Attorney-Client Privilege: Is There a Fiduciary Exception? – Part Two

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This article continues with a discussion of the problems with an uncertain attorney-client privilege and developments regarding a fiduciary exception in the states over the last 10 years.

Courts in other jurisdictions have recognized the dangers associated with a judicially imposed fiduciary exception. For instance, in *Hubbell v. Ratcliffe*, the Superior Court of Connecticut refused to adopt the fiduciary exception, holding that it "is important not to weaken the privilege with various exceptions because ... even the threat of disclosure would have a detrimental effect on attorneys' ability to advocate for their clients while preserving the duty of confidentiality." See 2010 Conn. Super. LEXIS 2853, at *8-9, 15 (Conn. Super. Nov. 8, 2010), citing *Hickman v. Taylor*, 329 U.S. 495, 511 (1947).

Courts of various jurisdictions have voiced similar concerns in refusing to recognize the fiduciary exception to the attorney-client privilege. See *Symmons v. O'Keeffe*, 644 N.E.2d 631, 640 (Mass. 1995) (holding that the attorney-client privilege protected memorandums prepared by a trustee's counsel). *Symmons* cited to Scott on Trusts for the proposition that "where there is a conflict of interest between the trustee and the beneficiaries and the trustee procures an opinion of counsel for his own protection, the beneficiaries are not entitled to inspect the opinion." This is own protection, the beneficiaries are not entitled to inspect the opinion." This comment fails to recognize, however, that there is always a latent conflict of interest between a trustee and beneficiaries. Every time the trustee acts or fails to act, it does so at the risk of later challenge by one or more beneficiaries. In the real world, when the trustee procures an opinion of counsel, it is always doing so for its own protection, in addition to doing so for the benefit of the trust.

PENNSYLVANIA LAW SINCE FOLLANSBEE

Although Allegheny County Court of Common Pleas Judge R. Stanton Wettick's opinion in Follansbee v. Gerlach, 56 Pa. D. & C. 4th 483, 22 Fiduc. Rep. 2d 319, 6 All. Co. Disc. Op. 15 (Civ. Div. Allegh., June 13, 2002), has been cited in numerous secondary sources, no Pennsylvania appellate authority adopting the Follansbee holding exists. Follansbee is clearly and explicitly founded on the Delaware Chancery Court's opinion in *Riggs National Bank v. Zimmer*, 355 A.2d 709, 713 (Del Ch. 1976). In fact, the only Pennsylvania case (picked up by Shepard's) to have cited to Riggs is Follansbee. But, even *Follansbee* rejects the first of the two rationales adopted in *Riggs*, i.e., that beneficiaries are "clients" of the trustee's counsel.

As explained in Part I, compelling policy arguments argue against the adoption of the fiduciary exception in this commonwealth. Several states have already recognized these policy concerns, acknowledged the dangers associated with the fiduciary exception and rejected it altogether.

AUG. 20, 2002: NEW YORK REJECTS THE EXCEPTION

On Jan. 24, 2002, approximately five months before *Follansbee* was decided, the U.S. District Court for the Southern District of New York in *Lawrence v. Cohn*, 2002 U.S. Dist. LEXIS 1226, applied the fiduciary exception and required the production of various documents by Weil, Gotshal & Manges, which had represented the executor of an estate in a proceeding in which the executor sought approval from the Surrogate's Court to take a property interest for himself rather than for the estate. In *Follansbee*, Wettick specifically stated, "I also find to be persuasive the recent opinion in *Lawrence v. Cohn*." Thereafter, a challenge by the beneficiaries resulted in a settlement in which the executor and the beneficiaries would equally share the purchased realty interest. Later, however, plaintiffs in the Lawrence case filed an action under the federal securities laws claiming that the executor had fraudulently concealed from them the fact that a bank was prepared to take a net lease on the entire building involved on extremely favorable terms, and, had that fact been disclosed, the beneficiaries would have insisted on taking the entire interest available. The magistrate judge, in the course of substantially granting the plaintiffs' motion to compel documents, relied heavily on the Riggs case and its analysis:

> "Simply stated, WGM represented Cohn in that case only in his capacity as executor. In that capacity, he owed certain fiduciary responsibilities to the estate and, thus, to its beneficiaries. Given those obligations, he cannot assert the privilege, nor can WGM invoke the work-product rule, against the estate or its beneficiaries. ...
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> Thus, the firm's services, which are paid for by the estate, were rendered, in effect, on behalf of the estate and, by extension, on behalf of the beneficiaries."

Shortly after this decision, the New York Legislature amended Article 45 of its Civil Practice Law and Rules relating to attorney-client privilege, adding Section 4503(a)2, specifically dealing with the privilege in the context of a personal representative of an estate. That provision, L 2002, ch. 430 § 1, effective Aug. 20, 2002, was added to make explicit that a beneficiary is not the client of an attorney who represents a fiduciary; the fact that the fiduciary owed duties to the beneficiary did not mean that there was a waiver of the attorney-client privilege for confidential communications made in the course of professional consultation between the attorney and the personal representative who is his or her client.

AUG. 1, 2007: DELAWARE REJECTS A FUNDAMENTAL RATIONALE

Even Delaware, which started all this debate, has moved away from the exception. In 2007, the legislature added a new section to its Decedent's Estates and Fiduciary Relations Code, 12 Del. Code § 3333, as follows:

> " § 3333. Retention of Counsel by Fiduciary. Except as provided in the governing instrument, a fiduciary may retain counsel in connection with any claim that has or might be asserted against the fiduciary, and the payment of counsel fees and related expenses from the fund with respect to which the fiduciary acts as such shall not cause the fiduciary to waive or to be deemed to have waived any right or privilege including, without limitation, the attorney-client privilege. However, in the event that the fiduciary is found to have breached some fiduciary duty, the court may, in its discretion, deny such fiduciary the right to have some part or all of such fees and expenses paid from such fund and may require the fiduciary to reimburse any such fees and expenses that have previously been paid."

In *Riggs*, the Chancery Court had stated that "payment to the law firm out of the trust assets is a significant factor, not only in weighing ultimately whether the beneficiaries ought to have access to the document, but also it is in itself a strong indication of precisely who the real clients were." The statutory amendment rejects that position where a fiduciary retains counsel "in connection with any claim that has or might be asserted against the fiduciary." As a result of this change, "payment to the

law firm out of the trust assets" would no longer be a "significant factor" in determining whether a document was privileged or not, nor would it be an indicator of who the client was.

MAY 13, 2008: SOUTH CAROLINA REJECTS THE EXCEPTION

In *Floyd v. Floyd*, 615 S.E.2d 465 (2005), the Court of Appeals of South Carolina embraced the fiduciary exception, noting: "We find the Riggs rationale persuasive." However, on May 13, 2008, the South Carolina legislature enacted S.C. Code Ann. § 62-1-110 (2011) providing as follows:

> "Whenever an attorney-client relationship exists between a lawyer and a fiduciary, communications between the lawyer and the fiduciary shall be subject to the attorney-client privilege unless waived by the fiduciary, even though fiduciary funds may be used to compensate the lawyer for legal services rendered to the fiduciary. The existence of a fiduciary relationship between a fiduciary and a beneficiary does not constitute or give rise to any waiver of the privilege for communications between the lawyer and the fiduciary."
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> As the legislative history makes clear, the section was enacted and intended to:
> "(i) expressly reject the concept of a 'fiduciary exception' to any attorney-client privilege; (ii) encourage full disclosure by the fiduciary to the lawyer to further the administration of justice; and (iii) foster confidence between a fiduciary and his lawyer that will lead to a trusting and open attorney-client dialogue. See Estate of Kofsky, 487 Pa. 473 (1979). This section also expressly rejects the holding set forth in the case of *Riggs Natl. Bank v. Zimmer*, 355 A.2d 709 (Del. Ch. 1976) (trustee's invocation of the attorneyclient privilege does not shield document from disclosure to trust beneficiaries) as applied by the court in *Floyd v. Floyd*, 365 S.C. 56, 615 S.E.2d 465 (Ct. App. 2005)."

JUNE 9, 2010: N.M. FED. COURT PREDICTS REJECTION

In *Murphy v. Gorman*, 271 F.R.D. 296, 318 (D.N.M. 2010), the U.S. District Court for the District of New Mexico predicted that the Supreme Court of New Mexico would not recognize the fiduciary exception. In refusing to create a fiduciary exception to the attorney-client privilege, courts have acknowledged that the existence of a fiduciary exception could lead trustees to take protective action that could ultimately detriment the trust and its beneficiaries "Without the privilege, trustees might be inclined to forsake legal advice ... [or] feel compelled to blindly follow counsel's advice." See Huie v. DeShazo, 922 S.W.2d.

JUNE 13, 2011: JUSTICES ADDRESS 'ASSUMED' EXCEPTION

On June 13, 2011, the U.S. Supreme Court handed down its opinion in United States v. Jicarilla Apache Nation, 2011 U.S. LEXIS 4381, 131 S. Ct. 2313 (2011). In that case, the court held that communications between the United States and its attorneys regarding the administration of a trust benefiting a Native American nation were not subject to the fiduciary exception because of the unique sovereign interests at issue and because the U.S. government's disclosure requirements are governed by statute rather than by the common law. In doing so, it acknowledged:

> "Today, 'courts differ on whether the [attorney-client] privilege is available for communications between the trustee and counsel regarding the administration of the trust.' A. Newman, G. Bogert & G. Bogert, 'Law of Trusts and Trustees' § 962, p. 68 (3d ed. 2010) (hereinafter 'Bogert'). Neither party before this court disputes the existence of a common-law fiduciary exception, however, so in deciding this case we assume such an exception exists."

The section of the Bogert text referred to includes a comprehensive review of the laws of various jurisdictions with respect to the fiduciary exception, noting that most jurisdictions have upheld the privilege. With respect to the distinction between matters of administration and matters of liability, at oral argument, Chief Justice John Roberts stated that he didn't see this distinction as a "workable"

one. Justice Anthony Kennedy referred to it as "murky." Justice Antonin Scalia said it was "artificial," adding:

> "What I ask ... for from the attorney is advice as to how I can manage the trust so as to avoid liability. I mean, the – the two are connected. You can't separate out advice as to how to manage, how to manage the trust from advice as to how to avoid liability. In the - in the context of asking, of a trustee's asking advice, the two are the same."

JUNE 21, 2011: FLORIDA REJECTS THE EXCEPTION

One week later, the Florida Legislature enacted HB 325, which in effect abrogated the fiduciary exception. In relevant part, HB 325 states that:

> "A communication between a lawyer and a client acting as a fiduciary is privileged and protected from disclosure under s. 90.502 to the same extent as if the client were not acting as a fiduciary." See §90.5021(2) Florida Statutes.
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> This section makes clear that "the communications between the fiduciary and client should be privileged and protected from disclosure, regardless of whether the communications were for the ultimate benefit of the beneficiary. See Jack A. Falk Jr., "Are the Client's Secrets Safe? The Fiduciary Privilege and Post-Death Ethical Obligations of the Planner; and a Primer on Clarified Deadlines for Seeking Fees in Trust Litigation." See also *Paskoski v. Johnson*, 626 So.2d 338, 339 (Fla. App. 1993) (holding that a trustee could properly assert the attorney-client privilege with respect to communications between the trustee and the trustee's lawyer).

EXCEPTION LACKS ADEQUATE JUSTIFICATION

Over the last decade, several states, reaffirming the important policy considerations behind the attorney-client privilege in the context of fiduciary relationships, have rejected, through case law or by statute, the fiduciary exception.

Protecting the attorney-client privilege between trustees and their counsel is in the best interest of both trustees and trust beneficiaries because it promotes conversations about fiduciary obligations between fiduciaries and their counsel; to do otherwise would, as the *Gillard v. AIG Insurance* court points out, restrain such communications by "require[ing] the disclosure of communications which likely would not exist ... but for the participants' understanding that the interchange was to remain private."

The attorney-client privilege is the oldest privilege known to the common law. Exceptions to that privilege erode it. The fiduciary exception lacks an adequate justification or rationale to support it. It exists in a minority of states and in the recent past has been rejected more often than accepted. Pennsylvania should do likewise.