispute over the LLC's dissolution. In either case the company would have discovered that the LLC was a Delaware entity.

NY Court of Appeals Upholds Contractual Waiver of Member's Fiduciary Duties

Pappas v. Tzolis, 2012 N.Y. Slip Op. 08053 (Court of Appeals, Nov. 27, 2012), involved a dispute among three members of a New York LLC that owned a lease to a building. The defendant member bought the plaintiffs' membership interests for $1 million and $500,000 respectively. The parties executed a Certificate in which the plaintiffs stated that the defendant, as the buyer, owed no fiduciary duties to them as the sellers. Shortly after the defendant became the sole member he assigned the LLC's lease for $17.5 million. The plaintiffs brought an action alleging, among other claims, that the defendant breached his fiduciary duties by failing to disclose his negotiations for the sublease before buying their interests. The trial court dismissed the complaint, relying on the Certificate. The Appellate Division allowed the breach of fiduciary duty claim to proceed and the defendant appealed.

The New York Court of Appeals reversed. The court noted that a sophisticated principal may release a fiduciary from claims of breach where the relationship is no longer one of unquestioning trust and it is no longer reasonable to rely on the fiduciary's representations without making additional inquiry. In this case the plaintiffs were sophisticated businessmen, represented by counsel. Their allegations made it clear that at the time of the buyout they had an antagonistic relationship with the defendant. Thus they could no longer rely on the defendant as trustworthy and the release contained in the Certificate was valid.

CA Appellate Court: Alter Ego Doctrine May Not Be Used to Circumvent Licensing Statute

In *Twenty-Nine Palms Enterprises Corp. v. Bardos*, E051769 (Cal. App. 4 Dist., Nov. 10, 2012), the plaintiff entered into a contract with the defendant, a sole proprietorship, whereby the defendant was to construct a road and parking lot. The defendant was not a licensed contractor at the time. The plaintiff filed a suit to recover the more than $750,000 it paid the defendant pursuant to a section of California law providing that an unlicensed contractor must disgorge all compensation paid under a contract. The trial court found for the plaintiff. On appeal the defendant's sole proprietor argued that because he was also the sole shareholder and managing officer of a corporation that was a licensed contractor, the court should pierce the corporate veil and find that the defendant was operating under the corporation's license.

The California Court of Appeal rejected the defendant's argument, stating that the alter ego and piercing the corporate veil doctrines were not created to circumvent regulatory requirements. They were founded on equitable principles and are designed to prevent injustice. Here, the sole proprietor admitted he created the defendant to hide the fact that he hired himself to do the work on the contract. The court stated that it failed to see how equity required piercing of the corporate veil to remedy an injustice when the defendant was formed to hide self-dealing. Judgment for the plaintiff was affirmed.

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rulings will apply in subsequent litigation.

- Corporate counsel must diligently protect against the disclosure of privileged information, and the legitimate goals of saving on e-discovery expenses should not impair counsel's diligence.

Conclusion

In considering whether technology-assisted software is the right method to identify and collect electronically stored information, corporate counsel should consider how this technology may make privilege review more accurate and allow for a more thorough attorney review at a more efficient cost.

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Metadata

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company's outside counsel should be aware that distinct ethical duties and considerations arise any time that metadata is sent or received in the course of representing a company. Moreover, the scope and nature of those duties and considerations may directly turn on whether the transmission or receipt of metadata occurs in the context of discovery or non-discovery communications. Finally, practitioners should bear in mind that there are state-specific distinctions with respect to some of those duties and considerations (*e.g.*, the ability to "mine" for metadata) that require close and particular attention to existing and future ethical opinions, rules and amendments in an attorney's state(s) of practice.

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