

EMERGING ISSUES IN PRIVILEGE AND TRIAL PREPARATION IN TAX LITIGATION AND BEYOND

November 15, 2012

Court of Federal Claims Judicial Conference

Judge Marian Horn
U.S. Court of Federal Claims

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Attorney–Client Privilege

▶ Necessary Elements:

- (1) Where **legal advice** of any kind is sought
- (2) from a professional legal adviser in his capacity as such
- (3) the **communications relating to that purpose**
- (4) made in confidence
- (5) **by or to the client**
- (6) are protected from disclosure by himself or by the legal adviser
- (7) **unless the protection is waived.**

Attorney–Client Privilege: Recent Developments

- ▶ *Schlicksup v. Caterpillar, Inc.*, 2011 WL 4007670 (C.D. Ill. Sept. 9, 2011)
 - Court held that documents containing **tax analysis and tax-saving proposals** prepared by PwC were not protected by the attorney–client privilege primarily because they were not communications to or from attorneys.
 - Court added in *dicta*: “even if these communications were made by a lawyer, many of them would still not be protected by the attorney–client privilege. Proposals on tax-saving strategies and the creation, analysis and implementation of business ideas to bolster the bottom line are not confidential communications of legal advice.”

Attorney–Client Privilege: Recent Developments

- ▶ *Oracle America, Inc. v. Google, Inc.*, 2011 WL 3794892 (N.D. Cal.).
 - Court held that email from Google software engineer to management employees, copying in–house counsel, was not privileged because it concerned a business deal (negotiation of a license) and did not “further the provision of legal service.”
 - “When attempting to demonstrate that an internal communication involving in–house counsel deserves privileged status, a party ... must make a ‘clear showing’ that the ‘speaker’ made the communication for the purpose of providing legal advice.” (quoting *Chevron–Texaco Corp.*, 241 F.Supp.2d 1065 (N.D. Cal. 2002)).

Kovel/Relationships

- ▶ *Kovel* does not create a new privilege but extends the attorney–client privilege to communications with consultants (e.g., accountants) when the communications are made “in confidence for the purpose of obtaining legal advice from a lawyer.” *United States v. Kovel*, 296 F.2d 918 (2d Cir. 1961).
- ▶ “In order for the privilege to apply, the third party's presence must be necessary, or at least highly useful, for the effective consultation between the client and the lawyer which the privilege is designed to permit.” *Banco do Brasil, S.A. v. 275 Washington Street Corp.*, 2012 WL 1247756 (D. Mass.); *see also Ceglia v. Zuckerberg*, 2012 WL 3527935 (W.D.N.Y.).

Kovel Relationships: Recent Developments

- ▶ *Panasonic Communications Corp. of America v. United States*, 2011 WL 1760028 (Fed Cl.).
 - Court applied the *Kovel* doctrine in holding that the IRS's confidential communications with its consultant on scientific issues were protected by the attorney-client privilege.
 - Court found that the consultant was the "client's agent":
 - The consultant was engaged to develop an analytical procedure for detecting ozone-depleting chemicals (ODCs) in commercial products and to assist the IRS in taxpayers audits for ODCs through lab testing.
 - IRS counsel relied upon the consultant's technical expertise and knowledge of laboratory findings in advising regarding the applicability of the excise tax.
 - Court indicated that it may revisit the issue of waiver if the IRS identified the consultant as a testifying expert.

Kovel/Relationships: Recent Developments

- ▶ *Gucci Am., Inc. v. Guess?, Inc.*, 271 F.R.D. 58 (S.D.N.Y. 2010)
 - Court found that certain communications between Gucci America and a non-attorney employee of Gucci's Italian affiliate ("in-house intellectual property counsel") were privileged.
 - As the attorney's agent, the employee "coordinated Gucci and [the affiliate's] global efforts to assemble evidence supporting claims in both [the U.S. and Italy]. He communicated with [the attorney] at every step of his investigation and continued each phase solely at [the attorney's] instruction."
 - To the extent the employee performed an investigative role at the direction of the affiliate's attorney, he acted as the attorney's agent in preparation for litigation and his communications with Gucci America were not protected by the attorney-client privilege under the *Kovel* doctrine.
 - However, to the extent that, prior to the investigation, and before the hiring of an attorney, the employee did not act at the direction of an attorney, the *Kovel* doctrine did not apply, and his communications with other employees were not protected by the attorney-client privilege.

Kove/ Relationships: Recent Developments

- ▶ *Ravenell v. Avis Budget Group, Inc.*, 2012 WL 1150450 (E.D.N.Y.)
 - Management consultant retained by in-house counsel
 - (1) created “an online platform for the dissemination and collection of questionnaires for” an internal audit, and
 - (2) summarized the collected data in a chart and based on the criteria provided by the attorneys “made a preliminary assessment of whether the individuals ... met the requirements of an exempt position” under the Fair Labor Standards Act.
 - Court held that the latter function waived the attorney–client privilege:
 - There was no *Kove/* relationship with the company, since their “preliminary assessments neither improved the comprehension of the communications between the attorney and the client, nor provided advice outside the general expertise of attorneys yet essential to the ability of defendant’s lawyers to provide legal service.”

Kovel/Relationships: Practical Tips

- The engagement letter should clearly establish that the consultant is engaged to assist the attorney in rendering legal advice and the specific role of the consultant.
- The consultant should identify communications as being prepared at the request of legal counsel.
- The consultant should segregate files related to the *Kovel* engagement and keep them confidential.
- The consultant should send separate invoices for the *Kovel* engagement.

FRE 502: Limitations on Waiver

- ▶ FRE 502 was signed into law September 19, 2008.
- ▶ FRE 502 does not modify the substantive federal and state laws concerning the attorney–client privilege.
- ▶ FRE 502 limits the circumstances under which the **intentional disclosure of privileged documents** in a federal proceeding or to a federal agency will effect a subject–matter waiver.
- ▶ FRE 502 also limits the consequences of an **inadvertent disclosure of privileged documents**, assuming reasonable precautions were taken.

FRE 502(a) and (b): Limitations on Waiver

- ▶ **Rule 502(a):** Disclosures made either
 - In a federal proceeding, or
 - To a federal office or agency (including the IRS)waive related, undisclosed communications or information, in federal or state proceedings, **only if**
 - The waiver is **intentional**,
 - The disclosed and undisclosed communications or information concern the **same subject matter**, *and*
 - They **ought in fairness to be considered together**.
- ▶ **Rule 502(b):** Inadvertent disclosures *do not* operate as a waiver in federal or state proceedings, *as long as*
 - The holder of the privilege or protection took **reasonable steps to prevent disclosure**; *and*
 - The holder promptly took **reasonable steps to rectify the error**, including (if applicable) following FRCP 26(b)(5)(B) (return, sequester, or destroy any copies; do not use or disclose the information, etc.).

FRE 502(a): Recent Cases

▶ “Ought in Fairness” Test:

- *San Francisco Residence Club, Inc. v. Baswell–Guthrie*, 2012 WL 4339316 (N.D. Ala.): Court held that subject–matter waiver had been effected; fairness dictated that communications related to the “post closing clean–up” of transactions ought to be considered with communications regarding the transactions’ planning and execution.
 - *Hall v. U.S.*, 2012 WL 3822163 (S.D. W.Va.): Intentional disclosure of privileged attorney–client communications by criminal defendant in connection with motion to set aside or correct sentence on the basis of ineffective assistance of counsel effected a subject–matter waiver of all related attorney–client communications.
 - *Century Aluminum Co. v. AGCS Marine Ins. Co.*, 2012 WL 3731561 (N.D. Cal.): Disclosure by insurer of attorney–client communication related to favorable report by weather expert in insurance dispute over loss incurred during sea travel waived privilege over all communications with counsel regarding the weather investigation.
- ▶ The Federal Circuit held that the “fairness balancing test” under FRE 502(a) applied to disclosure of confidential communications made during settlement negotiations in contemplation of a federal proceeding. *Wi–LAN, Inc. v. Kilpatrick Townsend & Stockton LLP*, 684 F.3d 1364 (Fed. Cir. 2012) (remanding for reconsideration of the scope of waiver).

FRE 502(b): Recent Cases

- ▶ Court held that a disclosure was “inadvertent” for purposes of Rule 502(b) where the party failed to recognize the privileged nature of the document at the time of production.
 - The protected nature of the documents was only “readily apparent ... if the reader understands the context of [them]: when they were created and by whom. Since ... counsel did not acquire that information until after production, the disclosure was inadvertent.” *Valentin v. Bank of New York Mellon Corp.*, 2011 WL 1466122 (S.D.N.Y.).
- ▶ “Mistaken production due to an unexpected software glitch that occurred despite the use of standard discovery software falls squarely on the inadvertent side of the divide between intentional disclosure under Rule 502(a) and unintentional disclosure under Rule 502(b).” *Datel Holdings Ltd. v. Microsoft Corp.*, 2011 WL 866993 (N.D. Cal.).

FRE 502(b): Recent Cases

- ▶ Since the three-part analysis of Rule 502(b) draws on prior common law analysis of waiver, pre-Rule 502 case law regarding waiver remains relevant.
- ▶ *Sikorsky Aircraft Corp. v. U.S.*, 2012 WL 4018026 (Fed. Cl.): In applying FRE 502(b) to the deliberative process privilege, court found privilege had been waived when the document was inadvertently disclosed during discovery, and the Government failed to assert the privilege until 15 months after producing the document and 10 months after realizing that it may be privileged.
- ▶ *Inhalation Plastics, Inc. v. Medex Cardio-Pulmonary, Inc.*, 2012 WL 3731483 (S.D. Ohio): Requesting party sought to depose three witnesses based on documents obtained during production. Producing party then asserted attorney-client privilege over emails sent or received by those witnesses. Court applied a five-factor test (pre-dating FRE 502) in finding that a subject-matter waiver had been effected under FRE Rule 502(b):
 1. The reasonableness of precautions taken in view of the extent of document production;
 2. The number of inadvertent disclosures;
 3. The magnitude of the disclosure;
 4. Measures taken to mitigate the damage of the disclosures; and
 5. The overriding interests of justice.

FRE 502: IRS Limited Waiver Agreements

- ▶ IRS Notice CC-2009-023, August 3, 2009, “Federal Rule of Evidence 502.”
- ▶ IRS Office of Chief Counsel has advised that FRE 502 rendered “moot” its prior practice of entering into limited waiver agreements with taxpayers.
- ▶ Any agreements regarding privilege waiver and the application of FRE 502 must be pre-approved by the Associate Chief Counsel (Procedure & Administration).

FRE 502(c)–(e): Limitations on Waiver

- ▶ **FRE 502(c):** Disclosures made in state proceedings **do not operate as a waiver** in a later federal proceeding *as long as either*.
 - The disclosure **would not be a waiver** under FRE 502 had it occurred in a federal proceeding, **or**
 - It is **not a waiver under the law of the state** where disclosure occurred.
- ▶ **FRE 502(d):** A *federal* court may **order** that a disclosure in litigation before it **does not operate as a waiver**, in which case the order is binding on any other *federal or state* proceeding.
- ▶ **FRE 502(e):** **Agreements** on the effect of a disclosure in a federal proceeding **are only binding to the parties** to the agreement.

FRE 502(d): Recent Development

- ▶ *Potomac Elec. Power Co. (PEPCO) v. U.S.*, 2012 WL 4127637 (Fed. Cl. 2012).
 - In tax refund litigation, PEPCO moved for:
 - 1. An FRE 502(d) order preventing any disclosure of privileged documents from operating as a waiver, and
 - 2. Approval of a “claw-back” arrangement, allowing the parties to retract any inadvertent disclosures of privileged material, without a court order, if requested within ten business days of the party becoming aware of the disclosure.
 - PEPCO had not yet decided whether it would rely on an “advice-of-counsel” defense to the asserted tax liability, which would result in the subject-matter waiver.

FRE 502(d): Recent Development

▶ Court in *PEPCO* held that:

- 1. FRE 502(d) orders apply almost exclusively to *inadvertent* disclosures.
 - “[A]lthough FRE 502(d) is not expressly limited to unintentional disclosures, the context of the Rule as a whole makes clear that this provision exists to ‘close the loop’ on the protections that the Rule extends to [unintentional] disclosure.”
 - There are “certain limited circumstances in which a purposeful disclosure” will be protected from waiver by a FRE 502(d) order, including a mandatory disclosure pursuant to FRCP 26(a).
- 2. The proposed claw-back agreement was too broad, because “the more specific portion of PEPCO’s proposal, the ten-days-from-discovery grace period, appears to swallow the more general one, nominally requiring that the party take ‘reasonable precautions’ in order to reap the benefit of the proposed order.”

FRE 502(d): Recent Development

- ▶ Court in *PEPCO* issued a protective order that:
 - Emphasizes that disclosure must be inadvertent to be protected,
 - Requires the producing party to “promptly” notify opposing counsel of an inadvertent disclosure (presumably in fewer than 10 days),
 - Requires the receiving party to notify opposing counsel of “potentially privileged or protected” material, and
 - Requires a court order for claw-back to be effective.

I.R.C. § 7525

- ▶ I.R.C. § 7525 extends the protections of the attorney–client privilege to communications between any “federally authorized tax practitioner” and his/her client in noncriminal matters before the IRS or in court against the United States.

- ▶ A federally authorized tax practitioner is any individual “authorized under Federal law to practice before the Internal Revenue Service.” I.R.C. § 7525(a)(3)(A).
 - Practitioners can be outside or in–house tax advisors. *See U.S. v. Eaton Corp.*, 2012 WL 3486910 (N.D. Ohio) and *United States v. Textron Inc.*, 577 F.3d 21 (1st Cir. 2009).

- ▶ In order to be protected, the communications must be in the nature of legal advice.
 - “Information provided for the purpose of preparing a tax return is not privileged, nor are communications between the preparer and client for the simple purpose of preparing the return.” *U.S. v. PricewaterhouseCoopers, LLP*, 2012 WL 1517687 (D. Minn.).

I.R.C. § 7525: Tax Shelter Exception

- ▶ The tax practitioner privilege does not apply to communications “in connection with the promotion of the direct or indirect participation of the person in any tax shelter.” I.R.C. § 7525(b).
- ▶ What constitutes “promotion”?
 - *Valero Energy Corp. v. United States*, 569 F.3d 626 (7th Cir. 2009): Court defined “promotion” as any written communication of a plan or arrangement a significant purpose of which is to avoid or evade federal taxes, even if the plan is not mass marketed or cookie cutter in nature.
 - “Promotion” does not include “documents that merely inform a company about such schemes, assess such plans in a neutral fashion, or evaluate the soft spots in tax shelters that a company has used in the past.” *Id.*
 - *Salem Financial, Inc. v. U.S.*, 102 Fed. Cl. 793 (2012): Court held that promotion does not include a tax advisor’s communications regarding a transaction that the taxpayer has already engaged in.
 - Court found that taxpayer waived protection by asserting a reasonable cause defense to penalties.

Work Product Doctrine

- ▶ Fed. R. Civ. Proc. 26(b)(3): A party may *not* obtain discovery of documents and tangible things:
 - Prepared *in anticipation of litigation or for trial*;
 - By or for a party or by or for that party's representative;
 - Except upon a showing of a substantial need and undue hardship.
- ▶ Heightened level of protection for “core” or “opinion” work product.
- ▶ A waiver of work product occurs when a party discloses material “in a way inconsistent with keeping it from the adversary.” *Evergreen Trading, LLC v. United States*, 80 Fed. Cl. 122 (2007).

Work Product: What Is “Litigation”?

- ▶ *United States v. Eaton Corp.*, 2012 WL 3486910 (N.D. Ohio): In IRS summons enforcement proceeding, court held that taxpayer demonstrated that its “ ‘adversarial administrative proceedings’ with the IRS [were not] just routine audits but, instead, [had] been ongoing and contentious such that documents generated ... in connection with the IRS’s examination ... [were] aptly characterized as prepared ‘in anticipation of litigation.’ ”
- ▶ *United States v. Roxbury*, 457 F.3d 590 (6th Cir. 2006): “[A] document prepared in anticipation of dealing with the IRS ... may well have been prepared in anticipation of an administrative dispute and this may constitute ‘litigation’ within the meaning of Rule 26.” (internal quotations omitted).
- ▶ *Deseret Management Corp. v. United States*, 76 Fed. Cl. 88 (2007): “In general, a proceeding is adversarial when evidence or legal argument is presented by parties contending against each other with respect to legally significant factual issues.”
- ▶ *Fidelity International Currency Advisor A Fund LLC v. United States*, 2008 WL 4809032 (D.C. Mass. 2008): “Where ... advice is given in anticipation of litigation with the IRS, or a tax audit or investigation, the advice may ... be subject to the protections of the work product doctrine.”
- ▶ *But see United States v. Baggot*, 463 U.S. 476 (1983): Court held that an IRS civil audit is not “preliminary to or in connection with a judicial proceeding” for purposes of current Federal Rule of Criminal Procedure 6(e)(3)(E)(i).

Work Product: What Is “Litigation”?

- ▶ Not all administrative proceedings constitute “litigation,” but “litigation” may be anticipated during the IRS audit.
 - *Consolidated Edison Co. of N.Y., Inc. v. United States*, 90 Fed. Cl. 228 (2009):
 - The taxpayer did not anticipate litigation until it became clear that the dispute could not be resolved through administrative proceedings.
 - “[N]ot ... all audits by the IRS, or even extensive, IRS administrative proceedings to challenge results of those audits ... will necessarily lead to litigation....”
 - “Although there is a point in time during interaction with the IRS that it is reasonable to conclude that litigation is likely or should be anticipated, that determination will differ in every case.”

Work Product Doctrine: Recent Cases

- ▶ *Gulf Group General Enterprises Co. v. United States*, 98 Fed. Cl. 647 (2011).
 - Court held that testimony by Government's civilian attorney was not protected by the attorney-client privilege or work product.
 - The testimony sought from the attorney concerned her role in providing facts to assist the Government's contracting officer in his decision regarding claim against United States challenging termination of an Army contract.
 - The attorney-client privilege did not apply, as the civilian attorney's role was fact-finding, not the provision of legal advice.
 - The work product doctrine did not apply as there was no anticipation of litigation.

Work Product Doctrine: Recent Cases

- ▶ *Gulf Group General Enterprises Co. v. United States*, 96 Fed. Cl. 64 (2011).
 - Court held that verbatim transcript of plaintiff's pre-deposition interview of Army contracting officer (who received plaintiff's initial claim of improper contract termination) was prepared in anticipation of litigation and protected by work product.
 - Transcript constituted opinion work product, and defendant did not satisfy the higher standard of "undue hardship" required to discover opinion work product. (quoting *In re Seagate Tech, LLC*, 497 F.3d 1360 (Fed.Cir. 2007) and Rule 26(b)(3)(A) of the Rules of the United States Court of Federal Claims).
 - Court held that because the Government had numerous opportunities to interview the witness, and the witness was in fact in federal custody (in prison), the requisite showing of undue hardship had not been made.

Tax Accrual Workpapers and the Work Product Doctrine

- ▶ The IRS defines tax accrual work papers (TAWs) broadly as:
 - “those audit workpapers, whether prepared by the taxpayer, the taxpayer’s accountant, or the independent auditor, that relate to the tax reserves for current, deferred and potential or contingent tax liabilities, however classified or reported on audited financial statements, and...footnotes disclosing those tax reserves on audited financial statements.” I.R.M. 4.10.20.2(2).

- ▶ Announcement 2010–76, I.R.B. 2010–41, September 24, 2010.
 - In the event that a taxpayer reveals a privileged document to an independent auditor for purposes of complying with FIN 48 requirements, the IRS will not assert during an examination that the disclosure waived privilege arising from the attorney–client privilege, the I.R.C. § 7525 tax advice privilege or the work product doctrine.

 - This policy:
 - Applies to requests for documents made during the administrative process of determining a taxpayer’s correct tax liability.
 - Does not apply if the taxpayer claims the benefit of a “listed transaction.”

Tax Accrual Workpapers and the Work Product Doctrine

- ▶ Federal courts are divided on whether TAWs are prepared “in preparation for litigation” and are protected as work product.
- ▶ *United States v. Textron Inc.*, 577 F.3d 21 (1st Cir. 2009)
 - TAWs were not work product, since they would have been prepared even in the absence of any imminent threat of litigation.
- ▶ *Regions Fin. Corp. v. United States*, 2008 WL 2139008 (N.D. Ala. 2008).
 - TAWs were work product, and taxpayer correctly withheld (or redacted) documents in response to an IRS subpoena.
 - “Were it not for anticipated litigation, [taxpayer] would not have to worry about contingent liabilities and would have no need to elicit opinions regarding the likely results of litigation.”

Tax Accrual Workpapers and the Work Product Doctrine

- ▶ *Salem Fin., Inc. v. U.S.*, 102 Fed. Cl. 793 (2012): Court did not address whether TAWs were protected, as it held that “Plaintiff waived any work product protection that may have applied to its tax reserve documents by relying on PwC’s advice as a defense to IRS penalties.”
- ▶ *Wells Fargo & Co. v. U.S.* (D. Minn.) (pending): Court expected to address whether TAWs prepared in order to meet the accounting requirements of FIN 48 are protected by the work product doctrine.
- ▶ Practice Tip: Segregate privileged/protected documents from documents prepared to comply with accounting or regulatory requirements.

Rule 26: 2010 Amendments

- ▶ Identical changes to FRCP 26 and RCFC 26.
- ▶ Rule 26: Experts that are “retained or specially employed to provide expert testimony in the case” or those “whose duties as the party’s employee regularly involve giving expert testimony” are **required to provide a written report** along with the party’s initial disclosures, which include, *inter alia*, opinions, qualifications, and compensation.
- ▶ **Previous Rule 26(a)(2)(B):** The written report must include a statement of “**data or other information considered by**” the expert in forming his/her opinion for the case.
- ▶ **Revised Rule 26(a)(2)(B):** The written report need only disclose “**the facts or data considered by**” the expert witness.

Rule 26 Amendments: Rule 26(a)(2)(B)

- ▶ The Advisory Committee Notes to Revised Rule 26(a)(2)(B):
 - “The refocus on ‘facts or data’ is meant to limit disclosure to material of a factual nature by excluding theories or mental impressions of counsel.”
 - “[T]he intention is that ‘facts or data’ be interpreted broadly to require disclosure of any material considered by the expert, from whatever source, that contains factual ingredients.”
- ▶ “The [2010] amendments are meant to alleviate the perceived uncertainty and rising costs associated with attorneys’ limited interactions with their retained experts as a result of court opinions allowing discovery of an expert’s draft reports and of all communications with counsel.” *Republic of Bjorkman*, 2012 WL 12755 (D. Colo.).

Rule 26 Amendments: Rules 26(b)(4)(B)–(C)

- ▶ Amendments also added current Rules 26(b)(4)(B) and (C).

- ▶ Rule 26(b)(4)(B):
 - Protects drafts of an expert’s written report as work product.
 - Protects drafts of an expert’s “summary of ... facts and opinions” (if expert is not required to provide a written report).

- ▶ Rule 26(b)(4)(C):
 - Protects communications between the attorney and the expert as work product.
 - Three Exceptions:
 - Communications relating to the expert’s compensation,
 - Identification of facts or data provided by the attorney that the expert considered in forming his/her opinion, and
 - Identification of assumptions provided by the attorney that the expert relied on in forming his/her opinion.

Rule 26 Amendments: Recent Developments

- ▶ *In re the Application of the Republic of Ecuador*, 280 F.R.D. 506 (N.D.Cal. 2012).
 - A “draft report” for purposes of Rule 26(b)(4)(B):
 - Must be authored (or co-authored) by the expert or his/her assistants; *and*
 - A draft of a report ultimately submitted in the underlying litigation.
 - Draft worksheets created by the expert or his/her assistants for use in the expert report were protected as “drafts.”
 - Various notes, letters, memoranda and outlines created by expert and his/her assistants were not “drafts” for purposes of Rule 26(b)(4)(B) protection.
 - Copying an attorney on a communication among employees of the party and the expert does not automatically protect the communication as work product. The communication must “include the theories or mental impressions of counsel.”

Rule 26 Amendments: Recent Developments

- ▶ *In re Application of Republic of Ecuador.*
- ▶ Discoverable “facts/data considered, reviewed or relied upon for the development, foundation, or basis” of the expert testimony include:
 - Testing of material involved in litigation,
 - Notes of any such testing,
 - Communications with anyone other than the party’s counsel about the opinions expressed, or
 - Alternative analyses, testing methods, or approaches to the issues proffered, whether or not considered in forming the opinions expressed.

Rule 26: Recent Developments

- Rule 26(b)(4)(C), by its terms, only protects communications between an attorney and an expert providing a written report.
- Courts have held that Rule 26(b)(4)(C) does not apply to communications with non-reporting experts. *In re the Application of the Republic of Ecuador*, 280 F.R.D. 506 (N.D. Cal. 2012) (“Nor does protection exist for communications between an expert witness and a consulting expert”); *See also Republic of Ecuador v. Bjorkman*, 2012 WL 12755 (D. Colo. 2012).
- One court has applied Rule 26(b)(4)(C) to protect communications between an attorney and a non-reporting expert. *PACT XPP Technologies, AG v. Xilinx, Inc.*, 2012 WL 1205855 (E.D. Tex.).

Rule 26 Amendments: Recent Developments

- ▶ *Fialkowski v. Perry*, 2012 WL 2527020 (E.D. Pa.)
 - A party's business records and explanations thereof provided to her accountant expert witness for the purpose of assisting her attorney in litigation constituted "facts and data" considered and "assumptions" relied on by the expert and were not protected by work product.
 - Providing work product protection would not serve the amendment's purpose of protecting counsel's mental impressions, rather than those of the party or the witness.
- ▶ *In re Abestos Products Liability Litigation (No. VI)*, 2011 WL 6181334 (E.D. Pa.)
 - Information provided by attorneys to the diagnosing doctors of plaintiffs in asbestos litigation regarding the plaintiffs' "exposure, medical, and smoking histories" constituted "facts or data" considered by the witnesses and was not protected by work product.

Duty to Preserve Electronically Stored Information

- ▶ A duty to preserve evidence “arises when the party has notice that the evidence is relevant to litigation or when a party should have known that the evidence may be relevant to future litigation.”
Zubulake v. UBS Warburg LLC, 220 F.R.D. 212 (S.D.N.Y. 2003).
- ▶ Courts have held that if a party claims that litigation was reasonably foreseeable as of a certain date for purposes of seeking work product protection, they are conceding that a duty to preserve ESI arose no later than that date. *Siani v. SUNY Farmingdale*, 2010 WL 3170664 (E.D.N.Y.).

Duty to Preserve Electronically Stored Information

- ▶ IRS Notice CC-2012-017, “Update to Procedures for Complying with E-Discovery Obligations” (Sept. 13, 2012):
- ▶ “When the Service is or will be a plaintiff ... a notice of a litigation hold should be issued no later than when a manager within the Office of Chief Counsel” authorizes suit.
- ▶ “When the Service is a defendant ... the litigation hold procedures ... should be begun ... generally within twenty one business days after a filed petition or complaint is received by a manger for assignment to an attorney.”
- ▶ The Service requires a litigation hold of “any nonprivileged matter that is relevant to any party’s claim or defense” by reference to FRE 401.

Duty to Preserve Electronically Stored Information

- ▶ IRS Notice CC-2012-017:
- ▶ “In Tax Court cases, it is important that our attempts to cooperate and any lack of cooperation by the opposing party ... be documented ... Written documentation describing our attempts ... may be needed to support or defend against a motion to compel.”
- ▶ Counsel should discuss whether metadata is “clearly relevant,” and if not, oppose the production of metadata.
- ▶ “Courts have imposed a duty on parties to offer ... assistance in suggesting possible search terms, especially when a party knows that certain search terms are more likely to locate relevant material....”
- ▶ *See also* “Reissuance of Guidance for Complying with E-Discovery Rules,” IRS Memorandum SBSE-025-0911-080 (Sept. 16, 2011).

Duty to Preserve ESI: Possible Sanctions

- ▶ *Zubulake v. UBS Warburg LLC*, 229 F.R.D. 422 (S.D.N.Y. 2004): Court granted adverse instruction sanction and costs for spoliation of ESI.

- ▶ A party seeking sanctions on the basis of spoliation must show:
 1. The party having control over the evidence had an obligation to preserve it at the time it was destroyed,
 2. The records were destroyed with a culpable state of mind, and
 3. The destroyed evidence was relevant to the party's claim or defense such that a reasonable trier of fact could find that it would support that claim or defense.

Duty to Preserve ESI: Possible Sanctions

- ▶ *Micron Technology, Inc. v. Rambus Inc.*, 645 F.3d 1311 (Fed. Cir. 2011)
 - “When litigation is reasonably foreseeable is a flexible–fact specific standard ... [but] not so inflexible as to require litigation [to] be imminent, or probable without significant contingencies.”
 - Rambus routinely litigated against parties that adopted a technology that competed with its patented technology.
 - Rambus’s policy was to regularly destroy documents until litigation was actually commenced.
 - Court found litigation was reasonably foreseeable no later than the date the Vice President of Intellectual Property drafted an outline of the plan to sue manufacturers of competing technology
 - Litigation was anticipated even though no specific litigants had been identified; when drafted, the outline noted that the “proper litigants will be obvious” when it is time to litigate.

Duty to Preserve ESI: Possible Sanctions

▶ *Micron Technology, Inc. v. Rambus:*

- Federal Circuit vacated the trial court's sanction of dismissal.
- Dismissal is a “harsh sanction,” that “should not be imposed unless there is clear and convincing evidence of both **bad-faith spoliation** and **prejudice** to the opposing party.”
 - “The fundamental element of **bad faith spoliation** is advantage-seeking behavior by the party with superior access to information necessary for the proper administration of justice.”
 - **Prejudice** to the opposing party requires a showing that the spoliation “materially affects the substantial rights of the adverse party and is prejudicial to the presentation of his case.” (*quoting Wilson v. Volkswagen of Am., Inc.*, 561 F.2d 494, 504 (4th Cir. 1977)).
 - If it is shown that the spoliator acted in bad faith, they bear a “heavy burden” of showing that the spoliation did not cause prejudice. (*quoting Anderson v. Cryovac, Inc.*, 862 F.2d 910 (1st Cir. 1988)).

Duty to Preserve ESI: Possible Sanctions

- ▶ *K-Con Bldg. Systems, Inc. v. U.S.*, 2012 WL 3744672 (Fed. Cl.):
- ▶ The level of culpability to impose sanctions remains “an open question.”
- ▶ Court found that where the Coast Guard’s witness destroyed relevant paper documents:
 - The Government’s conduct was at least willful and grossly reckless,
 - The witness’s conduct was grossly negligent, and
 - This culpability justified exclusion of the Government’s evidence and an award of costs.
- ▶ In choosing a spoliation sanction, “the court must consider:
 - The degree of culpability attributable to the government,
 - The amount of prejudice to plaintiff, and
 - The court’s need to manage its docket and maintain the integrity of the judicial process.”
- ▶ Court interpreted *Micron* as introducing a “prejudice” requirement for spoliation generally, not just dismissal.

Protective Orders: Recent Developments

- ▶ *Bayer–Onyx v. United States*, No. 08–693 (W.D. Pa.).
 - Government obtained production of “confidential and proprietary information, trade secrets, [and] commercial information,” over which Bayer sought a protective order in research tax credits case.
 - Government proposed a protective order that allowed documents to be disclosed to other Government agencies if the information indicated “a violation or potential violation of law – criminal, civil or regulatory in nature.”
 - Bayer sought to require court review before disclosure to other Government agencies, arguing that sensitive trade secrets might be released inadvertently upon a FOIA request or otherwise.
 - Court adopted the Government’s proposed language, noting that any agency to which Bayer’s information was disclosed would be similarly bound by the protective order.

Protective Orders: Recent Developments

- ▶ *Russian Recovery Fund Ltd. v. United States*, 2012 WL 3985966 (Fed. Cl. Sept. 11, 2012).
 - Plaintiff trust claimed the IRS's final partnership administrative adjustment was barred by the statute of limitations.
 - Court ordered that several documents submitted in connection with motion to dismiss be unsealed, with redactions only as to social security numbers, employee identification numbers, and some names.
 - Court held that the party seeking to seal the documents must show "compelling reasons supported by specific factual findings ... [to] outweigh the general history of access and the public policies favoring disclosure." (*quoting Kamakana v. City & Cnty. of Honolulu*, 447 F.3d 1172 (9th Cir. 2006)).
 - Court cited *Lugosch v. Pyramid Co. of Onondaga*, 435 F.3d 110 (2d Cir. 2006) for the principle that a heightened showing is necessary to justify redaction in the context of a dispositive motion.

Circular 230 Disclaimer

- ▶ This presentation may not be used to avoid tax penalties under U.S. law.
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