



INVESTIGATIONS QUARTERLY



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How Privilege Fits into the Compliance Puzzle

The DC Circuit's KBR Decision



to bring this matter to the U.S. Supreme Court. The following article explores the potential impacts that the Barko case may have on corporate compliance and internal investigations in the future.

Almost every major regulatory regime relies on a basic principle of law enforcement policy, that by creating incentives for self-policing, companies are more likely to adopt effective compliance. This notion inexorably depends upon the certainty that the protections afforded by the attorney-client privilege and related privileges are available. In *Barko*, United States District Court Judge Gwin issued an alarming order granting a motion to compel that threatened to destabilize the bedrock principles of privilege.¹ Although the D.C. Circuit has now vacated Judge Gwin's opinion, counsel for the relator in *Barko* has petitioned the D.C. Circuit for a rehearing en banc.²

There is no question that the attorney-client privilege is the oldest and most sacrosanct of the privileges for confidential communications.

In a society as complicated in structure as ours and governed by laws as complex and detailed as those imposed upon us, expert legal advice is essential. To the furnishing of such advice the fullest freedom and honesty of communication of pertinent facts is a prerequisite. To induce clients to make such communications, the privilege to prevent their later disclosure is said by courts and commentators to be a necessity. The social good derived from the proper performance of the functions of lawyers acting for their clients is believed to outweigh the harm that may come from the suppression of the evidence in specific cases.

Comment to Rule 210 of the A.L.I. Model Code of Evidence.³

The attorney-client privilege has been one of the oldest cornerstones of our adversarial system of justice. Periodic debates over whether the privilege helps or hinders the search for truth have proven inevitable. That is precisely what happened in March of this year, after a federal District Court in DC

issued an opinion (U.S. ex rel. Barko v. Halliburton Company) that some feared would have undermined the attorney-client privilege. A three-judge panel of the U.S. Court of Appeals for the DC Circuit overturned the District Court's decision, and a rehearing en banc was denied. The relator, however, has pledged

1. United States ex rel. *Barko v. Halliburton Co.*, No. 1:05-CV-1276, 2014 WL 1016784 (D.D.C. Mar. 6, 2014) ("*Barko*").

2. Petition of Harry Barko for Rehearing En Banc, In Re Kellogg Brown & Root, Inc., No. 14-5055 (D.C. Cir. July 28, 2014).

3. See also *Upjohn Co. v. United States*, 449 U.S. 383, 389 (1981) (noting that the attorney-client privilege is the "oldest of the privileges for confidential communications known to the common law").

The tenet that protecting privilege encourages corporate compliance has been widely recognized, from the U.S. Department of Justice to the U.S. Supreme Court. The U.S. Attorney's Manual acknowledges that "[s]uch communications can naturally have a salutary effect on corporate behavior – facilitating, for example, a corporation's effort to comply with complex and evolving legal and regulatory regimes."⁴ The U.S. Supreme Court recognized the importance of protecting privilege in *Upjohn Co. v. United States*, 449 U.S. 383 (1981). It was the principles underlying the Court's decision in *Upjohn* that were threatened by the D.C. District Court's recent decision in *Barko*. Although the D.C. Circuit has now vacated Judge Gwin's opinion, counsel for the relator in *Barko* has made it clear that he will appeal the Circuit Court's decision. This article will touch on the reasons why we believe the lower court's decision was wrongly decided and will address the unintended consequences that will likely result if the D.C. Circuit's decision in *Barko* is reversed by the Circuit en banc.

The Barko Holdings

Barko is a False Claims Act (FCA) case alleging, among other things, that the Kellogg Brown and Root Inc. defendants ("KBR") overcharged the U.S. Army for services performed in Iraq under

the Logistics Civil Augmentation Program ("LOGCAP III") contract. Specifically, Barko, the relator, alleged that KBR incurred excessive and fraudulent costs on work performed by its subcontractor, Dauod and Partners ("D&P"), which it then passed on to the Army. The government declined to intervene in the case, and the relator proceeded to pursue the case under the FCA's qui tam provisions.

During the course of discovery, the relator sought internal "audits, inspections, studies, or self-evaluations" undertaken by KBR concerning its compliance with government contracting regulations. In response, KBR produced "tips" that KBR employees made to KBR's ethics and compliance hotline, including complaints about D&P and possible wrongdoing. In response to the tips, KBR conducted Code of Business Conduct ("COBC") investigations. Notwithstanding that it turned over the tips to the relator, KBR withheld as privileged the COBC investigative reports on the grounds that they were protected from disclosure by both the attorney-client privilege and the work product doctrine.

Applying a "but for" test, the court held that they were not protected by the attorney-client privilege or the work product doctrine because the COBC investigation was a "compliance investigation" undertaken pursuant to "regulatory law" and "corporate policy." As such, the investigation and reports were done to serve KBR's business needs, not to provide legal advice. Judge Gwin held:

The COBC investigation was a routine corporate, and apparently ongoing, compliance investigation required by regulatory law and

corporate policy. . . . As such, the COBC investigative materials do not meet the "but for" test because the investigations would have been conducted regardless of whether legal advice were sought. The COBC investigations resulted from the Defendants need to comply with government regulations.⁵

In concluding that the investigation was "required," Judge Gwin relied principally on Department of Defense Federal Acquisition Regulation Supplement provisions 48 C.F.R. §§ 203.7000 - 7001 (2001), which provided that government contractors "should have standards of conduct and internal control systems" and that such "system of management controls should provide for . . . [t]imely reporting to appropriate Government officials of any suspected or possible violation of law in connection with Government contracts or any other irregularities in connection with such contracts." (Emphasis added).

After Judge Gwin refused to certify the privilege question to the Court of Appeals, KBR immediately filed a petition for writ of mandamus in the D.C. Circuit Court of Appeals. Less than two months after hearing oral argument on the petition, the D.C. Circuit issued its opinion vacating Judge Gwin's order directing KBR to turn over the investigation materials in question. Judge Kavanaugh, writing for the Court of Appeals, began by noting that the Supreme Court in *Upjohn* "explained that the attorney-client privilege for business organizations was essential in light of 'the vast and complicated array of regulatory legislation confronting the modern corporation,' which required corporations to 'constantly go to lawyers to find out

4. U.S. Attorney's Manual § 9-28.720(b). This section explains more fully:

Separate from (and usually preceding) the fact-gathering process in an internal investigation, a corporation, through its officers, employees, directors, or others, may have consulted with corporate counsel regarding or in a manner that concerns the legal implications of the putative misconduct at issue. Communications of this sort, which are both independent of the fact-gathering component of an internal investigation and made for the purpose of seeking or dispensing legal advice, lie at the core of the attorney-client privilege. Such communications can naturally have a salutary effect on corporate behavior—facilitating, for example, a corporation's effort to comply with complex and evolving legal and regulatory regimes.

5. *Barko*, 2014 WL 1016784, at *3.

how to obey the law, . . . particularly since compliance with the law in this area is hardly an instinctive matter’.”⁶

The D.C. Circuit then held that “KBR’s assertion of the privilege in [Barko] is materially indistinguishable from Upjohn’s assertion of the privilege in [Upjohn].”⁷ In reaching this conclusion, the D.C. Circuit made clear that, for the privilege to apply, use of “outside counsel is not a necessary predicate,” that witness interviews can be conducted by non-attorneys as long as they are conducted at the direction of counsel, and that “no magic words” must be used to convey to interviewees that the purpose of the interview is to assist the company in obtaining legal advice.⁸

More importantly, the D.C. Circuit found that Judge Gwin’s use of a but-for test was improper and “would eliminate the attorney-client privilege for numerous communications that are made for both legal and business purposes and that heretofore have been covered by the attorney-client privilege” and “would eradicate the attorney-client privilege for internal investigations conducted by businesses that are required by law to maintain compliance programs, which is now the case in a significant swath of American industry.”⁹ In rejecting the but-for test, the D.C. Circuit further held that the proper test is the following question: “Was obtaining or providing legal advice a primary purpose of the communication, meaning one of the significant purposes of the communication?”¹⁰

Regulatory Compliance and Legal Advice Are Not Mutually Exclusive

Though couched in terms of a “but for” analysis, the underlying premise in Judge Gwin’s decision is that the investigation has to be undertaken either for purposes of seeking and providing legal advice or for purposes of complying with a regulatory requirement or corporate policy. We do not always operate in an either/or world, however, and, as the D.C. Circuit recognized, obtaining or providing legal advice is one of the significant purposes of a compliance investigation regardless of whether the investigation is conducted pursuant to a corporate compliance program required by statute, regulation or company policy.¹¹ In fact, regulatory compliance is often itself a determination for which legal advice should be and is sought.

Let’s take, for example, compliance with the federal contractor mandatory disclosure rule (“MDR”) in the Federal Acquisition Regulation (FAR) 48 C.F.R. § 52.203-13, which superseded the regulation upon which Judge Gwin relied in Barko. The MDR requires contractors to timely disclose when the contractor has “credible evidence” of “[a] violation of federal criminal law involving fraud, conflict of interest, bribery or gratuity violations . . . or [a] violation of the civil False Claims Act . . .” 48 CFR § 52.203-13(b)(3)(i). Whether the “credible evidence” standard is met, whether conduct rises to the level of a violation of criminal law or the

FCA, and whether a particular law involves fraud, conflict of interest, bribery or a gratuity are all legal conclusions that lie at the very heart of attorney client/work product privilege. An investigation to determine whether there is “credible evidence” of such violations is almost, per se, for the purpose of seeking legal advice on these subjects. As the U.S. Chamber of Commerce and other associates put it:

*This approach makes little sense where the aim of the corporate policy (here, as in many cases) is to provide in-house attorneys with facts relevant to the corporation’s compliance with the law. “The first step in the resolution of any legal problem is,” of course, “ascertaining the factual background and sifting through the facts with an eye to the legally relevant.” Upjohn, 449 U.S. at 390-391. Communications made pursuant to a corporate policy and protected by privilege enable the corporation to seek candid legal advice from in-house lawyers.*¹²

Given the legal nature of the regulatory requirement, it makes little sense to say that “the purpose of the investigation was for business rather than legal advice.”¹³ To classify this kind of highly legal regulatory compliance into a non-legal category (and therefore non-privileged) seems to engage in semantic acrobatics.¹⁴ The very purpose of the investigation is to gather and analyze the facts to determine what further actions, if any, should be taken including a legal determination of whether disclosure is required by law or regulation.

As Judge Kavanaugh urged in oral argument before the DC Circuit, it is better

6. In re Kellogg Brown & Root, Inc., Opinion at 4-5 (quoting Upjohn, 449 U.S. at 392).

7. Id. at 5.

8. Id. at 6-7. To be sure, there is no requirement that outside counsel be used for the privilege to apply. However, because in-house counsel often wear multiple “hats,” in-house counsel directing the investigation must act clearly in their capacity as legal counsel (and not, for example, business advisor) to protect the privilege. See, e.g., Andy Liu et al., FEATURE COMMENT: How to Protect Internal Investigation Materials From Disclosure, The Government Contractor, Vol. 56, No. 14 (Apr. 9, 2014).

9. In re Kellogg Brown & Root, Inc., Opinion at 9.

10. Id. at 10 (emphasis in original). Judge Kavanaugh quoted one of the authors: “Helping a corporation comply with a statute or regulation – although required by law – does not transform quintessentially legal advice into business advice.” Opinion at 10.

11. Id. (citing Andy Liu et al., FEATURE COMMENT: How to Protect Internal Investigation Materials From Disclosure, The Government Contractor, Vol. 56, No. 14 (Apr. 9, 2014)).

12. U.S. Chamber of Commerce, et al., Brief of Amici Curiae, at 6-7, In re Kellogg Brown & Root, Inc., No. 14-5055 (D.C. Cir. Mar. 19, 2014).

13. Barko, 2014 WL 1016784, at *3.

“to get the semantics exactly right.” The District Court, however, got the semantics wrong when it implicitly held that a primary purpose of the investigation necessarily constitutes the sole purpose of the investigation. In the real world, there are multiple legitimate and important purposes served by investigations. One such purpose is “ascertaining the factual background and sifting through the facts with an eye to the legally relevant” (Upjohn, 449 U.S. at 390-91) in order to determine whether a disclosure must be made. In other words, the legal ramifications of the investigation must be determined by attorneys. That is, by definition, an investigation undertaken for the purpose of seeking legal advice and, as such, privilege attaches to documents created in the process of the investigation.

The District Court’s Decision in Barko Renders Privileges Uncertain and Therefore Worthless, and Would Lead to Absurd Results

As the Supreme Court noted in Upjohn, “If the purpose of the attorney-client privilege is to be served, the attorney and client must be able to predict with some degree of certainty whether particular discussions will be protected. An uncertain privilege, or one that purports to be certain but results in widely varying applications by the courts, is little better than no privilege at all.”¹⁴ But certainty is precisely what Judge Gwin’s but-for test in Barko would have eviscerated.

The lower court’s ruling in Barko would also lead to absurd outcomes. Take, for example, a government contractor that put into effect a compliance program prior to the MDR rule.¹⁶ Would the primary purpose of those investigations be to seek legal advice? More so than a government contractor that put its compliance program into effect after the MDR rule? Why would the purpose of the later one be “business rather than legal advice”? Yet, this is where Judge Gwin’s opinion leads.

This problem is not limited to government contractors. There are numerous regulated industries and a wide variety of laws and regulations that in-house and outside counsel must address daily, many of which either require internal compliance procedures like the MDR rule or, at a minimum, strongly encourage them such as the DFARS provision at issue in Barko. For example, Section 301 of the Sarbanes-Oxley Act, P.L. 107-204 (2002), as implemented, requires audit committees of public companies to establish procedures for the “receipt, retention, and treatment of complaints received by the listed issuer regarding accounting, internal accounting controls, or auditing matters.” The Department of Justice encourages compliance by considering factors such as “the existence and effectiveness of the corporation’s pre-existing compliance program,” and its “self-reporting,” in deciding whether to pursue charges against a company for violations of the Foreign Corrupt Practices Act. See Department of Justice, “A Resource Guide to the U.S. Foreign Corrupt Practices Act,” 52-54 (2012).¹⁷



The District Court’s Decision in Barko Would Also Have Led to Reduced Compliance

The importance of the attorney-client privilege is not limited to “clients,” in-house counsel or outside counsel. Privilege is, as some have noted, a compliance officer’s best friend because it leads to increased compliance and compliance reviews.¹⁸ As such, compliance officers had the most to lose from the recent Barko

14. The D.C. Circuit quoted one of the authors: “Helping a corporation comply with a statute or regulation – although required by law – does not transform quintessentially legal advice into business advice.” Opinion at 10. Andy Liu et al., FEATURE COMMENT: How to Protect Internal Investigation Materials From Disclosure, *The Government Contractor*, Vol. 56, No. 14 (Apr. 9, 2014).

15. Upjohn, 449 U.S. at 393.

16. The same illogical result would come from a company that is not subject to the MDR rule conducting a compliance investigation. Its investigation may be considered to have a legal purpose while the purpose of a government contractor’s investigation regarding compliance with the MDR rule is considered “business”, not legal.

17. See other incentives for compliance programs catalogued in Michael Goldsmith & Chad W. King, Policing Corporate Crime: The Dilemma of Internal Compliance Programs, 50 *Vand. L. Rev.* 1, at 1 n.2 (1997).



decision which, if it had not been overturned, would have vitiated the privilege. The positive effect that the certainty of privilege has on compliance is recognized by the federal government¹⁹, as well as by state governments, which have passed statutes extending privilege to cover audit documents in the medical and environmental contexts.²⁰ Rather than wringing their hands over how to protect privilege, companies should be conducting more compliance reviews and establishing more robust compliance programs.

Ironically, the lower court's Barko decision would have undercut the very goal – increased compliance – of the regulation upon which its holding relied. For example, one of the key ideas behind the MDR is that it would encourage contractors to increase efforts to comply with

federal laws, regulations, and contract terms. Additionally, the drafters thought that self-policing would be beneficial to the federal taxpayers in the long term, because contractors would repay improperly paid monies that might never have been identified and recovered without the contractor's compliance program and disclosure. Another key aspect of the MDR is that it would foster better relationships between Offices of Inspector General and corporate counsel. And, in many ways, it was working – at least, prior to the lower court's ruling in Barko, and as long as the D.C. Circuit's decision vacating that ruling is upheld.

The increased compliance sought by the MDR, however, is hindered if the investigations that would be prompted by the MDR are no longer privileged. By eliminating the protections of the attorney-client privilege in a corporation's internal investigations, Barko may perversely discourage companies from conducting internal investigations and making disclosures. That is precisely why the drafters of the FAR rule included explicit language making clear that the MDR did not vitiate the attorney-client privilege, and instead preserved it – the drafters recognized that the privilege was key to encouraging contractors to investigate alleged wrongdoing and to make disclosures when necessary.²¹ As the MDR specifically states:

*"It does not require — (i) A Contractor to waive its attorney-client privilege or the protections afforded by the attorney work product doctrine."*²²

Without the certainty of the privilege, a contractor may very well have concluded that

in light of Judge Gwin's decision in Barko it should not conduct as many internal investigations and should not make disclosures. The dilemma for the contractor would have been: Either you conduct a compliance investigation that may never be protected by attorney-client/work product privilege²³ or you do not conduct the investigation (or do not conduct it thoroughly) and risk facing other potential adverse consequences. In light of these two unfavorable choices, a contractor may simply choose not to conduct an internal investigation or not to create reports and other documents as part of an internal investigation. Such results were precisely what the clear language of the MDR protecting privilege sought to avoid and are contrary to the very purpose of the rule – increased and more effective compliance efforts.

In the face of an uncertain privilege, protecting privileges may be costly, time-consuming, and demanding for a contractor. These factors may all become impediments to ensuring compliance. The fewer impediments and the easier it is for contractors to run compliance programs, the more likely that they will do so and that their programs will achieve better compliance results. The simple common-sense idea is that the harder it is to comply, the less compliance will occur. This would have been the pernicious part of Judge Gwin's Barko ruling – however unintended. ■

The authors would like to thank Jamie Wohlert for her contribution to this article.

18. See Michael Volkov, "The Attorney-Client Privilege and Compliance," *Corruption, Crime & Compliance* (Jan. 14, 2013), <http://goo.gl/2WJSRm>, quoted in Reply of Petitioners to Relator's Response to the Brief of Amici Curiae, at 2.

19. See e.g., U.S. Attorney's Manual § 9-28.720(b). The United States Sentencing Guidelines provision of leniency for an effective compliance program reflects the underlying law enforcement policy that good corporate citizenship can be induced through incentives that promote self-policing. See other incentives for compliance programs catalogued in Michael Goldsmith & Chad W. King, *Policing Corporate Crime: The Dilemma of Internal Compliance Programs*, 50 Vand. L. Rev. 1, at 1 n.2 (1997).

20. Michael Goldsmith & Chad W. King, *Policing Corporate Crime: The Dilemma of Internal Compliance Programs*, 50 Vand. L. Rev. 1, at 8 & n. 25-27 (1997), cited in Reply of Petitioners to Relator's Response to the Brief of Amici Curiae, at 2, n. 3. Goldsmith and King argue for more certain and greater protection of documents produced as part of internal compliance programs, so that companies do not face a dilemma between effective compliance and disclosure of documents produced as part of that compliance.

21. The preamble to the rule states: "DoJ and an agency OIG indicated awareness of these concerns in their comments and recommended clarification in the final rule. DoJ proposed that the final rule state explicitly: 'Nothing in this rule is intended to require that a contractor waive its attorney-client privilege, or that any officer, director, owner, or employee of the contractor, including a sole proprietor, waive his or her attorney-client privilege or Fifth Amendment rights.' 73 Fed. Reg. 67064, 67077, FAR Case 2007-006, Contractor Business Ethics Compliance Program and Disclosure Requirements (Nov. 12, 2008).

22. 48 CFR § 52.203-13(a)(2)(i).

23. Under a strict interpretation of the lower court's decision in Barko, a compliance investigation will never be privileged because it is for a business purpose. Even if a strict interpretation of Barko does not obtain, it will be much more difficult, costly, and time-consuming to protect privilege. A contractor may have to do many things to make it more likely that a court will find that the purpose of the investigation was to seek legal advice or done in anticipation of litigation, rather than for a business purpose. Recent literature on the now vacated Barko decision abounds with checklists on how to do this.