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Application of the Attorney-Client Privilege to Compliance Officers

Program Moderator: Maria Chiodi, Credit Suisse

Paper Submitted by: James L. Bernard, Stroock & Stroock & Lavan LLP

Application of the Attorney-Client Privilege to Compliance Officers[1]

The question of whether the attorney-client privilege can attach to communications with a compliance officer is a perplexing one. As a threshold matter, we assume for purposes of this article that the compliance officer is an attorney, though that will not always be the case. With that assumption, the answer to the question can become even more difficult if the compliance officer is also part of a company's legal department, or if the compliance officer "wears two hats," (i.e., is both an attorney in a firm legal department and has compliance functions). And of course, the answer to the question depends on what precisely the compliance officer is doing. To take two examples on possibly opposite ends of the spectrum, the difference between the compliance officer preparing a compliance report for submission to a regulatory agency, as opposed to the compliance officer assisting a trader "in real time" on compliance with specific rules and restrictions (e.g., position limits). This article addresses these matters and essentially concludes that in some instances, the attorney-client privilege could attach to communications with a compliance officer, while in other instances it does not, but whether to assert the privilege in any given case often depends on who is requesting the information and for what purpose.

As is now well-understood, the Dodd-Frank Act[2] amended sections of the Commodity Exchange Act to require registrants to designate an individual to serve as its Chief Compliance Officer "CCO."[3] The board or senior officer must appoint, and may remove, the CCO. They are required to meet with the CCO annually and at the request of the CCO.[4]

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[1] James Bernard, Francis Healey & Gilana Keller, Stroock & Stroock & Lavan LLP

[2] *See* Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, 124 Stat. 1376 (2010); 82 C.F.R. § 21330-01.

[3] 7 U.S.C. § 6d(d) and § 6s(k)(1).

[4] 17 C.F.R. § 3.3(a)(1) and (a)(2); 7 U.S.C. § 6sk.

CCOs have several responsibilities, including "administering the registrant's policies and procedures,"[5] resolving conflicts of interests,[6] "taking reasonable steps to ensure compliance" in connection to the "swap dealer's or major swap participant's swaps activities, or to the futures commission merchant's business,"[7] and "establishing procedures, in consultation with the board of directors or the senior officer, for the remediation of noncompliance issues" that the CCO identifies through, for example, a "compliance office review."[8] As this list suggests, some of these functions seem more like business, or non-legal, functions ("administering the registrant's policies and procedures" whereas some are more legal in nature ("taking reasonable steps to ensure compliance").

The CCO is also tasked with preparing and signing an annual compliance report. The written report includes a "description of the written policies and procedures" of the FCM, SD, or MSP.[9] The report "review[s] each applicable requirement" under the Act and regulations,[10] "identif[ies] the policies and procedures that are reasonably designed to ensure compliance,"[11] "provide[s] an assessment as to [their] effectiveness,"[12] and delineates "areas for improvement" and recommends changes.[13] Additionally, the report should "list any material changes to

[5] 17 C.F.R. § 3.3(d)(1).

[6] *Id.* § 3.3(d)(2).

[7] *Id.* § 3.3(d)(3).

[8] *Id.* § 3.3(d)(4).

[9] *Id.* § 3.3(e)(1).

[10] *Id.* § 3.3(e)(2).

[11] *Id.* § 3.3(e)(2)(i).

[12] *Id.* § 3.3(e)(2)(ii).

[13] *Id.* § 3.3(e)(2)(iii).

compliance policies and procedures,"[14] describe the resources allocated for compliance[15] and "any material non-compliance issues identified" and action taken.[16] Before presenting the annual report to the Commission, the CCO delivers it to the board or senior officer for review.[17]

The CCO has supervisory authority over employees acting at the CCO's direction.[18] Often, CCOs oversee desk compliance officers, who are available to advise traders on the floor.[19] These compliance officers respond to questions that are related to both legal and business issues, although a compliance officer does not need to be an attorney.[20] While some of their answers may be purely business related, they also respond to a mixture of legal and business questions.

There is a dearth of case law specifically applying attorney-client privilege law to compliance officers. But general principles from other contexts provide guidance on how such questions may get resolved.

In 2014, in a widely-discussed decision, the D.C. Circuit held that communications are privileged if providing legal advice was a "significant purpose" of the communication.[21] In *In re*

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[14] *Id.* § 3.3(e)(3).

[15] *Id.* § 3.3(e)(3).

[16] *Id.* § 3.3(e)(4)-(5).

[17] *Id.* § 3.3(f)(1).

[18] 17 C.F.R. § 37.1501.

[19] The privilege may still apply to communications to non-attorneys acting under the direction of attorneys in internal investigations. *In re Kellogg Brown & Root, Inc.*, 756 F.3d 754, 758 (D.C. Cir. 2014). This article does not address the question of whether compliance officers who are not lawyers should be covered by attorney-client privilege.

[20] The CCO "shall have the background and skills appropriate for fulfilling the responsibilities of the position." 17 C.F.R. § 3.3(b).

[21] *In re Kellogg Brown & Root, Inc.*, 756 F.3d 754, 759 (D.C. Cir. 2014).

Kellogg Brown & Root, Inc., plaintiff demanded documents during discovery that were created during defendant's previous internal investigation, which was conducted "pursuant" to its Code of Business Conduct, and supervised by the company law department.[22] The Court found that "[s]o long as obtaining or providing legal advice was one of the significant purposes of the internal investigation, the attorney privilege applies, even if there were also other purposes for the investigation and even if the investigation was mandated by regulation rather than simply an exercise of company discretion."[23] Further, the D.C. Circuit explicitly rejected the district court's "but-for" analysis, finding that it would "eradicate the attorney-client privilege for internal investigations conducted by businesses that are required by law to maintain compliance programs, which is now the case in a significant swath of American industry.[24]

A New York district court, in addressing applicability of the privilege to an internal investigation, affirmed the "primary purpose test" from *Kellogg* and opined that "[r]are is the case that a troubled corporation will initiate an internal investigation solely for legal, rather than business, purposes… Accordingly, an attorney-client privilege that fails to account for the multiple and often-overlapping purposes of internal investigations would 'threaten[ ] to limit the valuable efforts of corporate counsel to ensure their client's compliance with the law.'"[25]

In a New York Court of Appeals case concerning application of the common interest privilege, the court emphasized the overlapping business and legal responsibilities of lawyers working in corporations. The court opined that "in the corporate context, where corporate staff

[22] *Id*. at 756.

[23] *Id*. at 758–59.

[24] *Id*. at 759.

[25] *In re Gen. Motors LLC Ignition Switch Litig.*, 80 F. Supp. 3d 521, 530 (S.D.N.Y. Jan. 15, 2015), *citing Upjohn Co. v. United States,* 449 U.S. 383, 393 (1981).

attorneys 'may serve as company officers, with mixed business-legal responsibility; whether or not officers, their day-to-day involvement in their employers' affairs may blur the line between legal and nonlegal communications."[26]

In contrast, some courts have found that communication between lawyers and clients would not be subject to privilege if the "the collection of information necessary to prepare those answers and the actual preparation of those answers was in the normal course of [the] business . . . and would have taken place with or without her involvement as an attorney."[27] Similarly, a communication would not be privileged if it was not from a lawyer, and was not "information gathered by corporate employees for transmission to corporate counsel for the rendering of legal advice[.]"[28]

Similar to in-house counsel, compliance officers often wear two hats, and the purpose for which communications are made may determine whether the attorney-client privilege attaches. For example, compliance officers on a trading floor often communicate with traders "in real time" to ensure that transactions comply with specific rules and regulations, including, but not limited to, applicable position limits, reporting of over-the-counter swap transactions, and pre-trade disclosure of mid-market marks for certain swaps. Similarly, in performing their ordinary duties and obligations, CCOs will often discuss compliance procedures, the annual report or disclosure requirements with the board of directors or senior officers. Because such communications are made within the capacity as a compliance officer, and not in any type of

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[26] *Ambac Assur. Corp. v. Countrywide Home Loans, Inc.*, 27 N.Y.3d 616, 634 (2016), *citing Rossi v. Blue Cross & Blue Shield of Greater New York*, 73 N.Y.2d 588, 592 (1989).

[27] *SR Int'l Bus. Ins. Co. v. World Trade Ctr. Properties LLC*, No. 01 CIV. 9291 (JSM), (S.D.N.Y. June 19, 2002).

[28] *ex rel. Baklid-Kunz v. Halifax Hospital Medical Center*, Case No: 6:09-cv-1002, 2012 U.S. Dist. LEXIS 158944 (M.D. Fla. Nov. 6, 2012).

"professional legal capacity" or at the direction of an attorney, a court may refuse to protect them as attorney-client privileged or attorney work product because they are performing a business function.

On the other hand, if a company decides to conduct an internal investigation concerning certain trading practices at the request of the legal department, that same lower-level compliance officer may interview those same traders concerning how certain transactions are executed or reported and transcribe those interviews in notes. The CCO may then discuss the compliance department's findings with the board of directors or senior officers, including the general counsel, and provide an oral or written recommendation on whether such findings should be reported to a regulator. Because the primary purpose for these communications is arguably more legal than business-related, as opposed to the annual compliance report submitted to the board, they may be more likely to be protected from disclosure as privileged. Such distinctions, however, may not always be clear cut.

A Tennessee district court found that "in-house counsel often performs more functions within a corporation than just providing legal advice, and ferreting out the particular "hat" in-house counsel may be wearing at a given moment can be very difficult.… [I]n-house counsel at issue in this case is also a compliance officer in the defendant's Compliance Department. There is likely overlap of legal and nonlegal duties in such a position."[29] Often, separating the legal and non-legal advice of compliance officers is extremely difficult, and therefore determining what is and is not privileged, or potentially privileged, is equally difficult.

The CFTC, in its rules, proposed rules and comments, has not taken a definitive position on the scope of the attorney-client privilege as applied to compliance officers. However, in

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[29] *Leazure v. Apria Healthcare Inc.*, No. 1:09-CV-224, at *4 (E.D. Tenn. 2010).

commentary on a 2012 rule, the CFTC indicated that when furnishing the annual report, the privilege does not attach: "The Commission expects the CCO and registrant to articulate clearly the segregation of that individual's CCO and non-CCO responsibilities. All reports required under sections 4d(d) and 4s(k) of the CEA, as well as the rules promulgated pursuant thereto, are meant to be made available to the Commission, and as such, they should not be subject to the attorney-client privilege, the work-product doctrine, or other similar protections."[30]

Additionally, in a 2013 comment to the proposed rule concerning chief compliance officers, a commenter "argued that it is unreasonable for the Commission to take the position that a CCO should not be able to receive privileged advice from counsel in an effort to comply with these new, complex, and uncertain rules." The CFTC responded that the final rule did not change "existing Commission policies regarding the assertion of attorney-client privilege by registrants." [31]

In sum, whether the attorney-client privilege attaches to communications with a compliance officer is often confusing and such determinations will be fact specific. While neither the case law nor statutes and regulations directly address this question, it seems that in certain situations, where the "primary purpose" of such communications is to provide legal advice, the privilege may apply.[32] However, where communications with a compliance officer

[30] 77 Fed. Reg. 20128, 20160-61. Additionally, in a 2017 Enforcement Advisory about evaluating cooperation during the agency's investigations and enforcement actions, the CFTC declared that attorney-client privilege "protections can promote a client's communications with counsel and thereby serve to promote the client's compliance with the law. These rights are not intended to be eroded or heighted by this advisory." *See* CFTC, Enforcement Advisory: Cooperation Factors in Enforcement Division Sanction Recommendations for Companies (Jan. 19 2017).

[31] 78 Fed. Reg. 33476, 33548.

[32] *In re Kellogg Brown & Root, Inc.,* 756 F.3d 754, 759 (D.C.Cir.2014).

are more business-focused, generated in the course of day-to-day transactions, such communications may not be protected if they were not also driven by a need for legal advice.

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Professional Conduct Issues Arising from Representations of Multiple Clients in CFTC and SRO Investigations

Program Moderator: Maria Chiodi, Credit Suisse

Paper Submitted by: William J. Nissen, Sidley Austin LLP

ABA Committee on Derivatives and Futures Law
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Professional Conduct Issues Arising from Representations of Multiple Clients in CFTC and SRO Investigations*

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Lawyers are often called upon to represent multiple clients in connection with investigations by the Commodity Futures Trading Commission ("CFTC" or "Commission") and self-regulatory organizations ("SROs"), including National Futures Association ("NFA"), CME Group Exchanges ("CME") and ICE Futures U.S., Inc. ("ICE"). These representations occur because employees of firms under investigation are called to testify in these investigations, and both the firm and its employees are subject to being charged in enforcement complaints arising from the investigations. In-house counsel representing these firms need to decide whether to engage the same counsel to represent both the firm and its employees, or whether separate representation is advisable. Outside counsel, if called upon to represent a firm and its employees jointly, need to decide whether they can take on a joint representation. In addition, outside counsel that undertake joint representations must be prepared to re-evaluate whether a representation should be terminated based on changes that may occur during the course of the investigation.

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Rules Pertaining to Investigations by the CFTC and SROs

1. CFTC – The Director of the Division of Enforcement of the CFTC has authority to conduct investigations under Part 11 of the CFTC Regulations. CFTC Reg. 11.7(c) provides that a person who is compelled to appear, or who appears in person by request or permission of the Commission or its staff, may be accompanied, represented and advised by counsel. Such representation may be by any attorney-at-law admitted to practice before the highest court of any state or territory or the District of Columbia, who has not been suspended or disbarred from appearance and practice before the Commission. Counsel may be present with a witness during any aspect of an investigative proceeding and may advise the client before, during and after the conclusion of an examination. At the conclusion of the examination, counsel may request the person presiding to permit the witness to clarify any answers that may need clarification in order that answers not be left unequivocal or incomplete on the record. Counsel may also make summary notes during the examination. The Commission may for good cause exclude a particular attorney from further participation in any investigation in which the Commission has found the attorney to have engaged in dilatory, obstructionist, or contumacious conduct. Under CFTC Reg. 11.8(b), when a reasonable basis exists to believe that an investigation may be obstructed or impeded, directly or indirectly, by an attorney's representation of more than one witness during the course of an investigation, the member of the Commission, or the Commission's staff, conducting the investigation may prohibit that attorney from being present during the testimony of any witness other than the witness on whose behalf counsel first appeared in the investigation.

2. NFA – NFA Compliance Rule 3-1(a) gives the NFA Compliance Director authority to compel testimony, subpoena documents, and require statements under oath from any NFA Member, Associate or person connected therewith.
3. CME – CME Rule 407 provides that the Market Regulation Department shall investigate potential or alleged rule violations. Parties and witnesses being interviewed shall have the right to representation, at their own cost, by legal counsel or anyone other than a member of any Exchange disciplinary committee, a member of the Board, an employee of CME or a person related to the investigation.
4. ICE – ICE Rule 21.04 provides that the President, the Board, the Vice President, the Compliance staff, any committee or subcommittee, or panel thereof, engaged in an investigation has the power to summon any member, any employee of a member or any non-member market participant to appear and give testimony under oath, and to produce documents.

Issues Arising Under the ABA Model Rules of Professional Conduct from Representation of Multiple Parties in CFTC and SRO Investigations

Although the ABA Model Rules of Professional Conduct ("ABA Model Rules") do not have any legal standing on their own, they are often adopted in whole or in part by state and federal courts as the governing rules of professional conduct. Following are issues that arise in representing multiple clients in CFTC and SRO Investigations, and references to the ABA Model Rules that provide guidance to practitioners in addressing these issues.

1. Taking on Representation of Multiple Parties in the Same Investigation

A lawyer cannot undertake common representation of clients where contentious litigation or negotiations between them are imminent or contemplated. ABA Model Rule 1.7, Comment 29

A lawyer cannot represent a client where there is a significant risk that the representation will be materially limited by the lawyer's responsibilities to another client. ABA Model Rule 1.7(a) (2)

If there is a conflict of interest between two clients in a common representation, a lawyer may nevertheless represent both if (1) the lawyer reasonably believes that the lawyer will be able to provide competent and diligent representation to each client, (2) the representation is not prohibited by law, (3) the representation does not involve the assertion of a claim by one client against another client represented by the lawyer in the same litigation or other proceeding before a tribunal, and (4) each client gives informed consent, confirmed in writing. ABA Model Rule 1.7(b)

A lawyer should, at the outset of a common representation, address information sharing and potential withdrawal from representation with the clients and obtain each client's informed consent. ABA Model Rule 1.7, Comment 31

For an organization to consent to a dual representation of the organization and one or more employees, the organization's consent must be given by an appropriate official other than an individual who is to be represented, or by the shareholders. ABA Model Rule 1.13(g)

Subject to any limitations agreed upon by common clients, each client in the common representation has the right to loyal and diligent representation and, after the

representation ends, the protection of ABA Model Rule 1.9 concerning obligations to a former client. ABA Model Rule 1.7, Comment 33

2. Confidentiality of Client Information

Subject to specific exceptions, with respect to each client, a lawyer shall not reveal information relating to the representation of the client unless the client gives informed consent or the disclosure is impliedly authorized to carry out the representation. ABA Model Rule 1.6(a)

This duty of confidentiality continues after the representation is terminated. ABA Model Rule 1.6, Comment 20

3. Use of Client Information in the Course of a Representation

In general, a lawyer may not use information relating to the representation of the client to the disadvantage of the client, unless the client gives informed consent. ABA Model Rule 1.8(b)

4. Withdrawal When a Conflict Arises

Subject to any requirements for notice to or permission of a tribunal when terminating a representation, a lawyer shall withdraw from a representation if continuing it will result in the violation of the rules of professional conduct. ABA Model Rule 1.16(a)

5. Settling on behalf of Commonly Represented Clients

A lawyer who represents two or more clients may not participate in making an aggregate settlement of claims against the clients, unless each client gives informed consent in a writing signed by the client. ABA Model Rule 1.8(g)

6. Representing a Current Client Against a Former Client

A lawyer who has formerly represented a client in a matter may not thereafter represent another person in the former or a substantially related matter in which that person's interests are adverse to the interests of the former client unless the former client gives informed consent, confirmed in writing. ABA Model Rule 1.9(a)

A lawyer who formerly represented a client in a matter or whose present or former firm has formerly represented a client in a matter shall not thereafter use information related to the representation to the disadvantage of the former client except to the extent that would be permitted as to a current client, or when information has become generally known. ABA Model Rule 1.9(c)

Provisions regarding obligations to former clients are for protection of the former clients and may be waived if the client gives informed consent, confirmed in writing. ABA Model Rule 1.9, Comment 9

Advance waivers of future conflicts may be requested, and the effectiveness of such waivers is generally determined by the extent to which a client reasonably understands the material risks that the waiver entails. ABA Model Rule 1.7, Comment 22

7. Application of Conflict Rules to a Law Firm

In general, lawyers in a firm may not knowingly represent a client when any one of them would be prohibited from doing so. ABA Model Rule 1.10(a)

There is an exception when the prohibition is based on a personal interest of one lawyer and does not represent a significant risk of materially limiting the representation of the client by the remaining lawyers in the firm. ABA Model Rule 1.10(a) (i)

There is also an exception where the prohibition is based on prior association of a lawyer with another firm, and specified screening and notice procedures are followed with respect to that lawyer. ABA Model Rule 1.10(a) (2)

Note: In analyzing any specific fact pattern, it is important to apply the rules as adopted by the relevant jurisdiction(s), which may vary from the ABA Model Rules.