

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

ADMINISTRATIVE PROCEEDINGS RULINGS
Release No. 4341/November 10, 2016

ADMINISTRATIVE PROCEEDING
File No. 3-17387

In the Matter of

DONALD F. (“JAY”) LATHEN, JR.,
EDEN ARC CAPITAL MANAGEMENT, LLC, and
EDEN ARC CAPITAL ADVISORS, LLC

ORDER ON PRIVILEGE WAIVER

The Division of Enforcement moves for an order declaring that Respondents have waived attorney-client privilege with respect to certain documents they produced to the Division during the investigation that led to this proceeding. Respondents oppose the Division’s motion. Except as described below, the Division’s motion is granted.

Background

According to the declaration filed by Respondents’ counsel, Harlan Protass, the Division issued Respondents investigative subpoenas in February 2015. Protass Decl. at 2. Among other things, the subpoenas required production of “all e-mails ‘concerning’ . . . Respondents.” *Id.* Respondents engaged counsel’s firm in March 2015, in connection with responding to the subpoenas. *Id.*

After identifying e-mail addresses from which responsive e-mails might have been sent or received, Respondents or their counsel—it is not clear which—determined the location of the e-mails. Protass Decl. at 3. Next, “pursuant to [Mr. Protass’s] instruction,” Michael Robinson, a former assistant to Respondent Donald F. Lathen, “searched for e-mails responsive to the Division’s subpoenas.” *Id.* at 3-4. After he found responsive e-mails, Robinson created files for various “classes” of senders and recipients. *Id.* at 5-6. Because none of these people had an attorney-client relationship with Respondents, Respondents or their counsel—again, it is not clear which—“believed” that the e-mails “could not, or, at least, should not, have included any privileged e-mails.” *Id.* at 6. After Robinson compiled the files, he electronically shared them with Mr. Protass who shared them in May 2015 with the Division via DropBox. *Id.* at 4-5. It was later discovered that this production included privileged material.

Respondents’ counsel does not claim that he or any other attorney reviewed the files compiled by Robinson before they were shared with the Division. Counsel does not claim that

Robinson is an attorney. Counsel does not assert that he provided Robinson with any guidance regarding privileged documents.

In August or September 2015, Respondents supplemented their response to the February subpoena. Protass Decl. at 7. “Pursuant to [Mr. Protass’s] instruction,” Robinson extracted non-responsive e-mails from those Respondents possessed and created files of all e-mails he and Lathen sent or received “concerning” Respondents. *Id.* Robinson electronically shared the files with Mr. Protass. *Id.* Each thought the other was responsible for extracting privileged documents. *Id.* Because he thought Robinson had reviewed the files for privileged material, Mr. Protass shared the files with the Division without reviewing them. *Id.* It was later discovered that this production also included privileged material.

In mid-December 2015, Respondents replaced Mr. Protass’s firm with Brune Law P.C. (Brune). Protass Decl. at 2. The Division issued Respondents a second subpoena in December 2015. *Id.* Brune compiled responsive e-mails into five different files. *Id.* at 8. Brune reviewed the e-mails and segregated privileged e-mails into separate files. *Id.* Brune then moved the privileged files to a “trash” file before producing all files to the Division. *Id.* at 8-9. Because no one at Brune emptied the trash file, in February 2016, it produced to the Division the privileged files in the trash file. *Id.* at 9.

The Division issued Respondents a third subpoena in late March 2016. Protass Decl. at 9. Respondents reengaged Mr. Protass’s firm in April 2016. *Id.* at 9-10. In late April, Lathen “advised [Mr. Protass] via e-mail that the documents responsive to the Division’s March 30, 2016 subpoena were ready for production to the Division.” *Id.* at 10. Lathen told Mr. Protass that Lathen had segregated privileged documents into a separate folder labeled “privileged” on a zip drive and that within each of the six e-mail folders on that zip drive were folders labeled “privileged.” *Id.* On reviewing the zip drive containing the responsive e-mails, Mr. Protass observed that there were, actually, eight folders, one of which was titled “privileged.” *Id.* Without reviewing the seven other folders “for purposes of privilege,” Mr. Protass produced the documents in them, together with a privilege log for the files in the privileged folder. *Id.* at 11. Respondents provide no evidence about how the documents in the seven folders were compiled, who compiled them, or whether anyone conducted any review of the documents.

According to Mr. Protass, he “assumed that all privileged documents on that zip drive were found in the folder entitled ‘Privileged.’” Protass Decl. at 11. Additionally, because Lathen created a privileged folder, “it did not occur to” Mr. Protass “that privileged documents could or would be found in any of the other folders on that zip drive.” *Id.* It was later discovered that there were privileged documents in the seven folders that were produced to the Division.

On September 13, 2016, Division counsel, Judith Weinstock, e-mailed Respondents’ counsel and informed them that the Division had located privileged material among the matters Respondents had previously disclosed. Div. Ex. D. Ms. Weinstock also stated that the Division would inform Respondents’ counsel if it located other privileged documents but that it had not searched for such documents. *Id.* There is no evidence Respondents’ counsel immediately responded to this e-mail. *See* Div. Ex. E; Protass Decl. at 12.

On September 18, 2016, Ms. Weinstock e-mailed again, forwarding three more privileged documents the Division had found among those produced by Respondents. Div. Ex. E. She added that because Respondents had not responded to the September 13, 2016 email, the Division would assume, unless Respondents said otherwise, that Respondents were waiving any claims of privilege. *Id.* Mr. Protass responded on September 18 that his firm was investigating the matter, he hoped to resolve it by the next day, and Respondents were not waiving claims of privilege. Div. Ex. F.

Mr. Protass e-mailed Ms. Weinstock on September 20. Div. Ex. G. He asserted that privileged documents had been inadvertently disclosed and requested the return of: (1) e-mails between Lathen and his attorney Kevin Galbraith; (2) e-mails between Lathen and Mr. Protass's firm, Clayman & Rosenberg LLP; and (3) e-mails between Lathen and attorneys at Brune. *Id.* at 1-2. He asked the Division to search the documents Respondents produced using terms he specified and asked the Division to refrain from reviewing the documents. *Id.* at 2. Mr. Protass also invited the Division to present any issue of waiver to me for adjudication. *Id.*

Ms. Weinstock responded on September 21 that the Division declined to search its files for allegedly privileged documents and instead asserted that Respondents should provide a list of privileged documents. Div. Ex. H. Mr. Protass responded the next day, disagreeing with several of Ms. Weinstock's points and stating that he would "shortly provide" a list of the documents in question. Div. Ex. I at 1-2.

There is no evidence that the parties corresponded further about the privilege issue between September 22, 2016, and October 25, 2016. On the latter date, the Division filed the motion at issue in this order.

Discussion

The Securities and Exchange Commission's Rules of Practice do not address the inadvertent disclosure of privileged documents. Rule of Evidence 502(b), however, does address the issue. Although the Rules of Evidence do not apply to this proceeding, Rule 502(b) provides a useful and helpful framework for evaluating the parties' claims.

Rule 502(b) provides that in cases of disclosure, a privilege is not waived if:

- (1) the disclosure is inadvertent;
- (2) the holder of the privilege or protection took reasonable steps to prevent disclosure; and
- (3) the holder promptly took reasonable steps to rectify the error, including (if applicable) following Federal Rule of Civil Procedure 26(b)(5)(B).

In addition to weighing the above factors, courts typically consider the number and extent of disclosures and whether the interests of justice support finding waiver. *See Smith v. Allstate Ins. Co.*, 912 F. Supp. 2d 242, 247 (W.D. Pa. 2012); *Peterson v. Bernardi*, 262 F.R.D. 424, 430-31 (D.N.J. 2009); *Victor Stanley, Inc. v. Creative Pipe, Inc.*, 250 F.R.D. 251, 258-59 (D. Md. 2008).

The party claiming the privilege's protection—the party that disclosed the documents in question—bears the burden to establish that the elements of Rule 502(b) have been met. *Gloucester Twp. Hous. Auth. v. Franklin Square Assocs.*, 38 F. Supp. 3d 492, 497 (D.N.J. 2014); *Williams v. District of Columbia*, 806 F. Supp. 2d 44, 48 (D.D.C. 2011).

Because the Division does not dispute that the documents in question are privileged, I proceed to the remaining factors, addressing each disclosure in turn. *See* Fed. R. Civ. P. 26 advisory committee's note ("Although the person from whom the discovery is sought decides whether to claim a privilege or protection, the court ultimately decides whether, *if this claim is challenged*, the privilege or protection applies.") (emphasis added).

1. *The May 2015 disclosures*

Robinson compiled the first set of disclosures. Although he did so "pursuant to" counsel's direction, no evidence has been presented about the actual guidance, if any, counsel gave Robinson. There is thus no evidence that Robinson was instructed about the concept of privilege or to look for privileged documents. And, in any event, no attorney reviewed the files Robinson compiled before they were disclosed. In other words, no privilege review took place. Absent proof that Respondents undertook a privilege review, Respondents have failed to show that their disclosures were inadvertent. *See Callan v. Christian Audigier, Inc.*, 263 F.R.D. 564, 566 (C.D. Cal. 2009).

Moreover, even assuming the documents were disclosed inadvertently, Respondents have not carried their burden. Because counsel took no steps to prevent the disclosure of privileged material, it is impossible to conclude that Respondents took reasonable steps to prevent disclosure. *Cf. Cudd Pressure Control, Inc. v. New Hampshire Ins. Co.*, 297 F.R.D. 495, 500 (W.D. Okla. 2014) (noting that absent evidence about the document review process, the court was left to speculate about what precautions were taken to prevent disclosure); *Williams*, 806 F. Supp. 2d at 49-50 (holding that a "conclusory statement is patently insufficient to establish that a party has discharged its duty of taking 'reasonable steps' to guard against the disclosure of privileged documents").

The evidence is neutral with respect to whether Respondents took reasonable steps after discovering the disclosure. Respondents' counsel asserted the privilege, but only after receiving two e-mails over five days. It then took another month before counsel produced a list of privileged documents. On the one hand, counsel did not immediately, on discovery of disclosure, specifically identify the privileged documents. *See Smith*, 912 F. Supp. 2d at 248. On the other hand, counsel did not wait months or years before asserting privilege or identifying privileged documents. *See Educ. Assistance Found. for the Descendants of Hungarian Immigrants in the Performing Arts, Inc. v. United States*, 32 F. Supp. 3d 35, 45 (D.D.C. 2014); *Williams*, 806 F. Supp. 2d at 52. This case falls somewhere between the two extremes. Counsel did not act with alacrity, but also did not wait an excessive amount of time to assert privilege, conduct an inquiry, and specifically identify the documents in question.

Finally, with respect to the interests of justice, the disclosure occurred because Respondents' counsel relied on an untrained, non-attorney to compile the documents at issue and

then failed to conduct any privilege review at all.¹ In this circumstance, it would not serve the interest of justice to absolve Respondents, whose inaction led to the disclosure, of the consequences of this failure. *See Peterson*, 262 F.R.D. at 431 (“It is rare that a Court will not find that a waiver occurred in an instance where a party presents only minimal evidence that it exercised reasonable precautions to prevent a waiver.”).

Except as is discussed below, the Division’s motion with respect to the May 2015 disclosures is GRANTED.

2. *August/September 2015 disclosures*

A similar result obtains for the August/September 2015 disclosures. Again, counsel relied on an untrained, non-attorney to compile the documents. This time he expected Robinson to conduct the privilege review. But counsel supplies no evidence that he gave Robinson any training regarding how to conduct a privilege review. Given Respondents’ burden and their failure to provide evidence on this point, I find that counsel gave Robinson no training. And, operating on the assumption that Robinson had done the review for which he received no training, counsel then disclosed the privileged documents. This is not a reasonable method designed to prevent the disclosure of privileged documents.

It is true that counsel and Robinson each thought the other was responsible for the privilege review. But that fact is of no consequence because it is unreasonable to solely rely on an untrained, non-attorney to conduct such a review.

The above analysis regarding the remaining factors also applies to this disclosure. The time taken after discovery of the disclosure weighs neither for nor against Respondents and the interests of justice weigh against them. Except as is discussed below, the Division’s motion with respect to the August/September 2015 disclosures is GRANTED.

3. *February 2016 disclosures*

The February 2016 disclosures are different. Counsel actually reviewed the documents to be produced, segregated the privileged documents, and produced a privilege log. That counsel accidentally disclosed documents she thought were deleted does not mean counsel failed to take reasonable steps to prevent disclosure.

¹ The overall number of privileged documents disclosed in the course of Respondents’ document production to the Division, 1,500 out of over 150,000, weighs in Respondents’ favor. *See Rhoads Indus., Inc. v. Bldg. Materials Corp. of Am.*, 254 F.R.D. 216, 224 (E.D. Pa. 2008) (finding the inadvertent disclosures equated to a marginal 1-2% of total documents produced), *clarified on other grounds by* 254 F.R.D. 238 (E.D. Pa. 2008). Respondents quantify the approximate percentage of privilege documents produced each time as follows: May 2015, 0.07%; August/September 2015, 0.09%; February 2016, 0.20%; and May 2016, 0.625%. Opp’n at 15. This positive factor is balanced, however, by the fact that Respondents disclosed privileged materials on four separate occasions.

As noted, counsel's actions after discovering the disclosures weigh neither for nor against Respondents. The interests of justice weigh in their favor, however. Unlike with the first two disclosures, this disclosure did not result from a failure to employ reasonable procedures. Forcing Respondents to forego the protection of the attorney-client privilege based on a simple mistake would be unjust and a heavy price for that simple mistake. *See Rhoads Indus.*, 254 F.R.D. at 227.

The Division's motion with respect to the February 2016 disclosures is DENIED.

4. The April 2016 disclosures

For the April 2016 disclosures, Respondents provide no evidence as to how or who compiled the folders counsel disclosed. All that is known is that Lathen provided the compilation of electronic folders to counsel, who disclosed the compilation to the Division without reviewing the documents at all. Who arranged the folders, how documents were chosen for placement in which folder, or what sort of review was performed is unknown. Respondents' failure to provide evidence means they have failed to show that their disclosures were inadvertent. *See Callan*, 263 F.R.D. at 566. This conclusion is bolstered by the fact that Lathen is the privilege holder and he is the person who provided the folders to counsel for production.

Assuming this disclosure was inadvertent, however, Respondents have presented no evidence that they acted reasonably to prevent disclosure. Indeed, they have provided no evidence at all concerning how the documents were compiled. Given the absence of evidence and Respondents' burden of proof, I am forced to conclude that they took no steps to avoid disclosure. As with the first two disclosures, Respondents did not act reasonably to prevent disclosure.

Like the 2015 disclosures, although counsel's actions after learning of the disclosure weigh neither for nor against Respondents, the interests of justice weigh against them. Except as is discussed below, the Division's motion with respect to the April 2016 disclosures is GRANTED.

Disclosure of Respondents' strategy

Respondents argue that finding they waived the attorney-client privilege

would . . . reveal [Lathen's] current and former attorneys' strategies in mounting a defense to the Division's allegations in this matter. These things are entirely irrelevant to the Division's allegations—yet, for obvious reasons, their revelation to the Division would be grossly unfair to Respondents and runs the risk of eviscerating the fundamental fairness of these proceedings.

Opp'n at 18. Respondents have a point. Lathen's discussions with his counsel about strategy are not relevant to the Division's case and revealing those discussions to the Division could seriously

prejudice Respondents' case. *See Rhoads Indus.*, 254 F.R.D. at 227. Given this fact and the fact the Division has no need to know Respondents' strategy, I order the following.

Within ten days, Respondents shall (1) specifically identify the documents, among those they have identified as privileged, that contain discussions between Lathen and his counsel regarding their strategy; and (2) produce these documents for *in camera* review. The Division shall continue to segregate the disclosed privileged documents until Respondents identify the documents containing discussions between Lathen and his counsel regarding their strategy. At that point, the Division will be free to consider the privileged documents that Respondents do not identify as containing discussions between Lathen and his counsel regarding their strategy.

James E. Grimes
Administrative Law Judge