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## ALL IN THE FAMILY— A LESSON IN PROPER TAILORING FROM *TELEGLOBE*

Jonathan Friedland and Mike Xu  
Schiff Hardin LLP  
Chicago, IL

Restructuring attorneys are always interested in the latest word from the Delaware Chancery Court on issues that are likely to have significant impact on bankruptcy practice. We're interested for the same reason, of course, in federal court decisions that interpret Delaware law.

More often than not, we concern ourselves with substantive areas like fiduciary duties that are commonly litigated in Chapter 11 cases. However, the way matters are litigated can also be outcome determinative and occasionally a decision comes along on a procedural aspect of our practice that necessitates careful study. The Third Circuit's decision in *Teleglobe USA Inc. v. BCE Inc. (In re Teleglobe Communications Corp.)*,<sup>1</sup> is just such a decision.

Teleglobe, Inc. was a subsidiary of Bell Canada Enterprises, Inc. (BCE). The subsidiaries of Teleglobe (but not Teleglobe itself), were Chapter 11 debtors. The debtors and the com-

**Managing Editors:** Hon. Keith M. Lundin, United States Bankruptcy Judge, Nashville, Tennessee  
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mittee sued BCE for causes of action of classic “corporate abandonment”—breach of contract, breach of fiduciary duties, estoppel, and misrepresentations.

The debtors and the committee sought to compel BCE to produce certain documents relating to BCE’s divestiture of Teleglobe. BCE asserted that those documents were privileged because “BCE attorneys consulted with attorneys, officers, or employees of Teleglobe, Inc. or its subsidiaries to discuss or provide legal service in matters where BCE and Teleglobe, Inc. (or its subsidiaries) shared a common legal interest.”<sup>2</sup>

The Third Circuit’s holding highlights an effect—and perhaps utility—of separate corporate form. Namely, separate corporate form not only can shield a parent from its subsidiaries’ liabilities, but also can make a difference in protecting a parent’s attorney-client privilege under many circumstances. However, this latter protection is anything but absolute, and that is what *Teleglobe* is about.

**Corporate Separateness**

The concept of corporate separateness is as central to corporate law as it is well understood: company A may own company B, but company A is generally not liable for the debts of company B. The nature of the exceptions to the general rule are also generally well understood: company A may be held liable for the debts of company B under various theories, such as on the basis that the two companies were run as one.

This is a vast oversimplification, of course, but the concept is that unless a plaintiff can provide some basis for penetrating the base-

line rule, company A will not be liable for the debts of company B. There are, of course, other claims company B may seek to bring against company A that rest on other theories. They too only succeed for the very reason that they enable company B and its creditors to reach the assets of company A, in derogation of the baseline rule.

**Lawsuits Against Former Parents**

When the telecom bubble burst in the year 2000, BCE cut off its funding for Teleglobe’s much flaunted fiber optic project, and divested itself of Teleglobe.<sup>3</sup> The debtors, Teleglobe’s subsidiaries, sued BCE for “corporate abandonment” and sought documents generated in the joint representation of BCE and Teleglobe in connection with the divestiture. Litigation against a former parent is by no means unique in the bankruptcy context.<sup>4</sup>

*Attorney-client privilege in joint representation*

A particular evidentiary issue that comes up time and again in this sort of litigation is the extent to which certain communications are subject to the joint-client privilege, with the subsidiary and parent being the co-clients.<sup>5</sup>

The attorney-client privilege, of course, is one of the bedrocks of the rules of evidence. The purpose of the privilege is to encourage full and frank communication between attorneys and their clients, and thereby it promotes administration of justice.<sup>6</sup>

Parents and subsidiaries will often use the same counsel for at least some of their respective legal needs. It just makes good business sense for a host of obvious reasons having to do with economy and efficiency. When this

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happens, that is, when one counsel (whether in-house or outside) represents two clients on the same matter, the result is a joint representation and each of the clients is considered a co-client.

Whether a joint representation exists—and the scope of such joint representation—is determined by the intent and expectation of the parties.<sup>7</sup> Any communications between counsel and co-clients in the joint representation are protected by attorney-client privilege from compelled disclosure by a third person—this is the co-client or joint privilege.<sup>8</sup>

However, a communication by a co-client to the common attorney is not privileged from the other co-client. This makes sense because there should be no secrecy between the co-clients at the time of communication concerning the common interest.<sup>9</sup>

Single counsel cannot represent co-clients where the clients' legal interests have diverged too far to justify using common counsel.<sup>10</sup> Moreover, when one former co-client later litigates against the other concerning the matter involving the joint representation, the communications in the joint representation *lose* the privilege protection and are subject to discovery. This is the adverse litigation exception to joint privilege, and it is true even if the former co-clients had agreed that communication between the attorney and each co-client would not be subject to discovery in subsequent adverse litigation.

It is essential to remember that the joint adverse litigation exception only applies to communication concerning matters that were the subject of the co-client relationship.

This presents a critical question: Does the adverse litigation exception mean that a debtor can invade its parent's privilege in later litigation? This issue was presented to the Third Circuit in *Teleglobe*, and for us it is one of the more significant issues addressed in the decision.<sup>11</sup>

### The Third Circuit's View

The Third Circuit, in *Teleglobe*, articulated two fundamental premises. First, corporate form ought to be respected and BCE and Teleglobe were two clients rather than one client. Second, the representation regarding BCE's divestiture of Teleglobe was a joint-representation, with BCE and Teleglobe being the co-clients. Much of the decision can be viewed as the Third Circuit's application of the rules governing joint privilege.

First, absent an agreement with co-clients to the contrary, each co-client may waive the privilege as to that co-client's own communications if the communication relates only to the communicating and waiving client, but one co-client cannot unilaterally waive the privilege as to another co-client's communications to their common lawyer.<sup>12</sup> When a document contains communications from two or more co-clients, all those co-clients must join in a waiver, unless a nonwaiving co-client's communication can be redacted from the document.<sup>13</sup>

Second, the doctrine developed in *Eureka Investment Corp., N.V. v. Chicago Title Insurance Co.*,<sup>14</sup> is applicable to parent and subsidiary. *Eureka* stands for the proposition that when one co-client consults a common attorney in confidence regarding the same matter but with an interest adverse to the other co-client, such communication should not be later discoverable by the opponent/co-client under the adverse litigation exception. In other words, the communication should not be deprived of the privilege even if the asserted attorney-client relationship, which is adverse to one co-client, should not have been created.<sup>15</sup>

Stated another way, when conflict develops during the joint representation, one client may consult the common attorney regarding a position adverse to the other co-client, and in that situation will expect confidence of that communication.<sup>16</sup> That communication is not part of the joint representation in subsequent adverse litigation, even if the communication relates to the subject under the joint representation.<sup>17</sup> Consequently, the communication is not

discoverable despite the fact that the common attorney conflicted himself by consulting the co-client.<sup>18</sup>

Finally, stockholders may access documents as to which the corporation holds attorney-client privilege when the corporation acted inimically to the stockholders' interests because the corporation owes a fiduciary duty to the stockholders.<sup>19</sup> This is the exception for breach of fiduciary duty. Similarly, the corporate parent owes a fiduciary duty to its subsidiary's creditors when the subsidiary is insolvent or in the zone of insolvency. The exception of breach fiduciary duty will apply against the corporate parent for the benefit of the subsidiary's creditors.<sup>20</sup>

*Take-aways for attorneys jointly representing parent and subsidiary*

Joint representation of parent and subsidiary, as we all know, and as we note above, is commonplace. It can happen in the context of joint defense in litigation, in financing matters, with respect to the provision of tax, environmental, real estate, and other advice, and a host of other situations.

So, how can a parent guard its communications against future invasion by its former subsidiaries, which may be outcome determinative in any future litigation?

Assuming there is a co-client relationship with respect to the matter at issue, the co-client privilege applies. However, that privilege will not do a parent-defendant any good if the adverse litigation (or another) exception applies. So, what's a parent to do?

To state the obvious, a parent should avoid any joint representation except when necessary. If joint representation is necessary, the parent should limit the scope of the joint representation and use outside counsel, if possible, in matters where a subsidiary is adverse to the parent. For example, in a spin-off and/or sale of a subsidiary, or when relying on a subsidiary's assets to borrow money, a parent should take care to limit the scope of joint representation and use outside counsel if necessary.

To reduce associated risk to zero, a parent should make sure to use counsel separate from its subsidiaries on any matter in which the parent and the subsidiary may later have differing interests. Pragmatically, though, this cannot always be known prospectively. Therefore, and in any event, care needs to be taken to define the scope of joint representations as narrowly as possible. What does this mean?

It means, in our view, that the mantra to take away from *Teleglobe* is: pay intense attention to properly tailoring the scope of joint representations. In this regard, an ounce of prevention is worth a pound of cure.

**West's Key Number Digest, Corporations**  
 ☞215; Antitrust and Trade Regulation 544;  
 ☞ Witnesses ☞199(2), 299(3)

**Notes**

1. *Teleglobe USA Inc. v. BCE Inc. (In re Teleglobe Commc'ns Corp.)*, 493 F.3d 345 (3d Cir. 2007).
2. *Teleglobe*, 493 F.3d at 354.
3. *Teleglobe*, 493 F.3d at 353.
4. See, e.g., *VFB LLC v. Campbell Soup Co.*, 482 F.3d 624 (3d Cir. 2007) (debtor's successor brought action against former parent to set aside spin-off of subsidiary as constructively fraudulent transfer and to recover for aiding and abetting directors' breach of duty of loyalty to the subsidiary before the spin-off); *Motorola, Inc. v. Official Committee of Unsecured Creditors (In re Iridium Operating LLC)*, 478 F.3d 452 (2d Cir. 2007) (a litigation vehicle was set up to sue debtor's former parent—Motorola); *Hopkins v. Plant Insulation Co.*, 342 B.R. 703 (D. Del. 2006) (asbestos claimants committee and future claims representative and heirs of deceased asbestos-injury claimant brought state-court action in California against debtor's former parent company and others, alleging that parent had alter-ego liability for any obligations owed by debtor to asbestos claimants); *In re Marvel Entm't Group, Inc.*, 273 B.R. 58 (D. Del. 2002) (debtor sued its former corporate parent, seeking to set aside certain transfers and obligations, and to impose liability on former parent for certain creditor claims).
5. See *In re Mirant Corp.*, 326 B.R. 646, 652 (Bankr. N.D. Tex. 2005) (debtor moved for 2004 examination of its former parent seeking documents from the law firm who represented the debtor and the parent in the spin-off); see also *Yorke v. Santa Fe Indus., Inc. (In re Santa Fe Trail Transp. Co.)*, 121 B.R. 794 (Bankr. N.D. Ill. 1990) (Chapter 7 trustee sued the debtor's former parent to avoid fraudulent transfers and sought documents that parent claimed were privileged); *Polycast Tech. Corp. v. Uniroyal, Inc.*, 125 F.R.D. 47, 49 (S.D.N.Y. 1989) (buyer of a subsidiary sued its former parent corporation and moved to compel production

of notes taken by officer of the subsidiary recounting substance of telephone conversations with parent corporation's general counsel concerning sale of subsidiary); *Medcom Holding Co. v. Baxter Travenol Labs., Inc.*, 689 F. Supp. 841, 842 (N.D. Ill. 1988) (buyer of a subsidiary sued the former parent, and the former parent withheld documents relating to the cases in which it and its former subsidiary were jointly represented in their defense by the same outside attorneys and documents containing attorney-client communications between officers of the subsidiary and the in-house attorneys at the parent relating to the sale of the subsidiary).

6. *Upjohn Co. v. United States*, 449 U.S. 383, 389, 101 S. Ct. 677, 66 L. Ed. 2d 584 (1981).
7. *Teleglobe*, 493 F.3d at 363.
8. See 8 J. Wigmore, Evidence § 2312, at 603 (McNaughton rev. ed. 1961).
9. 8 J. Wigmore, Evidence § 2312, at 606.
10. *Massachusetts Eye & Ear Infirmary v. QLT Phototherapeutics, Inc.*, 167 F. Supp. 2d 128, 129 (D. Mass. 2001).
11. *Teleglobe* is a lengthy decision. We confine our comments on *Teleglobe* in a number of significant respects. For a more detailed analysis of other aspects of the case, particularly with respect to the breach of fiduciary duty exception, we recommend Corrine Ball's article, *Teleglobe's Implications For Attorney-Client Privilege*, which appeared in the August 23, 2007 edition of the New York Law Journal. Yet other aspects of the decision were treated very nicely in *Parsing Teleglobe: Attorney/Client Privilege Rules for Jointly-Represented Corporate Entities*, which was authored by Lisa Schweitzer and Melissa Durkee and which appeared in the November/December 2007 edition of *The M & A Lawyer*.
12. *Restatement (Third) Of The Law Governing Lawyers* § 75 cmt. E.
13. *Restatement (Third) Of The Law Governing Lawyers* § 75 cmt. E.
14. *Eureka Inv. Corp., N.V. v. Chicago Title Ins. Co.*, 743 F.2d 932, 937 (D.C. Cir. 1984).
15. *Eureka*, 743 F.2d at 937.
16. See *Eureka*, 743 F.2d at 937.
17. *Teleglobe*, 493 F.3d at 381.
18. *Teleglobe*, 493 F.3d at 381.
19. *Garner v. Wolfinbarger*, 430 F.2d 1093 (5th Cir. 1970).
20. *Teleglobe*, 493 F.3d at 384.

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