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Privilege in Federal Diversity Cases

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COMMENTS

PRIVILEGE IN FEDERAL DIVERSITY CASES

The Federal Rules of Civil Procedure having been enacted to simplify the litigation process, it is surprising to note that one area of the law—that of privilege for witnesses testifying in diversity cases—is more confused than it was prior to the passage of the Rules in 1938. This problem area will be examined through the use of two hypothetical situations. There are three possible solutions to the problem. A court may view the issue as procedural, as substantive leading to an automatic application of the privilege statute of the forum state, or as substantive looking to the conflicts rules of the forum state to determine whether to recognize the privilege.

Assume that a certified public accountant is testifying in a case brought in federal district court due to the diversity of citizenship of the parties. The trial is being held in a state which has a statute extending to the accountant a privilege not to disclose information given to him in confidence. Does the federal court recognize this privilege? To further complicate the hypothetical, assume that the state in which the court sits does not recognize such a privilege but the state in which the accountant was hired and in which the confidential information passed does. Does the federal court in this case compel disclosure or recognize the privilege?

These two hypothetical situations, while appearing to be quite simple, are in reality among the most difficult questions a federal judge can be called upon to answer. As noted above, there are three possible answers, with cases and treatises to support each. Before these three positions can be understood, it is necessary to understand the background of the privilege issue. The treatment of privilege prior to the enactment of the Federal Rules of Civil Procedure is the basic reason for the confusion in this area today.

Prior to the promulgation of the Federal Rules in 1938, the two hypotheticals could have been dealt with quite easily. Under the rule of *Connecticut Mutual Life Insurance Company v. Union Trust Company*[1] it was

> . . . the duty of the courts of the United States, in trials at common law, to enforce—except where the laws of the United States otherwise provide – the rules of evidence prescribed by the laws of the State in which they sit.[2]

1. 112 U.S. 250 (1884).
2. *Id.* at 256.

The question of privilege being an evidentiary one, the federal court merely applied the privilege rule of the state in which it sat. This rather easy solution to the hypotheticals posed above lasted only until the adoption of the Federal Rules of Civil Procedure in 1938.

If the question of privilege were merely procedural, as was thought prior to the adoption of the Rules, then the solution to the two hypotheticals is obvious. Since the Federal Rules provided that procedural matters were to be governed by the Rules and substantive matters by state law in diversity cases, the question of privilege would be governed by the appropriate portion of the Rules.

> All evidence shall be admitted which is admissible under the statutes of the United States, or under the rules of evidence heretofore applied in the Courts of the United States on the hearing of suits in equity, or under the rules of evidence applied in the courts of general jurisdiction of the state in which the United States Court is held. In any case, the statute or rule which favors the reception of the evidence governs. . . .[3]

If the question of privilege is procedural, then clearly the rule which most favors the reception of the evidence is the one to be followed. In both the hypothetical situations posed above, the federal court would compel disclosure because in the first case there is no federal privilege for accountants and in the second the forum state does not recognize such a privilege.

The position that the question of privilege is procedural has found support both in treatises and cases. As Green points out:

> . . . the state law would not be binding when a state statute granted a privilege . . . but the law of the state would control when it denied a privilege and therefore made the particular evidence compellable.[4]

His position strictly follows Rule 43(a) in that whichever rule favors the disclosure is the one to be followed. A series of cases decided in the Northern District of Ohio have also held that the question of privilege is procedural and is to be governed by the rule most favoring the disclosure.[5] These four cases are not as strong as they might be since all involve the attorney-client privilege. All four hold the federal attorney-client privilege should be followed rather than the state privilege and that the federal privilege does not apply to pre-

3. Fed. R. Civ. P. 43(a).

4. Green, *The Admissibility of Evidence Under the Federal Rules*, 55 Harv. L. Rev. 197, 208-9 (1941).

5. Scourtes v. Fred W. Albrecht Grocery Co., 15 F.R.D. 55 (N.D. Ohio 1953); Brookshire v. Pennsylvania Railroad, 14 F.R.D. 154 (N.D. Ohio 1953); Humphries v. Pennsylvania Railroad, 14 F.R.D. 177 (N.D. Ohio 1953); and Panella v. Baltimore and Ohio Railroad, 14 F.R.D. 196 (N.D. Ohio 1951).

trial discovery proceedings. These cases have been criticized by Weinstein as incorrect[6] and seem doubtful since they hold that the information was privileged under either federal or state law, but is simply not privileged from discovery prior to trial. Privilege is indeed a hollow protection if it only applies at trial, since just as much damage can be done in discovery as at trial.

Perhaps the oddest case to hold that the question of privilege is procedural is *Ex parte Sparrow.*[7] This case involved the taking of a deposition in a state which recognized a privilege for use in a state which did not recognize that privilege. The court in this case refused to classify the question of privilege as substantive (thus leaving the assumption that the question is procedural), but it *did* apply the privilege law of the state in which it sat. The reasoning is indeed questionable. If the privilege area is procedural, as the court implied, then Federal Rule 43(a) should compel the disclosure. This was not the result. If, on the other hand, the court follows the law of the state, then the question must be substantive. This was not the result either. What this court found then was an impossibility—a procedural question which is governed by state law. Such a result violates the rule of *Erie Railroad Co. v. Tompkins*[8] and makes the case of very doubtful value.

Although there is some authority for the position that the question of privilege is procedural, the weight of authority holds that it is substantive. Before considering the substantive aspects of the question, it should be noted that the question is one which has not been ruled upon by the Supreme Court and that no sure answer is possible at this time.

If the question of privilege is not held to be procedural, then it must be substantive. This has been the result in most federal courts. As Weinstein points out:

> Under the acid test of *Erie,* privileges – whether statutory or common law – are clearly etched as policy matters, as matters of substance. . . .[9]

This result was reached judicially in the case of *Massachusetts Mutual Life Insuraance Company v. Brei*[10] where it was held:

> We find that reason, as well as authority, supports the view that the state rule as to the patient-physician privilege should govern. The

6. Weinstein, *Recognition in the United States of the Privileges of Another Jurisdiction,* 56 Colum. L. Rev. 535, 546 (1956).
7. 14 F.R.D. 351 (N.D. Ala. 1953).
8. 304 U.S. 64 (1938).
9. Weinstein, *supra* note 6 at 546.
10. 311 F.2d 463, 466 (2d Cir. 1962).

> privilege reflects a legislatively determined state policy. . . . The rule of privilege is unlike the ordinary rules of practice which refer to the process of litigation, in that it affects private conduct before litigation arises.[11]

The same reasoning led to a similar result in *Republic Gear Company v. Borg-Warner Corporation.*[12] In both cases the fact that the question of privilege in some respects governs the conduct of the parties prior to litigation was found to differentiate it from ordinary rules of procedure and make it substantive. This position can be seen clearly in *R. & J. Dick Co. v. Bass,*[13] where it was held that:

> Second, that matters of privilege and competency are ordinarily considered as being substantive within the meaning of Erie Ry. v. Tompkins . . . , so that, at least where a state statute is involved, a federal court will in a diversity case, follow the law of the state in which it sits.[14]

These cases are illustrative of the weight of authority which holds that the question of privilege is substantive. In the first hypothetical situation outlined above, the result is clearly that the federal court will follow the privilege statute of the forum state and not compel disclosure. The second situation is not so easily solved.

If it is assumed that privilege is a substantive matter, then it is certain that the federal court will apply state law, since under the doctrine of *Erie Railroad Co. v. Tompkins*[15] there is "no federal general common law."[16] A difficult question is raised by the second hypothetical. Which state law should the federal court apply? Should it apply the law of the state in which it sits or the law of the state where the transaction took place?

There is a great deal of authority to the effect that the federal court should apply the law of the state in which it sits on privilege questions. As has been pointed out by a treatise writer: "In so-called 'diversity' cases, the federal courts have followed in a majority of cases the privilege rule of the state in which they sit. . . ."[17] The line of authority for this statement began with *Munzer v. Swedish American Line*[18] which held that "On the question of privileged communications, the Federal Courts follow the law of the state of the forum."[19] A similar result was reached in a number of other cases.[20]

11. *Id.* at 466.
12. 381 F.2d 551 (2d Cir. 1967).
13. 295 F. Supp. 758 (N.D. Ga. 1968).
14. *Id.*
15. 304 U.S. 64 (1938).
16. *Id.* at 78.
17. Annot., 95 A.L.R. 2d 320, 327 (1964).
18. 35 F. Supp. 493 (S.D.N.Y. 1940).
19. *Id.* at 496.

The reasoning behind these decisions is perhaps best illustrated in *Krizak v. W.C. Brooks & Sons, Incorporated*[21] which, in reaching a similar result to these cases, held:

> There is, however, respectable authority for the position that federal equity courts followed state statutes on privilege of witnesses. . . . During the era before the Federal Rules of Civil Procedure were promulgated, when federal courts followed state procedural and statutory substantive law, this might have been the required result. . . . Also, a serious problem of interference with state policy might arise if the federal government were to completely ignore state created confidential relationships. . . . Relying more on the latter reasoning than on the former, probably the majority of federal courts have applied state statutorily created privileges, at least in diversity cases.[22]

The above cases would seem to solve the second hypothetical of the court sitting in a state without a privilege and the transaction having taken place in a state with a privilege quite easily. The federal court should simply apply the law of the state in which it sits. This would compel disclosure in the second hypothetical since the state of the forum does not recognize the privilege. The cases outlined above seem to lead to that result, but need not compel it. None of the cases cited above dealt with a situation like the second hypothetical. They all involved the rather easy case of the forum state and place of the transaction being the same. They did not involve the intricate conflict of laws problem found in the second hypothetical. The only case to automatically apply the privilege law of the state in which it sat was *Palmer v. Fisher,*[23] in which it was held that an Illinois federal court sitting in a diversity case could suppress a deposition for use in Florida when Illinois recognized a privilege and Florida did not. An automatic application of the law of the forum such as that in *Palmer v. Fisher*[24] may be incorrect in that it violates the outcome-determination test.

The outcome-determination test, which is an outgrowth of *Erie*

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20. Van Wie v. United States, 77 F. Supp. 22 (N.D. Iowa 1948); *In re* Albert Lindley Lee Memorial Hospital, 115 F. Supp. 643 (N.D.N.Y. 1953), *aff'd* 209 F.2d 122 (2d Cir. 1953), *cert. denied, sub nom.* Cincotta v. U.S., 347 U.S. 960 (1954); Padovani v. Liggett and Myers Tobacco Company, 23 F.R.D. 255 (E.D.N.Y. 1959); Spray Products Corporation v. Sprouse, Inc., 31 F.R.D. 244 (E.D. Pa. 1962); Hill v. Huddleston, 263 F. Supp. 108 (D.Md. 1967); and New York Underwriters Insurance Company v. Union Construction Company, 285 F. Supp. 868 (D.Kan. 1968).

21. 320 F.2d 37 (4th Cir. 1963).

22. *Id.* at 42-3.

23. 228 F.2d 603 (7th Cir. 1955), *cert. denied, sub nom.* Fisher v. Pierce, 351 U.S. 965 (1956).

24. *Id.*

Railroad Co. v. Tompkins,[25] was first formulated in *Guaranty Trust Co. v. York*,[26] in which the Supreme Court held:

> In essence, the intent of that decision *(Erie)* was to insure that, in all cases where a federal court is exercising jurisdiction solely because of the diversity of citizenship of the parties, the outcome of the litigation in the federal court should be substantially the same, so far as legal rules determine the outcome of a litigation, as it would be if tried in a State court.[27]

The strictness of the outcome-determination test was relaxed somewhat in *Byrd v. Blue Ridge Electric Cooperative, Inc.*,[28] in which the Supreme Court recognized that the test might have to be violated in the face of a compelling federal interest (in that case the right to a jury trial). The rationale behind the outcome-determination test is best illustrated in *Hanna v. Plumer, Executor*[29] in which it was said that:

> The outcome-determination test therefore cannot be read without reference to the twin aims of the Erie rule: discouragement of forum-shopping and avoidance of inequitable administration of the laws.[30]

The relationship of this test to the second hypothetical is that an automatic application of the privilege rule of the state in which it sits by the federal court could give a different outcome than if the case were tried in a state court.

Since under the rule of *Klaxon Company v. Stentor Electric Manufacturing Co., Inc.*,[31] it is quite clear that the federal court is obliged to follow the conflict of laws rules of the state in which it sits, the court should look to the conflicts rules of the forum before deciding the question of privilege. It is quite conceivable that in some instances a state court would not apply its own privilege rule. This could be the case if the state's conflicts rules said that the state of the transaction should govern as to privilege. This was indeed the case in *Application of Cepeda*.[32] In that case, plaintiff was suing in California which had a privilege and sought a deposition in New York which did not recognize the privilege. The New York Southern Dis-

25. 304 U.S. 64 (1938).
26. 326 U.S. 99 (1945).
27. *Id.* at 109.
28. 356 U.S. 525 (1958).
29. 380 U.S. 460 (1965).
30. *Id.* at 468.
31. 313 U.S. 487 (1941).
32. 233 F. Supp. 465 (S.D.N.Y. 1964) *rev. on other grounds* 328 F.2d 869 (9th Cir. 1964), *cert. denied*, 379 U.S. 844 (1964).

trict Court looked to the conflicts rules of New York and then found that the privilege granted by California should be enforced in New York. In view of the outcome-determination test this would seem to be a correct result and the most reasonable position on the question of privilege in diversity cases.

This position of looking first to the conflicts rules of the forum has found some support in treatises and cases outside *Application of Cepeda.*[33] As Louisell points out:

> To me it seems clear that under the constitutional rationale of the *Erie* case, as pronounced by Mr. Justice Brandeis and never receded from by the Supreme Court . . . , the federal courts in diversity cases now have the constitutional duty to follow the *proper* state law of privilege, whether statutorily or judicially declared.[34] (emphasis added)

This position is similarly supported by dicta in *Reid v. Moore-McCormack Lines, Inc.:*[35]

> Federally, privilege is perhaps best thought of as a procedural rule which looks outward to the substantive law of the *appropriate* local jurisdiction to receive its concrete form in a given case.[36] (emphasis added)

It can be implied from the emphasized language of these two sources that the choice of which state law to apply is not automatic. A choice must be made. If such a choice is to be made, under the rule of *Klaxon Company v. Stentor Electric Manufacturing Co., Inc.*[37] it can only be made by looking to the conflicts rule of the forum state to decide the privilege question.

There are three possible ways to answer the two hypotheticals posed at the first of this Note. It is possible to regard privilege as procedural. If this is the case, the federal court will compel the disclosure in both hypotheticals under Rule 43(a). This is not a theory much favored today. It is hard to characterize as procedural something which is as widespread in its effects on parties prior to litigation as is the privilege question. If the privilege is classified as substantive, state law must apply. An automatic application of the privilege rule of the forum will result in non-disclosure in the first hypothetical and disclosure in the second. The case for automatic

33. *Id.*
34. Louisell, *Confidentiality, Conformity and Confusion: Privileges in Federal Court Today*, 31 Tul. L. Rev. 101, 117 (1956).
35. 49 F.R.D. 91 (S.D.N.Y. 1970).
36. *Id.* at 93.
37. 313 U.S. 487 (1941).

application is weakened by the fact that it would in some cases violate the outcome-determination test. The better position would be for the court to look to the conflicts rules of the forum in deciding whether to recognize the privilege. To do so will result in a correct decision under the outcome-determination test in all cases. None of these alternatives has been ruled upon by the Supreme Court, and until that happens, each theory has support for its position. The better theory may not turn out to be the correct one.

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