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Federal Court Upholds Attorney-Client Privilege for Mutual Fund Independent Trustees

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In a decision affirming the importance of the attorney-client privilege in the mutual fund board setting, an Illinois federal court ruled on April 25, 2017 that fund shareholders were not entitled to access privileged communications between independent trustees and their counsel. The plaintiffs in *Chill v. Calamos Advisors LLC*, an "excessive fee" litigation under Section 36(b) of the Investment Company Act of 1940, moved for an order compelling the independent trustees of the Calamos family of funds to produce in discovery documents protected by the attorney-client privilege. The court rejected the plaintiffs' argument that the "fiduciary exception" applied to overcome the privilege, ruling that shareholders must establish they have "good cause" for piercing the privilege and had failed to do so. In upholding the privilege, the court declined to follow last year's decision of another federal court that had granted a plaintiff's similar request under the fiduciary exception.

In the *Chill* litigation, the plaintiffs allege that the adviser of the Calamos Growth Fund has received excessive investment management fees in breach of its "fiduciary duty with respect to the receipt of compensation" under Section 36(b). The case is pending in the United States District Court for the Southern District of New York. As is typical with Section 36(b) claims, the fund's independent trustees are not parties to the action – as they do not receive the fees being challenged – but they are subject to third-party discovery in the case. In the course of discovery, the plaintiffs – pursuing a new trend by 36(b) plaintiffs – sought all materials in connection with the independent trustees' annual review and approval of the investment advisory agreement at issue, *including* otherwise privileged communications between the trustees and their independent counsel. When the independent trustees refused to hand over their privileged communications, the plaintiffs filed a motion to compel production of those materials. Under the federal rules, this motion was required to be brought in the United States District Court for the Northern District of Illinois – where the fund is headquartered and a majority of the trustees reside – rather than in the New York court where the underlying litigation is pending.

The plaintiffs' motion largely relied on the so-called "fiduciary exception" – a principle that applies in some settings to preclude a fiduciary from withholding from a beneficiary any privileged legal advice related to the execution of the fiduciary's obligations on behalf of that beneficiary. The plaintiffs' motion pointed to a recent decision in another 36(b) litigation, *Kenny v. PIMCO*, pending in the Western District of Washington, that faced the issue of applying the fiduciary exception in the mutual fund context for the first time. There, the district court – in a thinly reasoned analysis – ruled that the fiduciary exception applied to the privileged communications between the independent trustees to the PIMCO funds and their independent counsel and granted the plaintiff's motion to compel production of those communications.

In last week's ruling in *Chill*, the court came out the other way, upholding the independent trustees' privilege and denying the plaintiffs' motion to compel. In a written opinion that can be found here, the court ruled that "[p]laintiffs have the burden to demonstrate good cause to overcome the attorney-client privilege based on the fiduciary exception." Given the importance of the privilege, courts being asked to pierce its protections "should not do so lightly without a compelling need." The plaintiffs were therefore required to make a "particularized showing of need for specifically identified documents" – namely, that they could "demonstrate the necessity of the information and its unavailability from other sources." The plaintiffs in *Chill* could not meet this high bar. As is typical in Section 36(b) cases, there had been extensive discovery regarding the board's review and approval of the challenged fees. The

plaintiffs could point to nothing from this record "to suggest that the privileged documents may contain information that is both necessary and unavailable elsewhere." The court specifically declined to follow the reasoning of the *Kenny* decision, as the court there did not apply a "good cause" requirement – instead only inquiring into whether a fiduciary duty existed.

Significantly, the *Chill* court concluded that, "[f]or the good-cause prong to have any meaning, the Court must require more than mere conjecture that otherwise privileged communications contain critical information. Under these circumstances, the Court is not willing to pierce the attorney-client privilege merely for Plaintiffs to go on a 'fishing expedition.'" This well-reasoned decision should stand as a model for courts facing this issue in future fund-related litigation. Given the comprehensive record typically available of how boards carry out their statutory duties in reviewing and approving fund fees, independent trustees will likely be well positioned to assert strong arguments in support of the privilege in the face of plaintiff challenges. Because, however, the facts and circumstances of a particular litigation can vary, independent trustees will be well advised to take care regarding the content of even their privileged communications as plaintiffs will undoubtedly continue to try to pierce this privilege.

Ropes & Gray's litigators represented the Calamos independent trustees in this matter and are actively involved in defending advisers in Section 36(b) litigation. For further information, please contact John Donovan, Robert Skinner, or Amy Roy, or your usual Ropes & Gray contact.