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9th Circuit: CFO's Statements to Counsel in an Internal Investigation Can Be Used at Trial

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In highlighting the "treacherous path which corporate counsel must tread under the attorney-client privilege when conducting an internal investigation," the Ninth Circuit recently held that statements made by a chief financial officer to outside counsel could be used in a subsequent criminal action against the officer because he knew his statements would be disclosed to the company's outside auditors.

In *United States v. Ruehle*, No. 09-50161, 2009 U.S. App. LEXIS 21450 (9th Cir. Sept. 30, 2009), the Ninth Circuit held that a district court erred in forbidding prosecutors from calling outside counsel for a company's Audit Committee to testify at the criminal trial of the company's former CFO regarding what was said when the lawyers interviewed the CFO during an internal investigation. Because the CFO knew his statements would be disclosed to third parties, the Court held that the CFO had made the statements without any expectation of confidentiality that would support his subsequent invocation of the attorney-client privilege. The decision addresses the heavy burden company officers bear when attempting to assert the privilege over statements made to company counsel in the context of internal investigations and reinforces the principle that companies or their Audit Committees—and not individual employees—control the decision whether to waive privilege with respect to those investigations.

Background

In May 2006, Broadcom Corporation, a publicly traded semiconductor supplier, came under scrutiny for the suspected backdating of stock options. Broadcom's Board Audit Committee retained Irell & Manella LLP ("Irell") to conduct an internal investigation of the company's option granting process. The same month various plaintiffs filed a derivative suit and a securities class action against Broadcom and several of its officers and directors. William Ruehle, then Broadcom's CFO, was among those personally named as a defendant in the civil actions. Mr. Ruehle reasonably believed that Irell initially undertook to represent both the company and the individual defendants in the civil litigation, himself included.

In June 2006, Irell interviewed Mr. Ruehle as part of the internal investigation. Mr. Ruehle discussed the company's option granting practices and his role as the company's CFO with Irell's attorneys, but the con-

versation did not relate to the ongoing civil litigation, and Mr. Ruehle did not seek legal advice in his individual capacity. At the time of the interview, Mr. Ruehle knew that Broadcom intended to disclose the information obtained through the internal investigation to the company's independent auditors; he knew this because before his interviews he had attended an Audit Committee meeting at which Irell lawyers had announced their intention to share the results of their investigation with Broadcom's auditors. While there was no dispute on this point, the Irell attorneys and Mr. Ruehle gave conflicting testimony at an evidentiary hearing held in Mr. Ruehle's criminal case as to whether, at his interviews, he was provided an "*Upjohn*" warning notifying him that Irell was representing only the company, and not him in his individual capacity.[1] In any event, later that month, after the interviews, Irell told Mr. Ruehle to secure his own counsel with respect to the investigation and the civil suits, and Mr. Ruehle did so.

At some point after the interviews, the Irell attorneys disclosed the substance of Mr. Ruehle's interview to Broadcom's auditors. A year later, in May and June 2007, and at the company's direction, Irell attorneys discussed the details of their conversations with Mr. Ruehle with government investigators.

In June 2008, a federal grand jury indicted Mr. Ruehle (along with Broadcom's founder and former CEO) for conspiracy and securities and wire fraud, in addition to other charges, in connection with alleged stock option backdating. The prosecutors then sought to use testimony from the Irell attorneys as to what Mr. Ruehle had said to them at the June 2006 interviews. Mr. Ruehle objected on the ground that his statements were protected by the attorney-client privilege. At the end of a three-day evidentiary hearing held in February 2009, the district court sided with Mr. Ruehle and ordered that his statements to Irell be excluded from the criminal action against him. The district court also referred Irell to the State Bar of California for failing to get written consent for dual representation of Mr. Ruehle and the company and for disclosing the communications with Mr. Ruehle to third parties.

The Ninth Circuit's Holding

The Ninth Circuit did not reverse the district court's factual conclusion that Mr. Ruehle reasonably believed the company's outside counsel represented him individually with respect to the ongoing civil suit. But, noting that not all attorney-client communications are privileged, the Court concluded that Mr. Ruehle lacked the requisite expectation of confidentiality because he knew the information he provided would be disclosed to Broadcom's independent auditors. Accordingly, the Court reversed the district court's blanket order forbidding the government from calling Irell attorneys to testify to the information they had learned from Mr. Ruehle in June 2006.

Federal Rules Govern Issues Concerning Attorney-Client Privilege

The Ninth Circuit criticized the district court for relying upon California state law to define both the attorney-client relationship and the attorney-client privilege instead of the eight-part test used by federal courts. *See In re Grand Jury Investigation*, 974 F.2d 1068, 1071 n.2 (9th Cir. 1992) (quoting *United States v. Margolis (In re Fischel)*, 557 F.2d 209, 211 (9th Cir. 1977)). Because it had relied on state law, the district court also made a "critical" legal error in adopting the state-law presumption that communications between Mr. Ruehle and the Irell attorneys were privileged. In contrast, under federal common law, the party asserting

[1] The *Upjohn* warning, which outside counsel conducting an internal investigation typically give at the outset of an interview of an individual employee, is based on the Supreme Court's decision in *Upjohn Co. v. United States,* 449 U.S. 383, 393-96 (1981). As part of the warning, counsel advise the employee that they do not represent the employee personally and that anything said by the employee to counsel will be protected by the company's attorney-client privilege, but that the company may choose, in its sole discretion, to waive the privilege in the future.

the privilege has the burden of establishing the privileged nature of the communications. The Court also noted that Mr. Ruehle's failure to define the scope of his claim and his inability to segregate the privileged communications from the non-privileged communications weighed in favor of disclosure.

Expectation of Confidentiality Required

The Court held that Mr. Ruehle's statements to Irell attorneys were not "made in confidence," as required by the test applied by federal courts. Instead, the Court held that Mr. Ruehle's statements were made for the purpose of disclosing the information to outside auditors. According to the Court, the record did not support the notion that Mr. Ruehle, with his knowledge of Broadcom's reporting obligations, believed his statements to Irell were confidential. Mr. Ruehle admitted in the district court's evidentiary hearing that he understood Irell would disclose its findings to independent auditors. He also admitted to believing that the information he provided during the June 2006 interviews was "factual in nature" and the "type of information he understood would be disclosed to third parties."

The Court further noted that Mr. Ruehle failed to object to any of the disclosures made to independent auditors despite being fully aware of meetings where those disclosures were being made. Indeed, he attended several of the meetings between Irell attorneys and the company's independent auditor. Mr. Ruehle also failed to object to the disclosures even after engaging independent counsel; instead, he waited until the "specter of criminal liability arose in 2008" to advocate his view that the statements were confidential. Further, Mr. Ruehle implicitly conceded that the information he provided regarding Broadcom's stock option granting practices was "largely inseparable, if not one and the same" as the information he provided relating to his defense in the pending civil securities litigation. The Court reasoned that his failure to distinguish statements he expected to be disclosed to third parties from statements he expected to remain confidential destroyed his claim of confidentiality as to both sets of information.

Professional Misconduct Is Not Sufficient to Exclude Evidence in Criminal Prosecutions

The Ninth Circuit also rejected Mr. Ruehle's argument that Irell's alleged breaches of professional duties warranted the exclusion of evidence in his criminal prosecution. The Court found "troubling" allegations that Irell had counseled one client to take actions that might be detrimental to the interests of another client without first obtaining informed written consent for dual representation from both parties. Obtaining valid written consent would have required Irell to inform Broadcom and Mr. Ruehle of the "actual and reasonably foreseeable adverse consequences" to the interests of each party. Cal. R. of Prof'l Conduct 3-310(A). Nonetheless, the Ninth Circuit held that Irell's alleged failure to do so did not provide an independent basis for exclusion. The Court noted that a state rule of professional conduct cannot provide an adequate basis for a federal court to exclude evidence that is otherwise admissible. The Court indicated that Mr. Ruehle's failure to establish a credible claim of privilege, and the absence of any evidence that prosecutors were "complicit in" Irell's alleged misconduct, prevented him from successfully relying on Irell's alleged misconduct as grounds for exclusion.

Significance of the Opinion

The *Ruehle* opinion highlights the need to define clearly attorney-client privileged relationships during internal investigations. This is particularly important where outside counsel represent the company and its employees in multiple but related matters. Companies and their counsel must be careful to ensure that directors, officers and employees who are interviewed during an internal investigation are fully aware that

counsel represent the company alone in the investigation and that the company has sole discretion to enforce or waive any attorney-client privilege covering those discussions.

If you have any questions about the content of this alert, please contact the Pillsbury attorney with whom you regularly work, or the authors of this alert.

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