M&A Update

New York Court of Appeals Rejects Extension of Common Interest Privilege to Merger Talks

June 15, 2016

On June 9, 2016, a divided New York Court of Appeals in a much-anticipated ruling held that the attorney-client privilege can only be maintained for communications involving third parties in situations where litigation is pending or reasonably anticipated. The decision reversed an intermediate appeals court's expansion of the privilege to situations where the parties shared a "common legal interest" short of pending or reasonably anticipated litigation. The opinion provides important guidance for corporate boards and financial advisors in determining whether sensitive information disclosed to deal parties and other members of the transaction team may have to be produced to plaintiffs in any subsequent litigations.

Background

The discovery dispute underlying the case involved monoline insurer Ambac Assurance Corporation's attempts to gain access to approximately 400 pre-merger attorney-client communications shared between Bank of America and Countrywide Home Loans in order to support Ambac's contention that Bank of America knew about alleged fraud at Countrywide prior to the merger. Bank of America refused to produce the documents, claiming that they were protected by the common interest privilege. The common interest privilege is an extension of the attorney-client privilege to communications that involve third parties. The trial court ruled that the disputed communications were not protected in the absence of pending or reasonably anticipated litigation. The appeals court recognized that business entities have important legal interests to protect even without the threat of litigation and rejected the litigation requirement that New York courts have historically imposed in cases involving application of the common interest privilege. The New York Court of Appeals overturned the intermediate appeals court's decision because it did not perceive a need to extend the doctrine and "any benefits that may attend such an expansion of the doctrine are outweighed by the substantial loss of relevant evidence, as well as the potential for abuse."

Takeaways

1. The Common Interest Privilege Is Generally Not Available Under New York Law In Situations Involving M&A Negotiations. The Court made clear in resolving an unsettled area of New York law that communications by merger parties with their attorneys in the presence of third parties may be subject to production in discovery should a lawsuit ensue. Merger parties should, therefore, seek to limit third parties as much as possible from participating in discussions where a claim of privilege may be asserted and New York law applies.

2. A Signed Merger Agreement Reflecting The Parties' Agreement To Protect Shared Privileged Information Will Not By Itself Shield The Information From Disclosure. The Court rejected Bank of America's argument that the parties' signed merger agreement evidenced the parties' common legal interest in the merger's successful completion and the parties' commitment to confidentiality. The merger agreement had explicitly directed the parties to share privileged information related to pre-closing legal issues and had purported to protect such information from disclosure.

3. The New York Approach Conflicts With a Number of Other State and Federal Jurisdictions. A number of state jurisdictions and federal courts have held, either through case law or by statute, that the common interest privilege can apply even if litigation is not pending or reasonably anticipated. Delaware, for example, has codified the common interest doctrine in its rules of evidence to allow parties to share attorney-client privileged information on any "matter" of common interest. The majority opinion cited to Delaware's codification of the doctrine in inviting the New York legislature to consider the dissenting opinion's arguments for expanding the doctrine as other jurisdictions have done.

4. Corporate Boards and Their Advisors May Consider Adopting Forum Selection Clauses and Choice Of Law Provisions To Help Avoid Application of New York Law. Including a forum selection clause and choice of law provision in a merger agreement and advisor engagement letters designating a state with a broader take on common interest privilege law as the forum and the applicable law for disputes arising out of the transaction will help to avoid the application of New York law in the event a privilege dispute arises. The Delaware Chancery Court, for example, in looking at which state had the most significant relationship with the communications at issue in a recent case chose Delaware solely based on Delaware forum selection and choice of law provisions in a merger agreement. The court chose to apply Delaware law despite the fact that the communications at issue largely took place in Massachusetts. A corporate board may also consider adopting a forum selection provision in its charter or bylaws covering disputes arising out of the Company's governance and internal affairs. Forum selection bylaw provisions have been

upheld in Delaware, New York, and a number of other jurisdictions in recent years. Because some courts treat privilege questions as a matter of local procedural law that are not governed by a contractual choice of law provision, forum selection clauses should be coupled with a choice of law clause to minimize the risk of adverse rulings.

For a full copy of the opinion, click here.

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If you have any questions, please contact any of the following attorneys or your Cadwalader contact:

William P. Mills	+1 212 504 6436	william.mills@cwt.com
Martin L. Seidel	+1 212 504 5643	martin.seidel@cwt.com
Nathan Bull	+1 212 504 5752	nathan.bull@cwt.com
Heather E. Murray	+1 212 504 6610	heather.murray@cwt.com