ACCOUNTANTS, ATTORNEY-CLIENT PRIVILEGE, AND THE *KOVEL* RULE: WAIVER THROUGH INADVERTENT DISCLOSURE VIA ELECTRONIC COMMUNICATION

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ABSTRACT

Under certain circumstances, a lawyer may shield a non-testifying accountant or other business expert under the Kovel *rule. This rule extends the attorney-client privilege to accountant-client communications and to work product when the accountant is hired to help in rendering legal services. The party claiming the privilege bears the burden of proving the existence of the factors required to sustain it. Various protective measures reviewed in this article are vital to preserve the extension of the privilege to accountants and other business experts.*

I. INTRODUCTION

Attorneys and accountants must be concerned with the risks of inadvertent disclosure and eavesdropping from the use of cordless and cellular telephones, faxes, and e-mail. In some cases, inadvertent disclosure leads to the loss of the attorney-client and *Kovel* privileges. We suggest numerous steps to minimize the likelihood of loss of the privileges.

Accountants will increasingly find themselves being hired by attorneys and other clients as consultants in complex financial litigation cases. Open communication between the accountant and client is essential to providing high quality consulting services. In many instances,

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accountant-client communications contain information that the client would prefer to remain confidential. In a litigation scenario, however, the content of such communications may require disclosure to an adversary or government agency. Often such disclosure can result in undesirable costs and consequences for accountants, attorneys, and clients.

The inability to insulate and protect accountant communications and work product from disclosure in a litigation or government investigation setting presents a unique challenge.[1] Despite the existence of accountant-client privilege statutes in some states,[2] these statutes often are of little value to the accountant-client relationship in a litigation environment.[3] Because accountant-client privilege is not recognized under federal common law and does not attach to communications between the client and accountant,[4] state accountant-client privilege statutes may not be applied in federal cases.[5]

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[1]The CPA's ability to deliver quality services while still maintaining the confidentiality necessary to promote client openness is paramount. A client's failure to provide all requisite information may be material to the ultimate quality of the advice an accountant provides to the attorney. Mark A. Segal, *Accountants and the Attorney-Client Privilege*, J. ACCT., Apr. 1997, at 53.

[2]*See* ARIZ. REV. STAT. ANN. § 32-749 (West 2002); COLO. REV. STAT. § 13-90-107(1)(f) (West 1997); CONN. GEN. STAT. ANN. § 20-281j (West 1999); FLA. STAT. ANN. § 473.316 (West 2001); GA. CODE ANN. § 43-3-32(b) (2002); IDAHO CODE § 9-203A (Michie 1998); 225 ILL. COMP. STAT. ANN. § 450/27 (West 1998); IND. CODE ANN. § 25-2.1-14-1 (Michie 1996); KAN. STAT. ANN. § 1-401(b) (2001); KY. REV. STAT. ANN. § 325.440 (Michie 2002); LA. REV. STAT. ANN. § 37:87 (West 2000); ME. REV. STAT. ANN. tit. 32, § 12279 (West 1999); MD. CODE ANN., CTS. & JUD. PROC. § 9-110(b) (2002); MASS. GEN. LAWS ANN. ch. 112, § 87E (West 1996); MISS. CODE ANN. § 73-33-16 (1999); MO. ANN. STAT. § 326.151 (West 2001); MONT. CODE ANN. § 37-50-402 (2001); NEV. REV. STAT. ANN. § 49.185 (Michie 2001); N.M. STAT. ANN. § 38-6-6 (Michie 2003); PA. STAT. ANN. tit. 63, § 9.11a (West 1996); R.I. GEN. LAWS § 5-3.1-23 (1999); TENN CODE ANN. § 62-1-116 (1997); VT. ST. ANN. tit. 26, § 82 (1998); WASH. REV. CODE ANN. § 18.04.405 (West 1999).

[3]The accountant-client privilege has been recognized by twenty-five states. "The application and scope of these statutory privileges varies [sic] by jurisdiction but overall ha[ve] been severely limited by judicial interpretation" and various exceptions. For example, "various state statutes are inapplicable in criminal and bankruptcy proceedings." Alicia Corcoran, *The Accountant-Client Privilege: A Prescription for Confidentiality or Just a Placebo?* 34 NEW ENG. L. REV. 697, 727-28 (2000).

[4]In *Couch v. United States,* 409 U.S. 322 (1973), the Supreme Court examined the case of a restaurant owner who, after a number of years of providing her business records to her accountant for tax preparation, was confronted with an IRS investigation. The IRS issued a summons to the accountant for the production of the restaurant owner's business records upon discovering evidence that gross income had been substantially understated. *Id.* at 323. The accountant transferred the business records to the restaurant owner's attorney. *Id.* at 325. In response to an action to enforce the summons, the taxpayer argued that the Fourth and Fifth Amendments barred production of the business records because of the confidential nature of the accountant-client relationship and an expectation of privacy. *Id.* The Court held "that no Fourth or Fifth Amendment claim can prevail where . . . there exists no legitimate expectation of privacy." *Id.* at 336.

[5]*Couch*, 409 U.S. at 335.

Federal courts cite numerous reasons for disallowing an accountant-client privilege.[6]

[6]One reason is that attorneys and accountants serve different roles. An attorney is a confidential advisor and an advocate with a duty of undivided loyalty to the client. United States v. Arthur Young, 465 U.S. 805, 817 (1984). The attorney-client privilege encourages full disclosure by the client which is necessary for proper representation. *See* Hunt v. Blackburn, 128 U.S. 464, 470 (1888); United States v. Grand Jury Investigation, 401 F. Supp. 361, 369 (W.D. Pa. 1975). An accountant, on the other hand, owes a duty of loyalty not just to the client, but to investors, lenders, regulators, and society at large. *Arthur Young,* 465 U.S. at 817-18.

Although section 7525 of the Internal Revenue Code (IRC) established an accountant-client privilege for tax advice in noncriminal matters before the IRS and in noncriminal tax proceedings in federal court involving the United States,[7] the statutory privilege is very narrow and uncertain,[8] and "[a]n uncertain privilege . . . is little better than no privilege at all."[9] Despite the protection provided by IRC section 7525, taxpayers are still "exposed to testimony by their accountants in all private civil actions, all criminal proceedings, and in civil tax proceedings where written communications regarding corporate tax shelters are involved."[10]

[7]I.R.C. § 7525 (a)(1) (2003).

[8]*See generally* Alyson Petroni, *Unpacking the Accountant-Client Privilege Under I.R.C. Section 7525*, 18 VA. TAX REV. 843, 857-58 (1999) (explaining problems with reliance on the privilege).

[9]Upjohn Co. United States, 449 U.S. 383, 393 (1981).

[10]Petroni, *supra* note 8, at 858.

Accountants also cannot normally protect their work under a work-product privilege. This privilege differs from the accountant-client privilege in that the work-product privilege relates to the introduction of materials and documents into evidence during a judicial proceeding.[11] In *United States v. Arthur Young*,[12] the United States Supreme Court ruled that accountants had no work-product privilege because of a potential conflict of interest, or at a minimum, the appearance of a conflict, which may result when a CPA is granted privilege. The conflict occurs because a CPA, who is supposed to be independent regarding the attestation of financial statements or preparation of tax returns, is cast in the role of advocate (e.g., tax consulting). This "role of advocacy" is evidenced by the need for a work-product, or even communication, privilege between the accountant and client.

Despite the difficulties associated with the accountant-client privilege, accountant-client communications and work product may still be shielded from disclosure when an accountant works as an agent of an attorney rendering legal services.[13] Accountants and the attorneys who hire them should be aware, however, of the risks posed to the attorney-client privilege by the use of electronic communications such as cordless/cellular phones, faxes, and e-mail. In some cases, the privilege may be lost by inadvertent disclosure of confidential information.

The purposes of this article are fourfold. First, we will examine the attorney-client privilege and its application and extension to accountants (the

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[11]The work-product privilege, contained in the Federal Rules of Civil Procedure, provides that documents prepared in anticipation of litigation or trial are not subject to discovery without a showing of substantial need and undue hardship to obtain equivalent material. For example, an attorney's "mental impressions, conclusions, opinions, or legal theories" included in documents are immune from disclosure even with a showing of substantial need and undue hardship. FED. R. CIV. P. 26(b)(3).

[12]465 U.S. 805, 808, 812-20 & n.15 (1984). In this case, Arthur Young & Co. had reviewed financial statements, including the preparation of tax accrual workpapers, for Amerada Hess Corporation. In a subsequent IRS criminal investigation of Amerada Hess tax returns, the IRS summoned all of Arthur Young's files including the tax accrual workpapers. Arthur Young refused to comply with the summons. The Supreme Court held that Arthur Young possessed no work-product privilege with respect to the tax accrual workpapers. "For example, a CPA, who is supposed to issue a qualified or adverse opinion" under various circumstances may fail to disclose a material issue communicated during an advising session because of privilege. Therese LeBlanc, *Accountant-Client Privilege: The Effect of the IRS Restructuring and Reform Act of 1998*, 67 U.M.K.C. L. REV. 583, 591 (1999).

[13]United States v. Judson, 322 F.2d 460, 462 (9th Cir. 1963); United States v. Kovel, 296 F. 2d 918, 921 (2d Cir. 1961). Communications and work product involving "an expert who testifies are generally discoverable, however. An accountant-consultant serving as an expert witness should be insulated from the client as much as possible and limited to 'need to know' information about the case." Edward M. Spiro & Caroline Rule, *Kovel Experts Cloaked By Attorney-Client Privilege*, N.Y. L.J., Feb. 22, 1994, at S10.

Kovel rule). Second, we will outline how the inadvertent disclosure of confidential information in cordless/cellular telephone calls, faxes, and e-mails may lead to the waiver of the attorney-client privilege. Third, we will suggest practical ways to help protect the attorney-client and *Kovel* privileges from challenge. Fourth, we will offer practical suggestions on how to minimize the loss of privilege via the use of electronic communications.

II. OVERVIEW OF ATTORNEY-CLIENT PRIVILEGE

Federal Rule of Evidence 501 is the basis for the attorney-client privilege in federal courts. The rule provides that "the privilege of a witness . . . shall be governed by the principles of the common law as they may be interpreted by the courts of the United States in the light of reason and experience."[14] The attorney-client privilege is the oldest privilege established by the common law.[15] The privilege developed to preclude an attorney from having to testify against his client.[16] Originally, the privilege attached or belonged to the attorney, but today, it is considered to belong to the client.[17] The attorney, however, can assert the privilege on the client's behalf.[18]

The policy behind the attorney-client privilege is to "encourage clients to make full disclosure to their attorneys."[19] Most clients are more willing to disclose pertinent information to their counsel if they know their communications will remain confidential.[20] Invasion of the privilege would permit the prosecution of more criminals. This invasion, however, would have a negative impact on the American justice system. Clients, knowing that their communications would be subject to disclosure, would ultimately be less forthright with their lawyers or sacrifice legal services completely.[21] The small amount of empirical data available that either supports or refutes the policy or assumption underlying the privilege is not conclusive.[22]

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[14]FED. R. EVID. 501.

[15]United States v. Schwimmer, 892 F.2d 237, 243 (2d Cir. 1989).

[16]8 WIGMORE, EVIDENCE IN TRIALS AT COMMON LAW § 2290 (McNaughton rev. 1961).

[17]United States v. Bilzerian, 926 F.2d 1285, 1292 (2d Cir. 1991).

[18]*In re* Grand Jury Subpoena Duces Tecum, 391 F. Supp. 1029, 1033 (S.D.N.Y. 1975).

[19]Fisher v. United States, 425 U.S. 391, 403 (1976).

[20]Swidler & Berlin v. United States, 524 U.S. 399, 407 (1998).

[21]*In re* Grand Jury Proceeding, 898 F.2d 565, 569 (7th Cir. 1990).

[22]At least two of the studies conducted on the issue of attorney-client privilege have concluded that people seeking legal advice may misunderstand the privilege. One early study at Yale University concluded that non-attorneys had an erroneous understanding of the privilege and that it was more important to attorneys than clients. Comment, *Functional Overlap Between the*

Lawyer and Other Professionals: Its Implications for the Privileged Communications Doctrine, 71 YALE L.J. 1226, 1232 (1962). Another study found that clients had some misunderstanding about confidentiality but that a substantial number had relied on confidentiality when providing information to their attorneys. Fred C. Zacharias, *Rethinking Confidentiality,* 74 IOWA L. REV. 351, 364 (1989).

Moreover, "[i]f the privilege is to encourage disclosure, the client must be" certain that the "communicated disclosure will enjoy the privilege in any possible future legal proceeding."[23] "If the professional knows that he might be forced to disclose communications, he may be hesitant to aggressively solicit information from his client."[24] "If a lawyer could not promise to maintain the confidentiality of his client's secrets, the only advice he or she could provide would be 'Don't talk to me.'"[25]

Proposed Rule of Evidence 503, also known as Supreme Court Standard 503, sets the general boundaries for determining the scope of the attorney-client privilege:

> A client has a privilege to refuse to disclose and to prevent any other person from disclosing confidential communica-tions made for the purpose of facilitating the rendition of professional legal services to the client,
> (1) between [the client or client's] representative and his lawyer or his lawyer's representative, or
> (2) between [the client's] lawyer and [that] lawyer's representative, or
> (3) by [the client] or his lawyer to a lawyer representing another in a matter of common interest, or
> (4) between representatives of the client or between the client and a representative of the client, or
> (5) between lawyers representing the client.[26]

The existence of the attorney-client relationship alone is not sufficient to invoke the attorney-client privilege.[27] The privilege must be claimed with

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[23]Grace M. Giesel, *The Legal Advice Requirement of the Attorney-Client Privilege: A Special Problem for In-House Counsel and Outside Attorneys Representing Corporations,* 48 MERCER L. REV. 1169, 1186 (1997). It can be seen that:

> [t]o obtain a degree of certainty, any utilitarian balancing of the benefits and burdens of the privilege should occur on a rule basis, not on an ad hoc basis. . . . Balancing in individual cases cannot occur if the underlying rationale of the privilege is to succeed because the communicator client can never with any degree of certainty predict whether a court will later determine that in the particular facts of a litigation, the benefits of the privilege outweigh the burdens.

Id. at 1187.

[24]Alison M. Hill, *A Problem of Privilege: In-House Counsel and the Attorney-Client Privilege in the United States and the European Community,* 27 CASE W. RES. J. INT'L L. 145, 173 (1995).

[25]Southern Cal. Gas Co. v. Public Utils. Comm'n, 784 P.2d 1373, 1375-76 (Cal. 1990).

[26]PROPOSED FED. R. EVID. 503(b).

[27]Emily Jones, *Keeping Client Confidences: Attorney-Client Privilege and Work-Product Doctrine in Light of* United States v. Adlman, 18 PACE L. REV. 419, 422 (1998).

regard to a particular communication and extends only to the communication and not to facts.[28] "The privilege must also be invoked before any disclosure of the communication sought to be protected has occurred, otherwise the privilege is waived."[29] If the client communicates with an attorney solely for a business purpose, then the privilege does not apply.[30]

[28]*See* Shiner v. American Stock Exch., 28 F.R.D. 34 (S.D.N.Y. 1961). The cloak of the privilege protects only the communication from discovery not the underlying information contained in the communication. *See* Sneider v. Kimberley-Clark Corp., 91 F.R.D. 1, 4 (N.D. Ill. 1980).

[29]Jones, *supra* note 27, at 422.

[30]Giesel, *supra* note 23, at 1190.

If a client communicates a matter to his lawyer in the presence of a third party who is not an agent of the lawyer, the communication is not confidential.[31] Courts presume that the presence of a third person (who is not an agent of the attorney or client) during the communication indicates a lack of intent for the communication to remain confidential.[32] One exception to the third party waiver rule is the joint defense or common interest rule, which protects the confidentiality of communications between multiple parties and their attorneys when such parties share a common legal interest.[33]

Various tests have been set forth by the courts to determine whether the attorney-client privilege applies to a particular case. Each test, however, requires that the party claiming the privilege prove the existence of each of the following elements:

1. The holder of the privilege is or sought to become a client;
2. The person to whom a communication is made is a licensed attorney or his agent;
3. The attorney is acting as the client's lawyer with regard to the communication; and
4. The communication relates to a matter of which the attorney was informed by his client, without the presence of third parties, for the purpose of securing

[31]United States v. Workman, 138 F.3d 1261, 1263 (8th Cir. 1998) ("Voluntary disclosure of attorney client communications expressly waives the privilege . . . ."); United States v. Evans, 113 F.3d 1457, 1462 (7th Cir. 1997) ("[T]he attorney-client privilege will not shield from disclosure statements made by a client to his or her attorney in the presence of a third party who is not an agent of either the client or attorney.").

[32]*See, e.g.*, United States v. Gurtner, 474 F.2d 297, 298 (9th Cir. 1973).

[33]It is unnecessary that there be actual litigation in progress for the joint defense or common interest rule of the attorney-client privilege to apply. United States v. Zolin, 809 F.2d 1411, 1417 (9th Cir. 1987), *vacated in part on other grounds,* 842 F.2d 1135 (9th Cir. 1988) (en banc), *aff'd in part and vacated in part on other grounds,* 491 U.S. 554 (1989).

> legal services and not for the purpose of committing a crime or tort.[34]

Although each element above must be supported by facts, deciding whether the attorney-client privilege exists is done on a case-by-case/common sense basis.

[34]United States v. United Shoe Mach. Corp., 89 F. Supp. 357, 358 (D. Mass. 1950); Colton v. United States, 306 F.2d 633, 637 (2d Cir. 1962), *cert. denied*, 371 U.S. 951 (1963).

Application of the privilege to corporations, including situations involving in-house counsel, has been problematic because corporations can act only through their agents. Various arguments have been raised against applying the attorney-client privilege to corporations, but have been dismissed by the courts.[35]

In *Upjohn Co. v. United States*,[36] the Supreme Court faced the question of which corporate employees could claim attorney-client privilege on behalf of the corporation. In response to a criminal investigation involving allegations of bribery, Upjohn declined to produce various documents demanded by the IRS. The court held that the documents were

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[35]One argument against application of attorney-client privilege to corporations comes from Radiant Burners, Inc. v. American Gas Ass'n, 207 F. Supp. 771 (N.D. Ill. 1962), *rev'd.,* 320 F.2d 314 (7th Cir. 1963). This argument has two components. First, the attorney-client privilege has its roots in the privilege against self-incrimination that can only be claimed by individuals. *Id.* at 773. Second, underlying the attorney-client privilege is the fact that the communication is completely confidential between the attorney and client. In a corporation, the larger number of people with access to the information increases the likelihood of waiver. *Id.* at 773-74. A second argument is that application of the attorney-client privilege to corporations will create manipulative practices. A corporation could structure its operations so that much of its routine business decisions become privileged by transmittal to corporate counsel. Michael L. Waldman, *Beyond Upjohn: The Attorney-Client Privilege in the Corporate Context,* 28 WM. & MARY L. REV. 473, 483 (1987). This argument does not take into consideration the fact that even though a communication is privileged, the underlying facts are still discoverable. Hill, *supra* note 24, at 170.

[36]449 U.S. 383, 388 (1981).

protected by privilege.[37] Interestingly, the court rejected the IRS' argument that in order for the privilege to apply, an employee must be a member of the "control group" of a client, i.e., those with decision-making authority.[38] Although the Court did not draft a set of formal criteria for all situations involving the attorney-client privilege in the corporate setting, the following guidelines were offered for application on a case-by-case basis:

[37] *Id.* at 402.

[38] The Court reasoned that :

> [t]he control group test adopted by the court below thus frustrates the very purpose of the privilege by discouraging the communication of relevant information by employees of the client to attorneys seeking to render legal advice to the client corporation. The attorney's advice will also frequently be more significant to noncontrol group members than to those who officially sanction the advice, and the control group test makes it more difficult to convey full and frank legal advice to the employees who will put into effect the client corporation's policy.

Id. at 392.

> [A] communication is privileged at least when . . . an employee or former employee speaks at the direction of the management with an attorney regarding conduct or proposed conduct within the scope of employment. The attorney must be one authorized by the management to inquire into the subject and must be seeking information to assist counsel in . . . (a) evaluating whether the employee's conduct has bound or would bind the corporation; (b) assessing the legal consequences, if any, of that conduct; or (c) formulating appropriate legal responses to actions that have been or may be taken . . . .[39]

The protection afforded by the attorney-client privilege is limited to those situations where the communication would not have been made but for the client's need for legal services or advice.[40] The *Upjohn* decision left no doubt that the privilege applies to in-house counsel, but lower courts have disagreed on the scope of the privilege.

In-house counsel often have dual business and legal responsibilities within a corporation. Under *Hardy v. New York New, Inc.*, when a corporate decision is based on both business policy and a legal evaluation, the business aspects of that decision are not protected by the privilege simply because legal considerations are involved.[41] In *In re Sealed Case,* the Court of Appeals for the District of Columbia held that advice rendered by in-house counsel, who had managerial as well as legal responsibilities, falls under the attorney-client privilege only upon a clear showing that the advice was given in a professional legal capacity.[42] Examples of business advice not protected by the attorney-client privilege are preparation of tax returns and rendition of investment advice.[43]

It has been argued that in-house counsel is held to a higher standard than outside counsel for attorney-client privilege to attach.[44] The higher standard would require a clear showing by in-house counsel that it is legal advice for which the protection of the attorney-client privilege is sought.[45] Outside counsel does not face a higher standard because an outside attorney lacks business responsibilities within a corporation.[46] If no such require-

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[39] *Id.* at 403.

[40] John E. Sexton, *A Post-Upjohn Consideration of the Corporate Attorney-Client Privilege,* 57 N.Y.U. L. REV. 443, 487 (1982).

[41] 114 F.R.D. 633, 646 (S.D.N.Y. 1987).

[42] 737 F.2d 94, 99 (D.C. Cir. 1984).

[43] *In re* Witness Before the Grand Jury, 631 F. Supp. 32, 33 (E.D. Wis. 1985).

[44] United States v. Adlman, 68 F.3d 1495 (2d Cir. 1995).

[45] *In re Sealed Case*, 737 F.2d at 99.

[46] *Id.*

ment were placed upon in-house counsel, all advice, legal or otherwise, would fall within the attorney-client privilege.[47]

III. EXTENSION OF ATTORNEY-CLIENT PRIVILEGE TO ACCOUNTANTS: THE *KOVEL* RULE

[47] *Id.*

A lawyer may cloak an accountant with the protection of the attorney-client privilege. The landmark decision in *United States v. Kovel*[48] extended the attorney-client privilege to communications between a client and a third party hired by an attorney to provide accounting services. Louis Kovel was a former IRS agent hired by a law firm to assist in advising the firm's clients on accounting issues. Kovel met with a client who was under IRS investigation for tax fraud and received the client's personal financial statement along with a cover letter indicating the purpose for sending the financial statement.[49] After being subpoenaed by a grand jury, Kovel refused to answer questions about his conversations with the client and the effect of various transactions.[50] Kovel was held in contempt of court.[51]

The Second Circuit Court of Appeals reversed the ruling and held that the presence of an accountant as an attorney's agent does not negate the attorney-client privilege.[52] The court balanced two competing theories in reaching its holding. The first theory is that the "investigation of truth . . . demand[s] the restriction . . . of these privileges."[53] The court noted that nothing in the policy underlying the attorney-client privilege suggests that all communications between clients and accountants, investigators, and other third parties should be privileged merely by the third party being on an attorney's payroll.[54] The second theory is that because of the complexities of modern existence few lawyers could operate without the aid of secretaries, clerks, telephone operators, law clerks, and others.[55] No reason could be found to limit extension of the privilege to those who perform ministerial or clerical duties while excluding accountants.[56] The court ruled that the

[48]296 F.2d 918, 919 (2d Cir. 1961).
[49]*Id.* at 919-20.
[50]*Id.* at 920.
[51]*Id.*
[52]*Kovel*, 296 F.2d at 922.
[53]*Id.* at 921.
[54]*Id.*
[55]*Id.*
[56]*See Kovel*, 296 F.2d at 921.

privilege shields communications with an accountant retained by the lawyer or client to assist in providing legal services to the attorney's client.[57]

[57] *Id.* at 924.

The appellate court opinion also attempted to define the boundaries of the *Kovel* privilege. In ruling that the privilege applies only to communications for the purpose of obtaining legal advice, not accounting services, the court acknowledged that an "arbitrary line" was being drawn.[58] That arbitrary line falls between a case in which the client communicates first to his own accountant and then later with his lawyer (in which case no privilege exists) and one in which the client initially retains an attorney who then hires an accountant, or the client first consults with both the lawyer and accountant simultaneously (in which case privilege exists).[59] Although arbitrary, this distinction was upheld by the Eighth Circuit in *United States v. Cote*.[60] The distinction is necessary to prevent the privilege from being unduly expanded.

The *Kovel* privilege is extended to an accountant so long as a communication is made to assist an attorney in disseminating legal services to the client.[61] In *United States v. Gurtner*, an attorney directed a client to consult with an accountant regarding the client's conviction for willful failure to file a federal income tax return. On appeal, the Ninth Circuit refused to extend attorney-client privilege to the accountant because there was insufficient evidence to show that the accountant's services were for the purpose of rendering legal advice.[62] If accounting advice is sought rather than legal advice, no privilege attaches.[63] Moreover, extension of the privilege to a communication means that "the accountant's presence must be more than a convenience."[64] "[E]ven legal advice is unprivileged if it is

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[58]*Id.* at 922.

[59]*Id.*

[60]456 F.2d 142 (8th Cir. 1972).

[61]United States v. Schwimmer, 892 F.2d 237, 243 (2d Cir. 1989).

[62]474 F.2d 297, 298 (9th Cir. 1973).

[63]Corcoran, *supra* note 3, at 725.

[64]*Id.* In *Himmelfarb v. United States*, 175 F.2d 924 (9th Cir. 1949), the court ruled that an

merely incidental to business advice."[65] In contrast, in *United States v. Judson*, the Ninth Circuit applied the *Kovel* rule to various memoranda and a personal net worth statement prepared by an accountant who was hired by an attorney because the former's role was to "facilitate an accurate and complete consultation between the client and the attorney about the former's financial picture."[66]

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accountant's presence at a conference between the lawyer and taxpayer-client was only a convenience. The appellate court refused to accept the argument that all agents of a lawyer who receive client communications are beneficiaries of the privilege.

[65]Durham Indus., Inc. v. North River Ins. Co., No. 79 Civ. 1705 (RWS), 1980 U.S. Dist. LEXIS 15154, at *8 (S.D.N.Y. Nov. 21, 1980).

[66]322 F.2d 460, 462 (9th Cir. 1963).

The *Kovel* rule received further clarification in *United States v. Adlman*.[67] In this case, Sequa Corporation's in-house counsel, Adlman, hired Arthur Andersen, the corporation's auditor, to prepare a memorandum of the tax consequences of a proposed corporate reorganization.[68] The draft and final memoranda were delivered by Arthur Anderson to Sequa's in-house counsel after discussions between Arthur Anderson and Adlman.[69] Two days after delivery of the final memorandum to in-house counsel, Arthur Anderson sent a summary of recommendations directly to Sequa's management.[70] Sequa consummated the transaction as recommended by Arthur Anderson.[71]

Sequa claimed attorney-client privilege in response to an IRS subpoena to produce the memorandum.[72] Sequa argued that it relied on in-house counsel for legal advice about the transaction and that the memorandum was prepared to aid in-house counsel in rendering legal services.[73] The Second Circuit Court of Appeals held that attorney-client privilege did not apply because the evidence indicated that Sequa consulted with an accounting firm for tax advice rather than in-house counsel receiving accounting advice to assist in rendering legal services.[74] The court noted that Sequa had not produced adequate documentation, such as a separate retainer agreement or itemized billings, for the tax advice to support a claim

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[67]68 F.3d 1495 (2d Cir. 1995).

[68]*Id.* at 1497.

[69]*Id.*

[70]*Id.*

[71]"On its 1989 tax return, Sequa claimed a tax loss of approximately $290 million from the transaction. Part of that loss was carried back to offset millions of dollars of Sequa's capital gains from 1986, thereby generating a large tax refund." *Adlman*, 68 F.3d at 1497.

[72]*Id.* at 1498.

[73]*Id.*

[74]*Id.* at 1500.

of privilege.[75] The only evidence offered to uphold privilege was a series of affidavits prepared by interested parties four years after the transaction at issue.[76] Thus, it is incumbent upon those claiming attorney-client privilege to produce adequate documentation to demonstrate that the main purpose in hiring the accountant was to assist the attorney in providing legal services.

[75] *Adlman*, 68 F.3d at 1500.
[76] *Id.*

The holding in *Adlman* has implications for experts other than accountants, as the *Kovel* rule has been extended beyond accountants to other third-party experts. Although few court decisions address *Kovel's* application to consultants other than accountants, it has been applied to communications with a psychiatrist,[77] an operator of a polygraph,[78] a patent agent assisting an attorney,[79] and a public relations consultant who assisted an attorney.[80] In *Federal Trade Commission v. TRW, Inc.*, the D.C. Circuit

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[77]*See generally* United States v. Alvarez, 519 F.2d 1036 (3rd Cir. 1975). In this case, the Third Circuit Court of Appeals cited *Kovel* with approval in holding that "[w]e see no distinction between the need of defense counsel for expert assistance in accounting matters and the same need in matters of psychiatry." *Id.* at 1046.

[78]*See generally* People v. George, 428 N.Y.S.2d 825 (N.Y. Sup. Ct. 1980). A polygraphist, who was retained by a criminal defendant's attorney, was privy to certain inculpatory statements made by the defendant in confidence (during a lie detector test). The polygraphist was called as a witness by the prosecution and refused to answer claiming privileged communications. The court ruled that the *Kovel* privilege applied to the polygraphist.

[79]*See generally* Golden Trade S.r.L. v. Lee Apparel Co., 143 F.R.D. 514 (S.D.N.Y. 1992). Golden Trade, an Italian corporation and an owner of a U.S. patent, sued Lee Apparel Company for patent infringement. During discovery, Lee Apparel sought production of communications between a patent licensee of Golden Trade (IGD) and patent agents the licensee had retained to prosecute patent applications in other countries. The court found that the *Kovel* rule applied to patent agents acting to assist attorneys to provide legal services.

[80]*See generally* H.W. Carter & Sons, Inc. v. William Carter Co., No. 95 Civ. 1274 (DC), 1995 U.S. Dist. LEXIS 6578 (S.D.N.Y. May 15, 1995). During discovery, plaintiff corporation sought to depose defendant corporation's former officers. Plaintiff hoped to receive information about investigations into potential trademark infringements that the officers performed for defendant. The court ruled that *Kovel* privilege applied to the officer-public relations consultant.

Court of Appeals suggested that the *Kovel* privilege could apply to a situation in which a research institute was hired by an attorney for TRW, Inc., a credit reporting agency, to prepare a study of the company's computerized credit reporting system. The court, however, ultimately did not uphold the privilege: "Where, as here, we have not been provided with sufficient facts to state with reasonable certainty that the privilege applies, this burden is not met. As noted earlier, TRW's claim lies at an outer and indistinct boundary of the law of attorney-client privilege."[81]

[81] 628 F.2d 207 (D.C. Cir. 1980).

In a more recent case, *In re Bieter Co.*, a federal appellate court approved application of the attorney-client privilege to various communications between a law firm and a real estate consultant engaged by the client, who was a real estate developer.[82] The real estate consultant was hired as an independent contractor under a written agreement during the initial phase of land development. The consultant worked with architects, engineers, and counsel, and appeared at public hearings involving local government officials.[83] He also received many communications from attorneys both directly and indirectly.[84] The legal issue of attorney-client privilege was complicated by the consultant not being an employee of the client, but rather an independent contractor who was a representative of the client.

The Eighth Circuit Court of Appeals held that, when applying the attorney-client privilege, "it is inappropriate to distinguish between those on the client's payroll and those who are . . . independent contractors."[85] The court upheld the extension of the attorney-client privilege to the consultant, identifying several factors for determining whether the privilege protects the communications at issue.[86]

"The first requirement is that the communication be made for the purpose of seeking legal advice."[87] The burden is on those seeking application of the privilege to show that the end result of the communication was the rendition of legal services or advice to the client. Second, the third-party expert involved in the communication(s) must have communicated at the direction of the client.[88] The third requirement is that the client requested the communication to obtain legal advice.[89] Fourth, the subject matter of the communication must be within the scope of the consultant's duties.[90] Fifth, the communication must not be disseminated beyond those parties who need to know.[91] These factors were applied in upholding the extension of attorney-client privilege to a public relations firm hired as an independent contractor in *In re Copper Market Antitrust Litigation*.[92]

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[82]16 F.3d 929, 933-34 (8th Cir. 1994).

[83]*Id.* at 934.

[84]*Id.*

[85]*In re Bieter Co.*, 16 F.3d at 937.

[86]*See id.* at 938-39.

[87]*Id.* at 938.

[88]*Id.* at 939.

[89]*In re Bieter Co.*, 16 F.3d at 939.

[90]*Id.*

[91]*Id.*

[92]200 F.R.D. 213 (S.D.N.Y. 2001). Viacom, Inc. and Emerson Electric Co. brought an action against Sumitomo Corporation and others for an alleged conspiracy to manipulate global

copper prices. Sumitomo hired Robinson Lerer & Montgomery (RLM), a crisis management public relations firm, to deal with issues relating to publicity arising from high profile litigation. RLM conferred frequently with Sumitomo's outside and in-house counsels. "RLM was the functional equivalent of an in-house public relations department with respect to western media relations, having authority to make decisions and statements on Sumitomo's behalf, and seeking and receiving legal advice from Sumitomo's counsel . . . ." *Id.* at 215-16.

Despite the significance of the *Bieter* decision, the boundaries of the *Kovel* rule are still tightly drawn and application of the privilege is strictly interpreted. For example, in *United States v. Ackert*, the Second Circuit Court of Appeals refused to extend the *Kovel* privilege to a communication between a third-party investment banker, who was not a client or an agent of a client, and an attorney solely because a communication proved important to the attorney's ability to represent the client.[93] The attorney in this case was not relying on a third-party expert (Ackert) to interpret information given to the attorney by his client.[94] The lawyer sought out the expert for information that was not possessed by either the attorney or the client.[95] The Second Circuit thus appears to have held in *Ackert* that *Kovel* applies to communications with non-legal professionals only if the non-attorney acted "'as a translator or interpreter of client communications.'"[96]

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[93]169 F.3d 136, 138 (2d Cir. 1999). In 1989, Goldman, Sachs, and Co., an investment banking firm, approached Paramount with an investment proposal. Along with other Goldman, Sachs representatives, David Ackert pitched the investment proposal to Paramount representatives at a meeting on September 15. Although Ackert discussed the possible tax consequences of investments with potential clients, he did not provide legal or tax advice. After September 15, Meyers, Paramount's tax counsel, contacted Ackert several times to discuss various aspects of the Goldman, Sachs proposal. Paramount paid Goldman, Sachs a fee of $1.5 million for services rendered. In connection with an audit of Paramount, the IRS issued a summons to Ackert seeking his testimony about the 1989 proposal. Paramount asserted attorney-client privilege. *Id.* at 138.

[94]*Id.* at 139.

[95]*Id.* at 139-40.

[96]Stuart M. Riback, *Protecting Communications: When Attorneys and Non-Legal Professionals Talk,* N.Y.L.J., May 10, 1999, at S9 (quoting United States v. Ackert, 169 F.3d 136, 140 (2d Cir. 1999)).

Another case which draws a tight bound on *Kovel* is *ECDC Environmental, L.C. v. New York Marine & General Insurance Co.*[97] A federal court declined to extend the *Kovel* rule to reports by consultants who assisted counsel in examining the effectiveness of an environmental cleanup.[98] The court reasoned that none of the documents purportedly shielded by *Kovel* contained technical information from the client transmitted to a consultant to "translate" for counsel's benefit.[99] These various decisions illustrate that a carelessly structured *Kovel* relationship can leave the attorney-client privilege vulnerable to attack. The attorney-client and *Kovel* privileges are also susceptible to attack by interception or inadvertent disclosure of privileged information in electronic communications.

[97]No. 96 Civ. 6033 (BSJ) (HBP), 1998 U.S. Dist. LEXIS 8808 (S.D.N.Y. June 4, 1998).
[98]*Id.* at *51.
[99]*Id.* at *23-*24.

IV. WAIVER OF THE *KOVEL* PRIVILEGE BY INADVERTENT DISCLOSURE AND ELECTRONIC COMMUNICATIONS

A. *Inadvertent Disclosure and Theories of Waiver*

Generally, the client, not the attorney, is the holder of the attorney-client privilege. The client decides whether to claim or waive the privilege. In practice, however, the attorney has limited authority to waive the privilege.[100] Moreover, the privilege is not absolute.[101] Courts have restricted the attorney-client privilege and held that "[a]ny disclosure inconsistent with maintaining the confidential nature of the attorney-client relationship waives the . . . privilege."[102] In fact, the privilege may even be waived by an inadvertent disclosure.[103]

The widespread use of electronic communications, such as cordless/cellular telephones, faxes, and e-mail, has increased the risk of inadvertent disclosure and loss of the attorney-client privilege. An inadvertent disclosure involving electronic communications can take many forms, ranging from unintentionally faxing a document to an opposing attorney to the employment of sophisticated espionage methods by adversarial parties.[104] The loss of the attorney-client and *Kovel* privileges through inadvertent disclosure remains a very unsettled area of the law.

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[100]CHRISTOPHER B. MUELLER & LAIRD C. KIRKPATRICK, EVIDENCE § 5.28, at 440 (1995).

[101]*See In re* Subpoena Duces Tecum, 738 F.2d 1367, 1369 (D.C. Cir. 1984).

[102]United States v. Jones, 696 F.2d 1069, 1072 (4th Cir. 1982) (per curiam).

[103]*In re* Grand Jury Investigation of Ocean Transp., 604 F.2d 672, 673 (D.C. Cir. 1979); Western Fuels Ass'n, Inc. v. Burlington N. R.R. Co., 102 F.R.D. 201, 203 (D. Wyo. 1984).

[104]Edward H. Freeman, *Attorney-Client Privilege and Electronic Data Transmission,* 7 INFO. SYS. SEC. 46 (1999). An example of e-mail espionage occurred in 1998 in Boston. An

Internet bookseller, Interloc, allegedly used a computer program to intercept thousands of e-mail messages from Amazon.com to booksellers. Interloc, a dealer in rare and used books, also operated a small Internet service provider, called Valinet. Interloc's customers, many of them booksellers, had e-mail accounts at Valinet through which they would receive messages from Amazon.com. Interloc employees broke into other Internet service provides and stole passwords. Interloc was charged by federal prosecutors with ten counts of unlawfully intercepting e-mail messages and one count of unauthorized possession of passwords with intent to defraud. Steve Wilmsen, *Internet Merchant Accused of Intercepting Rival's E-Mail*, BOS. GLOBE, Nov. 23, 1999, at A1.

In cases involving inadvertent disclosure of privileged information, courts apply one of three waiver standards that exist along a continuum. The first is the strict responsibility approach, where any disclosure constitutes a waiver of the attorney-client privilege.[105] The second is the modern or no-waiver approach, wherein the client's intent to waive the privilege governs, and inadvertent disclosures cannot result in a waiver, because inadvertent disclosures are by definition, unintended.[106] The third or "balancing" approach favors looking at the facts surrounding the disclosure before determining that the privilege has been waived.[107] We now examine each of the three approaches.

B. *Strict Responsibility Approach*

The strict responsibility approach treats any inadvertent disclosure of privileged information as a waiver of the attorney-client privilege. Courts that follow the strict responsibility approach do not require intent as an element of waiver.[108] In fact, some courts insist that disclosure itself is deemed evidence of the client's intent not to keep the information privileged.[109] The rationale is that once a third party obtains possession of a privileged communication, confidentiality is lost and cannot be restored, regardless of a disclosure's inadvertency.[110]

The seminal case for the strict responsibility approach is *Underwater Storage, Inc. v. United States Rubber Co.* In that case, the plaintiff's lawyer inadvertently provided a privileged letter to the defendant pursuant to a

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[105]Underwater Storage, Inc. v. United States Rubber Co., 314 F. Supp. 546, 549 (D.D.C. 1970).

[106]Franzel v. Kerr Mfg. Co., 600 N.W.2d 66, 74-75 (Mich. Ct. App. 1999).

[107]United States v. Keystone Sanitation, 885 F. Supp. 672, 676 (M.D. Pa. 1994).

[108]FDIC v. Singh, 140 F.R.D. 252, 253 (D. Me. 1992).

[109]*Id.*

[110]International Digital Sys. Corp. v. Digital Equip. Corp., 120 F.R.D. 445, 449 (D. Mass. 1988).

consent order.[111] The plaintiff requested the return of the letter based on involuntary production, and further argued that if it was voluntary then the privilege was waived only as to the produced piece of paper.[112] The court dismissed the plaintiff's argument stating that:

[111] *Underwater Storage*, 314 F. Supp. at 548-49.

[112] *Id.* at 549.

> The plaintiff turned over to his attorney the documents to be produced. This letter was among them. The Court will not look behind this objective fact to determine whether the plaintiff really intended to have the letter examined. Nor will the Court hold that the inadvertence of counsel is not chargeable to his client. Once the document was produced for inspection, it entered the public domain. Its confidentiality was breached thereby destroying the basis for the continued existence of the privilege.[113]

The *Underwater Storage* court goes on to note that mere blind adherence to a mechanical formula would result when the policy underlying the attorney-client privilege can no longer be served.[114] The need for the privilege disappears once the opposing party knows the contents of the privileged communication.[115]

The strict responsibility approach is easy to administer and yields predictable results.[116] Courts that favor this approach also assert that it encourages attorney diligence during document production.[117] The strict responsibility approach implies "that the narrower the privilege, the more

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[113] *Id.*

[114] *Id.*

[115] United States v. Kelsey-Hayes Wheel Co., 15 F.R.D. 461, 464-65 (E.D. Mich. 1954).

[116] Transp. Equip. Sales Corp. v. BMY Wheeled Vehicles, 930 F. Supp. 1187 (N.D. Ohio 1996).

[117] *In re* Sealed Case, 877 F.2d 976, 980 (D.C. Cir. 1989) ("[I]f a client wishes to preserve the privilege, it must treat the confidentiality of attorney-client communications like jewels—if not the crown jewels."); Ares-Serono, Inc. v. Organon Int'l B.V., 160 F.R.D. 1, 4 (D. Mass. 1994) ("A strict rule applying a waiver to inadvertently disclosed documents serves to protect . . . secrecy . . . by ensuring that attorney's [sic] will more diligently install precautionary measures to avoid such disclosures.").

likely it is that the parties will obtain a fair adjudication of their dispute."[118] "Finally, the lawyer's duty of zealous advocacy" may be the most potent "argument in favor of the strict responsibility approach."[119] "If an attorney does not want an adversary to use information she considers confidential, she should take care not to disclose it in the first place."[120]

[118]Joshua K. Simko, *Inadvertent Disclosure, the Attorney-Client Privilege, and Legal Ethics: An Examination and Suggestion for Alaska,* 19 ALASKA L. REV. 461, 466 (2002).

[119]*Id.* at 467.

[120]*Id.*

Critics of the strict responsibility approach warn that it could have a chilling effect upon attorney-client relationships. Open communication may be hampered if clients know that regardless of security precautions, an inadvertent disclosure will abrogate the privilege.[121] "The strict responsibility approach also punishes the client for the attorney's mistake."[122] "[E]ven if the attorney's secretary accidentally pushed the wrong speed-dial button, the client would lose the privilege."[123] Moreover, critics of the strict responsibility rule contend that it ignores the role of the attorney-client privilege and reduces an attorney's ability to provide effective legal representation by "'undermin[ing] any confidence that parties can place in that privilege.'"[124]

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[121]*Id.* at 469; Amy Fulmer Stevenson, *Making a Wrong Turn on the Information Superhighway: Electronic Mail, the Attorney-Client Privilege, and Inadvertent Disclosure,* 26 CAP. U. L. REV. 347, 360 (1997).

[122]Simko, *supra* note 118, at 469.

[123]*Id.* In *United States v. Zolin*, 809 F.2d 1411 (9th Cir. 1987), *aff'd in part and vacated in part on other grounds*, 491 U.S. 554 (1989), the government claimed that the defendant waived the attorney-client privilege with regard to tapes that the personal secretary of one of the defendants had mistakenly delivered to a third party. The Ninth Circuit held that the privilege had not been waived because the delivery of the tapes was "sufficiently involuntary and inadvertent as to be inconsistent with a theory of waiver." *Id.* at 1417.

[124]Harry M. Gruber, *E-Mail: The Attorney-Client Privilege Applied,* 66 GEO. WASH. L. REV. 624, 641 (1998) (quoting Remington Arms Co. v. Liberty Mut. Ins. Co., 142 F.R.D. 408, 413 (D. Del. 1992)).

C. *Modern or "No Waiver" Approach*

The modern or "no waiver" approach considers any truly inadvertent disclosure of privileged information as no waiver of the attorney-client privilege. Under this approach, the client's intent is paramount because the privilege is waived only when the disclosing party intended to waive it.[125] The court need only determine whether the inadvertently disclosed material is protected by the attorney-client privilege; if so, the receiving party may not introduce it at trial.[126] One rationale for this approach is that only the client, not the attorney, can waive the privilege because the privilege belongs to the client.[127] A second rationale is that "a 'waiver' is by definition the intentional relinquishment of a known right, and the concept of an 'inadvertent waiver' is therefore inherently contradictory."[128]

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[125]Robert A. Pikowsky, *Privilege and Confidentiality of Attorney-Client Communication Via E-Mail,* 51 BAYLOR L. REV. 483, 496 (1999).

[126]Roberta M. Harding, *Waiver: A Comprehensive Analysis of a Consequence of Inadvertently Producing Documents Protected by the Attorney-Client Privilege,* 42 CATH. U. L. REV. 465, 471-72 (1993).

[127]*See* Georgetown Manor, Inc. v. Ethan Allen, Inc., 753 F. Supp. 936, 939 (S.D. Fla. 1991); Helman v. Murry's Steaks, Inc., 728 F. Supp. 1099, 1104 (D. Del. 1990).

[128]Bank Brussels Lambert v. Credit Lyonnais(Swisse) S.A., 160 F.R.D. 437, 442 (S.D.N.Y. 1995); Mendenhall v. Barber-Greene Co., 531 F. Supp. 951, 955 (N.D. Ill. 1982).

Mendenhall is the seminal case for the modern approach. In that case, defendant Barber-Greene sought production of four letters in plaintiff's possession as part of a patent infringement action.[129] The defendant contended that the inadvertent disclosure of the four letters by plaintiff's counsel waived attorney-client privilege.[130] The court dismissed the defendant's claim:

> We are taught from first year law school that waiver imports the "intentional relinquishment or abandonment of a known right." . . . Inadvertent production is the antithesis of that concept. In response to a production request . . . Seiler provided Barber-Greene with 28 complete files. When he pored over the files . . . Fleming found the four letters now at issue. Mendenhall's counsel now says their delivery was unintended. . . . But if we are serious about the attorney-client privilege and its relation to the *client's* welfare, we should require more than such negligence by *counsel* before the client can be deemed to have given up the privilege.[131]

Practically, the inadvertently disclosed documents had lost their confidential status, but the client had not waived attorney-client privilege.

The modern approach offers ease of administration and yields predictable results.[132] Because the "no waiver" approach looks to the intent of the client, it seems more fair to the parties, especially because it does not punish the client for the attorney's negligence.[133] The modern approach promotes the attorney-client privilege by making sure that "the client remains free from apprehension that consultations with a legal advisor will be

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[129]*Mendenhall*, 531 F. Supp. at 952.
[130]*Id.* at 954-55.
[131]*Id.* at 955.
[132]Harding, *supra* note 126, at 495.
[133]Simko, *supra* note 118, at 471.

disclosed."[134] This approach values confidentiality more than it does the open search for truth.[135] Moreover, the modern approach does not hinder zealous advocacy because an adversary still benefits from the knowledge of the contents of an inadvertent disclosure. Attorneys still possess an incentive to protect privileged materials.[136]

[134]Berg Elecs., Inc. v. Molex, Inc., 875 F. Supp. 261, 261-62 (D. Del. 1995).

[135]Simko, *supra* note 118, at 471.

[136]Anne G. Bruckner-Harvey, *Inadvertent Disclosure in the Age of Fax Machines: Is the Cat Really Out of the Bag,?* 46 BAYLOR L. REV. 385, 392 (1994).

Modern approach critics claim that it is too difficult to discern the client's intent. Every client would deny intent to waive the privilege.[137] Also, this approach may cause judicial instability because the receiving party will not know whether a disclosed document will be admitted into evidence. Critics also argue that the "no waiver" approach removes all incentives for attorneys to protect clients' confidential documents.[138]

D. *The Balancing Test Approach*

The balancing test approach examines the circumstances surrounding an inadvertent disclosure to determine whether the attorney-client and/or *Kovel* privilege has been waived. Such an approach has been adopted by most state and federal courts.[139] The disclosing party must first persuade the court that the disclosure was truly inadvertent, and then must convince the court that the privilege has not been waived.[140]

In the event of inadvertent disclosure, courts using this approach often apply a five-factor test enunciated in *Lois Sportswear, U.S.A., Inc. v. Levi Strauss & Co.*[141] The five factors are as follows: (1) "the reasonableness of

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[137]Hydraflow, Inc. v. Enidine, Inc., 145 F.R.D. 626, 637 (W.D.N.Y. 1993).

[138]Simko, *supra* note 118, at 471-72.

[139]Fleet Business Credit Corp. v. Hill City Oil Co., No. 01-02417-MaV, 2002 U.S. Dist. LEXIS 23896, at *9 (W.D. Tenn. Dec. 5, 2002); Gruber, *supra* note 124, at 644.

[140]Parkway Gallery Furniture, Inc. v. Kittinger/Pa. House Group, Inc., 116 F.R.D. 46, 50 (M.D.N.C. 1987).

[141]*See generally* Lois Sportswear, U.S.A., Inc. v. Levi Strauss & Co., 104 F.R.D. 103 (S.D.N.Y. 1985). In that case, Lois Sportswear moved to require production of certain documents of Levi Strauss in a trademark infringement and unfair competition action. Twenty-two documents

the precautions taken to prevent inadvertent disclosure"; (2) "the number of inadvertent disclosures"; (3) "the extent of the disclosure"; (4) "any delay and measure taken to rectify the disclosures"; and (5) "whether the overriding interests of justice would or would not be served by relieving a party of its error."[142]

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consisting of correspondence between lawyers were inadvertently disclosed to Lois as part of Levi's response to a request for production of documents. Levi claimed that the twenty-two documents were protected by the attorney-client privilege. The court stated that the issue is whether or not the release of the documents was a knowing waiver or simply a mistake. In deciding in Levi's favor, the court applied the five-factor balancing test. *Id.*

[142]United States v. Keystone Sanitation, 885 F. Supp. 672, 676 (M.D. Pa. 1994). *See also* Alldread v. City of Grenada, 988 F.2d 1425, 1433 (5th Cir. 1993); Sampson Fire Sales, Inc. v. Oaks, 201 F.R.D. 351, 360 (M.D. Pa. 2001); Wallace v. Beech Aircraft Corp., 179 F.R.D. 313, 314 (D. Kan. 1998).

Examining the reasonableness of precautions taken under a given set of circumstances can be difficult. Courts consider the mechanics of disclosure, such as whether the disclosing party had a screening process in place, how it was implemented, and what kind of legal expertise was possessed by those implementing the screening process.[143] Many courts find that failure to take any action to protect the privilege is indicative of the client's lack of intent to preserve confidentiality.[144] For example, leaving a file on a large conference table is a failure to take reasonable precautions.[145] Properly marking a document, such as by stamping it "confidential" or "privileged" may be considered adequate precaution.[146] In sum, the precautions taken need only be reasonable, not necessarily successful, to satisfy the first factor of the balancing test.[147]

With regard to the second factor, the number of inadvertent disclosures, the lower the number of disclosures, compared to the number of documents, the more likely the court is to maintain the privilege.[148] In *Rotelli v. 7-Up Bottling Co. of Philadelphia*, a federal court ruled there was no waiver of attorney-client privilege when ten inadvertent disclosures occurred out of a large number of documents.[149] Conversely, in *Prebilt Corp. v. Preway, Inc.*, the court found that a waiver occurred where about 100 documents were disclosed out of several thousand available.[150]

In examining the extent of inadvertent disclosure, courts consider whether the receiving attorney has learned the contents of a document or is merely aware of its existence.[151] If the attorney has only limited knowledge of the contents, a greater chance exists that the court will uphold the privilege.[152]

As to the fourth factor, the time taken to rectify inadvertent disclosures, the less time taken, the more likely the court is to maintain the

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[143]*In re* Grand Jury Investigation, 142 F.R.D. 276, 279-80 (M.D.N.C. 1992); Fed. Deposit Ins. Corp. v. Marine Midland Realty, 138 F.R.D. 479, 483 (E.D. Va. 1991).

[144]Gruber, *supra* note 124, at 644.

[145]Meridian Mortgage Corp. v. Spivak, No. 91-3932, 1992 U.S. Dist. LEXIS 12319, at *11 (E.D. Pa. Aug. 14, 1992), *aff'd,* 22 F.3d 302 (3d Cir. 1994).

[146]Local 851 of Int'l Bhd. of Teamsters v. Kuehne & Nagel Air Freight, Inc., 36 F. Supp. 2d 127, 132 (E.D.N.Y. 1998).

[147]*Bank Brussels Lambert*, 160 F.R.D. at 443.

[148]*See* Trina Jones, *Inadvertent Disclosure of Privileged Information and the Law of Mistake: Using Substantive Legal Principles to Guide Ethical Decision-Making,* 48 EMORY L.J. 1255, 1274 n.65 (1999).

[149]No. 93-6957, 1995 WL 234171, at *3 (E.D. Pa. Apr. 19, 1995).

[150]No. 87-7132, 1988 U.S. Dist. LEXIS 10764, at *8 (E.D. Pa. Sept. 23, 1988).

[151]Audrey Rogers, *New Insights on Waiver and the Inadvertent Disclosure of Privileged Materials: Attorney Responsibility as the Governing Precept,* 47 FLA. L. REV. 159, 173 (1995).

[152]*See* Jones, *supra* note 148, at 1274 n.65.

privilege.[153] In any event, counsel must make some effort, such as timely filing a supplemental motion for a protective order, to protect the attorney-client or *Kovel* privilege.[154]

[153] *See Sampson Fire Sales*, 201 F.R.D. at 361 (weighing favorable efforts taken within five days).

[154] *See In re* Grand Jury (Impounded), 138 F.3d 978, 983 (3d Cir. 1998); Fid. & Deposit Co. of Md. v. McCulloch, 168 F.R.D. 516, 523 (E.D. Pa. 1996).

The fifth factor in the balancing test approach is a catchall provision that considers the interests of fairness. Courts look to the unique circumstances of each case and the fairness doctrine as a means of considering policy issues underlying the attorney-client privilege.[155] In *Monarch Cement Co. v. Lone Star Industries, Inc.*, a federal district court held that attorney-client privilege had not been waived because it would be unfair to penalize the client for an attorney's mistake, especially when the latter made every effort to rectify the error.[156] In another case, *Edwards v. Whitaker*, the court found waiver of the privilege because the disclosing attorney had not taken adequate steps to prevent inadvertent disclosure of several letters.[157]

Courts claim that the balancing test approach "serves the purpose of the attorney-client privilege," which is protecting communications that clients intend to remain confidential.[158] The balancing test also means that those asserting the privilege feel "the consequences of their carelessness if the circumstances surrounding the disclosure do not clearly demonstrate that continued protection is warranted."[159] What the balancing test lacks in ease of application (due to case-by-case analysis), it makes up for in professionalism and fairness to the parties.[160]

Critics of the balancing test argue that it leads to inconsistent results. For example, the test is unclear as to how each court will "define 'reasonable precautions to prevent disclosure.'"[161] Ad hoc determinations of reasonableness and fairness encourage parties to litigate every dispute involving inadvertent disclosure of privileged documents.[162] As a result, the

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[155]Simko, *supra* note 118, at 474.

[156]132 F.R.D. 558, 560 (D. Kan. 1990).

[157]868 F. Supp. 226, 229 (M.D. Tenn. 1994).

[158]*Alldread*, 988 F.2d at 1434; *Bank Brussels Lambert*, 160 F.R.D. at 443; *Lois Sportswear*, 104 F.R.D. at 105.

[159]*Alldread*, 988 F.2d at 1434.

[160]Rogers, *supra* note 151, at 196; Simko, *supra* note 118, at 475.

[161]Bruckner-Harvey, *supra* note 136, at 390.

[162]*Berg Elecs.*, 875 F. Supp. at 263.

balancing test approach promotes overexpenditure and wastes judicial resources.

We now turn to an examination of the relation between various modes of electronic communication, inadvertent disclosure and the attorney-client and *Kovel* privileges.

E. *Modes of Electronic Communication, the Attorney-Client Privilege and the* Kovel *Rule*

The law governing attorney-client relationships requires communications between the attorney, client (and some third-party experts) to be surrounded in a reasonable expectation of privacy.[163] The attorney-client and *Kovel* privileges are "'limited to those communications which the client either expressly made confidential or which he could reasonably assume under the circumstances would be understood by the attorney as so intended.'"[164] The lack of a reasonable expectation of privacy surrounding any means of electronic communication may prevent the attorney-client and/or *Kovel* privilege from attaching.[165]

1. Telephones

Generally, a conversation on a hard-wire telephone between an attorney and client or an attorney and a third-party expert is protected by the attorney-client or *Kovel* privileges.[166] In *United States v. Hall,* the Ninth Circuit Court of Appeals held that "[w]hen a person talks by telephone, he can reasonably assume privacy."[167] The ABA has stated that "a lawyer has a

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[163]Anthony S. Higgins, Comment, *Professional Responsibility—Attorney-Client Privilege: Are Expectations of Privacy Reasonable for Communications Broadcast Via Cordless or Cellular Telephones?* 24 U. BALT. L. REV. 273, 280 (1995).

[164]*Id.* at 280-81 (quoting 1 JOHN WILLIAM STRONG, MCCORMICK ON EVIDENCE § 91, at 33 (4th ed. 1992)).

[165]*Id.* at 281.

[166]Sean M. O'Brien, Note, *Extending the Attorney-Client Privilege: Do Internet E-Mail Communications Warrant a Reasonable Expectation of Privacy?* 4 SUFFOLK J. TRIAL & APP. ADV. 187, 197 (1999).

[167]488 F.2d 193, 196 (9th Cir. 1973).

reasonable expectation of privacy in the use of a [land-line] telephone."[168] Traditional land-line telephone communications are confidential "because such communications are made under circumstances that reasonably ensure their confidentiality."[169] The law is less clear, however, with regard to cordless and cellular telephones.

[168]ABA Comm. on Ethics and Prof'l Responsibility, Formal Op. 99-413, at 3 (1999).

[169]David Hricik, *Lawyers Worry Too Much About Transmitting Client Confidences by Internet E-Mail,* 11 GEO. J. LEGAL ETHICS 459, 479 (1998).

Despite protection afforded to wireless communications under the Electronic Communications Privacy Act of 1986 (ECPA),[170] one federal appeals court has held that a client's cordless phone conversation with his attorney was not protected by the attorney-client privilege.[171] Other courts have ruled that no reasonable expectation of privacy exists in cordless phone conversations.[172] Cordless telephones use FM frequencies between the

[170]18 U.S.C. § 2511 (West 1999). The ECPA protects wire, oral, or electronic communications against warrantless interceptions by law enforcement officers and criminalizes interception by others. 18 U.S.C. §§ 2511, 2516 (West 1999). One provision even states that "no otherwise privileged wire, oral, or electronic communication intercepted in accordance with, or in violation of, the provision of this chapter shall lose its privileged character." 18 U.S.C. § 2517(4) (West 1999). No reported case, however, considers the impact of the ECPA's privilege provision on the interception of attorney-client communications. The statute's privilege protection applies only to those privileged communications that are protected under common law principles. The ECPA has not necessarily protected application of the attorney-client privilege to cordless and cellular telephones. Joshua M. Masur, Comment, *Safety in Numbers: Revisiting the Risks to Client Confidences and Attorney-Client Privilege Posed by Internet Electronic Mail,* 14 BERKELEY TECH. L.J. 1117, 1141, 1144 (1999).

[171]United States v. Mathis, 96 F.3d 1577, 1583 (11th Cir. 1996), *cert. denied*, 520 U.S. 1213 (1997).

[172]Tyler v. Berodt, 877 F.2d 705, 706 (8th Cir. 1989), *cert. denied,* 493 U.S. 1022 (1990); State v. Smith, 438 N.W.2d 571, 578 (Wis. 1989).

headset and telephone base.[173] "[C]ordless phone users broadcast their messages in the same manner as radio stations."[174] In *State v. Smith*, the court cited a Federal Communications Commission requirement that cordless telephones must bear a legend indicating that privacy of communications may not be ensured as support for concluding that there is no expectation of privacy in cordless telephone conversations.[175] This principle of law may be subject to challenge, however, as communications technology changes.

In *United States v. Smith*, a defendant convicted of drug-trafficking argued on appeal that all of the evidence against him was discovered as a result of intercepted cordless telephone conversations in violation of the Fourth Amendment.[176] The court acknowledged that since 1992 cordless phones began broadcasting on radio frequencies not utilized by conventional radios, and also scrambling the radio signal.[177] Although the court expressed no opinion as to which cordless phone features would give rise to a reasonable expectation of privacy, it noted that at some point technological advances will mean cordless communications are entitled to Fourth Amendment protection.[178]

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[173]Christopher C. Miller, *For Your Eyes Only? The Real Consequences of Unencrypted E-Mail in Attorney-Client Communication*, 80 B.U. L. REV. 613, 620 (2000).

[174]*Id. See* State v. Howard, 679 P.2d 197 (Kan. 1984).

[175]*Smith*, 438 N.W.2d at 577; *see also* McKamey v. Roach, 55 F.3d 1236, 1239-40 (6th Cir. 1995) (finding no confidentiality in a cordless telephone conversation as the owner's manual cautioned that it is not possible to ensure privacy of communication).

[176]978 F.2d 171, 180 (5th Cir. 1992).

[177]*Id.* at 179.

[178]*Id.* at 180.

Moreover, in *People v. Stone*,[179] the Michigan Supreme Court ruled that under the state's eavesdropping statute,[180] a conversation held on a cordless telephone was a "private" conversation.[181] The Washington Supreme Court has also held that a cordless telephone user has an expectation of privacy under that state's privacy statute.[182]

Today, it is arguable that any determination of one's reasonable expectation of privacy when using a cordless phone is fact-intensive and depends on the specific technology used.[183] Because cordless phone technology will continue to evolve, courts will eschew the use of bright-line rules in this area. It is reasonable to conclude that the state of attorney-client privilege for confidential communications over cordless phones is unsettled.[184] Communication of privileged information to an unknown third party via eavesdropping or inadvertent disclosure continues to be a risk.

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[179]621 N.W.2d 702, 703 (Mich. 2001). In that case, defendant Brian Stone became estranged from his wife, Joanne Stone, and moved out. The defendant's neighbor, Ronald Pavlik, told him he had been intercepting and recording Joanne's cordless phone calls. Defendant told Pavlik to keep on listening and recording. Ultimately, defendant was arrested and tried under the state eavesdropping statute.

[180]MICH. COMP. LAWS ANN. § 750.539 (West 2001).

[181]*Stone*, 621 N.W.2d at 706.

[182]State v. Faford, 910 P.2d 447, 450 (Wash. 1996). The State of Washington has one of the most restrictive privacy laws in the nation. It reads as follows: "Private communication transmitted by telephone . . . or other device between two or more individuals between points within or without the state by any device electronic or otherwise designed to record and/or transmit said communication . . . without first obtaining the consent of all the participants . . . ." WASH. REV. CODE § 9.73.030(1)(a) (1994).

[183]*Smith*, 978 F.2d at 180.

[184]One court has actually held "that the law is not clearly established" on whether a cordless phone user "has a reasonable expectation of privacy under the Fourth Amendment." Frierson v. Goetz, 227 F. Supp. 2d 889, 899 (M.D. Tenn. 2002).

Accountants and other third-party experts would be well-advised to avoid communicating privileged material over cordless phones.

The use of cellular telephones has also raised questions concerning the attorney-client and *Kovel* privileges. Cellular phones broadcast messages using radio signals, but not at standard FM frequencies.[185] In fact, cellular telephones cannot be intercepted without an illegal scanning device.[186] Nonetheless, cellular phones can still be intercepted.[187] This fact has led some courts to hold that a cellular phone user lacks a reasonable expectation of privacy.[188]

In *People v. Wilson*, an Illinois appellate court refused to recognize a reasonable expectation of privacy for a cellular phone user under the state's eavesdropping statute.[189] The court noted that it is common knowledge that conversations transmitted by radio waves may be intercepted.[190] The same result using identical reasoning was reached by a Georgia appellate court in *Salmon v. State*.[191] Both these cases appear to illustrate that ease of interception is a key factor in determining the existence of a reasonable expectation of privacy.[192]

A few state bar associations have addressed the issue of confidentiality (or reasonable expectation of privacy) in cellular telephones. State bar associations in New York, Iowa, and Illinois have released ethics opinions stating that attorneys should warn clients that cellular telephone conversations are not secure. Attorneys should obtain client consent to communicate using such devices.[193]

Given that the state of attorney-client privilege for confidential communications over cellular phones is not clear, accountants and other third-party experts should avoid communicating confidential material over

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[185]Stephen Masciocchi, *Internet E-Mail: The Attorney-Client Privilege, Confidentiality, and Malpractice Risks,* COLO. LAW., Feb. 1998, at 61.

[186]*Id.*

[187]Analog cellular phones use radio frequencies that can be intercepted by police scanners or illegally modified, commercial scanners. It can be accomplished as evidenced by a Florida couple's interception of a sensitive conversation between Newt Gingrich, his attorney, and several Congressmen in January 1997. Digital cellular phones were once thought to be a secure form of communication but the code was cracked by two computer hackers in March 1997. Lucy S. Leonard, Comment, *The High-Tech Legal Practice: Attorney-Client Communications and the Internet,* 69 U. COLO. L. REV. 851, 881 n.177 (1998).

[188]Masciocchi, *supra* note 185, at 62.

[189]554 N.E.2d 545, 552 (Ill. App. Ct. 1990).

[190]*Id.* at 551.

[191]426 S.E.2d 160, 162 (Ga. Ct. App. 1992).

[192]Leonard, *supra* note 187, at 883.

[193]*Id. See also* New York Bar Ass'n Ethics Comm., Op. 1994-11 (1994); Iowa Bar Ass'n Ethics Comm., Op. 90-44 (1991); Illinois Bar Ass'n Ethics Comm., Op. 90-7 (1990).

cellular telephones. "A failure to inform a client of the possibility that . . . communications can jeopardize [the attorney-client and/or *Kovel* privileges] may be grounds for malpractice actions and disciplinary sanctions."[194]

2. Fax Machines

[194]Higgins, *supra* note 163, at 276.

The use of fax machines also presents unsettled legal questions regarding the attorney-client and *Kovel* privileges. Fax communications, however, differ from cordless and cellular telephone communications because they use land-line telephone technology for transmission, eliminating the interception problem associated with radio waves.[195] Fax machines digitally transmit a document over telephone lines.[196] "Despite possible misdirection . . . of a fax transmission, a reasonable expectation of privacy is still afforded this medium."[197] In general, a fax communication is considered to be protected by the attorney-client privilege.[198] When privilege rules are applied to a fax communication, waiver is usually the primary issue.[199]

The law is somewhat unsettled with regard to whether an inadvertent disclosure via a fax communication means a waiver of the attorney-client or *Kovel* privilege. In a recent case, however, *Sampson Fire Sales, Inc. v. Oaks*,[200] a federal court addressed the issue. The court mentioned the

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[195]Leonard, *supra* note 187, at 884.

[196]Patricia Boardman, *Telefacsimile Documents: A Survey of Uses in the Legal Setting,* 36 WAYNE L. REV. 1361, 1361-62 (1990).

[197]O'Brien, *supra* note 166, at 201.

[198]United States Fidelity & Trust Co. v. Canady, 460 S.E.2d 677, 689 (W. Va. 1995); Peter Jarris & Bradley Tellam, *Competence and Confidentiality in the Context of Cellular Telephone, Cordless Telephone and E-Mail Communications,* 33 WILLAMETTE L. REV. 467, 478 (1997).

[199]Leonard, *supra* note 187, at 885.

[200]201 F.R.D. 351, 361 (M.D. Pa. 2001). When plaintiff Sampson sold his business to defendants, the facility and equipment formerly owned by the plaintiff, including the business telephone and fax number, were used by the defendant as successor owners. Plaintiff's counsel inadvertently sent a one page fax with a cover sheet (which noted that the material was privileged and confidential) to the fax number, believing his client was still in possession of the fax number in

existence of the three standards for cases involving inadvertent disclosure of privileged information.[201] The plaintiff argued for application of the no-waiver approach and the defendant called for the application of the strict responsibility approach.[202] The court rejected both approaches and decided to employ the five factors of the balancing approach.[203]

Williamsport, Pennsylvania. In fact, the fax number forwarded all communications to the defendant in Alabama.

[201] *Id.* at 357.

[202] *Id.* at 357-58.

[203] *Id.* at 360.

With regard to the first factor, a key precaution taken by the plaintiff's attorney was the inclusion of a fax cover sheet that notified any receiving party that the information contained therein was privileged.[204] The cover sheet also contained a message that any party inadvertently receiving the fax should call a particular number. The court found the cover sheet to be an adequate precaution.[205] The court did not place any weight on the number of inadvertent disclosures because the fax was only one page.[206] The extent of the disclosure was not determined to be pivotal but still deserved protection as a privileged communication as it contained potential trial strategy.[207] Although the inadvertent disclosure was made on July 2, 2000, it did not come to plaintiff's attorney's attention until July 13, 2000 in a reply brief.[208] Plaintiff's attorney addressed the matter within a few days.[209]

In the eyes of the court, the most significant factor in its analysis involved the interests of justice.[210] Noting the lack of legal principles or ethical and professional rules on inadvertent disclosure, the court decided that defendant's attorney should have notified the plaintiff's lawyer about the incorrectly sent fax and abided by the cover sheet instructions.[211] The plaintiff and his attorney were found not to have waived attorney-client privilege, and the fax could not be used at trial.[212]

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[204] *Sampson Fire Sales*, 201 F.R.D. at 360.
[205] *Id.*
[206] *Id.* at 361.
[207] *Id.*
[208] *Sampson Fire Sales*, 201 F.R.D. at 361.
[209] *Id.*
[210] *Id.*
[211] *Id.* at 362.
[212] *Sampson Fire Sales*, 201 F.R.D. at 362.

3. E-Mail

Communication by e-mail is also a gray area of the law with regard to the attorney-client and *Kovel* privileges. E-mail is any private or public communication, including any attachments, that is transmitted over the Internet.[213] Private e-mail systems used by law firms do not create the potential for inadvertent waiver of the attorney-client privilege. Public e-mail systems, on the other hand, invoke questions concerning whether such a mode of communication carries a reasonable expectation of privacy.[214]

[213]Mathew J. Boettcher & Eric G. Tucciarone, *Concerns Over Attorney-Client Communication Through E-Mail: Is the Sky Really Falling?* 2002 L. REV. M.S.U.-D.C.L. 127, 130 (2002).

[214]*Id.* In fact, in *National Employment Service Corp. v. Liberty Mutual Insurance Co.*, No. 93-2528-G, 1994 Mass. Super. LEXIS 84, at *8 (Mass. Super. Ct. Dec. 12, 1994), a Massachusetts trial court held that a series of thirty-two e-mail messages sent over an internal e-mail system were protected by the attorney-client privilege.

Public e-mail travels from a sender's computer through a land-based line to several intermediate computers, called servers and routers, before reaching a recipient's mailbox.[215] E-mail messages are vulnerable to certain security risks such as "sniffing" and "spoofing."[216] Specialized software called "sniffers" search for key words in unencrypted e-mail as the mail travels through servers and routers.[217] "Spoofers" software configures an intermediate computer to resemble the recipient host, effectively intercepting an e-mail message.[218] E-mail also leaves records of its contents. A copy of an e-mail message is not only stored on the sender's computer but on each server or router through which the message travels.[219] Even deleted e-mail messages often can be retrieved indefinitely from a computer system.[220] The various means by which e-mail security can be compromised has lead to disparate treatment by courts, legal commentators, and ethics advisory committees.

In a lawsuit challenging the Communications Decency Act,[221] a federal district court found that unencrypted e-mail "is not 'sealed' or secure, and can be accessed or viewed on intermediate computers between the sender and recipient."[222] In *United States v. Maxwell*, a federal appellate court held that the sender of an e-mail message has a reasonable expectation of privacy, but limited the holding to e-mail transmissions on America OnLine (AOL).[223] The court noted that:

> AOL differs from other systems, specifically the Internet, . . . in that e-mail messages are afforded more privacy than similar messages on the Internet, because they are privately stored for retrieval on AOL's centralized and privately-owned computer bank located in Vienna, Virginia . . . . Just for comparison, the Internet has a less secure e-mail system, in which messages

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[215]David Hricik, *Confidentiality & Privilege in High-Tech Communications,* 60 TEX. B.J. 104, 112 (1997).

[216]*Id.* at 115.

[217]*Id.*; Aaron Grossman, *Is Opposing Counsel Reading Your E-Mail,?* MASS. LAW. WKLY., Nov. 18, 1996, at B4.

[218]Hricik, *supra* note 215, at 115.

[219]O'Brien, *supra* note 166, at 207.

[220]"When a user strikes the 'delete' key, the data is *not* physically removed from the hard drive. . . . The data remains undisturbed until more space is needed on the hard drive . . . ." Susan J. Silvernail, *Electronic Evidence: Discovery in the Computer Age,* 58 ALA. LAW. 176, 180-81 (1997). Stored electronic mail is discoverable under FEDERAL RULES OF CIVIL PROCEDURE 26(a)(1)(B) and 34. *See* FED. R. CIV. PRO. 26(a)(1)(B), 34.

[221]47 U.S.C. § 223(a) (1999).

[222]ACLU v. Reno, 929 F. Supp. 824, 834 (E.D. Pa. 1996).

[223]45 M.J. 406, 417 (C.A.A.F. 1996), *later proceeding*, 46 M.J. 413 (C.A.A.F. 1997).

must pass through a series of computers in order to reach the intended recipient.[224]

[224] *Id.*

The court makes clear that the more open the method of transmission, the less the likelihood of an expectation of privacy.[225] As with other modes of electronic communication, ease of interception of e-mail is an important factor in determining the existence of a reasonable expectation of privacy.[226]

In another recent case, *United States v. Keystone Sanitation Co.*, a federal district court did not address the e-mail security issue, but applied the balancing approach in holding that attorney-client privilege had been waived by the inadvertent disclosure of an e-mail.[227] In that case, numerous defendants requested Keystone Sanitation to produce all documents related to their transfer of assets because the Environmental Protection Agency commenced an investigation involving a polluted site.[228] The group of defendants suspected Keystone had disposed of assets to avoid paying its share of cleanup costs.[229] During document production, Keystone inadvertently disclosed various e-mail printouts.[230] The court applied each of the five factors in the balancing test approach to reach a decision.

The district court found that the first factor weighed in favor of a waiver. "Keystone's precautions were not reasonable since [the company] did not assert any privilege before it began producing documents."[231] The second and third factors, the number and extent of disclosures, also supported waiver.[232] The fourth factor, the issue of delay and measures

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[225] *Id.*

[226] *See Maxwell*, 45 M.J. at 417 (comparing e-mail to other forms of communication).

[227] 885 F. Supp. 672, 676 (M.D. Pa. 1994).

[228] *Id.* at 675.

[229] *Id.*

[230] *Id.*

[231] Karen M. Coon, Note, *United States v. Keystone Sanitation Company: E-Mail and the Attorney-Client Privilege*, 7 RICH. J.L. & TECH. 30, ¶ 30 (2001), *at* http://www.richmond.edu/jolt/v7i3/article4.html.

[232] *Id.*

taken to rectify any inadvertent disclosure, was not implicated.[233] The court placed the most weight on the fifth factor—the interests of justice. Discovery of evidence showing that Keystone dissipated assets to avoid liability runs counter to the interests of justice.[234] Hence, the court found Keystone's inadvertent disclosure waived attorney-client privilege.[235] Although a significant case, *Keystone Sanitation* does not address whether e-mail gives rise to a reasonable expectation of privacy. In many instances, the type of e-mail system used may influence whether an expectation of privacy attaches.[236]

V. PRESERVING APPLICATION OF THE *KOVEL* RULE

A. *Engaging the Accountant or Other Business Expert*

[233] *Keystone Sanitation*, 885 F. Supp. at 676.
[234] Coon, *supra* note 231, ¶ 31.
[235] *Keystone Sanitation*, 885 F. Supp. at 676.
[236] *See supra* notes 223-26 and accompanying text.

The attorney, not the client, should hire the accountant or other third-party expert. This strengthens the argument that the accountant was hired to assist the attorney in rendering legal services.[237] Preferably, the client's existing accountant should not be hired to perform consulting work for the attorney (unless absolutely necessary).[238] Use of the client's current accountant makes it more difficult to establish that he or she served as a litigation or legal assistant rather than as a financial advisor with regard to a particular communication.[239] This problem is compounded "if the accountant is called to testify before a grand jury or at trial."[240]

In the event counsel hires the client's present accountant, matters covered by the *Kovel* privilege should be adequately segregated to make plausible the argument that the *Kovel* engagement was not part of an overall package of services.[241] "Finally, if the accountant works for an accounting firm, he or she should explore the possibility of getting another accountant in the [same] firm to handle the investigation. A 'Chinese wall' could then be erected between the regular accountant and the investigative accountant and their respective files."[242]

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[237]John J. Tigue, Jr. et al., *The Kovel Accountant Privilege,* N.Y.L.J., May 19, 1994, at 4.

[238]Spiro & Rule, *supra* note 13, at S10.

[239]*Id.*

[240]*Id.*; Alan A. Schacter et al., *The Investigative Accountant and Confidentiality in a Criminal Tax Fraud Investigation,* CPA J., Mar. 1993, at 45.

[241]William L. Raby & Burgess J.W. Raby, *The Kovel Rule and CPA Privilege,* TAX NOTES, Nov. 1995, at 1126.

[242]Schacter et al., *supra* note 240, at 45.

In the case of a corporation, it is preferable that outside counsel, rather than in-house counsel, hire the accountant or other third-party expert.[243] The reason is that many courts seem to treat in-house attorneys differently because they assume in-house counsel do a substantial amount of non-legal work for the corporation.[244] On the basis of this assumption, courts often require corporations claiming the privilege to demonstrate that the communication in question relates to legal advice or services.[245] For instance, in *Avianca, Inc. v. Corriea,* the federal district court stated:

> Where the communication is with in-house counsel for a corporation, particularly where that counsel also serves a business function, the corporation must clearly demonstrate that the advice to be protected was given "in a professional legal capacity" . . . . This limitation is necessary to prevent corporations from shielding their business transactions from discovery simply by funneling their communications through a licensed attorney.[246]

Other federal courts have also indicated that such a heightened level of scrutiny does not apply to outside counsel.[247] Given the higher standard applied to in-house counsel to trigger application of the attorney-client privilege, any and all steps that delineate between business and legal advice should be taken by the corporate client.[248]

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[243]Stanley A. Twardy & Michael G. Considine, *Procedures to Protect Attorney-Client Privilege,* N.Y.L.J., Feb. 1, 1996, at 4.

[244]Giesel, *supra* note 23, at 1208.

[245]Giesel, *supra* note 23, at 1208-09. Many courts apply a more strenuous analysis to a claim of privilege based on the assumption that outside attorneys do not provide a substantial amount of nonlegal services to corporations. This assumption appears to be unsubstantiated. In one study of New York executives, law firm partners, in-house counsel, and the judiciary, no statistically significant difference was found between in-house counsel and outside attorneys regarding the frequency with which they provide business advice. Empirical survey data indicates that 47.8 percent of outside counsel and 46.7 percent of in-house attorneys give business advice often. Vincent C. Alexander, *The Corporate Attorney-Client Privilege: A Study of the Participants,* 63 ST. JOHN'S L. REV. 191, 341-42 (1989). Such empirical data rebuts the assumption that outside attorneys do not provide a substantial amount of nonlegal advice to corporations. Clearly, courts should examine each case involving a claim of privilege on the basis of the facts.

[246]705 F. Supp. 666, 676 (D.D.C. 1989) (citations omitted).

[247]United States v. Chevron, No. C-94-1885 SBA, 1996 U.S. Dist. LEXIS 4154, at *8-*9 (N.D. Cal. Mar. 13, 1996); Kramer v. Raymond Corp., No. 90-5026, 1992 U.S. Dist. LEXIS 7418, at *2-*3 (E.D. Pa. May 26, 1992); Georgia-Pacific Corp. v. GAF Roofing Mfg. Corp., 93 Civ. 5125 (RPP), 1996 U.S. Dist. LEXIS 671, at *9-*10 (S.D.N.Y. Jan. 25, 1996).

[248]*See Kramer*, 1992 U.S. Dist. LEXIS 7418, at *4.

In the event that outside counsel cannot hire the accountant, the hiring probably should be done by in-house counsel rather than corporate management. The probability of a successful claim of privilege may be diminished even further when the accountant or other third-party expert is hired by corporate management.

Another important step is that the attorney should document the relationship with the accountant or other business expert using a written engagement agreement that precisely defines the terms of any arrangement.[249] The engagement agreement should also set forth the legal purpose of the accounting services.[250] If appropriate, the engagement agreement should state that the accountant is being hired in anticipation of litigation.[251] It may also be worthwhile for the attorney to state in the retainer agreement the likelihood of hiring one or more consultants as experts.

The engagement agreement should expressly state that all communications among the attorney, client, and accountant are incidental to the rendering of legal services and are intended to be confidential.[252] The holding in *Kovel* indicates that the accountant and client may communicate outside the attorney's presence as long as they do so at counsel's direction.[253] The guidance of counsel is critical because in *United States v. Bein*,[254] a federal appeals court held that attorney-client privilege did not cover a conversation between an accountant and client outside the presence of the client's attorney, even though the conversation dealt with the client's liability. In the case of a corporation, a written directive from top management or a board resolution should indicate that any communications between employees and/or agents and the attorney or consultants hired by the attorney

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[249]Twardy & Considine, *supra* note 243, at 5.

[250]Segal, *supra* note 1, at 55.

[251]Spiro & Rule, *supra* note 13, at S10.

[252]*Id.*; Tigue et al., *supra* note 237, at 4.

[253]United States v. Kovel*,* 296 F. 2d 918, 921-22 (2d Cir. 1961).

[254]728 F.2d 107 (2d Cir. 1984). This case involved the activities of E-K Capital Corporation and its officers. Bein and DeAngelis were both officers of E-K Capital. Enchelmeyer was both an officer and a shareholder. The company owed $11 million in profits to its customers whose contracts had matured. In March 1980, E-K Capital was shut down after being raided by the FBI.

During the grand jury proceedings, Stitt, an accountant, testified about meetings he attended where Bein, DeAngelis, and two attorneys discussed E-K's business. After the meetings, in the absence of the attorneys, Stitt and Bein discussed corporate and individual liability for selling illegal option contracts. At trial, the conversations between Bein and DeAngelis and the attorneys were deemed privileged. Stitt's conversation with Bein was not cloaked with privileged status. The court found the conversation had occurred after legal advice had been obtained and without the direction of counsel. *Id.* at 110, 112-13.

are made at the direction of top management. Moreover, none of the parties should disclose the nature or content of any communications or work product to any third party, including government officials, lest the privilege be waived.[255]

[255]Tigue et al., *supra* note 237, at 4.

In *United States v. South Chicago Bank*, officers of Advance Bancorp found evidence indicating that the president of Advance Bank, a subsidiary bank, had embezzled funds.[256] Prior to joining Advance, the president had worked at South Chicago Bank, another subsidiary of Advance Bancorp.[257] Because fraud may also have been perpetrated against South Chicago Bank, the board of directors created a Special Fraud Audit Committee.[258]

The law firm of Winston & Strawn was hired to conduct an investigation.[259] In turn, Winston & Strawn retained Coopers & Lybrand to assist in the investigation.[260] Upon completion of the investigation, Winston & Strawn provided a copy of its final report to the Illinois Commissioner of Banks & Trusts, at the latter's request.[261]

The federal government subpoenaed the final report as part of an investigation. South Chicago Bank asserted attorney-client privilege despite an involuntary disclosure to a regulatory agency.[262] A federal district court held the attorney-client privilege had been waived because the report had been disclosed to the Bank Commissioner without seeking judicial intervention, and to uphold attorney-client privilege would interfere with the criminal investigative process.[263]

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[256]No. 97CR 849-1, 2, 1998 U.S. Dist. LEXIS 17445, at *1 (N.D. Ill. Oct. 16, 1998).

[257]*Id.*

[258]*Id.* at *2.

[259]*South Chicago Bank*, 1998 U.S. Dist. LEXIS 17445, at *2.

[260]*Id.*

[261]*Id.* at *12.

[262]*Id.* at *1, *12.

[263]*South Chicago Bank*, 1998 U.S. Dist. LEXIS 17445, at *13-*15.

The outcome of this case indicates the importance of counsel alone having the right to decide whether any disclosure is made to third parties. Disclosure of confidential material to a regulatory agency, for example, does not necessarily lead to a waiver of the privilege.[264] The attorney-accountant engagement agreement should state that all documents, including workpapers, prepared during the engagement are the property of the lawyer and are held by the accountant solely for the attorney's convenience.[265] Moreover, documents prepared by an accountant should be labeled "Protected by the Attorney-Client and Work-Product Privilege."[266] Any written work product should clearly state that it is being produced pursuant to requests from the law firm or corporate legal department name.[267]

The accountant should directly bill the law firm for whom work is being done. Neither invoices nor copies of any invoices should be sent to the law firm's client. Payments to the accountant should be made by the law firm. The law firm's invoice(s) sent to the client should separately itemize the accountant's fees as expenses.[268]

B. *Means to Prevent Inadvertent Disclosure Via Electronic Communications*

Until advancements in cordless and cellular telephone technology result in the recognition of a reasonable expectation of privacy, two methods are available to enhance confidentiality. One method is to "scramble" communications at a cost of several hundred dollars per scrambling device.[269] A more expensive technique is to ensure lack of *interception* by

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[264]*See In re Leslie Fay Companies, Inc. Securities Litigation*, 161 F.R.D. 274 (S.D.N.Y. 1995). A federal district court considered whether the voluntary disclosure to the SEC of a report summarizing the results of a law firm's fraud investigation waived attorney-client privilege. In January 1993, the board of directors of Leslie Fay Companies, Inc. was informed of certain accounting irregularities. The board requested its audit committee to start an investigation and report its findings. *Id.* at 277-78. The audit committee hired the law firm of Weil, Gotshal, & Manges to assist in the investigation. The law firm, in turn, hired Arthur Andersen. In April 1993, Leslie Fay filed for protection under the federal bankruptcy laws. In September 1993, the SEC was given a copy of the audit committee's report. *Id.* at 277-78, 278 n.2.

The district court held that the audit committee's production of the report to the SEC waived any attorney-client privilege covering the report itself. The court went on to add "that production, by itself, may not have constituted a broad waiver of privilege attending all of the documents underlying the report . . . ." *Id.* at 283.

[265]Spiro & Rule, *supra* note 13, at S10.

[266]Twardy & Considine, *supra* note 243, at 6.

[267]Riback, *supra* note 96, at S12.

[268]Twardy & Considine, *supra* note 243, at 6.

[269]James J. Harrison, Jr., *Plugging Cellular Leaks*, THE RECORDER, July 9, 1993, at 6.

using an encryption device.[270] The expense of both methods is probably a deterrent to widespread acquisition of scrambling and encryption devices by attorneys and business experts. Hence, both cordless and cellular telephone communications remain vulnerable to interception and inadvertent disclosure.

Fax machines are less vulnerable to interception than cordless and cellular telephones but still present a risk for inadvertent disclosure. For example, privileged materials could be accidentally transmitted to opposing counsel.[271] One practical means to reduce the likelihood of waiver of the attorney-client and/or *Kovel* privileges is to place a confidential legend on the fax cover sheet.[272]

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[270] *Id.*

[271] Mitchel L. Winick et al., *Playing I Spy with Client Confidences: Confidentiality, Privilege, and Electronic Communications,* 31 TEX. TECH L. REV. 1225, 1240 (2000).

[272] Such a legend may read as follows:

> Privileged and Confidential—All information transmitted hereby is intended only for the use of the addressee(s) named above. If the reader of this message is not the intended recipient or the employee or agent responsible for delivering the message to the intended recipient(s), please note that any distribution or copying of this communication is strictly prohibited. Anyone who receives this communication in error should notify us immediately by telephone and return the original message to us at the above address via the U.S mail.

Bruckner-Harvey, *supra* note 136, at 385.

The legal effect of the confidential legend depends on which of the three waiver theories a court follows. A legend will have no impact on a court that adheres to the strict responsibility approach. A court which subscribes to the "no waiver" approach may not even require a legend to put opposing counsel on notice. A court which follows the balancing approach would probably consider the legend as a reasonable precaution under most circumstances.[273] Moreover, the ABA's Formal Opinion, "Inadvertent Disclosure of Confidential Materials," mandates that opposing counsel should (1) not examine the materials once the inadvertence is discovered; (2) notify the sending lawyer of their receipt; and (3) follow the sending lawyer's instructions as to disposition.[274]

E-mail is also vulnerable to both interception and inadvertent disclosure. Two reliable methods are available to enhance the confidentiality of e-mail communications themselves and the probability of a successful claim of attorney-client privilege. One of the most common methods in use is encryption. "Encryption software takes a readable message, called plaintext, and processes it with a key through a mathematical algorithm, called a cipher, to scramble the message into unreadable ciphertext. The ciphertext is transmitted to a receiver, who uses a key to decode the ciphertext back into readable plaintext."[275] The use of encryption can substantially reduce the likelihood of waiver of the attorney-client and *Kovel* privileges due to the inadvertent disclosure of confidential materials. A second technique is the use of an Internet service provider, such as AOL, in which access to e-mail communications is protected by a password.[276]

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[273] *Id.* at 393.

[274] ABA Comm. on Ethics and Professional Responsibility, Formal Op. 92-368 (1992).

[275] William Hillison et al., *Electronic Signatures and Encryption*, CPA J., Aug. 2001, at 23.

[276] In *Maxwell,* 45 M.J. at 417, *later proceeding*, 46 M.J. 413 (C.A.A.F. 1997), a federal appellate court held that the sender of an e-mail message on AOL has a reasonable expectation of privacy.

The vulnerability of electronic communications, particularly cordless and cellular telephones and e-mail, demands that attorneys and third-party experts exercise vigilance in the use of these mediums. "A failure to inform the client of the vulnerabilities of radio wave communications could result in the destruction of the attorney-client privilege, depending upon the jurisdiction . . . ."[277] "If a client's conviction or the loss of a case turns on" the inadvertent disclosure of an electronic communication, the attorney or accountant could be sued for malpractice or subject to disciplinary proceedings.[278]

VI. CONCLUSION

Accountants and others are frequently hired by clients or attorneys as non-testifying experts or consultants. The ability to deliver quality services requires the ability to protect communications and work product from disclosure or interception. Although some states recognize an accountant-client privilege, such recognition is of dubious value because it is not applicable in federal cases. Federal common law does not recognize an accountant-client privilege.

A lawyer may shield a non-testifying, third-party expert under the *Kovel* rule with the attorney-client privilege. This rule insulates expert-attorney-client communications and work product when the expert is hired by the attorney to help provide legal services. The privilege extends only to specific communications, not facts. It is critical to the privilege that the communication be made in confidence and for the purpose of obtaining legal advice from the attorney. The privilege may be waived unless it is claimed before any disclosure of the communication sought to be protected. Also, the party claiming the privilege bears the burden of proving the existence of the various factors required to sustain it.

A carelessly structured *Kovel* arrangement leaves the attorney-client privilege susceptible to challenge. Various protective measures are vital to preserve the extension of the privilege to accountants and other experts. The attorney should hire the expert under a written engagement agreement that precisely states the terms of the arrangement. The agreement should state the legal purpose of the expert's services. Moreover, the engagement agreement should indicate that all communications among the attorney,

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[277] Higgins, *supra* note 163, at 287-88.

[278] *Id.*

expert, and client are to remain confidential and that all workpapers are the attorney's property.

Accountants, other experts, and attorneys should be concerned about the risks of inadvertent disclosure and eavesdropping from the use of cordless and cellular telephones, faxes, and e-mail. In some cases, inadvertent disclosure leads to the loss of the attorney-client and *Kovel* privileges. Cordless and cellular telephones should not be used to discuss privileged information. Privileged material sent by fax should be transmitted using a cover sheet bearing a confidential legend. Unencrypted e-mail discussing privileged information should not be sent over the Internet. As technology advances, however, various forms of electronic communication may become endowed with a reasonable expectation of privacy.