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THE SO-CALLED “FIDUCIARY EXCEPTION” TO THE ATTORNEY-CLIENT PRIVILEGE IN SECTION 36(B) CASES

A court recently held that the fiduciary exception to the attorney-client privilege applied to communications between independent trustees of a mutual fund and their independent counsel. The authors take issue with the decision. After discussing the background and case law involving the exception, they find that the rationale for applying it in common law trusts is inapplicable, and its effects may be harmful to shareholders, if applied against independent trustees in lawsuits under Section 36(b) of the ICA. They close with suggested steps independent trustees can take in light of uncertainties created by the decision.

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In *Kenny v. Pacific Investment Management Company*, for the first time in the nearly 50-year history of litigation under Section 36(b) of the Investment Company Act of 1940 (the “ICA”),¹ a federal district court ruled that the independent trustees of a mutual fund board must produce certain privileged communications with their independent legal counsel under the so-called “fiduciary exception” to the attorney-client privilege.² In those jurisdictions where it is recognized, the fiduciary exception precludes certain fiduciaries from asserting the attorney-client privilege

against beneficiaries who seek disclosure of fiduciary-attorney communications.

Kenny’s application of the fiduciary exception against the attorney-client privilege of mutual fund independent trustees is difficult to reconcile with the unambiguous, longstanding endorsement of independent trustees’ reliance on independent counsel by courts and the SEC, or with the nuances of independent trustees’ fiduciary relationship within the complex statutory framework of the ICA. But, irrespective of the merits of *Kenny*, the decision is important because of its practical consequences. Specifically, because *Kenny* makes it uncertain whether communications between independent trustees and their counsel are privileged, it discourages independent trustees from seeking and obtaining the best possible legal advice to the detriment of millions of

¹ Section 36(b) imposes upon investment advisers of mutual funds “a fiduciary duty with respect to the receipt of compensation” from the fund. 15 U.S.C. § 80a-35(b).

² *Kenny v. Pacific Inv. Mgmt. Co.*, No. 14-1987, 2016 WL 6836886 (W.D. Wash. Nov. 21, 2016).

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