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Commodity Futures Trading Commission v. Weintraub

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COMMODITY FUTURES TRADING COMMISSION V. WEINTRAUB

INTRODUCTION

The attorney-client privilege¹ is distinguished as the oldest of the privileges for confidential communications under the common law.² Although deeply rooted in American jurisprudence, the attorney-client privilege has come under recent criticism in the bankruptcy law domain. The dispute concerning the use of the privilege in that context concerns whether the trustee of a corporation in bankruptcy has the power to waive the debtor corporation's attorney-client privilege with respect to communications transpiring prior to the filing of a petition in bankruptcy. In *Commodity Futures Trading Commission v. Weintraub*,³ the Supreme Court has held recently that the trustee of a corporate debtor does have that authority.

The question of the trustee's authority over a corporate debtor's attorney-client privilege is one for which there are no explicit statutory guidelines.⁴ However, the issue can be discussed under a broad range of policy arguments. Prior to the Supreme Court's ruling in *Weintraub*, three United States circuit courts had considered that precise issue. Despite contrary rulings in the Second⁵ and Eighth⁶ Circuit Courts, the Seventh Circuit, in *Weintraub*,⁷ held that a trustee does not have authority to waive the privilege. The Solicitor General urged the Supreme Court to hear the case because of its potential impact on prosecutions of insider trading, commodities scams and other frauds.⁸ Although the Supreme Court reversed the Seventh Circuit's ruling in *Weintraub*, the rationale set forth by the Seventh Circuit should be carefully reviewed, along with other arguments tending to support the Seventh Circuit's holding. The strength of the Supreme Court's decision can be judged most effectively when considered against that background.

After presenting a general discussion of the attorney-client privilege, this casenote will discuss the facts underlying *Weintraub* and then review the ra-

"(1) Where legal advice of any kind is sought (2) from a professional legal adviser in his capacity as such, (3) the communications relating to that purpose, (4) made in confidence (5) by the client, (6) are at his instance permanently protected (7) from disclosure by himself or by the legal adviser, (8) except the protection be waived." 8 J. WIGMORE, EVIDENCE IN TRIALS AT COMMON LAW, §2292 (McNaughton Rev. 1961) (emphasis omitted).

²Upjohn Co. v. United States, 449 U.S. 383, 389 (1961).

³105 S. Ct. 1986 (1985), *rev'd*, 722 F.2d 338 (7th Cir. 1984).

⁴*Id.* at 1992.

⁵*In re O.P.M. Leasing Servs., Inc.*, 670 F.2d 383 (2d Cir. 1982).

⁶*Citibank N.A. v. Andros*, 666 F.2d 1192 (8th Cir. 1981).

⁷*Commodity Futures Trading Comm'n v. Weintraub*, 722 F.2d 338 (7th Cir. 1984), *rev'd*, 105 S. Ct. 1986 (1985).

⁸See 7 NAT'L L.J. Nov. 12, 1984, at 5, col. 1.

tionales of the Seventh Circuit and the Supreme Court in their respective holdings. This casenote will discuss other arguments which have been raised in support of the trustee's authority over the privilege. The casenote will conclude with a discussion of other policy and precedent arguments which urge that the trustee should not be given this authority.

THE ATTORNEY-CLIENT PRIVILEGE GENERALLY

The attorney-client privilege had its origin during the reign of Elizabeth I.⁹ Initially, the privilege was created to uphold the oath and honor of the attorney. Today, the privilege is understood to protect the client's right of privacy.¹⁰ The purpose of the privilege is to encourage clients to consult legal advisers by removing the fear of disclosure.¹¹ The availability of sound legal advice is an important societal interest, with maximum efficacy when the lawyer is fully informed of the totality of circumstances regarding his client's situation.¹² The privilege encourages such full disclosure and is "indispensable for the purposes of private justice."¹³

Initially, the privilege was held to apply only to natural persons, but was extended to corporations by the middle of the nineteenth century.¹⁴ Where the client is a corporation, the privilege may be asserted or waived by the board of directors.¹⁵

The attorney-client privilege has been recognized in bankruptcy litigation since 1872.¹⁶ The availability of the privilege to corporations entering bankruptcy has not been questioned.¹⁷ Rather, the issue raised is who may assert or waive the privilege. It is that precise issue which the Seventh Circuit and the Supreme Court addressed in *Weintraub*.

⁹See generally WIGMORE, *supra* note 1, §2290, at 542.

¹⁰See generally Klein & Lichtenstein, *Trustee or Debtor: Who May Assert the Attorney-Client Privilege in Bankruptcy Proceedings*, 57 N.Y. ST. B.J. 35 (1985) [hereinafter cited as Klein].

¹¹See Note, *Attorney-Client Privilege for Corporate Clients: The Control Group Test*, 84 HARV. L. REV. 424, 425 n.7 (1970). *But see* Note, *Functional Overlap Between the Lawyer and Other Professionals: Its Implications for the Privileged Communications Doctrine*, 71 YALE L.J. 1226, 1262 (1962). The Yale Law Journal surveyed 108 lay people on the subject of the attorney-client privilege. Fifty-five of those surveyed either thought attorneys could be compelled to disclose confidences of their client's or did not know those confidences were protected.

¹²See Klein, *supra* note 10, at 36.

¹³*Chirac v. Reinicker*, 24 U.S. (11 Wheat.) 280, 294 (1826).

¹⁴See *Radiant Burners, Inc. v. American Gas Ass'n*, 320 F.2d 314, 319 (7th Cir.), *cert. denied*, 375 U.S. 929 (1963). See also Note, *The Lawyer-Client Privilege: Its Application to Corporations, the Role of Ethics, and its Possible Curtailment*, 56 NW. U.L. REV. 235 (1961) (on the subject of the privilege as applied to corporations). The primary objection to extending the attorney-client privilege to cover corporations was that the privilege was regarded as fundamentally personal in nature and that it is often difficult to determine who may speak for a corporation.

¹⁵Director's powers are created by state law. See *Burks v. Lasker*, 441 U.S. 471, 478 (1979). See generally Note, *Bankruptcy/Waiver of Attorney-Client Privilege*, 73 ILL. B.J. 112 (1984).

¹⁶*In re Krueger*, 14 F. Cas. 870 (D. Mass. 1872) (No. 7942).

¹⁷*In re O.P.M.*, 670 F.2d at 386. *People's Bank v. Brown*, 112 F. 652, 654 (3d Cir. 1902).

THE FACTS

The Chicago Discount Commodity Brokers, Inc. (CDCB) was a futures broker with the Commodity Futures Trading Commission (Commission). On Oct. 27, 1980, the Commission brought a complaint against CDCB, alleging violations of the Commodity Exchange Act.¹⁸ The Commission and CDCB entered into a consent decree which provided *inter alia*, for the appointment of a receiver. On Nov. 4, 1980, the district court appointed John K. Notz Jr. as receiver.¹⁹ On Nov. 4, 1980, Notz filed a voluntary petition for bankruptcy on behalf of CDCB.²⁰ The petition was filed under Chapter Seven of the Bankruptcy Code²¹ which provides for liquidation. The bankruptcy court then appointed Notz as trustee of CDCB.²²

In its investigation of CDCB, the Commission deposed Gary Weintraub, former counsel to CDCB.²³ Weintraub answered approximately 800 of the Commission's questions but refused to answer twenty-three other questions on the basis of the attorney-client privilege.²⁴ Consequently, Notz, as trustee in bankruptcy, attempted to waive the privilege on behalf of CDCB as to any communications or information occurring before CDCB entered into receivership.²⁵

On Dec. 15, 1981, the Commission filed a motion to compel the answers to the remaining twenty-three questions.²⁶ In considering the motion, the United States magistrate hearing the case concluded that, although Weintraub had properly invoked the privilege, the trustee has the authority to waive that privilege.²⁷ On June 9, 1982, the district court upheld the magistrate's order granting the Commission's motion to compel discovery.²⁸

Frank McGhee, president and sole director of CDCB, and Andrew McGhee, an officer and former director of CDCB, sought leave to intervene in

¹⁸Commodity Exchange Act, 7 U.S.C. §§1-26 (1983). The allegations of the complaint concerned possible fraud on the part of CDCB and its president, Frank McGhee. See 7 NATL L.J., Nov. 12, 1984, at 5, col. 1.

¹⁹Weintraub, 722 F.2d at 339.

²⁰In re Chicago Discount Brokers, Inc., No. 80-B-14472 (Bankr. N.D. Ill. 1980).

²¹Bankruptcy Reform Act of 1978, 11 U.S.C. §§701-766 (1983).

²²Weintraub, 722 F.2d at 339. Under a Chapter Seven proceeding, the appointment or election of a trustee is automatic. Under a Chapter Eleven reorganization proceeding, a trustee may only be appointed upon a showing of "fraud, dishonesty, incompetence or gross mismanagement . . . by current management" or where necessary for the best interests of the estate and its beneficiaries. 11 U.S.C. §1104(a)(1) (1978).

²³Weintraub, 722 F.2d at 339.

²⁴Id. The questions to which Weintraub refused to reply concerned suspected misappropriations of customer funds by the brokerage's officers and employees. See 7 NATL L.J., Nov. 12, 1984, at 5, col. 3.

²⁵Weintraub, 722 F.2d at 339.

²⁶Id.

²⁷Id.

²⁸Id.

the Commission's action against Weintraub.²⁹ On June 30, 1982, the district court granted their motion to intervene.³⁰

On July 27, 1982, the district court ordered Weintraub to answer the questions at issue.³¹ The McGhees moved for a stay, pending appeal of that order.³² The district court denied their motion and the McGhees appealed.³³ The Seventh Circuit reversed the district court, concluding that a trustee in bankruptcy could not waive a debtor corporation's attorney-client privilege.³⁴

THE SEVENTH CIRCUIT'S RATIONALE

The Seventh Circuit gave four justifications for its holding that a trustee in bankruptcy has no authority to waive a corporate debtor's attorney-client privilege.

The first justification of the *Weintraub* court was that the trustee does not "succeed to the positions of the officers and directors of the corporation."³⁵ The court noted that the broad delegation of powers given to the trustee through the Bankruptcy Reform Act are not plenary.³⁶ The court observed that once a corporation files a petition in bankruptcy, it continues to serve as a legal entity and it retains many of its former powers.³⁷ Accordingly, the court asserted that the corporation should retain control over the attorney-client privilege,³⁸ since the trustee's power to manage the bankrupt corporation's property does not give rise to absolute control over the corporation's legal rights.³⁹

²⁹*Id.* Weintraub had declined to appeal the district court's rejection of the privilege claim and was prepared to supply the information, but the McGhees appealed to preserve the privilege. See 7 NAT'L L.J. Nov. 12, 1984 at 5, col. 4.

³⁰*Weintraub*, 722 F.2d at 339.

³¹*Id.*

³²*Id.*

³³*Id.* at 340.

³⁴*Id.* at 343.

³⁵*Id.* at 342.

³⁶*Id.* For a discussion of the powers and duties of a trustee in bankruptcy, see Note, *Waiver of the Attorney-Client Privilege by the Trustee in Bankruptcy*, 51 U. Chi. L. Rev. 1230 (1984). Generally, the code authorizes the trustee to oversee all the debtor's operations within the ordinary course of business.

³⁷*Weintraub*, 722 F.2d at 342. The powers retained by a corporation during bankruptcy proceedings include the power to borrow money, transact business and elect officers and directors. See generally 15 A.W. FLETCHER, PRIVATE CORPORATIONS, §7657 (rev. ed. 1981).

³⁸*Weintraub*, 722 F.2d at 342.

³⁹*Id.* One bankruptcy court refused to allow the trustee of a debtor corporation to waive the corporation's attorney-client privilege partly on the ground that, as the powers delegated to the trustee under the Bankruptcy Code are enumerated, the absence of an express grant of authority in the area of testimonial privilege indicates the intention of Congress that this power not be included. *In re Vantage Petroleum Corp.*, 40 Bankr. 34, 40 (Bankr. E.D.N.Y. 1984).

The legislative history of the code provides little guidance on the question of the trustee's authority in this area. In §542(e) of the code, which deals with the subject of the turnover of financial information to the trustee, the drafters wrote that this duty is "subject to any applicable claim of privilege, such as attorney-client privilege." H.R. REP. No. 989, 95th Cong., 1st Sess. 369 (1977). In other discussions of §542(e) of the code, Congress has plainly stated that the issue is unresolved, announcing "the extent to which the attorney-

The second justification offered by the *Weintraub* court was the apparent inequity of prohibiting the trustee of an individual in bankruptcy from waiving the attorney-client privilege,⁴⁰ while affording different treatment to the trustee of a corporation in bankruptcy.⁴¹ The court based its rationale on the fact that trustee waiver of the privilege, as to any information sought, creates an empty privilege.⁴² This result would be true regardless of whether the client were a private individual or a corporation.⁴³

The third justification, which the court offered for its holding, was that to allow the trustee of a corporate debtor to waive the attorney-client privilege would be to discriminate "against the corporate debtor solely on the basis of economic status."⁴⁴ The court noted that it would be discriminatory to allow solvent corporations to enjoy the power to assert or waive the attorney-client privilege, while denying that right to bankrupt corporations.⁴⁵ An economic classification did not impress the court as a valid criterion for selection as to proper privilege assertion or waiver.⁴⁶

The fourth justification concerned the potential chilling effect, on attorney-client communications, caused by a decision in favor of the corporate trustee.⁴⁷ The court reasoned that corporate clients may be reluctant to communicate freely with their legal counsel for fear that such communication would be subject to disclosure should the corporation enter bankruptcy.⁴⁸ The court noted that the "[f]ree interchange between attorney and client is the cornerstone of effective legal representation."⁴⁹

THE SUPREME COURT'S RATIONALE

The Supreme Court relied, principally, on two arguments in holding that the trustee of a debtor corporation has the authority to waive the corporation's attorney-client privilege.⁵⁰ The first argument presented by the Court focused

client privilege is valid against the trustee is unclear under current law and is left to be determined by the courts on a case by case basis." 124 CONG. REC. 32, 400 (1978). On the subject of legislative history of the code provisions relating to the attorney-client privilege, see Note, *supra* note 36, at 1240 n. 44.

⁴⁰*Cf. In re Smith*, 24 Bankr. 3 (Bankr. S.D. Fla. 1982) (holding that the trustee of an individual debtor could waive the debtor's attorney-client privilege based on the Eighth Circuit Court of Appeal's decision in *Citibank N.A. v. Andros*, 666 F.2d 1192 (8th Cir. 1981), which allowed the trustee of a debtor corporation to waive the corporation's privilege).

⁴¹*Weintraub*, 722 F.2d at 342.

⁴²*Id.* at 343. See also Note, *supra* note 15, at 116.

⁴³*Weintraub*, 722 F.2d at 343.

⁴⁴*Id.*

⁴⁵*Id.*

⁴⁶*Id.*

⁴⁷*Id.*

⁴⁸*Id.*

⁴⁹*Id.*

⁵⁰*Weintraub*, 105 S. Ct. at 1996. The opinion was written by Justice Marshall. It was joined by all of the Justices except for Justice Powell, who did not participate in the consideration or decision of the case.

on the position and powers of the trustee.⁵¹ The Court noted that when a solvent corporation undergoes a change in management through takeover, merger, loss of shareholder confidence or normal succession, the new management assumes control over the corporation's attorney-client privilege.⁵² The Court stated that where the Bankruptcy Code is silent on the powers of various actors in a corporate bankruptcy, the Court, in allocating those powers, must consider the relationship of those actors to the management of a solvent corporation.⁵³ The Court concluded that the powers of a solvent corporation's management are more analogous to the powers of a trustee than to those of the debtor corporation's directors.⁵⁴

As the Seventh Circuit noted, the trustee of a bankrupt corporation does not replace the corporation as an entity, nor succeed to the positions of the corporation's officers or directors.⁵⁵ Rather, the corporation continues to exist and retains a significant portion of its former functions after the filing of the petition in bankruptcy.⁵⁶ Since the bankrupt corporation's existence continues and the officers and directors retain their positions, the trustee's authority in managing the corporation's property should not be interpreted as a grant of absolute power over the corporation's legal rights.⁵⁷

In one significant respect, the directors of a bankrupt corporation more closely resemble the management of a solvent corporation than does the trustee. The fiduciary duties of a debtor corporation's directors are not divided between the shareholder and the corporation's creditors.⁵⁸ Conversely, the trustee's primary loyalty is to the corporation's creditors who elect him and who will often be the only beneficiaries of his efforts.⁵⁹ The Supreme Court noted that the trustee does owe a fiduciary duty to a corporation's creditors but dismissed this as "[o]ne of the painful facts of bankruptcy."⁶⁰

The Court stated that, where the corporation is a debtor in possession, its directors, like the trustee, also owe a fiduciary duty to corporate creditors.⁶¹ Further, the Court noted that it would be an anomaly to deny authority over

⁵¹*Id.* at 1993.

⁵²*Id.* at 1991.

⁵³*Id.* at 1992-93 (citing *Butner v. United States*, 440 U.S. 48, 55 (1979)).

⁵⁴*Weintraub*, 105 St. at 1993.

⁵⁵*Weintraub*, 722 F.2d at 342.

⁵⁶*Id.*

⁵⁷*Id.* The measure of authority which the trustee can exercise over a bankrupt corporation depends, to some degree, upon whether the bankruptcy proceeding is a liquidation or reorganization proceeding. Under a Chapter Seven liquidation proceeding, the trustee has extensive management authority, in contrast to the powers of a trustee in a Chapter Eleven reorganization case. See 2 COLLIER ON BANKRUPTCY §323.01, at 323-24 (15th ed. 1984).

⁵⁸See generally Note, *supra* note 15, at 116.

⁵⁹See 11 U.S.C. §§702, 726(a) (1983). See also *Weintraub*, 105 S. Ct. at 1994.

⁶⁰*Weintraub*, 105 S. Ct. at 1994.

the privilege to the trustee, while allowing the directors of a corporate debtor in possession to have this authority, when both share the same fiduciary duties.⁶² If the question of the actor's fiduciary duty is determinative of his authority over the privilege, it should be noted that, in this respect, the trustee does not resemble the management of a solvent corporation.⁶³ The directors of a corporation in bankruptcy, on the other hand, owe the same duty to the corporate shareholders as they did before the filing of the petition in bankruptcy.⁶⁴

The second principal argument on which the Supreme Court relied in deciding *Weintraub* focused on the federal interests at issue.⁶⁵ The Court stated that "no federal interests would be impaired by the trustee's control of the corporation's attorney-client privilege."⁶⁶ However, the central purpose of the privilege is to encourage full and frank disclosure between the attorney and his client.⁶⁷ The value of such communication is amplified in the corporate context where accurate legal advice is necessary for a corporation to conform its conduct to the law.⁶⁸ If allowing the trustee to exercise control over the privilege serves to discourage corporate clients from seeking legal advice, the likelihood of unlawful corporate activity increases.⁶⁹ Clearly then, the federal interest in ensuring that corporations do not stray into illegal activities would be impaired by allowing the trustee to exercise control over the privilege.

The Court noted that the trustee has a duty to "investigate the conduct of prior management to uncover and assert causes of action against the debtor's officers and directors."⁷⁰ The Court stated that the directors of a bankrupt corporation could impair the trustee's investigation by invoking the privilege.⁷¹ That criticism basically restates the classic conflict between a testimonial privilege and the public's right to every person's evidence.⁷² The traditional attorney-client privilege analysis provides a clear solution to that conflict.

The attorney-client privilege does not protect all forms of communication between the attorney and his client.⁷³ Where the communication concerns a

⁶²*Id.*

⁶³See generally Note, *supra* note 15, at 116 (discussing the contrasting duties of a debtor corporation's director and a trustee in bankruptcy).

⁶⁴*Id.*

⁶⁵*Weintraub*, 105 S. Ct. at 1993.

⁶⁶*Id.*

⁶⁷*Upjohn Co. v. United States*, 449 U.S. 383, 390 (1981).

⁶⁸*Id.* at 391.

⁶⁹See Note, *supra* note 15, at 116.

⁷⁰*Weintraub*, 105 S. Ct. at 1993.

⁷¹*Id.*

⁷²See Klein, *supra* note 10, at 40 (discussing the traditional limitations on the availability of the attorney-client privilege).

⁷³*Id.*

client's contemplated criminal act, the privilege does not apply.⁷⁴ Nor does the privilege apply where the purpose of the communication is to perpetrate a fraud.⁷⁵ The privilege does, however, protect communications relating to crimes already committed.⁷⁶ Additionally, communications made after the commission of a fraud or a tort are covered by the privilege in order to secure an attorney's adequate preparation of his client's defense.⁷⁷

By applying those principles to the question of the trustee's authority over the privilege, the resulting rule should require the trustee to make the necessary showing that the desired communications occurred prior to or during the commission of a crime, fraud or tort, for the purpose of assisting in its commission.⁷⁸

The Supreme Court noted that the "threshold showing of fraud necessary to defeat the privilege" can effectively bar a trustee's investigation.⁷⁹ While the necessity of such a showing may hinder the trustee's investigation, the social costs which attend the use of the privilege by directors of a corporate debtor do not differ from those arising when directors of a solvent corporation claim the privilege.⁸⁰ When board members of a solvent corporation engage in wrongful conduct, the shareholders may bring a derivative or class action against those directors on behalf of the corporation.⁸¹ That check on the corporate directors' activity continues to operate after a corporation enters bankruptcy.⁸² Additionally, the trustee can bring an action against the directors on behalf of the corporation.⁸³ Therefore, the use of the privilege by a debtor corporation's directors actually presents a reduced social cost when compared to the exercise

⁷⁴MODEL CODE OF PROFESSIONAL RESPONSIBILITY DR 4-101(c)(3) (1979) ("A lawyer may reveal the intention of his client to commit a crime and the information necessary to prevent the crime.")

⁷⁵Clark v. United States, 289 U.S. 1, 15 (1933) ("There is a privilege protecting communications between attorney and client. The privilege takes flight if the relation is abused. A client who consults an attorney for advice that will serve him in the commission of a fraud will have no help from the law. He must let the truth be told.")

There are two basic policy reasons for denying effect to the privilege regarding communications made prior to the commission of a crime, fraud or tort. The first is that to allow the privilege to attach under such conditions would permit an attorney to be a principal or an accessory to a crime, fraud or tort without fear of discovery. The second reason for disallowing the privilege under those conditions is that clients should not be permitted to commit crimes, frauds or torts with the benefit of prior legal advice. An attorney who offers such advice would be committing conspiracy. See *Duplan Corp. v. Deering Milliken, Inc.*, 397 F. Supp. 1146, 1172 (D.S.C. 1974). See generally, Klein *supra* note 10, at 40.

⁷⁶See *United States v. Valencia*, 541 F.2d 618, 621 (6th Cir. 1976).

⁷⁷*Duplan Corp.*, 397 F. Supp. at 1172.

⁷⁸The party seeking to compel such discovery must present a prima facie case of an intended crime or fraud before the privilege can be disallowed. *Clark*, 289 U.S. at 15.

⁷⁹*Weintraub*, 105 S. Ct. at 1994.

⁸⁰See generally Note, *supra* note 15, at 116 (discussing the comparative social costs of the attorney client privilege in the bankruptcy and non-bankruptcy contexts).

⁸¹*Id.*

⁸²*Id.* During a bankruptcy proceeding, contingent claims may be litigated and will be treated as general creditor's claims. *Northern Pipeline Constr. Co. v. Marathon Pipe Line Co.*, 458 U.S. 50 (1982).

⁸³See Note, *supra* note 15, at 116.

of the privilege by a solvent corporation. The argument that a special rule governing the privilege should apply in the bankruptcy context because of the social costs at issue is therefore unsound.

ARGUMENTS FOR ALLOWING THE PRIVILEGE TO PASS TO THE TRUSTEE

1. *The Property Theory*

Some courts, which have considered the issue, have allowed the trustee to waive the corporate debtor's attorney-client privilege on the ground that the privilege is property of the estate and, as such, it passes to the trustee along with the other assets of the debtor.⁸⁴

The Eighth Circuit Court, in *Citibank N.A. v. Andros*,⁸⁵ held that the trustee of a corporate debtor could waive the corporation's attorney-client privilege based upon the property theory. Citibank, the principal secured creditor of a bankrupt corporation,⁸⁶ sought to inspect documents of the bankrupt's legal counsel in a Rule 205 examination.⁸⁷ The corporation's legal counsel refused to allow the inspection on the ground of the attorney-client privilege.⁸⁸ The trustee in bankruptcy then waived the corporation's privilege.

Citibank's attempts to compel production of the documents in the bankruptcy and district courts⁸⁹ were unsuccessful. On appeal to the Eighth Circuit, the circuit court reversed the rulings of the lower courts on the ground that "the right to assert or waive the privilege passes with the property of the corporate debtors to the trustee."⁹⁰

The Seventh Circuit, in *Weintraub*, declined to follow the holding in *Citibank*, partly on the ground that *Citibank* failed to address the important policy considerations underlying the attorney-client privilege.⁹¹ In rejecting the rationale offered in *Citibank*, the Seventh Circuit might have addressed the property theory as inappropriate under the provisions of the Bankruptcy Code. Under §541 of the Code, the property of the estate is "all legal and equitable interests of the debtor in property as of the commencement of the case."⁹² Under §542, such property is to be transferred to the trustee.⁹³ However, the power to

⁸⁴See, e.g., *In re O.P.M. Leasing Servs., Inc.*, 13 Bankr. 54, 61 (Bankr. S.D.N.Y.), *aff'd*, 13 Bankr. 64 (S.D.N.Y. 1981), *aff'd sub nom.* Weissman v. Hassett (*In re O.P.M. Leasing Servs., Inc.*), 670 F.2d 383 (2d Cir. 1982); *Citibank N.A. v. Andros*, 666 F.2d 1192, 1195 (8th Cir. 1981).

⁸⁵666 F.2d 1192 (8th Cir. 1981).

⁸⁶The corporation was the Hy-Gain Electronics Systems Corporation.

⁸⁷*Citibank*, 666 F.2d at 1193.

⁸⁸*Id.*

⁸⁹*In re Hy-Gain Elecs., Inc.*, 11 Bankr. 119 (D. Neb. 1978).

⁹⁰*Citibank*, 666 F.2d at 1195.

⁹¹*Weintraub*, 722 F.2d at 342.

⁹²11 U.S.C. §541(a)(1) (1979).

⁹³11 U.S.C. §542 (1979).

assert or waive the attorney-client privilege is not a right that can be bought, sold or levied upon by creditors and is, therefore, not property within the meaning of §541. Since the attorney-client privilege is not property within the meaning of §541, it is not intended to be transferred to the trustee under §542.⁹⁴

2. *The Trustee As Representative Of The Estate*

Some courts, holding that the trustee of a corporate debtor should be allowed to waive the attorney-client privilege, have reasoned that the privilege was designed to "protect and foster the interests of actual litigants."⁹⁵ Therefore, as representatives of the property interests of the debtor, the trustee should be the party to exercise the privilege. That argument contains flaws, since under the Bankruptcy Code, the trustee does not acquire ownership of property which passes to him; rather, he becomes the representative of the estate.⁹⁶ The argument, therefore, fails to explain why the corporate debtor's directors, rather than the trustee, should not have authority over the privilege.⁹⁷

The arguments offered to support the trustee's power to waive the attorney-client privilege of a corporate debtor are thus open to serious question. To explore the issue more expansively, one must consider arguments, that were lacking in *Weintraub*, which urge that the trustee not be given authority over the corporate debtor's attorney-client privilege.

POLICY AND PRECEDENT ARGUMENTS

The modern corporation must operate within a complicated network of regulatory legislation.⁹⁸ Corporations frequently call upon their attorneys to ensure that their operations are in compliance with the law.⁹⁹ If the threat of compelled disclosure discourages communication between attorneys and their corporate clients, it is likely that corporations may needlessly forego legitimate business activities that might have been pursued under counsel's approval.¹⁰⁰ More disturbing is the prospect that a corporation might lose the attorney's warning when contemplating activities it thought lawful, which, in fact, were not.¹⁰¹

⁹⁴See Note, *supra* note 36, at 1238 (discussing the attorney-client privilege in relation to the property theory).

⁹⁵*In re Amjoe, Inc.*, 11 COLLIER BANKR. CAS. (MB) 45, 49 (Bankr. M.D. Fla. 1976).

⁹⁶11 U.S.C. §323(a) (1979).

⁹⁷See Note, *supra* note 36, at 1238 (discussing the theory of trustee as representative of the estate, relative to the exercise of the attorney-client privilege).

⁹⁸*Upjohn*, 449 U.S. at 392.

⁹⁹*Id.*

¹⁰⁰*Id.*

¹⁰¹*Id.* The Court noted the rebuttal argument that the risk of civil or criminal liability ought to override a cor-

When a corporation becomes financially insecure, the need for effective legal advice is particularly great.¹⁰² Corporations in desperate financial condition will call upon attorneys for advice in developing survival strategies.¹⁰³ On the eve of a corporate bankruptcy, the need for legal counsel would be at its strongest.¹⁰⁴ The corporation must be aware of the options and must accurately assess the advantages and consequences of each option in light of its own particular circumstances.¹⁰⁵ If the attorney-client privilege were allowed to pass to the trustee in bankruptcy upon the initiation of bankruptcy proceedings, the fear of compelled disclosure would be most acute precisely at the time when the need for legal advice is greatest.¹⁰⁶ The privilege should not be undercut at the point when its value is richest and its contemplated purpose most plainly served.

In *Butner v. United States*,¹⁰⁷ the Supreme Court considered the question of how rights should be distributed in bankruptcy proceedings when bankruptcy law is silent on the subject.¹⁰⁸ The issue in *Butner* concerned the manner of rent distribution in bankruptcy, when the rents accrued and were paid to the debtor's estate, while the bankruptcy proceeding was in progress.¹⁰⁹ Since the Bankruptcy Act was silent on this issue,¹¹⁰ the Court was asked to decide between applying the state law, which operated in non-bankruptcy cases, or a federal rule of equity, which would apply only in bankruptcy cases.

The Court announced, in a unanimous decision, that the non-bankruptcy law would always apply in such situations.¹¹¹ The reasoning of the Court stressed the need for uniformity as a means of reducing uncertainty, discouraging forum shopping and preventing one party from receiving "a windfall merely by reason of the happenstance of bankruptcy."¹¹² The Court's ruling in *Butner*, therefore, would suggest that a separate evidentiary rule should not apply in the context of bankruptcy proceedings, from the rule which operates in non-bankruptcy cases.

poration's fears of compelled discovery in considering whether or not to seek legal advice. This argument, the Court said, ignores the fact that even if the corporation chose to seek legal advice, an investigation undertaken to ensure compliance with the law would be less than thorough without the security of the attorney-client privilege.

¹⁰²See Note, *supra* note 15, at 116 (discussing the value of the privilege in the bankruptcy setting).

¹⁰³*Id.*

¹⁰⁴*Id.*

¹⁰⁵*Id.*

¹⁰⁶*Id.*

¹⁰⁷440 U.S. 48 (1979).

¹⁰⁸See Note, *supra* note 36, at 1241 (discussing *Butner* as a guideline in determining the issue of who may assert and waive the attorney-client privilege).

¹⁰⁹*Butner*, 440 U.S. at 49.

¹¹⁰*Id.* at 54.

¹¹¹*Id.* at 55.

¹¹²*Id.* (citing *Lewis v. Manufacturers Nat'l Bank*, 364 U.S. 603, 609 (1961)).

The manner in which the Supreme Court has treated the privilege against self incrimination in bankruptcy proceedings reveals considerable insight to the Court's assessment of the effect of those proceedings on testimonial privileges in general.¹¹³ In *McCarthy v. Arndstein*,¹¹⁴ the Court recognized the right of an individual to claim the privilege against self-incrimination in proceedings under the Bankruptcy Act. In *McCarthy*, the Court held that a party's right to assert the privilege was limited only by the "general rules governing the admissibility of evidence and competency of witnesses"¹¹⁵ and that the privilege was not affected by bankruptcy proceedings.

The privilege against self-incrimination holds a special position among testimonial privileges by virtue of its express recognition in the Bill of Rights and its highly personal nature.¹¹⁶ The Court did not base its decision, in *McCarthy*, on these unique features but, instead, addressed the distinction between adjective law¹¹⁷ and substantive law. The Court held that testimonial privileges are part of adjective law, distinct from the substantive law of bankruptcy.¹¹⁸ Essentially, the Court, in *McCarthy*, held that the Bankruptcy Act cannot directly affect testimonial privileges but can only apply them where appropriate.¹¹⁹

Although the attorney-client privilege can be distinguished from the privilege against self-incrimination,¹²⁰ the broad language used by the Court in *McCarthy* logically applies to all testimonial privileges. Under this reasoning, the trustee in bankruptcy cannot look to the Bankruptcy Code for authority over the debtor's attorney-client privilege since the substantive law of bankruptcy cannot alter the adjective law of testimonial privilege.

CONCLUSION

The question of the trustee's authority to waive a corporate debtor's attorney-client privilege is one which requires careful analysis and reasoned judgment. As in all matters of testimonial privilege, the costs which attend its

¹¹³See generally Hoffman, *The Attorney-Client Privilege in Proceedings Under the Bankruptcy Act of 1898 and The Bankruptcy Reform Act of 1978*, 53 AM. BANKR. L.J. 231, 240 (1979) (discussing the analogous relationship between the attorney-client privilege and the privilege against self-incrimination).

¹¹⁴266 U.S. 34 (1924).

¹¹⁵*Id.* at 39-40.

¹¹⁶See *Radiant Burners, Inc. v. American Gas Ass'n.*, 320 F.2d 314, 322 (7th Cir.), cert. denied, 375 U.S. 929 (1963) (recognizing the highly personal nature and constitutional grounding of the privilege against self-incrimination as distinguishing factors between that privilege and the attorney-client privilege).

¹¹⁷"The aggregate of rules of procedure or practice. As opposed to that body of law which the courts are established to administer (called "substantive law"), it means the rules according to which the substantive law is administered." BLACK'S LAW DICTIONARY 38 (5th ed. 1979).

¹¹⁸*McCarthy*, 266 U.S. at 39-42.

¹¹⁹*Id.*

¹²⁰Unlike the attorney-client privilege, the privilege against self-incrimination does not apply to corporations. See, e.g., *United States v. White*, 322 U.S. 694 (1944). Another distinction is that the privilege against self-incrimination can only be asserted by its holder. See *Fisher v. United States*, 425 U.S. 391 (1976).

use are clear in the form of hindered investigations and obstructions to discovery.¹²¹ Since the benefits of the privilege are less visible than its attendant costs, a decision on this issue should be particularly sensitive to those benefits. On the basis of the policy reasons underlying the attorney-client privilege, the Seventh Circuit held that bankruptcy proceedings should not affect the general rules governing the use of the privilege. In light of the relevant legal and policy considerations, the Seventh Circuit's decision, that authority over the privilege should remain with the debtor corporation's directors, was correct.

Permitting the directors of a debtor corporation to retain control over the attorney-client privilege would minimize the chilling effect on attorney-client communications caused by the fear of compelled disclosure. A consideration of the comparative fiduciary duties of the debtor corporation's directors and its trustee also urges that authority over the privilege properly lies with the directors. Finally, prior rulings of the Supreme Court recognizing testimonial privilege as an area of law distinct from the substantive law of bankruptcy urge that a separate rule regulating use of the privilege should not apply in bankruptcy proceedings. For each of these reasons, the Seventh Circuit's decision, in *Weintraub*, was correct in permitting authority over the attorney-client privilege to remain with the debtor corporation's directors.

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¹²¹In the case of *Weintraub*, the ruling of the court may actually have little impact on the Commission's investigation of CDCB. In 1983, Frank McGhee, president of CDCB, entered a guilty plea to the charge of embezzlement for which he was given a three year sentence. Subsequent to his conviction, McGhee has cooperated with the trustee and has supplied answers to most of the questions the Commission had asked of Weintraub. See 7 NAT'L L.J. Nov. 12, 1984, at 25, col. 1.

