

How to Manage Litigation Risk Before it Even Arises

Charlotte ACC CLE Presentation

August 18, 2020

Agenda

- I. Introductions
- II. The Story Begins
- III. Contract Drafting
- IV. Internal Communications Practices
- V. Protecting Privileged Material
- VI. Questions

The “So What”?

- **The problem:** Seemingly small decisions now can have big effects later if a dispute or lawsuit arises.
 - Routine contract provisions
 - Communications practices
 - Preserving attorney-client privilege
- **The solution:** Even when “best practices” are not feasible, marginal improvements can reduce risk.

The Story

- You are corporate counsel for High-Tech Hardware Co., a technology company developing cutting-edge teleportation devices.
- High-Tech recently entered a joint development agreement with Jetsons Sprocket Co. to develop motors for the teleportation devices.
- The relationship starts out well, but problems later arise—and eventually there is a nasty dispute.

At the Beginning

- Your business team asks you to negotiate the joint development agreement with Jetsons and gives you a draft term sheet. Time is of the essence because competitors are working on similar technology. The business team emphasizes that, although contract terms obviously matter, “we really need to get the deal done.” After all, what could go wrong?

Substantive Obligation

Contract Provision

Jetsons will use reasonable efforts to deliver a prototype of the Motor and related equipment in a timely manner no later than one (1) year after execution of this Agreement.

Don't Leave it to the Court

- Courts will scrutinize the dictionary and four corners of the contract before they look at extrinsic evidence (such as the parties' emails about their understanding of the contract) to construe disputed contract language.
- The results can be unintended and counterintuitive.
- “The issue is, what is chicken?”
 - *Frigalment Importing Co. v. B.N.S. Int'l Sales Corp.*, 190 F. Supp. 116 (S.D.N.Y. 1960)
- What is a “building”?
 - *Kroger Ltd. I v. Guastello*, 177 N.C. App. 386 (2006)

Damages

Contract Provision

Each Party's liability shall not exceed amounts actually paid to the other Party under the Agreement.

Choice of Law

Contract Provision

Disputes under or related to the Agreement shall be governed by the law of the State of North Carolina.

Attorney's Fees

Contract Provision

In the event of a lawsuit under the Agreement, the prevailing party shall be entitled to attorney's fees, costs, and expenses.

Employees Say The Darndest Things

- One day, a member of the business team handling the Jetsons project forwards you an email she received from another team member, Manager Marcus. Marcus's email says:

“Bad news. The additional motors Jetsons delivered today don't meet our specs and are unusable. This will set us back at least a year. Unfortunately, this is our fault. We had poor quality control (despite my warnings on this issue) and weren't clear to Jetsons about our requirements. We'll have to eat this cost. Let's discuss.”

- What do you do?

Preventing the “Smoking Gun” Document

- Sensitive discussions are best had by phone
- But emails are often unavoidable, so train employees to avoid unnecessary speculation and conclusions
 - Draft like your email will be on the cover of the New York Times!
- **If the communication implicates legal concerns, go to corporate counsel first**

Poll

- You talk with Manager Marcus about the email. It turns out Marcus did not have all the facts. He now believes Jetsons is to blame for the faulty motors.
- Manager Marcus asks you: “Should I send a ‘clean-up’ email to correct my prior email? Take some other action?”

Privilege



"But . . . most of all, I'm thankful for things that are privileged and confidential."

Myths

- Labeling a document “privileged” makes it privileged
- Copying attorneys on an email makes it privileged

Privileges – General Rules

Lawyer-Client Privilege

Communications are privileged if they are:

- Confidential
- Sent to or prepared for an attorney
- By a client
- For legal advice

Work Product

Materials are protected if they are:

- Prepared by or for an attorney
- In anticipation of litigation

Paper Trail

- Your business team confronts Jetsons about the bad motors. Your team demands a new shipment of motors at no further cost and refuses to pay the current installment fee of \$1M until Jetsons complies.
- Jetsons responds via email. They say your side is to blame and that unless you pay the \$1M installment now, Jetsons will have no choice but to terminate the contract and sue.
- Manager Marcus recaps the dispute in an email.

Marcus's Email

To: CEO Sally

From: Manager Marcus

Cc: Corporate Counsel Kemal

Subject: Jetsons and Better Motor Co. deal issues

We haven't been able to reach a resolution with Jetsons' business team about the faulty motors. Jetsons still blames us, even though I sometimes think this is really their fault (despite what I said in my prior email). I'm concerned this delay will hurt us when our competitors launch their own products.

Since we no longer have faith in Jetsons, I think we need a new partner. We've identified Better Motor Co. as a possibility, but they're expensive. Also I think our Jetsons contract is exclusive, but at this point breaking the contract seems worth it. Can we discuss?

Practice Tips

- Pick up the phone
- If it must be an email:
 - Separate business and legal discussions to the extent possible
 - Clearly indicate when counsel is wearing their “lawyer hat”
 - But don’t overuse privilege labels
 - Have counsel send a recap of legal issues and decisions in terms of legal advice: “I advise” or “based on my analysis”
 - Don’t copy counsel on everything
 - Don’t forward counsel’s advice, even internally. Write a new email.

Ideal Email Example

None.

Better Email Example (if an email is unavoidable)

To: CEO Sally

From: Manager Marcus

Cc: Corporate Counsel Kemal

Subject: Jetsons motors

Sally, the situation with the Jetsons motors has reached the point where we need legal advice. I have some business ideas, but we need to be sure they make legal sense. Kemal, I am copying you to make you aware of the situation.

I'll send a separate calendar invitation to schedule a video meeting of us three. Many thanks.

Video Chat

- As the Jetsons dispute intensifies, CEO Sally asks for a video conference to discuss strategy. No lawyer participates. Manager Marcus records the conference so the team (including the lawyers) will have it as a reference.
- During the conference, two business team members use the chat feature to have a sidebar conversation about their opinions of potential liability. They also opine on the competency of the management team.
- Is the entire video discoverable? How about the chats?

A court would take it in pieces

- The video itself
 - Privileged?
 - Work product?
- The side chat
 - Privileged?
 - Work product?
 - Employees' assessment of potential liability
 - Carping about the management team

Privileges – General Rules

Lawyer-Client Privilege

Communications are privileged if they are:

- Confidential
- Sent to or prepared for an attorney
- By a client
- For legal advice

Work Product

Materials are protected if they are:

- Prepared by or for an attorney
- In anticipation of litigation

Tests for “in anticipation of litigation”

- The “specific claim” test
 - When the participants prepared the item, they had in mind an identified claim that was likely to lead to litigation
- The “primary purpose” test
 - The main motive of preparing the item was litigation prep, as opposed to doing business

The North Carolina test for “anticipation of litigation”

- Closer to a “but for” test:
 - Would the item exist if not for fear of litigation?
 - If the item would **not** exist, it could be work product
 - If the item **would** exist anyway, it’s not work product
- Items prepared because of a general policy probably fail the “but for” test
 - E.g., incident reports
 - Cf. tailored investigations led by lawyers

A court would take it in pieces

- The video itself
 - Privileged?
 - Work product?
- The side chat
 - Privileged?
 - Work product?
 - Employees' assessment of potential liability
 - Carping about the management team

Third Parties

- As litigation with Jetsons looks likely, your team decides they need to get to the bottom of who is at fault for the bad motors so they can decide how to proceed.
- They tell you they need to engage a consulting engineer to examine the faulty motors.
- **Poll**: Are communications with the engineer privileged?

Waiver

General Rule

Any disclosure of a privileged communication to a third party destroys privilege

Exceptions

- Common interest
- Consultants/Agents/Experts
- “Functional” employees

Former Employee

- Unfortunately, Jetsons sued your company for failing to pay the \$1M installment. Jetsons also alleges that your company has misappropriated their IP and is sharing it with your new partner, Better Motor Co.
- As the litigation proceeds, your outside counsel needs to interview Manager Marcus, who left the company several months ago on friendly terms.
- Is the interview privileged? Should you have taken a statement from Marcus before he departed?

Scope of Privileged Communications

Two potential rules:

- Control Group (narrower) – only those in control who have power to bind corporation.
- Subject-Matter Test (broader) – communications with (i) lower-level employees with facts necessary to representation and (ii) employees with a “need to know” lawyer’s advice

North Carolina has not explicitly adopted either approach, but cases frequently apply subject-matter analysis

Practice Tip: The *Upjohn* Instruction

- Ethics – avoid misunderstanding about lawyer’s role
- Establish and define privilege
 - *Counsel to company/not individual*
 - *Privilege belongs to company, which may waive it*
 - *Confidentiality expectations*
 - *Right to retain counsel*

Former Employee

Majority Rule

- Protects communications with former employees if the communications (1) meet the *Upjohn* standard and (2) focus on facts from the period of employment

Practice Tips:

- Use the *Upjohn* warning to explain role and protect privilege.
- Recognize line between topics that can be protected by privilege and those that cannot.

Family Affair

- Some of the work on the Jetsons contract was performed by a partially owned subsidiary of your company. You need to talk with the subsidiary about its role in the Jetsons dispute.
- **Poll**: Will this conversation be privileged?

Attorney-Client Relationship: Who is the Client?

- For Subsidiaries and affiliates, what level of affiliation is enough?
 - *SCR-Tech LLC v. Evonik Energy Services LLC*, 2013 WL 4134602 (N.C. Bus. Ct.)
 - In concluding that communications were protected, court considered both:
 - Degree of ownership interest; and
 - Existence of a shared legal interest.

Exit Opportunity

- A private equity firm has approached your company with a generous offer to acquire 100% ownership. Your company is inclined to sell.
- Diligence begins. The lawsuit is still pending. The PE firm says it needs to see your counsel's work product estimating your company's potential liability in the suit.
- Do you share it?



Travis Hinman



Mark Merritt



Matt Sawchak



Gabe Wright

ROBINSON

BRADSHAW