By Joshua Portnoy

Implied Waiver of the Attorney-Client Privilege in Contractual Disputes

Companies rely heavily on both in-house and outside counsel to assist with the day-to-day drafting, review, and negotiation of contracts, including service agreements, purchase agreements, employment agreements, and settlement agreements, to name a few. In fact, contracts regularly contain voluntary execution provisions indicating that each party has consulted with an attorney and has executed the agreement after independent investigation, voluntarily and without fraud, duress or undue influence. Some agreements even include separate signature blocks for attorneys to acknowledge that they have reviewed and approved the terms of the agreement. Companies do this all the time, so it's no big deal, right? Insert a typical attorney answer—"It depends."

Although I am not a betting man, I would be willing to wager that most companies have, at some point in time, been involved in a contract dispute with another company or individual in which either in-house or outside counsel was involved in the negotiation, review, or drafting of the contract at issue. While many of these disputes are resolved without the need to resort to litigation, there are instances in which the parties reach an impasse and litigation is unfortunately the only option. When this happens, the attorneys may turn from legal counsel to fact witnesses due to their involvement in the drafting and negotiation of the agreement.

In addition to conflicts of interest that arise when an attorney serves as a fact witness, companies must be mindful of the potential risk of waiving the attorney-client privilege. Merely designating an attorney as a fact witness or a 30(b)(6) corporate representative, alone, does not result in a waiver of the attorney-client privilege. *Motley v. Marathon Oil Co.*, 71 F.3d 1547, 1552 (10th Cir. 1995). However, doing so does increase the risk of impliedly waiving the attorney-client privilege, especially where a company is claiming that the contract at issue is ambiguous, a certain provision is unenforceable, or it was fraudulently induced into entering the agreement even though it relied on in-house or outside counsel during the negotiation or drafting process. Under such circumstances, courts have found that companies have impliedly waived the attorney-client privilege pursuant to the "at issue" (or "subject matter") exception.

The purpose of this article is to provide companies and attorneys a greater understanding of when the "at issue" exception applies to avoid falling victim to it. The first part of this article explains the history of the attorney-client privilege and the development of the exception. The article next discusses the application of the "at issue" exception to contract disputes. It then addresses the general scope of the waiver, before concluding with general advice and recommendations that a company should consider to avoid unknowingly waiving the attorney-client privilege and to limit potential harm in the event it does so.

History of the "At Issue" Exception to the Attorney-Client Privilege

Although the Supreme Court recognized in *Upjohn Co. v. United States*, 449 U.S. 383 (1981), that the attorney-client privilege is "the oldest of the privileges for confidential communications to common law," it is important to remember that the privilege (1) is not a constitutional right but is based solely on policy considerations and (2) "has the effect of withholding information from the fact finder." *Fisher v. United States*, 425 U.S. 391, 403 (1976). Because the attorney-client privilege is an exception to the principle of full disclosure, the party asserting protection under the privilege generally bears the burden of proving the applicability of the privilege. Courts also typically construe the attorney-client privilege to its narrowest permissible limits. *See, e.g.*, *Fisher*, 425 U.S. at 403; *United States v. Goldberger & Dubin, P.C.*, 935 F.2d 501, 504 (2d Cir. 1991); *Garner v. Wolfinbarger*, 430 F.2d 1093, 1101 (5th Cir. 1970). Such a narrow construction serves the policy goal "that the ascertainment of as many facts as possible leads to the truth." *Camacho v. Nationwide Mut. Ins. Co.*, 287 F.R.D. 688, 692 (N.D. Ga. 2012).

Consistent with these principles, courts throughout the country have found that the attorney-client privilege is subject to a number of exceptions and may be expressly or impliedly waived. Generally speaking, waiver refers to the intentional relinquishment of a known right. This concept of waiver can be misleading because it does not require that the party knowingly intend to waive the right. Rather, the intent requirement refers to the act resulting in the waiver of the right. Accordingly, courts have found that a party can

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implicitly waive the attorney-client privilege, "even if contrary to the party's actual intent." *Tackett v. State Farm & Cas. Ins. Co.*, 653 A.2d 254 (1995).

One circumstance in which a party impliedly waives the attorney-client privilege exists where the party uses the privilege as a sword by placing information protected by the attorney-client privilege in issue through some affirmative act for its own benefit, while simultaneously relying on the privilege as a shield to protect against the disclosure of potentially harmful information. This implied waiver doctrine is known as the "subject matter" or "at issue" exception to the attorney-client privilege.

The seminal case on the "at issue" exception is *Hearn v. Rhay*, 68 F.R.D. 574 (E.D. Wash. 1975). In *Hearn*, an inmate sued the superintendents of a state penitentiary, alleging that his confinement in the mental health unit violated his constitutional rights under the Due Process Clause and the Eighth Amendment. The defendants denied these allegations and claimed that they were entitled to qualified immunity because they acted in good faith. To counter this defense, the plaintiff sought discovery of legal advice provided to the defendants by the state attorney general related to the plaintiff's confinement. The plaintiff "argue[d] that, by asserting the good faith immunity defense, defendants have ipso facto waived the attorney-client privilege to the extent the privilege would protect information relevant to that defense from disclosure." *Id.* at 580. In support of this argument, the plaintiff relied on instances where courts have found a party to have impliedly waived the attorney-client and other statutory privileges, such as the physician-patient privilege. In considering the plaintiff's argument, the court found that

> All of these established exceptions to the rules of privilege have a common denominator: in each instance, the party asserting the privilege placed information protected by it in issue through some affirmative act for his own benefit, and to allow the privilege to protect against disclosure of such information would have been manifestly unfair to the opposing party. The factors common to each exception may be summarized as follows: (1) assertion of the privilege was a result of some affirmative act, such as filing suit, by the asserting party; (2) through this affirmative act, the asserting party put the protected information at issue by making it relevant to the case; and (3) application of the privilege would have denied the opposing party access to information vital to his defense.

Id. at 581.

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After reaching this conclusion, the court held that even though the defendants did not instigate the lawsuit, they impliedly waived the attorney-client privilege with regard to their good faith defense. The court reasoned:

> [D]efendants invoked the privilege in furtherance of an affirmative defense they asserted for their own benefit; through this affirmative act they placed the protected information at issue, for the legal advice they received is germane to the qualified immunity defense they raised; and one result of asserting the privilege has been to deprive plaintiff of information necessary to 'defend' against defendants' affirmative defense, for the protected information is also germane to plaintiff's burden of proving malice or unreasonable disregard of his clearly established constitutional rights.

Id.

Although the court found that the defendants impliedly waived the attorney-client privilege, it placed "a major limitation" on the application of the "at issue" exception by requiring that a "substantial showing of merit . . . be made before a court should apply the exception to the attorney-client privilege . . . ." *Id.* at 582. Despite this limitation and the fact that the court in *Hearn* restricted its analysis to the specific defense of good faith asserted by the defendants in that case, courts quickly began to apply *Hearn* in other contexts. *See, e.g.*, *McLaughlin v. Lunde Truck Sales, Inc.*, 714 F. Supp. 916 (N.D. Ill. 1989) (applying *Hearn* in suit brought by Secretary of Labor to enjoin defendant from violating the Fair Labor Standards Act); *United States v. Exxon Corp.*, 94 F.R.D. 246 (D.C. 1981) (finding Exxon waived the attorney-client privilege by raising good-faith reliance on representations made by the Department of Energy). And it was not long before courts applied *Hearn* to contractual disputes.

Application of *Hearn* to Contractual Disputes

The first significant case to apply the "at issue" exception to a contractual dispute is *Pitney-Bowes, Inc. v. Mestre*, 86 F.R.D. 444 (S.D. Fla. 1980). In *Pitney-Bowes*, the plaintiff claimed that it was no longer required to pay royalties set forth in certain agreements that it entered with the defendant because the agreements in question had expired. 86 F.R.D. 444, 445 (S.D. Fla. 1980). The plaintiff alternatively argued that the royalty provision in the agreement was unenforceable because it violated public policy and that it had intended to enter into modifications of pure patent licensing agreements. *Id.* at 447.

When the defendant sought all documents and communications supporting the plaintiff's contentions, the plaintiff objected and withheld communications between its attorneys and executives on the basis that those communications were protected by the attorney-client privilege. In response, the defendant moved to compel production of the privileged communications on the ground that the plaintiff waived any claim of privilege that may have existed through "issue injection" of the plaintiff's intent. The court agreed and granted the defendant's motion to compel. In so doing, the court reasoned that the plaintiff "placed in issue the very soul of this litigation the intent of the par-

ties with regard to construction of certain terms of the Agreements" and that the "withheld documents are replete with references to points in time to which the contracts allegedly extended well beyond [the plaintiff's] assertions." *Id.* The court further found that documents "post-dating the contracts" were also discoverable because they supported the defendant's theory that the plaintiff asserted its interpretation of the agreements only after it was "unable to convince [the defendant] to reduce the royalties and thereupon conceived this argument to provide a basis for discontinuing royalty payments altogether." *Id.*

Courts have since relied on *Pitney-Bowes* to conclude that a party waives the attorney-client privilege where it places its intent or state of mind with regard to a contract or certain contractual provisions at issue. For instance, in *Sax v. Sax*, 136 F.R.D. 542 (D. Mass. 1991), the plaintiff brought suit seeking a declaration that a memorandum agreement entered between the parties was valid. Even though both parties were represented by counsel during the negotiation of the memorandum agreement, the defendant counterclaimed on the grounds that the agreement was executed as a result of fraud, misrepresentation, and coercion and that there was no meeting of the minds between the parties because the agreement was vague. Based on these claims, the plaintiff argued that the defendant "waived the right to invoke the attorney-client privilege with respect to discussions he had with his attorney regarding the subject matter of the [m]emorandum [a]greement." *Id.* at 543. The court agreed with the plaintiff, reasoning that the defendant

> raised an issue of his lack of understanding of the [m]emorandum [a]greement in circumstances in which perhaps the only person who would have explained the agreement to him was his attorney. His assertion of the counterclaims in this case was an implicit waiver of the privilege as to the subject matter of the agreement and the circumstances leading to its execution.

Id. at 544.

While *Pitney-Bowes* and *Sax* serve as cautionary tales, they do not mean a party waives the attorney-client privilege every time a contract dispute arises in which the parties relied on attorneys during the drafting and negotiation process. In fact, a number of courts have expressly limited the application of the "at issue" exception to only those situations where a party goes beyond the plain language of the agreement and seeks to introduce extrinsic evidence to support its interpretation of the agreement. *See IMC Chems., Inc. v. Niro Inc.*, Civ. Act. No. CIV.A.98-2348-JTM, 2000 WL 1466495 (D. Kan. July 19, 2000); *St. Louis Convention & Visitors Comm'n v. Nat'l Football League*, Civ. Act. No. 4:95CV2443 JCH, 1997 WL 1419394 (E.D. Mo. Sept. 10, 1997); *Medtronic, Inc. v. Intermedics, Inc.*, 162 F.R.D. 133 (D. Minn. 1995).

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Medtronic is illustrative of this limitation. In that case, Intermedics identified its general counsel as its 30(b)(6) representative with regard to a dispute between the parties regarding a settlement agreement. 162 F.R.D. at 134. When Medtronic asked Intermedics' general counsel questions about the company's intent and understanding of the settlement agreement, Intermedics objected on the ground that the information sought was protected by the attorney-client privilege and the work product doctrine. In response to these objections, Medtronic argued that "Intermedics should be precluded from asserting the attorney-client privilege for 30(b)(6) testimony about Intermedics' interpretation or understanding of the Agreement" because Intermedics put its interpretation and understanding of the settlement agreement between the parties at issue through its pleadings. *Id.* Intermedics, obviously, disagreed and claimed that it had not waived any privilege because its interpretation of the contract was limited to the unambiguous language of the settlement agreement. *Id.*

In addressing these arguments, the court ultimately concluded that Intermedics did not waive the attorney-client privilege so long as it claimed the contract was unambiguous and did not rely on extrinsic evidence to interpret the agreement. *Id.* at 135. However, the court went on to state that

> to the extent Intermedics intends to offer extrinsic evidence to bolster its interpretation of the document, it has waived the privilege attached to Intermedics' interpretation of the document. Once Intermedics offers any extrinsic evidence, it has affirmatively moved outside the four corners of the document to provide an understanding and interpretation of the Agreement. Extrinsic evidence is any evidence beyond the four corners of the Agreement, including testimony or documents, relevant to Intermedics' understanding or interpretation of the Agreement.
>
> Intermedics is asserting the privilege merely as a shield when it does not plan to offer extrinsic evidence of its own. However, if it offers its own evidence of the Agreement, then the privilege is asserted as a sword and a shield.

Id.

This distinction between using the attorney-client privilege "merely as a shield" versus using the privilege "as a sword and a shield" was directly addressed in *IMC Chemicals, Inc.*, 2000 WL 1466495. There, IMC waived the attorney-client privilege by going beyond the four corners of the agreement and offering extrinsic evidence to bolster its interpretation of the contract at issue. Specifically, IMC permitted its attorney to

testify "that he 'proposed' certain language be added to the contract" and willingly divulge the specific language that he proposed. *Id.*, at *12. Based on this testimony, the court found that IMC waived the attorney-client privilege because the attorney's testimony "essentially discloses his legal advice that [IMC] modify the proposed contract with specific proposed language. Such advice is confidential and privileged." *Id.* The court also found that IMC waived the attorney-client privilege when its attorney testified that "*we* wanted to add language that put some sort of a performance guarantee in the contract" and that "*we* wanted to make sure that we got a warranty . . . that would cover us in the event anything would go wrong." *Id.* (emphasis in original). The court reasoned that this testimony revealed IMC's intent regarding the proposed changes and its interpretation of the contract. The court also distinguished the specific testimony of IMC's attorney from other situations where an attorney testifies generally about facts "that outsiders already know or could deduce." *Id.*, at *11. In particular, the court noted that IMC's attorney "revealed more than the mere fact that communications took place and more than general topics of discussion. Certainly, his testimony revealed much more than his activities as attorney for [IMC]." *Id.*

Ultimately, if there is one thing to take away from these cases, it is this—where a company seeks to introduce extrinsic evidence regarding its interpretation or understanding of a contract that was drafted, reviewed, or negotiated by an attorney, it risks waiving the attorney-client privilege with regard to its understanding or interpretation of the agreement. Accordingly, when asserting a claim or defense in a lawsuit relating to a contractual dispute, a company should evaluate whether the claim or defense even arguably implicates privileged communications.

Scope of Implied Waiver

Determining whether a party waived the attorney-client privilege is only half the battle. After concluding that a party has impliedly waived the attorney-client privilege, a court must determine the scope of that waiver. While the waiver is generally limited to the company's intent or state of mind with regard to the contract at issue, courts have found that the waiver extends to documents "post-dating" the execution of the agreement at issue because those documents could relate directly to the company's state of mind. *Pitney*, 86 F.R.D. at 447. Courts also have found that the waiver extends to ordinary work product. *See Belmont Holdings Corp. v. Suntrust Banks, Inc.*, 2012 WL 6430598, at *4 (N.D. Ga. 2012) ("A party waives the protections provided by the work-product doctrine and the attorney-client privilege with regard to a protected subject matter where it selectively and intentionally introduces information and testimony into a litigation."); *Carpenter v. Mohawk Indus., Inc.*, 2007 WL 5971741 at *8, n. 5 (N.D. Ga. Oct. 1, 2007) ("The general principles of waiver [of the attorney-client privilege] . . ., however, would apply to the work product privilege as well."); *Northbrook Excess & Surplus Ins. Co. v. Procter & Gamble Co.*, 1988 WL74462, at *3 (N.D. Ill. 1988) ("Work product immunity may also be waived by the appearance of the attorney as a witness."); *Leybold-Heraeus Tech., Inc. v. Midwest Instrument Co., Inc.*, 118 F.R.D. 609, 614 (E.D. Wis. 1987) ("Upon naming two of their attorneys as witnesses, LHT and LHG assumed the risk that their claim of attorney-client communication and/or attorney work product would be abrogated."); *Handgards, Inc. v. Johnson & Johnson*, 413 F. Supp. 926, 928 (N.D. Cal. 1976) (directing production of a "wide range of materials, including all relevant records, opinion letters, interviews of witnesses, internal files, memoranda, and notes" so that the plaintiff may properly cross-examine and possibly impeach the opinions expressed by the attorneys). Where courts seem to disagree is whether the waiver extends to an attorney's opinion work product. *Cardtoons, L.C. v. Major League Baseball Players Ass'n*, 199 F.R.D. 677, 685 (N.D. Okla. 2001) (noting division among circuits regarding discoverability of opinion work product).

Accordingly, when asserting a claim or defense in a lawsuit relating to a contractual dispute, a company should evaluate whether the claim or defense even arguably implicates privileged communications.

This disagreement has its roots in the language of Fed. R. Civ. P. 26(b)(3), which provides that "[o]rdinarily, a party may not discover documents and tangible things that are prepared in anticipation of litigation or for trial by or for another party or its representative." Some courts have interpreted this language to justify an absolute (or near absolute) protection against the disclosure of opinion work product. *Dir., Office of Thrift Supervision v. Vinson & Elkins, LLP*, 124 F.3d 1304, 1307 (D.C. Cir. 1997) ("Opinion work product, on the other hand, is virtually undiscoverable."); *In re Murphy*, 560 F.2d 326, 336 (8th Cir. 1977) ("In our view, opinion work product enjoys a nearly absolute immunity and can be discovered only in very rare and extraordinary circumstances."); *Duplan Corp. v. Moulinage et Retorderie de Chavanoz*, 509 F.2d 730, 734 (4th Cir. 1974) ("[N]o showing of relevance, substantial need or undue hardship should justify compelled disclosure of an attorney's mental impressions, conclusions, opinions or legal theories."). As the Supreme Court stated,

> [w]ere such materials open to opposing counsel on mere demand, much of what is now put down in writing would remain unwritten. An attorney's thoughts, heretofore inviolate, would not be his own. Inefficiency, unfairness and sharp practices would inevitably develop in the giving of legal advice and in the preparation of cases for trial. The effect on the legal profession would be demoralizing. And the interests of the clients and the cause of justice would be poorly served.

Hickman v. Taylor, 329 U.S. 495, 511, 67 S. Ct. 385, 393–94, 91 L. Ed. 451 (1947).

On the other hand, some courts have found that opinion work product is discoverable where the mental impressions of an attorney are put directly at issue. *Holmgren v. State Farm Mut. Auto. Ins. Co.*, 976 F.2d 573, 577 (9th Cir. 1992); *Ivy Hotel San Diego, LLC v. Houston Cas. Co.*, No. 10CV2183-L BGS, 2011 WL 4914941, at *8 (S.D. Cal. Oct. 17, 2011). For instance, in *Holmgren*, the plaintiff sued State Farm for bad faith in the process of adjusting and settling her claim. 976 F.2d at 576. The court held that the plaintiff was entitled to handwritten memoranda drafted during the underlying litigation by State Farm even though the documents qualified as opinion work product. In so holding, the court reasoned that it "need not decide whether Rule 26(b)(3) provides any protection for material prepared for litigation that has terminated. For even if it does, the rule permits discovery when mental impressions are the pivotal issue in the current litigation and the need for the material is compelling." *Id.* at 577.

Although *Holmgren* involves a claim of bad faith, the reasoning arguably applies where a company interjects testimony that implicates the mental impressions and advice of its attorney regarding the interpretation of a contract. In such a case, the opposing party is arguably entitled to obtain documents and information that relate to the attorney's testimony to perform a thorough and sifting cross-examination of the attorney. This necessarily includes documents and information that contain the attorney's legal advice and opinions regarding the terms of the agreement and the company's understanding of those terms based on what the attorney told it.

Take, for example, a situation where a company sues its customer to enforce a liquidated damages clause contained in an agreement that the parties negotiated through their attorneys. As a defense, the customer claims that the liquidated damages provision constitutes an unenforceable penalty even though it was negotiated and approved by its attorney. In support of this defense, the customer identifies its attorney as a witness on the issue of enforceability. By identifying its attorney as a witness on this issue, the customer has arguably waived the attorney-client privilege with regard to any of communications relating to the enforceability of the provision. There also is a justifiable basis for the company to argue that the customer waived any claim of protection that may otherwise apply to the attorney's opinion work product so that it can perform a thorough and sifting cross-examination of the attorney. Any other result would effectively limit the company's ability to challenge the testimony of the customer's attorney.

If the parties were represented by counsel at any point during the drafting, review, or negotiation process, raising these claims or defenses can result in a waiver of the attorney-client privilege and protection under the work product doctrine.

Takeaways and Practice Pointers

Too often, companies allege that a contract is ambiguous or that they were fraudulently induced into entering an agreement as a claim or defense to a lawsuit without fully considering the possible repercussions of this decision. If the parties were represented by counsel at any point during the drafting, review, or negotiation process, raising these claims or defenses can result in a waiver of the attorney-client privilege and protection under the work product doctrine. A savvy opposing party can take advantage of this and move to compel privileged communications and other information, thereby increasing litigation costs due to the likelihood of additional discovery disputes; the volume of documents that the company will need to collect, review, and possibly produce; and the time and resources spent preparing for and defending depositions of the attorneys and other corporate representatives involved in the drafting, review, and negotiation process. These added costs can serve as leverage for the other side during settlement negotiations.

Fortunately, there are a number of things a company can do to protect itself from unknowingly waiving the attorney-client privilege in a contract dispute or, at least, limiting the potential harm in the event it does waive the privilege. At the outset of any lawsuit, a company should think twice before asserting boilerplate contractual claims or defenses that are based on extrinsic evidence. If the contract language is clear, stick to the four corners of the contract as much as possible. For example, in the situation addressed above involving the enforceability of a liquidated damages provision, the company could avoid waiving the attorney-client privilege and protection under the work product doctrine by relying solely on the plain language of the provision to support its defense.

Companies should also operate under the assumption that nothing is safe from disclosure. Extraneous comments in emails or other documents, no matter how innocent or innocuous they may seem, can always be taken out of context. Similarly, to the extent possible, limit the subject matter of emails and other correspondence to a single topic or related issues. Although it is often easier to address multiple unrelated issues or disputes in a single email, doing so can increase the risk of inadvertently disclosing irrelevant proprietary information to a competitor.

In the end, litigation is a stressful and time-consuming process. There is no need to make the process more stressful or expensive than it already is. Understanding how to avoid waiving the attorney-client privilege and the work product doctrine can help alleviate the stress of litigation and allow a company to focus on the merits of a lawsuit, rather than spending time and resources fighting unnecessary discovery disputes.