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Memorandum

Work Product Protection for Tax Accrual Workpapers: *U.S. v. Deloitte* Revives Hope for Taxpayers Despite *Textron*

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INTRODUCTION

In the wake of the First Circuit's regrettable *en banc* decision in *U.S. v. Textron Inc.*, 577 F.3d 21 (1st Cir. 2009), *cert. denied*, 130 S. Ct. 3320 (2010), one might have believed that documents prepared to support the financial accounting treatment of contingent tax liabilities enjoy little or no protection from disclosure to tax authorities. But the recent decision by the D.C. Circuit in *U.S. v. Deloitte LLP*, 610 F.3d 129 (D.C. Cir. 2010), confirms that such documents may contain information that is protected by the work product doctrine and remains protected even when provided to independent auditors to satisfy financial statement reporting obligations. Rejecting the First Circuit's view of the work product doctrine as focused on the intended physical use of, or role to be played by, a specific document, the D.C. Circuit applied a test focused squarely on the historical underpinnings of the doctrine; namely, whether the document contains, and thus production would disclose, information that was first prepared in anticipation of litigation.

The opinion in *Deloitte* resulted from a discovery dispute in a pending tax case in Louisiana district court involving two affiliates of Dow Chemical Company (''Dow''). The government issued a subpoena to Dow's independent auditor, Deloitte & Touche USA, LLP (now known as Deloitte LLP) for documents related to Dow's tax position. Dow objected to the production of certain documents under the work product doctrine, and the government filed a motion to compel the production of those documents.[2]

The D.C. Circuit's opinion addressed three documents. The first document, a memorandum prepared by Deloitte, summarized a meeting that discussed the potential tax litigation concerning the two Dow affiliates and the appropriate accounting treatment resulting from that possibility. The meeting included individuals from Deloitte and Dow as well as Dow's outside counsel. The court referred to this document as the ''Deloitte Memorandum.'' The second and third documents were prepared by Dow's inside and outside counsel to address tax issues related to the affiliates. The court referred to these two documents as the ''Dow Documents.'' The government argued that the Deloitte Memorandum was not work product and, although it conceded that the Dow Documents were initially protected by the work product doctrine, it argued that the protection had been waived when the documents were disclosed to Deloitte as part of its review of the adequacy of Dow's tax reserves.

The trial court denied the government's motion to compel, and the D.C. Circuit affirmed that decision,

[1] The author wishes to express his appreciation to his Miller & Chevalier colleagues who helped with the preparation of this article: Kevin Kenworthy, Alan Horowitz, George Clarke, and David Blair.

[2] Because the subpoena requested that the documents be produced in Washington, D.C., the subpoena was required under the Federal Rules of Civil Procedure to be issued by the U.S. District Court for the District of Columbia.

although it remanded the case to the trial court to determine whether all, or only a part, of the Deloitte Memorandum should be protected from production to the government. The time periods for the government to request either a rehearing *en banc* (as was done in *Textron*) or Supreme Court review have expired.

The D.C. Circuit's opinion is noteworthy in a number of respects. First, the decision exacerbates a split among the circuits over whether the work product doctrine protects tax accrual workpapers. Second, the opinion sharpens the dialogue around the work product analysis by focusing on the content of the document in question rather than the role that the particular document may play in a business. Finally, the D.C. Circuit is the first circuit court to address the important question of whether the protections afforded by the work product doctrine are waived by making the documents with protected material available to the independent auditor as part of the audit of the financial statements.

WORK PRODUCT PROTECTION FOR TAX ACCRUAL WORKPAPERS

Origins of the Work Product Protection

The protections afforded under the work product doctrine, which was first recognized in *Hickman v. Taylor*, 329 U.S. 495, 510–11 (1947), and later codified in the Federal Rules of Civil Procedure, are rooted in fundamental policies of our adversarial system. The work product doctrine seeks to protect a lawyer's mental impressions, legal theories, and preparatory work. This protection is set forth in the Federal Rules of Civil Procedure, Rule 26(b)(3)(A), which provides that ''a party may not discover documents and tangible things that are prepared in anticipation of litigation or for trial by or for another party or its representative (including the other party's attorney, consultant, surety, indemnitor, insurer, or agent).'' Further, Rule 26(b)(3)(B) provides that in considering requests for the production of documents, the court ''must protect against disclosure of the mental impressions, conclusions, opinions, or legal theories of a party's attorney or other representative concerning the litigation.''

While the attorney-client privilege encourages open communications between a lawyer and his or her client to ensure efficient and effective representation of the client, the work-product doctrine is based on fundamental notions of fairness in our adversarial system of dispute resolution. The work product protection ensures that a lawyer can proceed in preparing his or her case without fear that the lawyer's work will be shared with his or her adversary. The protection can be viewed from the perspective of both the party that prepares the work product and from the perspective of its adversary. Thus, the work product doctrine *protects* ''a zone of privacy in which a lawyer can prepare and develop legal theories and strategy 'with an eye toward litigation' free from unnecessary intrusion by his adversaries.'' *U.S. v. Adlman*, 134 F.3d 1194, 1196 (2d Cir. 1998) (citing *Hickman v. Taylor*, 329 U.S. 495, 510–11 (1947)). The work product doctrine also *prevents* ''a litigant from taking a free ride on the research and thinking of his opponent's lawyer,'' which ''avoid[s] the resulting deterrent to a lawyer's committing his thoughts to paper.'' *U.S. v. Frederick*, 182 F.3d 496, 500 (7th Cir. 1999).

Application of Work Product Protection for Tax Accrual Workpapers

The first question addressed by the D.C. Circuit was whether the Deloitte Memorandum was protected from discovery under the work product doctrine. The government argued that the document could not be protected because it was prepared by Deloitte and not by Dow or one of its representatives. Relying on the same policy considerations that led the Supreme Court to decline to recognize a federal ''accountant-client'' privilege in *U.S. v. Arthur Young & Co.*, 465 U.S. 805 (1984), the government argued that an independent auditor like Deloitte has a responsibility to the investing public and thus cannot be seen as representing Dow for purposes of the work product doctrine. The D.C. Circuit rejected this argument, noting that the government inappropriately focused on the party that created the documents, and that party's relationship to Dow, rather than the contents of the document itself. The only question should be ''whether the document contains work product — the thoughts and opinions of counsel developed in anticipation of litigation.'' [3] The trial court had found that the Deloitte Memorandum memorialized the thoughts and opinions of Dow's counsel prepared in anticipation of litigation. Finding that the contents of a document, not the identity of its author, is controlling, the court concluded: ''[t]he work product privilege does not depend on whether the thoughts and opinions were communicated orally or in writing, but on whether they were prepared in anticipation of litigation.'' [4]

The government next argued that the Deloitte Memorandum could not be afforded work product

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[3] *Deloitte*, 610 F.3d at 136.

[4] *Id.*

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protection because it was not prepared in anticipation of litigation but instead as part of the routine financial audit process. There was no dispute that the function of the Deloitte Memorandum, and the meeting memorialized in that document, were intended solely to support Deloitte's conclusions about the accuracy of Dow's financial statements. Nevertheless, in a resounding rejection of the government's litigating position in this and other cases, the court declined to accept the intended function of the document as controlling rather than its contents. Specifically, the court held that material developed in anticipation of litigation can be incorporated into a document that was generated ''for ordinary business purposes without losing its protected status.'' [5] Accordingly, the D.C. Circuit held that the role that the Deloitte Memorandum played in the financial audit process was irrelevant if that document otherwise contained protected work product. ''[A] document can contain protected work-product material even though it serves multiple purposes, so long as the protected material was prepared because of the prospect of litigation.'' [6]

Although the D.C. Circuit rejected the government's arguments that the work product doctrine did not apply at all to the Deloitte Memorandum, the court found that the record was insufficient to conclude that the entire document was protected work product. Thus, the court remanded the case to permit the trial court to assess whether it had correctly ruled that the memorandum was entirely work product, or whether a redacted version could be disclosed to the government without revealing the protected work product.[7]

The Growing Circuit Split

The D.C. Circuit's decision in *Deloitte* stands in stark contrast to the First Circuit's decision in *Textron*, and adds to the growing split among the circuits on whether the work product doctrine should apply to tax accrual workpapers. Like most circuits, the D.C. Circuit applies the ''because of'' test to evaluate whether a document was prepared in anticipation of litigation.[8] The ''because of'' test asks ''whether, in light of the nature of the document and the factual situation in the particular case, the document can fairly be said to have been prepared or obtained because of the prospect of litigation.'' [9] Prior to *Textron*, the majority of federal circuits had adopted the ''because of'' test in assessing work-product disputes.[10] Only the Fifth Circuit had adopted a different test, the ''primary purpose'' test, which asks whether the primary motivating purpose behind the creation of the document is to aid in possible future litigation.[11] Which standard to apply remains an open question in three circuits.[12]

Interestingly, in its brief opposing Supreme Court review in *Textron*, the government argued that there was no circuit split that required resolution by the Court.[13] The government noted that the only other circuit court case dealing with work product protection for tax accrual workpapers, *El Paso*, similarly held that the work product protection did not apply.[14] The government also noted that, ''[i]n the nearly 30 years since *El Paso*, none of the thousands of publicly traded companies that share tax-accrual workpapers with their independent auditor every year has persuaded a federal court of appeals to accord work product protection to those workpapers.'' [15] At least after *Deloitte*, this is no longer true.[16] Furthermore, the government also argued in *Textron* that cases approv-

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[5] *Id.* at 138.

[6] *Deloitte*, 610 F.3d at 138.

[7] *Id.* at 139.

[8] *Id.* at 137.

[9] *Id.*, quoting *In re Sealed Case*, 146 F.3d 881, 884 (D.C. Cir. 1998) (quotation omitted).

[10] *See, e.g., U.S. v. Roxworthy*, 457 F.3d 590 (6th Cir. 2006) (adopting the ''because of'' test); *U.S. v. Adlman*, 134 F.3d 1194, 1197–1205 (2d Cir. 1998) (discussing the different approaches taken by courts here, and concluding that the ''because of'' standard is the appropriate one); *Maine v. U.S. Dept. of Interior*, 298 F.3d 60, 68 (1st Cir. 2002); *U.S. v. Torf (In re Grand Jury Subpoena)*, 357 F.3d 900, 907 (9th Cir. 2004); *Nat'l Union Fire Ins. Co. v. Murray Sheet Metal Co.*, 967 F.2d 980, 984 (4th Cir. 1992); *Simon v. G.D. Searle & Co.*, 816 F.2d 397, 401 (8th Cir. 1987); *Senate of P.R. ex rel. Judiciary Comm. v. U.S. Dept. of Justice*, 823 F.2d 574, 587 (D.C. Cir. 1987); *Binks Mfg. Co. v. Nat'l Presto Indus., Inc.*, 709 F.2d 1109, 1119 (7th Cir. 1983); *In re Grand Jury Proceedings*, 604 F.2d 798, 803 (3d Cir. 1979).

[11] *See, e.g., U.S. v. El Paso Co.*, 682 F.2d 530, 543 (5th Cir. 1982) (''The primary motivating force behind the tax pool analysis . . . is not to ready El Paso for litigation over its tax returns. Rather, the primary motivation is to anticipate, for financial reporting purposes, what the impact of litigation might be on the company's tax liability.''); *U.S. v. Davis*, 636 F.2d 1028, 1040 (5th Cir. 1982) (tax return workpapers prepared by attorney not protected).

[12] The Tenth, Eleventh, and Federal Circuits have not yet expressly adopted any standard. A district court in the Eleventh Circuit stated in dicta that it was inclined to align itself with the majority of other circuits and adopt the ''because of'' test. *Regions Fin. Corp. v. U.S.*, 101 AFTR2d 2179, 2183 (N.D. Ala. 2008). The case was ultimately settled and dismissed before review by the Eleventh Circuit. Furthermore, although not addressed by the Federal Circuit, the U.S. Court of Federal Claims has applied the ''because of'' test. *Evergreen Trading, LLC v. U.S.*, 80 Fed. Cl. 122, 132 (2007).

[13] Brief for the United States in Opposition at 13, *Textron Inc. v. U.S.*, (U.S., No. 09-750) (hereinafter ''Brief in Opposition'').

[14] Brief in Opposition at 13.

[15] *Id.*

[16] At least one amicus supporting Supreme Court review in *Textron* disagreed with this assessment, pointing out that the *en banc* rationale would have ramifications beyond the tax area and could impact any dispute involving a contingent liability for

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ing work product protection for documents reflecting the analysis of potential tax disputes with the Internal Revenue Service (IRS), like *U.S. v. Roxworthy*, 457 F.3d 590 (6th Cir. 2006), and *U.S. v. Adlman*, 134 F.3d 1194 (2d Cir. 1998), did not actually conflict with *Textron* and *El Paso* because the tax documents in question were prepared in anticipation of litigation and not in the ordinary course of business for use by financial statement auditors.[17] This suggested distinction does not apply to *Deloitte*, which, like *Textron*, addressed documents prepared in the ordinary course of business for use by financial statement auditors, yet the two circuit courts reached opposite conclusions.

Perhaps even more interesting is the D.C. Circuit's discussion of whether the First Circuit's decision in *Textron* created a third standard for the application of the work product doctrine. The First Circuit in *Textron* went to great lengths to assert that it was embracing the same ''because of'' test that a prior First Circuit panel had adopted.[18] At a minimum, the First Circuit appears to have added a gloss to the ''because of'' test that would require the taxpayer to show that the document actually would be used in litigation. Nevertheless, the government steadfastly denied that the First Circuit deviated from the ''because of'' standard.[19] The D.C. Circuit opinion expressed skepticism of that assertion without attacking it directly. As the court tactfully stated, ''Judge Torruella's dissenting opinion in *Textron* makes a strong argument that while the court said it was applying the 'because of' test, it actually asked whether the documents were 'prepared for use in possible litigation,' a much more exacting standard.'' [20] Notably, when the D.C. Circuit cited to cases from the circuit courts that had adopted the ''because of'' test, it cited to the earlier First Circuit ''because of'' decision, *Maine v. U.S. Dept. of Interior*, 298 F.3d 60, 68 (1st Cir. 2002), rather than to *Textron*.[21] Whatever standard the First Circuit applied in *Textron*, it was not the same ''because of'' standard that has been traditionally applied by most circuits, and the D.C. Circuit recognized that fact.

Focus on the Information Contained In the Document, Not the Document Itself

Despite the court's polite efforts to ''distinguish'' *Textron* rather than formally reject it, the D.C. Circuit's reasoning is fundamentally at odds with that of the First Circuit. The First Circuit's fixation on the use of the particular document at issue improperly clouded the analysis and the conclusion in *Textron*. The D.C. Circuit, on the other hand, properly focused its attention on the information contained in the document, rather than the document's use, to assess whether the information in the document should be protected. With this focus, the D.C. Circuit found that protected material in a so-called ''dual use'' document will remain protected even if the document is used for an ordinary business purpose. After all, the premise of the ''because of'' test is that a document obtains its status as work product by being prepared *because of* the prospect of litigation. This test, by its terms, plainly does not require that the document be prepared directly and solely for *use* in litigation.

In applying its new test in *Textron*, the First Circuit focused almost exclusively on the document itself and whether it was the type of document that a litigator would use in preparing for actual or anticipated litigation. The court reviewed the trial court record, including the testimony of the witnesses, and concluded that the Textron workpapers were prepared for financial reporting purposes and were not intended to be used in the course of preparing for litigation. The First Circuit noted that ''[a]ny experienced litigator would describe the tax accrual workpapers as tax documents and not as case preparation materials.'' [22] Later, the First Circuit similarly commented that ''[e]very lawyer who tries cases knows the touch and feel of materials prepared for a current or possible (i.e., 'in anticipation of') lawsuit.'' [23] Ultimately, the First Circuit found that any conclusion that the Textron workpapers were prepared ''*for use* in possible litigation . . . would have been clearly erroneous.'' [24] Thus, while the First Circuit did not create a *per se* rule that any and all tax accrual workpapers would not be afforded work product protection, it came perilously close to such a result by disfiguring the work product doctrine under the ''because of'' standard.

The D.C. Circuit, however, focused not on the particular document or its use, but on the information contained in the document. The court looked beyond the language in Rule 26(b)(3), which refers to ''documents and tangible things,'' to note that the protec-

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which a company records a reserve on its financial statements. Br. for the Comm. on Tax'n & Comm. on Corporate Reporting of Fin. Execs. Int'l as Amicus Curiae in Support of Petitioner at 7–8, *Textron Inc. v. U.S.*, (U.S. No. 09-750). *See, e.g., In re Pfizer Inc. Sec. Litig.*, No. 90 Civ. 1260 (SS), 1993 WL 561125 (S.D.N.Y. 12/23/93) (communications involving reserves for individual product liability cases were protected work product), and *Simon v. G.D. Searle & Co.*, 816 F.2d 397 (8th Cir. 1987) (individual case reserves protected from discovery as opinion work product).

[17] Brief in Opposition at 14.

[18] *U.S. v. Textron Inc.*, 577 F.3d 21, 26 (1st Cir. 2009) (''We now conclude that under our own prior *Maine* precedent — which we reaffirm *en banc* — . . . that the work product privilege does not apply'' to Textron's workpapers.).

[19] Brief in Opposition at 15.

[20] *Deloitte*, 610 F.3d at 138.

[21] *Id.* at 136.

[22] *Textron*, 577 F.3d at 28.

[23] *Id.* at 30.

[24] *Id.* at 27 (emphasis in original).

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tions afforded by *Hickman v. Taylor* include intangible things such as an attorney's mental impressions. The arguments that the government raised regarding the role of the document in the financial audit process, the role of Deloitte in that process, and the fact that the document was prepared by someone at Deloitte, were all misplaced. The D.C. Circuit noted that the Deloitte Memorandum, even though prepared by someone from Deloitte, reflected ''the thoughts and opinions of counsel developed in anticipation of litigation.'' [25] It is those ''thoughts and opinions,'' the quintessential ''mental impressions'' of a lawyer, that the work product doctrine seeks to protect, rather than some specific piece of paper. As the D.C. Circuit held, it does not matter how those thoughts or opinions are communicated (or memorialized), or for what purpose those thoughts or opinions were communicated (or memorialized). The only question is whether those thoughts or opinions were formed in anticipation of litigation.

The D.C. Circuit also rejected the notion that a document cannot possibly have work product protection if the sole reason for the creation of the document is to facilitate a financial audit. As noted above, the D.C. Circuit recognized the existing authority that embraces the ''because of'' test and also allows material generated in anticipation of litigation to be used ''for ordinary business purposes without losing its protected status.'' [26] Again, the purpose for which those thoughts or opinions are to be used is not controlling; what controls is whether the anticipation of litigation is what originally gave rise to those thoughts or opinions. Accordingly, the D.C. Circuit embraced the ''dual use'' concept that a document prepared for ordinary business reasons (other than litigation) may still contain protected work product.

Without stating so directly, the D.C. Circuit's opinion would seem to reject two basic legal propositions from *Textron* that conflict with the ''dual use'' concept applied outside the First Circuit. First, the First Circuit in *Textron* believed that merely because the subject matter of a document relates to an issue that might be the subject of litigation is ''not enough to trigger work product protection.'' [27] Second, according to the First Circuit, work product protection does not extend to documents merely because they were prepared by lawyers or represent legal thinking.[28] To the extent that either of those concepts, or any variant of those concepts, ignores the content of the document in question or why the lawyer develops his or her thinking in the first place, they similarly ignore the underlying purposes of the work product doctrine, distort the ''because of'' test, reject the concept of dual use, and are incompatible with the analysis in *Deloitte*.

For the articulation of the ''dual use'' concept, the D.C. Circuit referred to the Second Circuit's decision in *Adlman*, in which ''a document containing legal analysis about possible future litigation qualified as work product when it was procured to assist the parties in deciding whether to go through with a proposed merger.''[29] The D.C. Circuit quoted from *Adlman*:

> a document created because of anticipated litigation, which tends to reveal mental impressions, conclusions, opinions or theories concerning the litigation, does not lose work-product protection merely because it is intended to assist in the making of a business decision influenced by the likely outcome of the anticipated litigation. Where a document was created because of anticipated litigation, and would not have been prepared in substantially similar form but for the prospect of that litigation, it falls within Rule 26(b)(3).[30]

Most ''experienced litigators'' would probably agree with the First Circuit's assessment that tax accrual workpapers are not thought of as ''case preparation materials'' and do not have the ''touch and feel'' of materials prepared for use in a trial. However, that is not the test under the ''because of'' standard, nor should it ever be the test. As the D.C. Circuit correctly framed the inquiry, the content of the document should control the work product determination, not the intended use of the document. Perhaps tax practitioners can do themselves a favor by not referring to a ''protected document'' but rather to ''protected information contained in a document.'' This may be a more cumbersome articulation, but it will remind us all that the focus of the analysis must be on the content of the document, and not the particular document itself, how it could be used, or even the particular context in which the documents are actually used.

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[25] *Deloitte*, 610 F.3d at 136.

[26] *Id.* at 138.

[27] *Textron*, 577 F.3d at 29.

[28] *Id.*

[29] *Deloitte*, 610 F.3d at 138.

[30] *Id.*, citing *U.S. v. Adlman*, 134 F.3d 1194, 1195 (2d Cir. 1998). Notably, as the dissent in *Textron* pointed out, the First Circuit in *Maine* relied almost entirely upon *Adlman* in originally adopting the ''because of'' test. The dissent in *Textron* then reviewed the analysis in *Adlman* in great detail to point out that the majority opinion in *Textron* was at odds with *Adlman*, and therefore also with *Maine*. It may not be coincidental that the D.C. Circuit selected *Adlman* as its example of a decision embracing the ''dual use'' concept.

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PROTECTION NOT WAIVED THROUGH DISCLOSURE TO FINANCIAL AUDITOR

The second important issue addressed in *Deloitte* was whether work product protection for tax accrual workpapers is waived by disclosure to independent financial auditors. The disclosure of work product to a third party does not ordinarily result in a waiver unless the disclosure enables an adversary to gain access to the information.[31] In this respect, the work product protection is more durable than the attorney-client privilege, which is generally waived whenever confidential communications are intentionally disclosed to any third party. Where a communication or document is protected by both the attorney-client privilege and the work product doctrine, a waiver of the attorney-client privilege does not automatically result in a waiver of work product claims.[32]

In *Deloitte*, the government conceded that the other two documents — the Dow Documents, prepared by Dow and its outside counsel — were properly viewed as work product. Nevertheless, the government argued that these documents should be turned over because Dow waived the work product protection when it disclosed the documents to its independent auditor, Deloitte. The D.C. Circuit noted that work product protection may be waived when a document or communication is disclosed to a litigation adversary or to any third party under circumstances that are inconsistent with keeping the work product secret from such an adversary.[33] However, the D.C. Circuit embraced a line of authority developed in the trial courts [34] and found that Deloitte was neither a potential adversary nor a conduit to an adversary. In so doing, the D.C. Circuit became the first court of appeals to adopt this position.[35]

The D.C. Circuit rejected government arguments that Deloitte was a potential adversary even though the court acknowledged that disputes sometimes arise between auditors and their clients. The court explained that ''the question is not whether Deloitte could be Dow's adversary in any conceivable future litigation, but whether Deloitte could be Dow's adversary in the sort of litigation the Dow Documents address. We conclude that the answer must be no.'' [36]

Addressing government arguments that Deloitte was a conduit to Dow's adversaries, the D.C. Circuit found that Dow had a reasonable expectation that Deloitte would not disclose the work product Dow had shared with the firm. The D.C. Circuit noted that the AICPA Code of Professional Conduct imposes a duty of confidentiality. Furthermore, although the D.C. Circuit accepted that theoretical circumstances might arise in which an auditor might be required to disclose confidential information obtained from a client, the court found that the government failed to point to any regulatory requirement or any specific circumstance requiring disclosure of the work product contained in these documents. In sum, an independent auditor can fulfill its duties without ''revealing every piece of information it reviews during the audit process.''[37] The D.C. Circuit distinguished *Arthur Young*, above, noting that in the present case the government was not merely seeking discovery of the auditor's views on a company's financial statements, but an attorney's thoughts and mental impressions developed in anticipation of litigation.[38] Closing with a quote from Justice Jackson's concurring opinion in *Hickman v. Taylor*, allowing the discovery of such materials would ''let the government litigate on wits borrowed from the adversary.'' [39]

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[31] *See*, *In re Grand Jury Subpoenas Dated Dec. 18, 1981 & Jan. 4, 1982* 561 F. Supp. 1247, 1257 (E.D.N.Y. 1982) (''Disclosure of work product to a third party does not waive its protection unless it substantially increases the opportunity for potential adversaries to obtain the information.'').

[32] *See Medinol, Ltd. v. Boston Sci. Corp.*, 214 F.R.D. 113, 114 (S.D.N.Y. 2002).

[33] *Deloitte*, 610 F.3d at 140, citing *Rockwell Int'l Corp. v. U.S. Dept. of Justice*, 235 F.3d 598, 605 (D.C. Cir. 2001).

[34] The D.C. Circuit cited to the following cases that found no waiver of work product upon disclosure to the independent auditor (610 F.3d at 139): *Regions Fin. Corp. v. U.S.*, No. 2:06-CV-00895-RDP, 2008 WL 2139008, at *8 (N.D. Ala. 5/8/08) (slip op.); *Lawrence E. Jaffe Pension Plan v. Household Int'l, Inc.*, 237 F.R.D. 176, 183 (N.D. Ill. 2006); *In re JDS Uniphase Corp. Sec. Litig.*, No. C-02-1486 CW, 2006 WL 2850049, at *1 (N.D. Cal. 10/5/06) (unpub. decision); *Am. S.S. Owners Mut. Prot. & Indem. Ass'n v. Alcoa S.S. Co.*, No. 04-Civ-4309, 2006 WL 278131, at *2 (S.D.N.Y. 2/2/06) (unpub. decision); *Frank Betz Assocs., Inc. v. Jim Walter Homes, Inc.* , 226 F.R.D. 533, 535 (D.S.C. 2005); *Merrill Lynch & Co. v. Allegheny Energy, Inc.*, 229 F.R.D. 441, 447–49 (S.D.N.Y. 2004); *In re Honeywell Int'l, Inc. Sec. Litig.*, 230 F.R.D. 293, 300 (S.D.N.Y. 2003); *Gutter v. E.I. Dupont de Nemours & Co.*, No. 95-CV-2152, 1998 WL 2017926, at *5 (S.D. Fla. 5/18/98) (unpub. decision); *In re Pfizer Inc. Sec. Litig.*, No. 90 Civ. 1260, 1993 WL 561125, at *6 (S.D.N.Y. 12/23/93) (unpub. decision).

[35] Note that in the vacated First Circuit panel decision in *Textron* (*U.S. v. Textron Inc.*, 553 F.3d 87 (1st Cir. 2009)), the court held that disclosures to an independent auditor would not automatically waive work product protection. However, the vacated decision would have remanded the case to the trial court for further proceedings to determine if Textron had waived the protection on the ground that, on the facts of that case, the independent auditor was a potential conduit to the IRS.

[36] *Deloitte*, 610 F.3d at 140.

[37] *Id.* at 143.

[38] *Id.*

[39] *Deloitte*, 610 F.3d at 143 (internal quotation and citation omitted).

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IMPLICATIONS GOING FORWARD

The law with respect to the application of the work product doctrine to tax accrual workpapers is far from settled. The mood across the country with respect to this issue has been on a roller coaster. After the original First Circuit decision in *Textron*, taxpayers felt as though they had obtained a landmark decision that could have nationwide impact in securing protection for tax accrual workpapers. The *en banc* decision in *Textron*, followed by the Supreme Court's denial of certiorari, had the equal and opposite effect — many thought the war was over and that the rule in *Textron* would effectively become the rule throughout the country. The decision in *Deloitte* has given renewed hope for taxpayers, but the reality is that the law is settled in only three circuits. Taxpayers in the First Circuit and the Fifth Circuit will have difficulty asserting that the work product protections apply to certain tax accrual workpapers. Taxpayers in the D.C. Circuit will be on solid ground.[40] Taxpayers in circuits that faithfully adhere to the ''because of'' standard can look to *Deloitte* for strong support.[41]

At this point, it is unclear whether and when the work product issues addressed in *Textron* and *Deloitte* will be revisited. Except for taxpayers who have engaged in ''listed'' transactions or who have experienced financial accounting irregularities, the IRS does not routinely seek tax accrual workpapers.[42] However, some number of requests are likely to be made (or currently remain pending), and it will only take one taxpayer in one of these other circuits to contest the request for another court to address the issue. In addition, the advent of the recently finalized Schedule UTP for disclosure of ''uncertain tax positions'' on certain corporate returns is likely to dominate the landscape of IRS audits for the foreseeable future.[43] Although there may remain potential work product objections to the disclosures required to be made on the new Schedule UTP, the IRS has blunted much of the early criticism about work product and privilege implications of the schedule with the recently announced revisions reflected in the final Schedule.[44] In any event, when the next case arises in an ''uncommitted'' circuit, neither side is likely to concede the issue. Taxpayers should feel emboldened by the victory in *Deloitte*; the IRS will almost surely continue to press its views. Thus, it may only be a matter of time before another case finds its way to the court of appeals level.

Practically, taxpayers can help themselves by seeking to distinguish the tax-risk assessment process from the financial reserve analysis. Even outside the First Circuit, work product protection may be difficult to sustain when the facts suggest that the taxpayer analyzed the tax risks only upon a request from the independent auditor. However, consistent with the analysis in *Deloitte*, taxpayers are in a much stronger position (even assuming that there must be some type of communication with the independent auditor) if the tax-risk assessment is undertaken irrespective of the taxpayer's dealings with its financial statement auditor. In that situation, the thoughts and opinions are first developed because of the anticipation of litigation with the IRS and are only later communicated to the independent auditor or otherwise reflected in the tax accrual workpapers. If the taxpayer truly is preparing its evaluation of potential litigation hazards solely for financial accounting purposes, then the taxpayer can expect greater difficulty sustaining a work product claim.

Work product cases may also develop in the context of the disclosure requirements in the newly finalized Schedule UTP. In releasing the final schedule and its instructions, the IRS indicated its hope to avoid work product disputes by eliminating the requirement contained in the draft Schedule and Instructions that a concise description of the issue must include the rationale and nature of the uncertainty.[45] Despite this effort, work product issues may arise. Stepping back

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[40] Consistent with the guidance from the D.C. Circuit, one might expect that any disclosed (unredacted) material would be of a purely factual nature that does not involve the thoughts, opinions, or impressions of Dow or its Dow's counsel. However, if Dow believes unredacted material may be encroaching on that zone of protection, we might yet see another opinion in that case.

[41] *Deloitte* could have implications for Tax Court litigation. Code §7453 provides that the proceedings of the Tax Court ''shall be conducted in accordance with such rules of practice and procedure (other than rules of evidence) as the Tax Court may prescribe and in accordance with the rules of evidence applicable in trials without a jury in the United States District Court of the District of Columbia.'' *See also* Tax Court Rule 143(a). However, it is unclear whether the application of the work product doctrine is subject to these provisions as a rule of evidence, or whether work product is subject to the *Golsen* rule as a substantive rule of law. (The Tax Court defers to the precedent for the circuit court to which the particular case would be appealed. *Golsen v. Comr.*, 54 T.C. 742 (1970).) The Tax Court has not addressed this work product issue in a published opinion. However, in *Director v. Comr.*, 55 T.C.M. 1059 (1998), the court addressed whether grand jury materials were protected from discovery. After referencing §7453 and Rule 143(a), the court applied the federal common law with respect to privilege giving special weight to precedent from the Second Circuit, the controlling circuit for that case. *Id.* at 1064–66.

[42] *See* Ann. 2002-63, 2002-2 C.B. 72.

[43] *See Reporting of Uncertain Tax Positions*, Ann. 2010-75, and the finalized Schedule UTP and Instructions released on Sept. 24, 2010, which can be found on the IRS website at *http://www.irs.gov/businesses/corporations/article/0,,id=221533,00.html*.

[44] *See id.*

[45] *See id.*

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from the detail of the schedule, the IRS is requiring taxpayers to identify which tax items are potentially controversial and which are not. This exercise itself can involve mental thoughts and impressions regarding the anticipation of litigation and taxpayers may well view the Schedule UTP as encroaching on their protected zone of privacy for strategic litigation planning. Again, it will take only one taxpayer to put the issue before a court to challenge the requirement for certain information in the schedule.

Similarly, the courts may address again the question of whether any work product protection is waived as a result of sharing the information with the outside auditors. As noted above, at the appeals level only the D.C. Circuit in *Deloitte* has expressly held that there is no waiver, but multiple trial courts have done so. It should be noted that the IRS recently announced a revision to its policy of restraint to provide that ''[i]f a document is otherwise privileged under the attorney-client privilege, the tax advice privilege in section 7525 of the Code, or the work product doctrine and the document was provided to an independent auditor as part of an audit of the taxpayer's financial statements, the [IRS] will not assert *during an examination* that privilege had been waived by such disclosure.'' [46] This new policy of restraint only applies ''during an examination.'' Thus, once a case advances beyond the examination phase and once it becomes docketed with a court, that policy is no longer in effect, and the IRS could at that stage raise the issue of waiver. While this new policy might alleviate some headaches during the examination phase, taxpayers would be wise not to alter their behavior in reliance on this new policy. The IRS is not likely to acquiesce in the D.C. Circuit decision, and thus taxpayers outside the D.C. Circuit that are confronted with discovery disputes may see the government arguing for a waiver of protections.

CONCLUSION

Deloitte is an important case for taxpayers, not only because it has buoyed the previously dour mood of taxpayers and tax professionals on the merits of work product protection for tax accrual workpapers, but also because it has righted the ship in terms of the legal analysis. *Textron* should be viewed as an aberration, and hopefully other courts will embrace the analysis of the D.C. Circuit. The battle over tax accrual workpapers is likely not over, but *Deloitte* revives the hope that the ''right'' answer will ultimately prevail.

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[46] *Request for Documents Provided to Independent Auditors, Policy of Restraint and Uncertain Tax Positions* at 2, Ann. 2010-76, which can be found on the IRS website at *http://www.irs.gov/businesses/corporations/article/0,,id=221533,00.html* (emphasis added).

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