



THE WHO AND WHOSE OF THE ATTORNEY-CLIENT PRIVILEGE IN MERGERS AND ACQUISITIONS

VORYS

**M&A GROUP
PRIVATE EQUITY GROUP**

What steps can parties take to protect pre-closing communications with their attorneys in post-closing legal disputes? In the midst of negotiations, parties to a transaction give brief, if any, attention to whether their confidential communications with their attorneys may fall into the other party's hands following closing. However, parties, particularly the selling parties, must be wary of assuming that their attorney-client communications will be protected after closing.

Under a general definition of attorney-client privilege, confidential communications between a client and its legal counsel made for the purpose of seeking legal advice may be protected from compelled disclosure in litigation. This privilege may be used to protect written communications between a client and its attorney from discovery or prevent a client or its attorney from being compelled to testify about privileged communications.

However, courts over the past several years have cautioned that the protection of the attorney-client privilege may be limited under certain circumstances in mergers and acquisitions or may be lost altogether if selling parties do not appropriately address the privilege's ownership in the definitive agreement. To retain the protection of this privilege for pre-closing communications in mergers and acquisitions, parties will want to understand the who and whose of the attorney-client privilege.

Overview

As discussed in this white paper, parties to a merger or acquisition, particularly the selling parties, should be aware of the circumstances under which courts have found that the "client" or persons acting on behalf of the "client" have lost of the benefit of the privilege without being aware of doing so.

First, parties may forfeit the attorney-client privilege with respect to sensitive communications that are shared between their attorneys and persons not covered by the privilege. Recent court cases have shown that a person fulfilling multiple roles on behalf of a party and its affiliates may not be entitled to protection under the privilege at all times when communicating with that party's attorney. Accordingly, persons acting on behalf of a party in a transaction should be aware of their capacity when communicating with that party's attorney. We identify below some practical steps that these persons can take to protect against the possibility that their communications will fall outside the scope of the attorney-client privilege.

Second, selling parties may lose the right to assert the attorney-client privilege over the target's or seller's pre-closing communications with its attorney when the target merges with, or is sold in its entirety to, the buyer or when the privilege is inadvertently included in the assets being sold

to the buyer. However, courts have consistently found that selling parties can protect against this loss through the definitive agreement. In a merger or sale of equity, the target becomes a part of the buyer (or its subsidiary) and the ownership of the privilege transfers with the target. In contrast, in an asset sale, the seller's attorney-client privilege will not be transferred to the buyer unless it is included among those assets being transferred in the definitive agreement. We describe below certain terms that selling parties have started to include in the definitive agreement to prevent the transfer or loss of the target's or seller's attorney-client privilege upon closing.

Who Is Covered by the Privilege?

Identifying *who* may be covered by the attorney-client privilege in transactions is the first step to protecting pre-closing communications. Because the "client" in a transaction is often a business, those officers, directors, managers, members, employees, and other agents communicating on behalf of the client with its attorney must be aware of whether their communications would be covered by this privilege.

Recent case law spins a cautionary tale that persons serving in multiple roles on behalf of a party and its related entities may not benefit from the attorney-client privilege at all times in communicating with that party's attorney.¹ In particular, the United States District Court in *Argos Holdings Inc. v. Wilmington N.A.*, considered the application of the attorney-client privilege to communications in a transaction involving PetSmart, Inc. ("PetSmart") and its parent company, Argos Holdings, Inc. ("Holdings"), that were received by individuals serving as both partners in the principal investor in PetSmart and Holdings, BC Partners, Inc. ("BC Partners"), and members of the board of Holdings' ultimate owner, Argos Holdings GP LLC ("Argos GP").² When litigation arose related to PetSmart's acquisition of an online pet retailer and subsequent restructuring, the District Court separated privileged communications from non-privileged communications by considering the capacities in which the persons claiming the privilege had received them.³ The privilege applied to the emails from Argos GP's attorneys that these persons received when they were acting as Argos GP's directors (as indicated by their email addresses) but not when they were acting as partners and/or employees of BC Partners.⁴ The District Court explained that the attorneys "were not retained by BC Partners in connection with these matters, and BC Partners was not their client."⁵

**IDENTIFYING *WHO*
MAY BE COVERED
BY THE ATTORNEY-
CLIENT PRIVILEGE
IN TRANSACTIONS
IS THE FIRST STEP
TO PROTECTING
PRE-CLOSING
COMMUNICATIONS.**

¹ See *Argos Holdings Inc. v. Wilmington N.A.*, No. 18cv5773(DLC), 2019 U.S. Dist. LEXIS 53104 (S.D.N.Y. 2019).

² *Argos*, at *1-2.

³ *Id.* at *6-7.

⁴ *Id.* at *7-8.

⁵ *Id.* at *1.

Argos raises two considerations in defining the *who* of the attorney-client privilege in transactions:

1. Persons acting on behalf of a party to a transaction must be aware of the capacity in which they are communicating with that party's attorney. Simply occupying a particular title on behalf of a party does not warrant application of the privilege. Instead, these persons should be cognizant of the indicators of their position, such as which email addresses and signature lines they are using in confidential communications.
2. Any communications with a party's attorney should be limited to a group of individuals with a "need to know" and those who would be entitled to the privilege as well for their communications. Once attorney-client communications extend beyond this limited group, the application of the privilege becomes much more uncertain and introducing any third parties into the communications may waive the privilege.



Whose Privilege Is It?

In addition to considering who is covered by the attorney-client privilege, selling parties should consider *whose* privilege it is. While the case law concerning ownership of the attorney-client privilege in post-closing legal disputes continues to develop, various state courts have clarified that a seller's or target's attorney-client privilege, as it relates to pre-closing communications, may be waived or transferred upon closing. However, parties can avoid any unintended transfers of the seller's or target's attorney-client privilege by addressing its ownership in the definitive agreement.

Case law addressing the ownership of the attorney-client privilege in transactions instructs that the nature of the transaction (*i.e.*, merger, stock purchase or asset purchase) may impact the ownership of the privilege following closing if the parties do not provide otherwise in the agreement. One example of the transfer of the attorney-client privilege arose from a dispute in the Delaware Court of Chancery over pre-closing attorney-client communications that occurred in connection with merger negotiations.⁶ Following the merger's closing, the buyer had discovered pre-closing communications between the target and its attorney regarding the merger on the target's computer systems, which had been physically transferred to the buyer.⁷ The target's former shareholders and representatives tried to assert the attorney-client privilege over these communications based on the argument that they, and not the buyer, retained the right to the attorney-client privilege with respect to the target's merger-related communications.⁸

⁶ *Great Hill Equity IV, LP v. SIG Growth Equity Fund I, LLLP*, 80 A.3d 155, 159 (Del. Ch. 2013).

⁷ *Great Hill*, at 156.

⁸ *Id.* at 158.

In citing to the statutory effects of a merger provided for in the Delaware General Corporation Law ("DGCL"), the Delaware Court of Chancery in *Great Hill* determined that the target's attorney-client privilege had transferred to the buyer (as the surviving corporation) as a result of the merger.⁹ The relevant portions of the DGCL stated that, following a merger, "all property, rights, privileges, powers and franchises, and all and every other interest shall be thereafter as effectually the property of the surviving or resulting corporation."¹⁰ Absent any indication to the contrary in the merger agreement, the statutory language in the DGCL determined the ownership of the target's attorney-client privilege following closing.¹¹

More recently, the Delaware Court of Chancery considered in *Shareholder Representative Services LLC v. RSI Holdco, LLC* whether the target's shareholders may prevent the transfer of the target's attorney-client privilege to the buyer as a result of the merger.¹² Although the emails in dispute had been physically transferred to the buyer with the target's computers and email servers (similar to *Great Hill*), the Delaware Court of Chancery found that the merger agreement explicitly preserved the right of the target's shareholders to assert the attorney-client privilege over the target's pre-closing communications regarding the merger.¹³

The specific provision of the merger agreement identified by the Delaware Court of Chancery stated as follows:

"Any privilege attaching as a result of [the target's attorney] representing [the target] . . . in connection with the transactions contemplated by this Agreement [1] shall survive the [merger's] Closing and shall remain in effect; provided, that such privilege from and after the Closing [2] shall be assigned to and controlled by [the shareholders' representative]. [3] In furtherance of the foregoing, each of the parties hereto agrees to take the steps necessary to ensure that any privilege attaching as a result of [the target's attorney] representing [the target] . . . in connection with the transactions contemplated by this Agreement shall survive the Closing, remain in effect and be assigned to and controlled by [the shareholders' representative]. [4] As to any privileged attorney client communications between [the target's attorney] and [the target] . . . prior to the Closing Date (collectively, the "Privileged Communications"), [the buyer], the Merger Subsidiary and [the target] (including, after the Closing, the Surviving Corporation), together with any of their respective Affiliates, successors or assigns, agree that no such party may use or rely on any of the Privileged Communications in any action or claim against or involving any of the parties hereto after the Closing."¹⁴

⁹ *Id.* at 157.

¹⁰ *Id.*

¹¹ *Id.* at 162.

¹² *Shareholder Representative Servs. LLC v. RSI Holdco, LLC*, No. 2018-0517-KSJM, 2019 Del. Ch. LEXIS 196, at *5 (Del. Ch. 2019).

¹³ *Id.*

¹⁴ *Id.* at *2-3.

**IN ADDITION TO
CONSIDERING WHO
IS COVERED BY
THE ATTORNEY-
CLIENT PRIVILEGE,
SELLING PARTIES, IN
PARTICULAR, SHOULD
CONSIDER *WHOSE*
PRIVILEGE IT IS.**



Through this language the parties had prevented the transfer of the target's attorney-client privilege to the buyer upon closing.

The lessons in *Great Hill* and *Shareholder Representative Services, LLC* can be extended to stock purchases as well. Similar to a merger, a stock purchase results in the transfer of the target company in its entirety, including all assets and liabilities, to the buyer. To preserve the right to assert the target's attorney-client privilege for pre-closing communications with the target's attorney, selling shareholders in stock purchases have started to address in the definitive agreement the right to assert this privilege following closing and the right of the target's attorney to represent the selling shareholders in post-closing legal disputes.

On the other hand, in an asset purchase, courts will typically consider the terms of the asset purchase agreement to determine the parties' intention as to whether this privilege should be included with the purchased assets. Unlike mergers and stock purchases, parties to an asset purchase pick and choose those assets and liabilities that will be transferred to the buyer. Therefore, the asset purchase agreement will be instructive in determining the ownership of the seller's privileges following closing.

In one recent example, the Delaware Court of Chancery in *Dlo Enters. v. Innovative Chem. Prods. Grp., LLC*, found that, in the absence of a clear waiver of the seller's attorney-client privilege for deal communications, the seller retains this privilege.¹⁵ The Delaware Court of Chancery explained that the "privilege regarding an asset purchase agreement and associated negotiations does not pass to the [buyer] by the default operation of any law, but rather, remains with the seller unless the buyer contracts for something different."¹⁶ Even though the buyer in *Dlo Enterprises* argued that the asset purchase agreement had expressed the parties' intention to transfer the seller's attorney-client privilege with the purchased assets, the Delaware Court of Chancery determined that the language excluding the seller's "rights under or pursuant to the [asset purchase agreement] and agreements entered into pursuant to [the asset purchase agreement]" from the purchased assets had prevented the transfer of this privilege.¹⁷

Ultimately, the parties in a merger, stock purchase or asset purchase have the power to define the *whose* of the attorney-client privilege in the definitive agreement. When the definitive agreement remains silent, the form of the transaction will decide the outcome. To preserve the target's or seller's attorney-client privilege, selling parties have started to incorporate the following terms in definitive agreements:

- In a merger or stock purchase, selling parties have addressed (1) preserving any privilege attaching to pre-merger attorney-client communications in connection with the transaction; (2) assigning

¹⁵ *Dlo Enters. v. Innovative Chem. Prods. Grp., LLC*, No. 2019-0276-MTZ, 2020 Del. Ch. LEXIS 202, at *2 (Del. Ch. 2020).

¹⁶ *Dlo Enters.*, at *4.

¹⁷ *Id.* at *5.

the control over such privilege to the shareholders or other representatives of the target; (3) requiring the shareholders and buyer to take steps necessary to ensure that the privileges remain in effect; and (4) preventing the buyer from using or relying on any privileged communications in post-closing litigation.¹⁸

- In an asset purchase, selling parties have specified in the asset purchase agreement that the attorney-client privilege constitutes an excluded asset that will be retained by the seller (or otherwise transferred to affiliates or representatives of seller) following the closing.

Due to contractual freedom, selling parties are well-positioned at the outset of a transaction to prevent unintended transfers of the attorney-client privilege. Parties to a transaction, regardless of whether a merger, stock purchase or asset purchase, will want to connect with their attorneys early in the process to ensure that the definitive agreement appropriately addresses their desired result.

**ULTIMATELY, THE
PARTIES IN A MERGER,
STOCK PURCHASE OR
ASSET PURCHASE HAVE
THE POWER TO DEFINE
THE *WHOSE* OF THE
ATTORNEY-CLIENT
PRIVILEGE IN THE
DEFINITIVE AGREEMENT.**

¹⁸ See *Shareholder Representative Servs. LLC* at *3.

About the Authors:



Jeffrey A. Fickes

Partner, Chair of Private Equity
jafickes@vorys.com
216.479.6123

Jeff is a senior M&A, private equity and corporate partner and chair of the Vorys private equity group. Jeff represents businesses located throughout the United States and internationally and is a trusted advisor to company owners, boards and senior executives on domestic and international merger, acquisitions, dispositions, joint ventures and other strategic transactions; private equity, venture capital, recapitalization and other debt and equity financings; and corporate governance and organizational matters.



Bruce P. Paige

Partner, Chair of M&A
bppaige@vorys.com
614.464.6359

Bruce is a partner and chair of the Vorys M&A group. He regularly assists clients, including numerous Fortune 1000 corporations, health care providers and various state instrumentalities, in the structuring and negotiation of joint ventures, mergers and acquisitions, and other strategic transactions involving both private and public companies and related corporate governance matters.



Lauren A. Brown

Associate
labrown@vorys.com
614.464.6224

Lauren is an associate in the corporate group. She assists both public and private companies in corporate and transactional matters, including mergers and acquisitions, securities offerings, proxy contests, periodic reporting and disclosure (Form 10-K, 10-Q and 8-K reporting and proxy statement disclosure) and corporate governance. Lauren regularly counsels companies on compliance with Securities and Exchange Commission regulations and with NYSE and

NASDAQ rules.

About the Vorys M&A Group:

We advise public companies, middle-market private companies, closely-held and family-owned businesses, and start-up and emerging companies, as well as boards of directors, special committees, financial sponsors, and private equity/venture capital firms, in global M&A transactions. Our M&A attorneys represent clients in a broad spectrum of industries, including retail, oil and gas, energy, consumer products, restaurants, manufacturing, insurance, health care, financial institutions, homebuilding, distribution, pharmaceuticals, technology/software, and real estate. Additionally, members of our M&A team have served as in-house General Counsel at public and private companies. To learn more, visit vorys.com/services-manda.html.

About the Vorys Private Equity Group:

Vorys represents private equity, venture capital, mezzanine funds and hedge funds, sponsors, family offices, investment firms, fund investors, senior and subordinated debt lenders and portfolio companies in all aspects of fund and entity formation, operation and fundraising, M&A and joint ventures, leveraged lending, recapitalizations and other debt and equity finance transactions, as well as other comprehensive full-service legal matters. Our private equity transactional experience ranges from \$1 million to more than \$1 billion and we have represented private equity related clients in transactions in almost all 50 states, as well as in cross-border transactions. To learn more, visit vorys.com/services-private-equity.html.

VORYS

