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The Common Interest Privilege: Two Recent Cases Clarify Its Application to Protect Plan Negotiations

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Two recent decisions from the United States Bankruptcy Court for the District of Delaware add clarity to the application of the common interest privilege to plan negotiations. In the case of Leslie Controls, Inc. ("Leslie"),[1] Bankruptcy Judge Christopher S. Sontchi held that parties to a plan pursuant to 11 U.S.C. § 524(*g*) could rely on their common interest in maximizing the debtor's assets to withhold from discovery certain documents exchanged during their prepetition negotiations. Following *Leslie*, Bankruptcy Judge Kevin J. Carey similarly concluded that plan proponents in the Tribune Company bankruptcy proceedings could rely on a common interest to withhold the communications they shared while mediating a settlement and proposed plan from discovery sought by proponents of a competing plan.[2]

LESLIE—SHARED INTEREST IN PRESERVING AND MAXIMIZING DEBTOR'S ASSETS

In *Leslie*, Judge Sontchi clarified the scope of the common interest privilege and found that the debtor's insurers were not entitled to discovery of certain documents exchanged by the debtor and other parties in the course of developing a prenegotiated plan.[3] *Leslie* demonstrates that the parties negotiating a plan need not share a complete unity of interests on a legal position for the common interest privilege to apply. Rather, the common interest privilege will apply to the extent they have a shared cognizable legal interest.

On July 12, 2010, Leslie filed a plan it had negotiated prepetition with an ad hoc committee representing asbestos plaintiffs (the "Ad Hoc Committee") and Leslie's proposed future claimants' representative (the "Pre-Petition FCR") (Leslie, the Ad Hoc Committee and the Pre-Petition FCR are collectively referred to as the "Plan Parties"). Subsequently, two of Leslie's insurers sought 26 documents that Leslie had shared with the Ad Hoc Committee and the Pre-Petition FCR. The Plan Parties withheld the documents on the grounds that they were protected under the common interest doctrine.[4] The documents included a memorandum from Leslie's insurance counsel analyzing the effect of the insurers' likely coverage positions and communications among the Plan Parties regarding that advice.[5] On September 21, 2010, Judge Sontchi resolved the discovery dispute by holding that the common interest privilege protected the documents because they concerned and were exchanged in furtherance of the Plan Parties' shared legal interest in preserving and maximizing the debtor's total asset "pie," even though the Plan Parties had conflicting interests as to how the "pie" ultimately would be distributed.

Preliminarily, the court found, based on *in camera* review, that the documents were protected by the attorney-client privilege and/or work product doctrine because they concerned counsel's legal analysis and mental impressions in anticipation of litigation in the bankruptcy and/or insurance-coverage proceedings.[6] Any waiver of that privilege turned on whether the debtor satisfied the standards of the common interest privilege: "The party invoking the protection of the common interest doctrine must establish: (1) the communication was made by separate parties in the course of a matter of common interest, (2) the communication was designed to further that effort, and (3) the privilege has not otherwise been waived."[7] While the privilege does not require a "complete unity of interests[,]. . . it is limited by the scope of the parties' common interest."[8]

The insurers argued that Leslie waived any privilege by sharing the documents with the Ad Hoc Committee and Pre-Petition FCR, because the Plan Parties lacked an interest that was *legal* and *common*.[9]

1 In re Leslie Controls, Inc., 437 B.R. 493 (Bankr. D. Del. 2010).
2 In re Tribune Co., Case No. 08-13141 (KJC), 2011 Bankr. LEXIS 299 (Bankr. D. Del. Feb. 3, 2011).
3 Id. at 493.
4 Id. at 495.
5 Id.
6 Id. at 497.
7 Id.
8 Id. at 500.
9 Id. at 497.

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The insurers asserted that the common interest asserted by the Plan Parties – that of preserving and maximizing the estate's insurance assets – was, at best, a shared *commercial*, not *legal*, interest.[10] Further, the insurers claimed that the Plan Parties lacked a common issue when the documents were exchanged because at that time they had yet to agree on the terms of a plan and were adversaries with respect to the debtor's insurance proceeds.[11]

The court rejected the insurers' argument, finding the precedent they cited factually distinguishable or favorable to Leslie. The cases established that the party claiming the common interest privilege must present evidence implicating a *legal* interest.[12] Leslie met that standard because, when it exchanged the documents, the Plan Parties all shared the interest of preserving and maximizing the debtor's insurance assets to pay asbestos claims:

> As representatives of the ultimate beneficiaries of at least a portion of the proceeds [the Ad Hoc Committee and the Pre-Petition FCR] were directly involved in the effort to maximize insurance coverage. They were working with the Debtor to maximize the size of the pie. Whether their competing interests in getting the biggest piece of the pie prevented the application of the common interest doctrine in this case is another matter.[13]

The interest of maximizing the insurance assets was "inherently legal" because it involved analysis of insurance documents and contract, insurance and bankruptcy law and proceedings in the bankruptcy court.[14]

The court declined to adopt a black-line rule "that parties engaged in negotiations cannot share a common interest[,]" because the particular facts of each case determine whether a common interest exists.[15] The facts of *Leslie* showed that, although the Plan Parties had conflicting interests as to distribution of the debtor's assets, they shared a common interest in maximizing those assets against the insurers, their "common enemy":

> To return to the pie analogy, the size of the pie and the size of the pieces are two separate questions. The parties are in accord as to the former and adversaries as to the latter. The information contained in the documents that were shared with the Ad Hoc Committee and the Pre-Petition FCR goes to the size of the asset pool – a matter of common interest.[16]

Because the Plan Parties shared a common legal interest, all 26 documents were protected from discovery under the common interest doctrine.[17]

Pursuant to the *Leslie* opinion, parties negotiating a chapter 11 plan of reorganization may rely on the common interest privilege to exchange documents in furtherance of the common legal interest of preserving and maximizing the debtor's assets. The protection is not negated simply because the exchange occurs before the parties agree to plan terms and have competing interests as to whose constituency will receive the biggest piece of the debtor's asset pie.

Tribune—Shared Interest in Obtaining Court Approval of Proposed Settlement and Plan

In *Tribune*, Judge Carey adopted and followed much of the reasoning of *Leslie* to resolve a discovery dispute between competing proponents of reorganization plans. The Tribune Company and certain of its subsidiaries (the "Debtors") filed for bankruptcy protection on December 8, 2008.[18] In 2007, Tribune had been the subject of a leveraged buyout, which gave rise to certain potential causes of action (the "LBO Causes of Action").[19] On September 1, 2010, the court appointed Bankruptcy Judge Kevin Gross to mediate negotiations among various parties with respect to a plan of reorganization and a resolution of the LBO Causes of Action.[20] After the mediation, four competing plans were filed, including one proposed by certain noteholders (the "Noteholders" or "Noteholder Plan Proponents") and one proposed by the Debtors, the Official Committee of Unsecured Creditors (the "Committee") and certain lenders (the "Lenders", collectively with the Debtors and the Committee, the "Debtor/Committee/Lender Plan Proponents" or "DCL Plan Proponents").[21]

The Noteholders filed a motion to compel documents from the Debtor/Committee/Lender Plan Proponents regarding their plan's proposed settlement of the LBO Causes of Action to "test the arms-length nature and good faith of the settlement negotiations."[22] The dispute focused on objections to producing documents (1) protected by the common interest privilege, (2) protected by a mediation order (the "Mediation Order", which directed that all mediation discussions, documents and communications were confidential, inadmissible, and could not be disclosed to any non-party[23]), Local Bankruptcy Rule 9019-5(d) and Federal Rule of Evidence 408, and (3) for the time period from the petition date to December 15, 2009, when the court entered an order authorizing the Debtors to create a centralized document depository program in connection with the Committee's investigation of the LBO Causes of Action (the "Document Depository Order").[24] With respect to the common interest privilege, the parties disputed whether the privilege applied and, if so, when the privilege arose and the scope of its protection.

The Noteholders argued that the common interest privilege did not apply because the Debtors, the Committee, and the Lenders shared no common interest; the former two wanted to maximize the estate, while the latter wanted to resolve the LBO Causes of Action by paying the least amount possible.[25] The DCL Plan Proponents asserted that they shared a common legal interest to gain court approval of their proposed plan and settlement.[26]

The *Tribune* Court adopted the reasoning of *Leslie* as to the elements and applicability of the common interest privilege and its recognition that the existence of a common interest "must be determined on a case by case basis."[27] Although their interests were not completely in accord, the court concluded that the DCL Plan Proponents shared a community of

10 Id.
11 Id. at 498
12 Id. at 500.
13 Id.
14 Id.
15 Id. at 501-02.
16 Id. at 502.
17 Id. at 503.
18 Tribune, 2011 Bankr. LEXIS 299, *3-4.
19 Id. at *4 n.6.
20 Id. at *7-8.
21 Id. at *2-3, 9.
22 Id. at *11.
23 Id. at *26-27 n.18.
24 Id.
25 Id. at *12-13.
26 Id. at *13.
27 Id. at *13-16.

interests based on their common legal interest to resolve the legal dispute among them by obtaining court approval of their proposed settlement and plan.[28]

As to when the common interest privilege arose, the DCL Plan Proponents asserted they had a common interest when the mediator filed the parties' term sheet on October 12, 2010.[29] The Debtors and two lenders claimed they shared an interest as of September 27, 2010, when they agreed to become plan proponents and resolve the LBO Causes of Action.[30] The Noteholders argued no privilege existed until the DCL Plan Proponents filed their plan on November 23, 2010, and the term sheets were not a sufficient trigger because the parties had continued to negotiate the plan terms.[31] The court agreed with the DCL Plan Proponents that their common interest arose on October 12 (and on September 27 for the Debtors and two lenders) because they had agreed upon the material terms of their settlement and "it is reasonable to conclude that the parties might share privileged information in furtherance of their common interest of obtaining approval of the settlement through confirmation of the plan."[32] Whether particular communications were protected based upon that common interest depended on the DCL Plan Proponents' ability to demonstrate that the communications were privileged and met the three-part test of *Leslie*.[33]

With respect to the scope of the privilege, the Noteholders argued the common interest covered only communications written or made by lawyers because the privilege only applied to communications protected by the attorney-client privilege or work product doctrine.[34] The DCL Plan Proponents objected that the Noteholders' attempt to limit the "common interest communications" to those prepared by lawyers would artificially limit the privilege and needlessly require the funneling of communications through attorneys.[35] The court concluded that the Noteholders' proposal was too restrictive, noting that the DCL Plan Proponents would have the opportunity to show that the discovery sought was covered by the privilege.[36]

The Noteholders argued that the mediation information sought was not protected by the Mediation Order, Local Rule 9019-5(d) or Fed. R. Evid. 408 because the DCL Plan Proponents put the requested discovery at issue by claiming their settlement was fair as a result of mediation with a judge and that it was unfair for the DCL Plan Proponents to use the Mediation Order as both a sword and a shield.[37] In response, the DCL Plan Proponents offered to disclose information regarding the mediation process, but not its substance, by producing communications (1) about the negotiation and abandonment of an earlier proposed plan, (2) prior to mediation, and (3) that occurred outside the mediator's presence or on a non-mediation day.[38]

The court noted that courts within the Third Circuit require a party seeking discovery about a settlement to make a particularized showing of relevance and that precedent and Delaware Bankruptcy Rule 9019-5(d) reflect a strong policy that confidentiality is "essential" to "promoting full and frank discussions during a mediation."[39] In light of the facts that the case was complex and involved a large media company, challenges to an $8 billion leveraged buyout, and mediation between twelve parties collectively owed billions of dollars, the court determined that the DCL Plan Proponents' proposal was reasonable and "an appropriate balance between allowing discovery of potentially relevant information and protecting the confidentiality of the mediation."[40] The court adjusted the proposal, however, to protect communications between or among mediation parties concerning the mediation to the extent the communications were exchanged on a mediation day only if the communications were between mediation parties who were present at the mediation or participated remotely.[41]

Finally, the court concluded that the appropriate start date for the discovery was the date of the Document Depository Order and not the earlier petition date.[42] That time frame allowed discovery as to the LBO-related settlements, while limiting the burden and expense of timely completing discovery.[43] The court rejected the Noteholders' contention that they should have full discovery of all settlement discussions that occurred during the Debtors' chapter 11 case because the LBO settlement was a part of plan confirmation.[44]

Accordingly, the court granted in part and denied in part the motion to compel. The court concluded that the common interest privilege applied to communications the DCL Plan Proponents shared in furtherance of their common interest after October 12, 2010 (or September 27, 2010 for the Debtors and two lenders). The Noteholders could not discover, *inter alia*, communications between a mediation party and the mediator, communications between or among mediation parties who were present or participating off-site in mediation with the mediator, and communications showing the substance of the mediation discussion. The Noteholders could, however, seek discovery of information since December 15, 2009.

Echoing the *Leslie* Court's refusal to issue a black-line rule, the *Tribune* Court cautioned against a broad reading of its decision and advocated a fact-specific inquiry with respect to the common interest privilege:

> A determination involving whether a community of interest privilege applies is an intensely fact-and-circumstance-driven exercise. The balancing of tensions which arise during the search for truth may, depending upon the particular circumstances involved, fall either way. Guided by Circuit precedent, other persuasive decisional law, applicable local rule, and orders governing mediation, I have decided that the matter before me involves circumstances warranting a determination that a community of interest privilege may be invoked by co-proponents of a plan. This is not to say that parties who are co-proponents of a plan or parties who reach settlements arising from mediation are always entitled to assert this privilege. Neither should it be said

28 Id. at *15-16.
29 Id. at *16-17.
30 Id. at *17.
31 Id.
32 Id. at *17-18.
33 Id. at *18 n.13.
34 Id. at *19.
35 Id. at *23.
36 Id. at *23-24.
37 Id. at *25.
38 Id. at *28.
39 Id. at *28-30.
40 Id. at *31-32.
41 Id. at *32.
42 Id. at *35.
43 Id.
44 Id. at *33.

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> that the privilege can never be invoked unless the circumstances involve the proposal of a joint plan or a settlement resulting from mediation.[45]

Thus, pursuant to the *Tribune* opinion, parties who engage in mediation that leads to a bankruptcy plan, the terms of which include settlement of litigation among them, may share a common legal interest in obtaining court approval of that plan and the settlement embodied in it. As a result, the common interest privilege will apply to protect the communications the parties exchanged in furtherance of their common legal interest from discovery of proponents of a competing plan.

Conclusion

Leslie and *Tribune* clarify that a complete alignment of interests among the parties exchanging documents or communications is not necessary to satisfy the common interest privilege. A shared interest in maximizing the debtor's asset pie, despite competing interests in how that pie is distributed, merited protection under the privilege in *Leslie*, while a shared interest in obtaining court approval of a proposed litigation settlement and plan of reorganization following mediation

45 Id. at *35-36.

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