

## 1st Circ. Crime-Fraud Ruling Challenges Atty-Client Privilege

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The First Circuit's recent decision in *United States v. Gorski*, applying the crime-fraud exception to advice sought in a highly regulated context, may prove to have some unintended and negative consequences for clients and legal practitioners alike.

The underlying criminal case involved alleged fraudulent representations by David Gorski, a founder of Legion Construction, related to the ownership and control of the company. Gorski, who was not a veteran, sought to bring veterans into his construction business in order to take advantage of government programs which gave preference to veterans, yet which also subjected such veteran-owned businesses to the programs' accompanying regulations. Gorski subsequently represented the company as a service-disabled veteran-owned small business entity when bidding on, and receiving, government contracts. Meanwhile, Gorski was alleged to have been effectively controlling the company, contrary to the percentage of his ownership interest would suggest. Such alleged methods of control included requiring owners with veteran status to sign employment agreements allowing Gorski to terminate them for cause. Gorski was also alleged to have added his wife to Legion's payroll, though she was employed full-time elsewhere, as a way to increase his own compensation above that of the owners with veteran status.

In 2010, a change to the regulations governing service-disabled veteran-owned small businesses resulted in updates to qualification criteria. In anticipation of the regulatory changes, Gorski retained counsel to represent Legion, to effectuate a corporate restructuring, aligning Legion's ownership interests to become consistent with the changes to the regulatory criteria. Gorski also hired a separate attorney to provide him with personal legal advice related to the restructuring.

Prosecutors alleged that Gorski fraudulently represented that the business was veteran-owned while he meanwhile maintained general control despite his nonveteran status and despite his minority ownership share. According to the prosecution, Gorski initiated the corporate restructuring in order to maintain outward compliance with the updated regulations. While the date of the share purchase required to complete the restructuring occurred on March 23, 2010, the documents themselves were dated "as of" Feb. 1, 2010. The new regulations went into effect Feb. 8, 2010, drawing suspicion from prosecutors that the documents were dated to give the appearance of compliance with the regulations. In response to a competitor's complaint filed with the United States Small Business Association, Legion submitted sworn affidavits containing falsities, drafted with the assistance of Legion's counsel based on information provided by Gorski.



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Gorski was indicted on one count of conspiracy to defraud the United States and four counts of wire fraud. The prosecution sought production of documents from Legion's counsel and Gorski's personal counsel related to the company's ownership and restructurings. Claiming attorney-client privilege, the parties withheld the documents.

### **Applying the Crime-Fraud Exception**

On the prosecution's motion, the district court received thousands of documents from Legion and Legion's counsel to determine if the crime-fraud exception applied, therefore negating the attorney-client privilege claim. The district court determined that the crime-fraud exception applied to communications between Legion's counsel and Gorski, but not to communications between Gorski's personal lawyer and Gorski, since Gorski's attorney had played no role in drafting the response to the Small Business Association complaint. The First Circuit affirmed in part, applying the crime-fraud exception to Legion's counsel's communications but also requiring production of the relevant communications between Gorski and his personal attorney.

Using a reasonable basis standard, the First Circuit applied the established two part crime-fraud exception test to determine: (1) if the defendant was engaged in, or was planning, criminal or fraudulent activity when the communications occurred; and (2) if the communications were intended by the client to facilitate or hide the criminal or fraudulent activity. The First Circuit concluded that the communications satisfied the first prong. For the second prong, the court reviewed the chronology of events and the nature of the communications between Gorski and his attorneys about the perceived necessity for the company restructure. The court concluded that there was a reasonable basis to believe that Gorski engaged his attorneys in order to perpetuate his ongoing scheme to demonstrate only outward compliance as a service-disabled veteran-owned small business entity.

Given the second prong's focus on client intent, the First Circuit, in a partial reversal, also applied the crime-fraud exception to communications with Gorski's personal attorney, concluding that Gorski's intent in engaging personal counsel was similarly to support his plan to conceal his true ownership and control of Legion. The court highlighted that its application of the crime-fraud exception did not reflect any view of the attorneys' conduct or intent since the crime-fraud exception is based on the client's intent. Further, the court noted that its decision on the crime-fraud exception did not represent an ultimate finding of wrongful conduct by Gorski.

### **A Troubling Precedent**

Although the Gorski decision may appear, at first blush, to be a run-of-the mill crime-fraud decision, the case may set an unclear and dangerous precedent for attorneys accustomed to relying on the privilege normally associated with their client communications in the context of highly regulated industries. Attorneys who advise clients on complex regulatory schemes may face uncertainty if their communications are subject to production. For example, should prosecutors allege False Claims Act violations where a defendant's consultation with counsel was relevant to structuring the activity under scrutiny, the crime-fraud exception may be raised as a pathway to access otherwise privileged documents. Unintended effects of the First Circuit's decision could be that clients may be reluctant to seek legal advice when encountering complex regulations and that outside counsel may feel obligated to warn their clients about the possibility of loss of privilege.

The First Circuit's ruling raises other questions as to the applicability of the crime-fraud exception. One

such potential scenario could be a company CEO who retains securities counsel to handle the company's securities filings. Should the CEO face allegations that he or she intended to defraud investors through the representations asserted in those filings, the Gorski decision may suggest that the communications regarding the securities filings could be ripe for production, regardless of the attorneys' knowledge of any such fraud.

### **Not So Fast**

Though the First Circuit ultimately applied the crime-fraud exception in Gorski, the decision resulted only after the court's inspection of the documents themselves during in camera review. The Ninth Circuit recently underscored the importance of the in camera review step by requiring court review of attorney-client communications before applying the crime-fraud exception in *In re Grand Jury Investigation*, No. 15-50450, 2016 U.S. App. LEXIS 580 (9th Cir. Jan. 14, 2016). The court's in camera review was required to determine if the communications in question were sufficiently related to, or in furtherance of, the alleged illegality before applying the crime-fraud exception. Taken together, the two circuit decisions demonstrate the importance of careful evaluation and consideration by the courts before destroying privilege. The crime-fraud exception is, as the name suggests, an exception to the privilege rule and to invoke the exception should not be taken lightly but should require careful assessment by courts.

### **Looking Ahead**

So where does that leave us? The Gorski decision may signal that neither counsel nor their clients may be able to rely on the sanctity of the attorney-client privilege. Attorneys should anticipate that the attorney-client privilege may not necessarily apply to communications with a client in the future. Since the privilege belongs to the client, not to the attorney, privilege can be challenged as the result of the client's activities. Privilege could be lost under a number of scenarios including: (1) prosecutors could raise the crime-fraud exception, even if the attorney was unaware of any crime; (2) a client could waive privilege with the intention of asserting advice of counsel as a defense; (3) privilege could be mistakenly waived by the client; or (4) an attorney could mistakenly send an email or other communication to the wrong incorrect party.

In light of Gorski, attorneys should follow the counsel so often advised with respect to their own clients: communications, particularly emails, should be composed with care and with the understanding that these communications may someday be disclosed and reviewed by individuals never contemplated or intended by the author.

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