

The New York Court of Appeals Rejects Attempted Expansion of the Common Interest Exception to the Attorney Client Privilege

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July 8, 2016

Last month, the New York Court of Appeals issued a decision rejecting the attempted expansion of the common interest exception to the attorney-client privilege to include communications that did not involve pending or anticipated litigation. In *Ambac Assurance Corporation v. Countrywide Home Loans, Inc.*, No. 80, 2016 N.Y. Lexis 1649, 2016 NY Slip Op 04439 (June 9, 2016), the Court of Appeals held that the common interest exception applies only where information shared between parties represented by separate counsel relates to the parties' legal interest in a pending or reasonably anticipated litigation. This ruling overturns an Appellate Division, First Department, decision that held, in the face of long-standing New York law to the contrary, that the exception applied even in the absence of a pending or anticipated litigation, so long as the communication related to a shared legal interest.

The *Ambac* decision is of interest to all attorneys and parties considering the disclosure of privileged information to a third party outside of a litigation context, whether in commercial transactions, mergers, regulatory compliance, or other situations where litigation is not pending or reasonably anticipated. By rejecting the First Department's broadening of the common interest doctrine, the Court of Appeals has established a narrower application of the common interest doctrine under New York law than the majority of federal courts and a substantial number of state courts that have considered the issue.

Ambac Assurance – Underlying Dispute

The *Ambac* decision arises out of a discovery dispute involving privileged documents Countrywide Home Loans, Inc. ("Countrywide") shared with Bank of America after signing a merger plan with Bank of America but before the merger between the two companies was finalized. The underlying litigation was brought by Ambac Assurance Company ("Ambac"), which had guaranteed payments on certain residential mortgage securities issued by Countrywide. When the mortgage-backed securities that Ambac insured failed during the financial crisis, Ambac brought an action against Countrywide alleging that Countrywide misrepresented the quality of the underlying loans to fraudulently induce Ambac to guarantee them. Ambac also named Bank of America as a defendant based on its 2008 merger with Countrywide.

During discovery, Ambac challenged Bank of America's withholding, based on the assertion of

privilege, of several hundred relevant communications between Bank of America and Countrywide that were exchanged after the two companies signed a merger plan in January 2008 but before the merger closed in July. Ambac argued that Bank of America and Countrywide waived the privilege because they were not affiliated entities at the time of disclosure and did not share a common legal interest in litigation or anticipated litigation. Conversely, Bank of America argued that although the documents at issue were shared with a third party (Countrywide), the privilege was preserved under the common interest exception, because Bank of America and Countrywide shared an interest in the successful completion of the merger at the time of the disclosure.

Ambac moved to compel the production of these documents and the Supreme Court held that the documents were not privileged. On appeal, however, the Appellate Division, First Department rejected the established holdings of New York appellate and trial courts that conditioned the common interest exception on the presence of a pending or anticipated litigation, holding that the “better approach”, consistent with the rule in the majority of federal courts including the Second, Third, Seventh, and Federal Circuit Courts of Appeals, would be to reject a litigation requirement. *Ambac Assurance Corp. v. Countryside Home Loans, Inc.*, 124 A.D.3d 128, at 134 (1st Dep’t 2014). Limiting the common interest exception to those instances in which parties faced pending or anticipated litigation, the First Department held, “would inevitably result... in the onset of regulatory or private litigation” because parties to a merger would be discouraged from seeking and sharing legal advice concerning the merger. *Id.* at 137. Ambac appealed the First Department’s decision.

Court of Appeals Decision

The Court of Appeals reversed the First Department’s decision in a divided opinion. The majority rejected the First Department’s approach to the common interest exception, noting that until the First Department’s decision, New York courts had “uniformly rejected efforts to expand the common interest doctrine to communications that do not concern pending or reasonably anticipated litigation.” 2016 N.Y. LEXIS 1649, at *14-15 (citing New York state cases). The majority explained that, in the litigation context, “[w]hen two or more parties are engaged in or reasonably anticipate litigation in which they share a common legal interest, the threat of mandatory disclosure may chill the parties’ exchange of privileged information” and therefore, application of the common interest exception “promotes candor that may otherwise have been inhibited.” *Id.* at *16-17. However, the Court held that “[t]he same cannot be said of clients who share a common legal interest in a commercial transaction or other common problem but do not reasonably anticipate litigation.” *Id.* at *17.

The Court of Appeals stressed that the potential for abuse that would arise from expanding the common interest exception to situations where litigation was not pending or anticipated outweighed the benefits. Specifically, the Court stated:

The difficulty of defining “common legal interests” outside the context of litigation could result in the loss of evidence of a wide range of communications between parties who assert common legal interests but who really have only non-legal or exclusively business interests to protect. Even advocates of a more expansive approach admit that “in a nonlitigation setting the danger is greater than the underlying communication will be for a commercial purpose rather than for securing legal advice.”

Id. at *19. The Court drew a distinction between the need for the common interest exception in litigation and its need in commercial or business contexts, noting that “[t]here is no evidence, for

example, that mergers, licensing agreements and other complex commercial transactions have not occurred in New York because of [New York's] keeping a litigation limitation on the common interest doctrine" and "therefore [the Court] maintain[s] the narrow construction that New York courts have traditionally applied." *Id.* at *17 and 24.

Case Implications and Concerns

While the *Ambac* decision maintains the well-established common law exception in New York that existed prior to the First Department's decision, it serves as an important reminder of how narrow the common interest exception is in New York as compared to other jurisdictions. Particularly in the context of corporate or intellectual property transactions and financial restructuring and mergers, parties should be cautious about sharing privileged communications with third parties unless there is pending or threatened litigation. Likewise, parties should be mindful of this law and its application when engaging in commercial transactions that occur in New York or entering into contracts governed by New York law.

Moreover, the scope of the common interest will continue to be evaluated on a case-by-case, fact specific basis, as the Court of Appeals expressly declined to decide what it means to "share legal interests in pending or anticipated litigation" and held only that "such litigation must be ongoing or *reasonably anticipated*, and the exchanged communication must relate to it in order for the common interest exception to apply." *Id.* at *21, n. 4 (emphasis added). Thus, how the "reasonably anticipated" requirement is defined by New York courts will be critical to the exception's application.

Finally, in its opinion, the Court of Appeals invited the New York legislature "to expand the common interest exception as other state legislatures have done." *Id.* at *25, n. 6. It remains to be seen whether this will be a legislative priority.