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What The DC Circ.'s KBR Decision Means For Compliance

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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, U.S. District Court Judge James Gwin recently issued an alarming order granting a motion to compel that threatened to destabilize the bedrock principles of privilege.[1] Fortunately, however, the D.C. Circuit has now vacated Judge Gwin's opinion, restoring — at least temporarily — stability to corporate compliance programs.[2]

The tenet that protecting privilege encourages corporate compliance has been widely recognized, from the U.S. Department of Justice,[3] to the United States Supreme Court in Upjohn Co. v. United States, 449 U.S. 383 (1981). It was the principles underlying the Supreme 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 addresses the unintended consequences that will likely result if the relator is successful and the D.C. Circuit's decision in Barko is reversed by the circuit en banc.

The Barko Holdings

Barko is a False Claims Act case alleging, among other things, that the KBR Inc. defendants 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.[4]

In concluding that the investigation was "required," Judge Gwin relied principally on U.S. Department of Defense Federal Acquisition Regulation Supplement provisions, 48 C.F.R. §§ 203.7000 - 7001 (2001), that 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."

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 Brett Kavanaugh, writing for the court of appeals, began by noting that 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 how to obey the law, ... particularly since compliance with the law in this area is hardly an instinctive matter.'"[5]

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]."[6] 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 nonattorneys so long as they are conducted at the direction of counsel, and that "no magic words" have to be used to convey to interviewees that the purpose of the interview is to assist the company in obtaining legal advice.[7]

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."[8] In rejecting the but-for test, the D.C. Circuit further held that the proper test is: "Was obtaining or providing legal advice a primary purpose of the communication, meaning one of the significant purposes of the communication?".[9]

Saving 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.[10] As such, compliance officers had the most to lose from the recent Barko decision which, if it had not been overturned, would have vitiated the privilege.

Ironically, the lower court's Barko decision would have undercut the very goal — increased compliance — of the regulation upon which its holding relied. Indeed, Judge Gwin's rationale for holding that KBR's investigation was not privileged would have, if valid, been even stronger if the investigation occurred post-2009 when the federal contractor mandatory disclosure rule in the FAR, 48 C.F.R. § 52.203-13 ("MDR"), was in place.[11] The drafters of the MDR 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.

By eliminating the protections of the attorney-client privilege in a corporation's internal investigations, Judge Gwin's decision would have perversely discouraged companies from conducting internal investigations and making disclosures. That is precisely why the drafters of the MDR included explicit language making clear that the mandatory disclosures did not vitiate the attorney-client privilege, and instead preserved it.[12] As the MDR specifically states, contractors are not required to "to waive its attorney-client privilege or the protections afforded by the attorney work product doctrine."[13]

The False Dichotomy

As Judge Kavanaugh reminds us, "uncertainty matters in the privilege context."[14] Without the certainty of the privilege, a contractor may very well conclude that it should not conduct as many internal investigations and should not make disclosures. The dilemma for the contractor is: Either you conduct a compliance investigation that may never be protected by attorney-client/work product privilege 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. As the D.C. Circuit put it:

The District Court therefore concluded that the purpose of KBR's internal investigation was to comply with those regulatory requirements rather than to obtain or provide legal advice. In our view, the District Court's analysis rested on a false dichotomy.

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.

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

[2] In re Kellogg Brown & Root Inc., No. 1:05-cv-1276, (D.C. Circ. June 27, 2014).

[3] See U.S. Attorney's Manual § 9-28.720(b) (the privilege has a "salutary effect on corporate behavior—facilitating, for example, a corporation's effort to comply with complex and evolving legal and regulatory regimes").

[4] Barko, 2014 WL 1016784, at *3.

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

[6] Id. at 5.

[7] 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).

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

[9] Id. at 10. 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.

[10] 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.

[11] The MDR superseded the regulation that Judge Gwin relied upon 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).

[12] 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).
[13] 48 CFR § 52.203-13(a)(2)(i).

[14] See In re Kellogg Brown & Root, Inc., Opinion at 15-16; see also Upjohn, 449 U.S. at 393 ("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.").
