MACFARLANES

LEGAL RISK MANAGEMENT
DOCUMENT CREATION AND COMMUNICATIONS

LITIGATION AND DISPUTE RESOLUTION

EXECUTIVE SUMMARY

This briefing deals with the legal effect of, and potential requirement to disclose in court proceedings, internal and external communications, both sent and received by employees, and the corresponding need for prudence and caution when circulating communications. Although it covers all forms of written communications, it is particularly relevant to emails which are often copied to large volumes of people without consideration of the potentially damaging effect on your legal position.

If you are party to a dispute, you are required to disclose all documents (including emails, drafts, and manuscript amendments on documents) relevant to the dispute even if they are adverse to your case. Only those documents which are "privileged" need not be disclosed. "Privilege" is a legal term of art and applies to certain categories of documents which do not have to be provided to the court or to the other side on a dispute. The two main forms of privilege relevant to your general business are legal advice privilege, which protects communications and documents passing between you and your legal advisors (whether in-house or external Counsel), and litigation privilege, which protects communications and documents created for the purposes of obtaining or providing legal advice in relation to litigation or the gathering of evidence for litigation. Without prejudice communications which are aimed at settling a dispute are also not disclosable.

In order to ensure that privilege attaches to as many of your documents and communications as possible, you should observe the following principal policies in respect of any documents (1) seeking or containing legal advice, or (2) relating to a dispute or potential dispute:

- Do not circulate documents internally, in particular legal advice, unnecessarily. Ask yourself who actually needs to see the document.
- Do not provide copies of documents to third parties. If this is not possible check with your legal department before proceeding.
- Check with your legal department before you undertake any sort of investigation or create documents relating to an actual or potential dispute (even if only a fact-finding exercise).
- Only discuss sensitive issues orally and seek advice from the legal department before committing anything to writing.
- All references to legal advice sought or received should be kept in a separate document
- Ensure all privileged documents are marked "confidential and privileged", and all correspondence which contains settlement negotiations is marked "without prejudice"; in both cases they should be stored separately.

General day to day internal and external communications will not be privileged and will therefore be discloseable to the court and the other side in the event of a dispute. Therefore:

- Do not write anything which you would not be comfortable for the Court or the FSA to read (for example, opinions or offensive comments): you could ultimately be cross-examined in court about what you have written in documents;
- Do not include unnecessary personal information about customers, brokers or other members of staff, because such communications could fall foul of data protection laws.

THE DUTY OF DISCLOSURE AND THE IMPORTANCE OF PRIVILEGE

You may become subject to legal proceedings, FSA or other regulatory investigations. You may also be required to disclose your records under data protection laws. If you are a party to a dispute, you are under a legal duty to disclose all documents which are relevant to the litigation. This duty includes not only those documents upon which you intend to rely, but also any documents which adversely affect your own case, adversely affect the other side's case or even support the other side's case. These categories of discloseable documents are therefore very broad and you could, for example, have to disclose all email traffic.

The meaning of a document is also very wide, encompassing everything which is or can be reproduced in written or printed form. This will include your emails, text messages, instant messenger conversations, diary entries, manuscript notes, informal jottings, databases, word documents, excel spreadsheets, hard drives and tape recordings. It covers draft documents as well as final versions and any manuscript amendments or comments on them.

The only relevant documents that are protected from disclosure are those which are privileged or without prejudice communications, the meaning of which is explained below. Therefore it is important that you ensure privilege attaches to as many of your documents as possible (and is not lost by subsequent circulation and use). Those documents which are not privileged should be created with the possibility of disclosure in mind.

This briefing explains the two main types of legal privilege (legal advice privilege and litigation privilege) and without prejudice communications in relation to the negotiation of the settlement of a dispute, and then highlights the practical steps which you can take to best protect your communications.

LEGAL ADVICE PRIVILEGE

Legal advice privilege protects confidential communications passing between a solicitor and his client which are created for the purpose of giving or obtaining legal advice. Such documents are not discloseable in the event of a dispute.

No protection for third parties

Legal advice privilege only attaches to documents which actually pass directly between you and your legal advisers (which covers both in-house Counsel and external Counsel). Therefore, general day to day internal communications will not attract legal advice privilege; nor will communications with your other professional advisors, for example, accountants, auditors, doctors, bankers, journalists or other non-lawyers, even if created to assist the giving or receiving of legal advice.

You cannot create privilege in an unprivileged document. So copying a non-privileged document to your legal advisors, will not create privilege in the document.

Who constitutes the client?

As legal advice privilege only attaches to communications between a client and his legal advisor, it is important to understand who constitutes the client. This has a very narrow meaning which places important practical limitations on the availability of legal advice privilege in corporate entities. The "client" will not include all employees or representatives. Instead, only a narrow group of your employees who have been specifically charged with seeking and receiving legal advice (whether internal or external legal advice) will constitute the client.

Other employees are effectively deemed to be third parties and, as such, documents created by them may not be privileged, even if prepared for the purposes of instructing legal advisors or to provide information requested by legal advisors and sent directly to them. Therefore, individuals who are charged with liaising with in-house or external legal advisors need to think very carefully before they ask other colleagues to prepare such background materials (for example, in the course of a due diligence exercise or fact-finding mission in relation to an area where advice is required).

Although some legal commentators suggest it may be possible to get round this by designating a wide group of employees as the client, this may be artificial and the courts are likely to view the matter objectively. However, if the group is too narrow this will hinder your ability to obtain legal advice. It is recommended that a realistic number of persons from whom instructions can be given should be specified in the retainer letter with external Counsel.

Practical tips: the narrow meaning of the client

Certain measures can be taken to try to reduce the risk of documents containing legal advice becoming disclosable:

- Internal communications within departments, regarding the need to take legal advice (whether internal or external), will not be privileged and should be made orally rather than recorded in writing.
- Any legal issue which arises should be discussed orally with in-house counsel in the first instance. Any emails which are necessary should be sent only to in-house counsel to limit the possibility of disclosure. Under English law, in-house lawyers attract legal advice privilege in the same way as external counsel. However, it should not be assumed that communications to the legal department will automatically be privileged (see privilege and in-house Counsel below).
- In relation to each legal issue which arises, members of the team who will be the key personnel (in terms of knowledge, instructing lawyers and decision-making) should be identified and specifically designated to deal with the matter. Only they should create and receive documents relating to the legal advice.
- Communications about legal issues with other employees should be kept to an absolute minimum and legal advice should not be communicated in writing to anyone who does not strictly need to know it. In particular, think carefully before adding people to the distribution list or forwarding emails (see losing privilege below) if the communication contains legal advice.

- Wherever possible, fact-finding internal investigations and interviews should be conducted and led by, or at least with, legal advisors. All written reports and documents relating to the legal issue should be produced by the legal advisors containing both the summary of facts and the legal advice.
- Communications with external Counsel should only be made via the legal department and the designated employees.

Privilege and in-house Counsel

There is no guarantee that a communication between a client (in the narrow sense of the word) and a legal advisor (external or in-house Counsel) will automatically be privileged as the protection extends only to giving or obtaining legal advice, as opposed, for example, to commercial advice.

Legal advice is not confined to telling the client the law; it includes advice as to what should prudently and sensibly be done in a relevant legal context. Therefore any advice relating to rights, liabilities, obligations or remedies should be privileged. Further, privilege will attach to information passed between a legal advisor and "the client" as part of the continuum of legal advice aimed at keeping both informed so that advice may be sought and given as required.

Pure business, non-legal advice will not be privileged e.g. advice on finance policy, even though it comes from in-house Counsel. However, there are many grey areas such as questions of document retention and organisation where it is not clear whether an advisor is providing legal advice or acting as a man of business. In practice this issue will arise more frequently in the context of in-house Counsel. Therefore, it should not be assumed that all communications with your legal department are automatically privileged. Any communications created for purposes such as administrative, compliance or company secretarial work are unlikely to be privileged. Therefore you should keep communications regarding business or administrative advice separate from communications regarding legal advice, which should be marked "confidential and privileged" and where practicable filed separately.

One anomaly is that communications with or documentation created by in-house counsel relating to a European Commission investigation into breaches of European competition law will not be privileged, even if made to obtain or receive legal advice. Therefore, all legal advice communications must be with external lawyers in this situation.

Draft documents

Draft documents are disclosable in the same manner as final versions. Any claim for legal advice privilege necessarily requires the communication of the document between you and your legal advisors. Therefore, if legal advisors are not involved, draft documents created by your employees will be disclosable to the extent that they are relevant and admissible (e.g. in a rectification claim). Remember even deleted drafts can be recovered from hard drives.

Data protection

Although not related to privilege, documents which contain personal data which is biographical in a significant sense (for example, an email containing a customer's name, address, age, mental and physical disabilities) may be subject to disclosure under the Data Protection Act 1998.

Practical tips: day to day internal communications

Ordinary day to day internal communications will not be privileged and should be treated as if they will be disclosable in the event of a dispute. Therefore:

- Do not write anything in an email or other document (even if only a draft) unless you would be comfortable for opposing Counsel, the FSA or the Court to read it. In particular, you should refrain from giving your own opinions on disputes, making offensive comments and jokes, swearing and making defamatory or unkind statements.
- Do not include any unnecessary personal or biographical details about customers, brokers, other members of staff or anyone else about whom you hold personal data.
- Speak to the legal department before commencing fact-finding investigations or creating documents setting out your understanding in relation to any legal issue which has arisen.
- If there is any doubt as to whether privilege will apply, the information in question should be communicated orally.

LITIGATION PRIVILEGE

Litigation privilege protects confidential communications passing between a client or his solicitor and a third party, if the communication was created for the dominant purpose of getting or giving legal advice in relation to existing or contemplated litigation, or for the dominant purpose of gathering evidence for such litigation. Again, such documents will not be discloseable in the event of a dispute.

Unlike legal advice privilege, litigation privilege is able to protect communications with third parties, both by you and your legal advisors, where evidence is being sought. However, it will not attach to unsolicited communications from third parties (e.g. emails or letters from potential witnesses) as these are not created for the dominant purpose of obtaining legal advice or gathering evidence.

Litigation privilege is important as there is a continuing obligation of disclosure from the moment litigation is in prospect to the end of the proceedings. Litigation privilege enables parties to prepare for a case without fear that those preparations will become disclosable.

Practical tip on document retention
All documents should be retained for a minimum period of 6 years and shredded only in accordance with your consistently applied shredding policy (to avoid negative inferences being drawn from a "one off" shredding exercise). As soon as a potential dispute arises, all documents relating to the matter should be set aside, excluded from the shredding procedure and specifically retained.

You should label all documents created for the purpose of litigation (including drafts) "privileged and confidential; prepared for the purpose of litigation" and store them separately. However, privilege is a question of substance over form and such a label will not be definitive.

There must be existing or contemplated litigation
For there to be litigation, there must be an adversarial process, as opposed to a fact-finding enquiry.

If litigation has not yet commenced, there must be a real likelihood that it will be i.e. a reasonable prospect rather than a mere vague anticipation. Therefore, in principle, a document which comes into existence before external (or even in-house) Counsel is instructed can be protected by litigation privilege. However, the courts will be more willing to question a claim for privilege where legal advisors are not involved.

Dominant Purpose
Documents are often created for a number of different purposes e.g. a fact-finding mission and to enable legal advice to be provided on the merits of a case. Provided the document came into existence for the dominant purpose of preparing for the litigation then the document will be privileged. However, if another reason is the dominant or even an equal purpose (e.g. to prevent reoccurrence of an error) then litigation privilege cannot be claimed.

Litigation advice can encompass tactics as well as the strengths and weaknesses of the claim.

Practical tips
As litigation privilege protects communications with third parties, the problems associated with internal communications and legal advice privilege are not such an issue. However, the practical points set out at page 3 are still good practice.

Issues particularly relevant to litigation privilege include:

- As there is a continuing obligation of disclosure, you should take care throughout the case to avoid creating documents which may be prejudicial or adversely affect your case. Categories of documents which might be created and be prejudicial include, for example, board minutes, internal memoranda and correspondence with other professional advisors (such as notes to accountants) commenting on the dispute and, even worse, its merits. Litigation privilege may not attach to such documents if they are not created for the purpose of preparing for litigation or advising the Board e.g. reporting on legal proceedings for information only.
- Advice from the legal department should be sought before the creation of any new documents relevant to the litigation.
- Experts should only be instructed by the legal department with clear letters of instruction.
- If you do not hold a copy or original of a document relevant to the dispute, do not request a copy from a third party as it will be an unprivileged document. Ask external legal advisors to obtain copies of the document (as the copy may attract privilege in their hands) or only review the document and do not take copies or make notes of its contents.

PRIVILEGE AND PITFALLS

Once privilege has been established in your documents, it is important that it is not lost unnecessarily.

PART PRIVILEGED DOCUMENTS

Where a document contains both privileged and unprivileged material, you are entitled to redact the privileged part. However, if part-privileged documents deal with a single subject matter (so that it cannot be severed) and you wish to rely on the unprivileged parts of the document as evidence in subsequent proceedings you would have to waive privilege in the entire document. For this reason, ideally any written reference to legal advice should be kept in a separate document from unprivileged material. For example, separate board minutes or internal memoranda should be created to deal with the legal issues and their ramifications, and kept separate from documents dealing with the commercial issues arising from the legal advice.

Practical tips: avoid the creation of part-privileged documents

Where possible, written references to legal advice should be kept in a separate document from unprivileged material.

Privileged documents and notes of legal advice should be kept in a separate file and marked "confidential and privileged".

Distribution of documents

Confidentiality is a necessary pre-requisite to any claim for privilege (for both legal advice and litigation privilege). If confidentiality is lost, a claim for privilege cannot be maintained in the original document. Therefore it is of paramount importance to ensure that circulation of legal advice and privileged documents is limited as much as possible, whether internally or to your advisors, and should only be provided once a confidentiality undertaking has been procured.

To third parties

Third parties can be required to disclose relevant documents. Even if a third party owes a duty of confidence, the court has wide powers to order disclosure, especially where the duty is owed to one of the parties to the litigation. Therefore, confidentiality alone is not sufficient to protect privilege.

A copy of a privileged document will itself only attract privilege (and, therefore, not be disclosable) if the copy is made for a privileged purpose i.e. for the purpose of obtaining legal advice or in preparation for litigation. If copies are made for a non-privileged purpose, for example for the purpose of providing information only to a third party, they will not be privileged.

By way of example, if you provide copy documents regarding potential litigation to your auditors for the purposes of accounting requirements, the copy will not be privileged and could be disclosed. Therefore, such documents should not be sent to auditors. Instead you should read the contents of the advice to them or, if copies are required, ensure they return them as soon as possible and do not take copies.

Similar issues are raised in relation to disclosure in data rooms. Again you should make such disclosure confidentially and for a limited purpose. You should permit inspection only, and require an agreement not to waive privilege in any notes produced by their lawyers in an attempt to prevent disclosure.

Some third parties may have a common interest in receiving the document so that it will also be privileged in their hands as part of your "circle of friends". Whether a common interest arises is a question of fact and the law is still undeveloped. Although group companies can sometimes have a common interest, the safest approach is to limit all external communications as far as possible.

Internally

All copy documents circulated internally and the internal dissemination of legal advice may also be disclosable unless the copies are provided for a privileged purpose (i.e. for the purpose of obtaining legal advice or in preparation for litigation). Extra caution must be exercised again in relation to reliance on legal advice privilege due to the narrow interpretation of "client".

By way of example, it will often be necessary for the Board of Directors to consider advice rendered by the legal department at Board meetings. The Board will then receive an update on the legal advice, perhaps by dissemination of copies of the legal advice or by a report from one of the directors to the Board. The update/report and the legal advice as recorded in the Board minutes, will attract privilege. However, if the Board minutes then go on to consider the policy and commercial implications of the legal advice, this part of the minutes will not be covered by legal advice privilege.

Practical tips on circulation

- Provide inspection or oral confirmation of legal advice to third parties (e.g. auditors) and not copy documents containing advice. If copies must be provided, ensure a confidentiality undertaking is entered into limiting the

purpose of the disclosure together with an obligation to return the copies and not to retain any further copies.

- Remember the narrow definition of "client" when dealing with internal circulations. Although it is unlikely that disclosure to the Board would result in a loss of legal advice privilege, the law is far from certain. Therefore, all communications should be kept to an absolute minimum and legal advice sought before circulating copies.

- Legal advice should not be copied to anyone who does not strictly need to know it and where it is not provided for a privileged purpose.

- Where dissemination is necessary, limit it, if possible, to a brief summary (taking into account the fact the summary may be disclosable) rather than providing relevant documents and copies of legal advice.

- Mark all documents relating to legal advice or litigation "privileged and confidential" and, if it is absolutely necessary to provide them to third parties, state when providing them that you are not waiving privilege by doing so.

WITHOUT PREJUDICE NEGOTIATIONS

This applies to communications between you and any party with whom you are involved in a dispute. The without prejudice rule is based on the public policy of encouraging the settlement of disputes by offering reassurance that communications between disputing parties during negotiations will not be disclosable if negotiations fail.

All communications representing a genuine attempt to reach a settlement of a dispute are generally treated as without prejudice and inadmissible in evidence.

Substance not form

It is the substance of the communication, rather than its form, which is relevant. A document marked "without prejudice" will not be automatically protected. Similarly, a genuine settlement offer not marked without prejudice may nonetheless be treated as being without prejudice unless it was clearly intended to be an "open" offer. In order for a communication to be without prejudice, there must be a genuine proposal or bona fide negotiation to compromise an existing dispute or to avoid litigation.

For example:

- a letter marked to the other side "without prejudice", but which merely amounts to an assertion of your legal rights and makes no offer to negotiate or to settle, will not be privileged. There is no such thing as an "off the record" communication in the eyes of the law and merely labelling a document "without prejudice" achieves nothing unless it contains a settlement offer or is part of an ongoing settlement negotiation;

- correspondence discussing repayment of an admitted liability will not be without prejudice as the negotiations do not relate to a disputed claim. There has to be a dispute for the without prejudice rule to apply;

- reports commissioned to assist one party in negotiations (e.g. surveyor reports), but which do not form part of the negotiation itself, may be admissible;

- without prejudice privilege will not extend to discussions with other parties to the dispute concerning tactics and case management generally.

Intention of parties

The parties must intend to communicate on a without prejudice basis. The courts assess this on an objective basis i.e. what, on a reasonable basis, was the intention of the author of a document and how would the communication be understood by a reasonable recipient?

Therefore, you should mark any settlement offers as being "without prejudice" as an indication of your intention. Although this will not be determinative, the absence of such a heading will not be without significance in deciding whether the document is in fact admissible. For example, a letter which offers a sum in settlement, but which is not marked without prejudice, in which the party reserves its position and refuses to admit liability, may be viewed as an open offer.

If the offer is not intended to be binding and will require further fine tuning by the lawyers, it should be marked not only "without prejudice", but also "subject to contract".

If the communications seeking to settle a dispute are in writing, protection is afforded to the whole chain of correspondence. This is so even if certain letters do not contain an offer of compromise, although the chain can be broken by "open" communications.

If you are making a change from without prejudice to "open" communication, you should make that change expressly clear to the other side.

Unlike legal advice and litigation privilege which you own unilaterally and which apply to documents on an individual basis, without prejudice privilege attaches to the entire chain of communications both ways between you and the other side, and so cannot be waived without the agreement of all parties to the correspondence.

Exceptions

In certain extreme circumstances, without prejudice correspondence will be admissible, for example communications which contain blackmail or make a clear admission of liability if you are then going to subsequently deny it in proceedings. Therefore, it is important that you do not act inappropriately in without prejudice correspondence.

Practical Tips

- Consider whether there is actually a dispute and whether the correspondence represents a genuine attempt to reach a settlement. If it does not, it will not be without prejudice.
- All negotiating correspondence should be marked with the words "without prejudice" and any change to that status should be communicated very clearly.
- If offers are made which will require some fine tuning by lawyers, these should be explicitly marked "subject to contract" as well as "without prejudice" to indicate that the document does not constitute a binding agreement.
- Never admit any liability in settlement negotiations without seeking legal advice.

CONTACT DETAILS

If you would like further information or specific advice please contact your usual Macfarlanes contact or:

GEOFF STEWARD

DD: +44 (0)20 7849 2341

geoff.steward@macfarlanes.com

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MACFARLANES LLP

20 CURSITOR STREET LONDON EC4A 1LT

T: +44 (0)20 7831 9222 F: +44 (0)20 7831 9607 DX 138 Chancery Lane www.macfarlanes.com