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A legal update from Dechert's Financial Services and Securities Litigation and White Collar Litigation Groups

Federal Court Rules on Critical Tool in Internal Investigations: the Employee Interview

If a company suspects that its employees may have been involved in illegal activity, speed in conducting the internal investigation is essential. Often the most critical component of an effective internal investigation is promptly conducting employee interviews. To facilitate investigation by counsel, it is usually appropriate for the company to require employees to participate in these interviews. It may even be appropriate to advise employees that they are subject to discipline and/or termination should they decline. A recent Fourth Circuit decision, *In Re Grand Jury Subpoena*,¹ drives home important lessons for companies conducting internal investigations.

At the outset of each interview, companies must ensure that outside investigating counsel states:

- Investigating counsel represents the company and not the employee
- The interview is covered by the company's attorney-client privilege
- The company may waive that privilege at any time without notice to the employee

It is critical that investigating counsel ensure that the employee understands these warnings. *In Re Grand Jury Subpoena* makes it clear that disclosures of this type are the bare minimum to sufficiently protect the company's attorney-client privilege and to avoid inadvertently creating an attorney-client

relationship between outside corporate counsel and the company's employees.²

In Re Grand Jury Subpoena

In *In Re Grand Jury Subpoena*, the Fourth Circuit upheld the trial court's refusal to quash grand jury subpoenas that sought outside counsel's reports on interviews conducted as part of an internal investigation. The case arose out of a familiar fact pattern. Outside counsel was conducting an internal investigation for AOL Time Warner ("AOL") that focused on AOL's relationship with PurchasePro, Inc. Presumably, AOL had some notion that certain of its employees may have been engaged in illegal conduct.

Investigating counsel sought to interview a number of employees during its internal investigation so that the company could quickly ascertain whether any wrongdoing had occurred, and whether it would consider disclosing such wrongdoing to the government to demonstrate the company's cooperation with the government's investigation.

¹ *In Re Grand Jury Subpoena*, Nos. 04-4410, 04-4411, 04-4673 (4th Cir. July 18, 2005).

² Creating an attorney-client relationship with an employee may pose problems for both the company and investigating counsel. Indeed, *In Re Grand Jury Subpoena*, the court stated, "the court would be hard pressed to identify how investigating counsel could robustly investigate and report to management or the board of directors of a publicly traded corporation with the necessary candor if counsel were constrained by ethical obligations to individual employees." Slip op. at 10. There may, however, be situations in which investigating counsel can represent employees in proceedings subsequent to the internal investigation, where there is no basis to conclude there is a conflict.

During the internal investigation, investigating counsel interviewing one employee stated:

We represent the company. These conversations are privileged, but the privilege belongs to the company and the company decides whether to waive it. If there is a conflict, the attorney-client privilege belongs to the company.

Memoranda from the interview indicated that investigating counsel also explained that they “could” represent the employee as well, “as long as no conflict appeared.” The employee was interviewed again by investigating counsel three days later. At the beginning of this interview, investigating counsel reiterated that they represented the company, that the privilege belonged to the company, and that the employee could retain personal counsel at the company’s expense.

Two other employees were interviewed and were given similar statements regarding representation by outside counsel. Investigating counsel made the following statement to both employees:

We represent the company. These conversations are privileged, but the privilege belongs to the company and the company decides whether to waive it. You are free to consult with your own lawyer at any time . . . We can represent [you] until such time as there appears to be a conflict of interest, [but] . . . the attorney-client privilege belongs to AOL and AOL can decide whether to keep or waive it.

At the end of the interview, one of the employees asked whether he needed personal counsel. One of the investigating attorneys stated that he did not recommend it, but that he would tell the company not to be concerned if the employee retained personal counsel.

The Securities and Exchange Commission (“SEC”) launched an investigation of AOL and PurchasePro, which was followed by a criminal investigation. AOL ultimately agreed to waive the attorney-client privilege and to produce documents in response to a grand jury subpoena seeking material about its internal investigation of the AOL-PurchasePro relationship. After AOL agreed to waive the privilege, the employees moved to quash the subpoenas on the grounds that each employee had an individual attorney-client relationship with outside counsel. This claim was based upon statements made by outside counsel in the interview that it “can” or “could” represent each employee.

The district court refused to quash the subpoenas and was affirmed by the Fourth Circuit. The Fourth Circuit based its decision on three factors:

- There was no evidence that outside counsel told the employees that they represented them or that the employees asked to be represented by them
- There was no evidence that the employees ever sought personal legal advice from the investigating attorneys, nor was there evidence that personal legal advice was rendered
- The employees were each advised that the information they were providing to the company’s outside counsel could be disclosed at the company’s discretion

The Importance of Clearly Articulated and Comprehended *Upjohn* Warnings

Based upon the facts in the record, it appears that part of the reason why the privilege issue was litigated *In Re Grand Jury Subpoena* was that the employees being interviewed may not have understood that they were not being represented during the interview by investigating counsel.

The set of statements or warnings to be given at the outset of an interview has come to be known as the *Upjohn* warnings. The name derives from the Supreme Court decision in *Upjohn Co. v. United States*, 449 U.S. 383 (1981), in which the Court held that the attorney-client privilege between a company and investigating counsel protected communications between investigating counsel and the company’s employees. The Court recognized that a protected mechanism for gathering facts from employees was necessary for the company to obtain legal advice from investigating counsel.

In the wake of *Upjohn*, it has become common practice for the following steps to be taken at the outset of an employee interview:

- Investigating counsel must clearly state that counsel represents the company and does not represent the employee being interviewed³

³ Given the possibility that an employee interview could result in the interests of the employee diverging from the interests of the company, this warning should be issued as part of the investigating attorney’s ethical obligations. Rule 1.13 (d) of the ABA Model Rules of Professional Responsibility provides that “[i]n dealing with an

- Investigating counsel must state that the information learned during the interview is privileged to the company, and that the company alone will determine whether to provide such information to the government without consulting the employee
- Investigating counsel must make clear to the employee that the information discussed at the interview is to be kept confidential so that the company's privilege can be preserved; this explicitly reinforces that the information covered in the interview is covered by the company's privilege
- Each employee interviewed should affirmatively state that he or she understands the warnings given by investigating counsel

In Re Grand Jury Subpoena reinforces how important it is for investigating counsel to give the full *Upjohn* warnings. Because the Fourth Circuit found no facts in the record supporting the existence of an attorney-client relationship between investigating counsel and the employees, the failure of investigating counsel to give the full *Upjohn* warnings did not, in this case, have adverse consequences for the company. However, the Fourth Circuit clearly expressed that it did not endorse what it referred to as the "watered-down" *Upjohn* warnings issued by counsel conducting the AOL-PurchasePro internal investigation.

A non-watered-down version certainly would include a definitive statement that outside counsel did not represent the individual employees. It also would not have included a statement to the effect that counsel "could" represent the individual or the expression of counsel's opinion that the individual did not need separate representation. If investigating counsel had ensured greater clarity on these issues, there likely would have been an understanding that investigating counsel represented the company (and not the employee). If these steps would have been taken by investigating counsel, there likely would have been no room for the employees to argue that an attorney-client relationship between investigating counsel and the employees had been formed.

organization's directors, officers, employees, members, shareholders, or other constituents, a lawyer shall explain the identity of the client when it is apparent that the organization's interests are adverse to those of the constituents with whom the lawyer is dealing."

The Feared Question: Do I Need a Lawyer?

One of the complexities of internal investigations is that they often create situations that require not only legal judgments but also strategic and corporate policy considerations as well. One situation that raises a variety of issues is when an employee asks investigating counsel whether he or she needs a lawyer. One of the employees in *In Re Grand Jury Subpoena* asked this very question. Investigating counsel, after previously indicating that he "can" represent the employee individually, responded by saying "I don't recommend it."

The Fourth Circuit, in summary fashion, declared that investigating counsel had not provided personal legal advice to any of the employees and that the employees had not sought such advice. The latter point is debatable given that at least one employee asked whether he needed his own lawyer. In addition, the court, without explanation, concluded that the response, "I don't recommend it," did not constitute personal legal advice. This statement could be construed as legal advice, but it was not enough for the court to find that an attorney-client relationship existed between investigating counsel and the employee in the context before it.

On these facts, a court could have found, at least as to the employee who asked whether he needed a lawyer, that personal legal advice had been rendered. This statement could have created the basis for a finding that an attorney-client relationship existed between the investigating counsel and the employee.⁴ Handling the "do I need a lawyer" question is a potential minefield for the company and investigating counsel. From the company's perspective, there are potential problems with either a "yes" or "no" answer by investigating counsel. A "yes" answer risks slowing down the internal investigation to wait for the employee to retain counsel. A "no" answer may lead to claims against the company and/or investigating counsel if the employee ultimately suffers legal consequences as a result of participation in the interview without counsel.

At the outset of an internal investigation, the company may decide that investigating counsel should decline to

⁴ This is more than a theoretical possibility. For example, in *In Re Grand Jury Subpoenas*, 144 F.3d 653 (10th Cir. 1998), the Tenth Circuit upheld the existence of the personal attorney-client privilege between investigating counsel and an officer of the company. The privilege was based upon "confidential communications between [the officer and investigating counsel] as to his personal situation."

answer the “do I need a lawyer” question. This response, of course, risks alienating the employees being interviewed. Alternatively, if the company is concerned that some of its employees will ask the “do I need a lawyer” question, it may wish to take steps at the outset of the internal investigation to make sure that separate counsel will be available if employees ask whether they need separate representation.⁵

The company may not be in a position to adopt either of these approaches at the outset of an internal investigation. Often investigating counsel must have candid discussions with the company’s senior executives to help the company frame the internal investigation and to determine how the company should proceed. In these discussions, and perhaps in other discussions between investigating counsel and company employees, the company may want to allow investigating counsel to respond to the “do I need a lawyer” question.

The following steps can be taken to address the question while minimizing the risk that a court will find that personal legal advice was rendered, thus preventing the basis for finding the existence of an attorney-client relationship between investigating counsel and the employees:

- Address the nature of the internal investigation and the possible responses of the company to any investigation of the conduct at issue by the government, making it clear that such statements are being made in investigating counsel’s role as counsel to the company
- Address the likelihood that the interests of the company may conflict with the interests of the employee or some group of employees, again making clear that this assessment is being made on behalf of the company
- Advise the employee whether or not the company will consider paying for personal legal counsel for employees

⁵ Companies using this approach should take steps to ensure that employees understand that separate counsel is being provided for their protection and that the company’s decision to do so does not mean that the company believes that they have done something wrong. Companies should also be aware that adopting this approach may slow the pace of the internal investigation considerably.

These responses clearly provide information to the employee to allow the employee to address the “do I need a lawyer” question without giving a “yes” or “no” answer. Certainly the circumstances of the representation will often dictate whether other responses would be appropriate to help the employee address this all-important question. In the current climate, where prosecutors are demanding that companies waive the attorney-client privilege as part of their cooperation,⁶ it will be increasingly important for investigating counsel to help employees address the question in a way that preserves the interests of the company while not alienating the employees.⁷



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⁶ An American Bar Association Task Force is currently studying the trend of government enforcement agencies requiring companies to waive the attorney-client privilege. Panelists at a recent meeting pointed out that individual employees are less likely to engage in meaningful, candid communications with the company if they are aware that those communications could become part of the government’s case and could be used against them down the road. *Attorneys - Corporate Counsel Uncertainly Over Attorney-Client Privilege Eroding Client Communication, Speakers Say*, U.S. Law Week, Vol. 73, No. 42, p. 2661 (May, 10, 2005).

⁷ It is also important for the company and investigating counsel to consider whether to advise employees of the likelihood that the company will agree to waive the attorney-client privilege and turn over the results of the internal investigation to the government. Resolution of this issue will depend on the type of internal investigation being conducted, the nature and status of the government’s investigation, and the underlying facts at issue.

Practice group contacts

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