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# New York Court of Appeals Limits Common Interest Doctrine in Context of M&A and other Commercial Transactions

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On June 9, 2016, the New York Court of Appeals,[1] in *Ambac Assurance Corp. v. Countrywide Home Loans, Inc.*,[2] reaffirmed New York's narrow interpretation of the "common interest" exception to waiver of attorney-client privilege, holding that it applies only to communications that relate to pending or anticipated litigation. This holding is particularly relevant in the context of mergers and acquisitions ("M&A"), where parties often seek to share information prior to the consummation of a transaction. In transactions where there is no pending or anticipated litigation, parties that are separately represented but share their attorney-client communications will waive the attorney-client privilege.

Under the "common interest" exception, an attorney-client communication disclosed to a third party remains privileged if the disclosure was made in furtherance of a common legal interest shared between the client and the third party. The court's holding reverses a December 2014 appellate court decision, which had held that the common interest exception applied regardless of whether litigation was ongoing or reasonably anticipated at the time the attorney-client communication was shared.

## Summary of the Case

The case arose out of a dispute between Ambac Assurance Corporation ("Ambac") and Countrywide Home Loans, Inc. ("Countrywide") regarding the failure of certain mortgage-backed securities issued by Countrywide and insured by Ambac. Ambac named Bank of America as a defendant in the suit in addition to Countrywide because of the acquisition of Countrywide by Bank of America in 2008. During the course of litigation, Ambac sought communications shared between Bank of America and Countrywide between January 2008, when Countrywide and Bank of America signed their merger agreement, and July

[1] The New York Court of Appeals is the State of New York's highest court.

[2] *Ambac v. Countrywide*, No. 80, NYLJ 1202759677360, at *1 (Ct. of App., June 9, 2016), available at: https://www.nycourts.gov/ctapps/Decisions/2016/Jun16/80opn16-Decision.pdf.

2008, when the acquisition closed. Bank of America refused to produce the communications, claiming attorney-client privilege.

Confidential communications between a client and attorney for the purpose of seeking legal advice are generally protected from disclosure by attorney-client privilege. The privilege is waived, however, when the communication is made in the presence of, or subsequently disclosed to, a third party. Where the common interest exception applies, however, the privilege is not deemed waived if attorney-client communications are shared between two or more parties that share the communications in order to advance a common legal interest.

According to Ambac, Bank of America and Countrywide waived the attorney-client privilege because they were not affiliated entities at the time of disclosure and did not share a common legal interest in pending or anticipated litigation. Bank of America contended that the common interest exception applied because the communications involved matters of a common legal interest between the parties, despite the absence of pending or anticipated litigation. The trial court agreed with Ambac, holding that, under New York law, the common interest exception does not apply in the absence of pending or anticipated litigation.

In a decision that broke with over 20 years of precedent in New York State – but was consistent with decisions from several federal and state courts – the intermediate appellate court reversed the trial court, holding that the communications at issue need not relate to pending or anticipated litigation for the common interest exception to apply. The question was then certified to the Court of Appeals to determine whether, under New York law, there must be pending or anticipated litigation to invoke the common interest exception.

## The Court of Appeals' Decision

In a widely anticipated decision, the Court of Appeals held that the common interest exception applies only where litigation is pending or anticipated. The court reasoned that when two or more parties are engaged in, or reasonably anticipate, litigation in which they share a common interest, the threat of mandatory disclosure may "chill the parties' exchange of privileged information and therefore thwart any desire to coordinate legal strategy." Thus, the common interest exception is necessary to promote candor between the parties. By contrast, that rationale disappears where the parties merely share a common legal interest in a commercial transaction or other "common problem," but do not reasonably anticipate litigation. "Put simply," the court said, "when businesses share a common interest in closing a complex transaction, their shared interest in the transaction's completion is already an adequate incentive for exchanging information necessary to achieve that end."

The court feared that extending the scope of "common legal interests" to situations not involving pending or anticipated litigation could result in the loss of

evidence of a wide range of communications between parties who assert common legal interests but who really have only non-legal or exclusively business interests to protect. The court noted that it was not deciding what it means to share common legal interests in pending or anticipated litigation. "We hold only," the court wrote, "that such litigation must be ongoing or reasonably anticipated, and the exchanged communication must relate to it, in order for the common interest exception to apply."

## The Federal and State Countertrend

In contrast, several recent federal and state court decisions have eliminated the requirement of pending or anticipated litigation from the common interest exception, including a 2015 decision by the United States Court of Appeals for the *Second Circuit in Schaeffler v. United States*, 806 F.3d 34 (2nd Cir. 2015). *Schaeffler* held that the common interest exception applies whenever "a joint defense effort or strategy has been decided upon and undertaken by the parties and their respective counsel," and thus the dispositive issue is whether the parties share a "common interest [that is] of a sufficient legal character to prevent a waiver by the sharing of those communications," not whether they are involved in an existing or anticipated litigation. Other federal appellate courts, including the Third,[3] Seventh,[4] Ninth,[5] and Federal Circuits,[6] have similarly ruled that the common interest exception is applicable regardless of whether attorney-client communications relate to pending or anticipated litigation, as have the Massachusetts Supreme Judicial Court,[7] the Delaware Chancery Court,[8] and the New Mexico Court of Appeals.[9]

The New York Court of Appeals acknowledged this trend, but refused to follow suit, finding that "the policy reasons for keeping a litigation limitation on the common interest doctrine outweigh any purported justification for doing away with it . . ." The *Ambac* decision has accordingly prolonged a situation in which waiver of the attorney-client privilege may depend upon complex choice of law rules as well as the particular forum in which parties find themselves. If, for example, a federal court in the Second Circuit exercises jurisdiction under a federal law or regulation, federal law regarding privilege will apply, and the pending or anticipated litigation requirement would not apply to the common interest exception. On the other hand, if a federal court in New York exercises jurisdiction simply because the parties are of diverse citizenship, state law will apply, the *Ambac* decision will control, and the pending or anticipated litigation requirement will apply.

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3 *In re Teleglobe Commc'ns Corp.*, 493 F.3d 345, 364 (3d Cir. 2007).
4 *United States v. BDO Seidman, LLP*, 492 F.3d 806, 816 (7th Cir. 2007).
5 *United States v. Zolin*, 809 F.2d 1411, 1417 (9th Cir. 1987).
6 *In re Regents of the Univ. of California*, 101 F.3d 1386. 1390 – 91 (Fed. Cir. 1996).
7 *Hanover Ins. Co. v. Rapo & Jepsen Ins. Servs., Inc.*, 449 Mass. 609, 616 (2007).
8 *3Com Corp. v. Diamond II Holdings, Inc.*, 2010 WL 2280734, *7 (Del. Ch. 2010).
9 *S.F. Pac. Gold Corp. v. United Nuclear Corp.*, 143 N.M. 215, 222 (2007).

## Practical Tips in Light of *Ambac*

Obviously, the surest way to protect against the inadvertent waiver of the attorney-client privilege is for M&A and other practitioners to manage transactions so as to avoid the disclosure of privileged material. Recognizing that complete nondisclosure may not be practicable in all cases, parties will need to structure their communications, and any written common interest agreements, to offer the best possible protection of the privilege. For example, given that mergers are prone to litigation and regulatory challenges, it may be desirable for parties to specifically reference the possibility of litigation in their common interest agreements. However, parties should be mindful that doing so will not guarantee preservation of the privilege and may ultimately trigger burdensome document preservation obligations. In addition, as the *Ambac* court noted, engaging a single law firm to address common legal issues may, in certain circumstances, be effective in preserving the privilege. Finally, while perhaps an unintended consequence of the Court of Appeals' decision, in cases where the parties anticipate the need to disclose privileged material, parties may seek to avoid the application of New York law (by, for instance, incorporating choice of law provisions into the parties' common interest and other non-disclosure agreements) and instead invoke the laws of more protective jurisdictions (Delaware, for example). In all cases, however, parties to mergers and other commercial transactions must balance the need for disclosure against the risk of waiver of the privilege.

## Conclusion

The Court of Appeals' decision affirms New York's narrow interpretation of the common interest exception. Although the decision is in direct contrast to some recent state and federal court decisions that have eliminated the element of pending or anticipated litigation from the exception, parties engaged in transactions that may be governed by New York law should be mindful of the court's decision. It is now clear that language in non-disclosure agreements and merger agreements asserting a commonality of legal interest cannot reasonably be relied upon to preserve attorney-client privilege under New York law, in the absence of pending or anticipated litigation.

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If you have any questions, please reach out to the people on the right or your usual Linklaters contact.



## Contacts

For further information please contact:

**Paul Hessler**
Partner
(+1) 212 903 9132
paul.hessler@linklaters.com

**Lance Croffoot-Suede**
Partner
(+1) 212 903 9261
lance.croffoot-suede@linklaters.com

**Adam Lurie**
Partner
(+1) 202 654 9227
adam.lurie@linklaters.com

**James Warnot**
Partner
(+1) 212 903 9028
james.warnot@linklaters.com

**Brenda DiLuigi**
Counsel
(+1) 212 903 9080
brenda.diluigi@linklaters.com

**Kate Machan**
Associate
(+1) 212 903 9289
kate.machan@linklaters.com

**Sean Mooney**
Associate
(+1) 212 903 9209
sean.mooney@linklaters.com

**Sean Solomon**
Associate
(+1) 202 654 9260
sean.solomon@linklaters.com

1345 Avenue of the Americas
New York, NY 10105

Telephone (+1) 212 903 9000
Facsimile (+1) 212 903 9100