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Sarah Seifert Mallett

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WORK-PRODUCT DOCTRINE—THE FIRST CIRCUIT FURTHER CONFUSES AN EXISTING CIRCUIT SPLIT IN *UNITED STATES V. TEXTRON INC.*

*Sarah Seifert Mallett**

IN *United States v. Textron Inc.*, the Court of Appeals for the First Circuit held that the work-product doctrine does not protect tax accrual work papers prepared by lawyers from an IRS summons connected with an investigation of a taxpayer's tax liability.¹ The First Circuit's decision incorrectly applied the precedent established in *Maine v. U.S. Department of the Interior*,² misinterpreted the text and policy of Federal Rule of Civil Procedure 26(b)(3), and overlooked the widespread consequences of further fragmenting an already divided interpretation of the phrase "in anticipation of litigation."

In preparing public financial statements, Textron, an "aerospace and defense conglomerate, with well over a hundred subsidiaries," calculates reserves to account for contingent tax liabilities, which include estimates of potential liability if the IRS challenges the positions in its tax returns.³ The work papers used in this process include spreadsheets, emails, and notes that reflect items in the tax return that could result in additional taxes, the dollar amount subject to dispute, and a percentage estimate of the IRS's chance of success in possible litigation.⁴ In 2003, the IRS conducted an audit of Textron's corporate income tax liability for the years 1998–2001.⁵ After examining the 2001 returns, the IRS believed that Textron Financial Corporation, a Textron subsidiary, engaged in sale-in, lease-out transactions, which the IRS lists as a potential tax shelter subject to abuse by taxpayers.⁶

Textron refused to comply with an administrative summons issued by the IRS seeking all the work papers generated for the 2001 tax year and

* J.D. Candidate 2011, Southern Methodist University Dedman School of Law; B.B.A. 2006, the University of Texas at Austin. The author would like to thank her husband and family for their love and support.

1. 577 F.3d 21, 31-32 (1st Cir. 2009) (en banc), *petition for cert. filed*, 78 U.S.L.W. 3375 (U.S. Dec. 24, 2009) (No. 09-750).

2. 298 F.3d 60 (1st Cir. 2002).

3. *Textron*, 577 F.3d at 22-23.

4. *Id.* at 23.

5. *Id.*

6. *Id.* at 23-24.

related work papers created by Ernst & Young, Textron's outside accountant.⁷ The contents of these work papers included disputable tax items and amounts, percentage estimates of a successful challenge by the IRS, and applicable reserve amounts.⁸ The IRS then brought an enforcement action in federal district court in Rhode Island.⁹ In defense, Textron asserted that the summons lacked a legitimate purpose, that the attorney-client and tax practitioner privileges applied, and that the papers were protected under the work-product doctrine.¹⁰ The district court agreed with Textron's position that the work-product doctrine protected the work papers and found they were prepared "because of"¹¹ the prospect of litigation and, consequently, the court denied the IRS's petition for enforcement.¹² The district judge noted that although work-product privilege does not apply to documents created within the ordinary course of business irrespective of litigation, the work papers, which contained dubious items identified by attorneys and accountants, estimated probabilities of litigation outcomes, and calculations of tax reserves would not have been prepared "but for" the anticipated possibility of litigation.¹³ Textron witnesses testified during trial that tax reserve calculations would not have been necessary without the possibility of litigation; therefore, the purpose behind generating the work papers was to ensure Textron was adequately prepared for future litigation.¹⁴

On appeal, a divided panel upheld the district court's decision, but the court later granted the IRS's petition for rehearing en banc and vacated the panel decision.¹⁵ The First Circuit initially looked to the origins of the work-product privilege in the Supreme Court's decision in *Hickman v. Taylor* and the later codification in Federal Rule of Civil Procedure 26(b)(3) for guidance on the triggering language and intent behind the protection of documents.¹⁶ Focusing on the protection for tax work papers specifically, the First Circuit discussed rulings from the only two circuits that have addressed the issue—its own ruling in *Maine v. U.S. Department of the Interior* and the Fifth Circuit's ruling in *United States v. El Paso Co.*¹⁷ Relying primarily on its direct precedent in *Maine*, histori-

7. *Id.* at 24.

8. *Id.* at 24-25. In some instances, the probability of IRS success was estimated at 100%. *Id.* at 25.

9. *Id.* at 24.

10. *Id.* Evidence showed that Textron's tax department attorneys were centrally involved with the preparation and generation of the work papers in question, and outside counsel advised Textron on tax reserve requirements. *Id.*

11. The district court followed the "because of" test adopted by the First Circuit in *Maine v. Department of the Interior*, 298 F.3d 60, 68 (1st Cir. 2002). *United States v. Textron Inc.*, 507 F. Supp. 2d 138, 149-50 (D.R.I. 2007).

12. *Textron*, 577 F.3d at 25-26.

13. *Id.* at 25-26; *Textron*, 507 F. Supp. 2d at 150.

14. *Textron*, 577 F.3d at 28.

15. *Id.* at 26.

16. *Id.* at 26-27 (citing FED. R. CIV. P. 26(b)(3); *Hickman v. Taylor*, 329 U.S. 495, 510-11 (1947)).

17. *Id.* at 30 (citing *Maine v. Dep't of the Interior*, 298 F.3d 60, 70 (1st Cir. 2002); *United States v. El Paso Co.*, 682 F.2d 530, 543-44 (5th Cir. 1982)).

cal context of the work-product doctrine, and underlying prudential concerns, the court reasoned that the work-product doctrine is aimed at protecting work prepared for and used in litigation and that IRS access to Textron's work papers is essential to the public interest.¹⁸

The court determined that the text of Rule 26(b)(3), Supreme Court doctrine, direct precedent in *Maine*, and public policy judgments applied together answer the legal questions involving work-product protection of tax accrual work papers.¹⁹ In referencing these sources, the court's decision turned on its interpretation of the key language in the codified rule—"prepared in anticipation of litigation"—which it determined meant "prepared for use in" litigation.²⁰

First, the court noted that the phrase "prepared in anticipation of litigation" as used in Rule 26(b)(3) is illustrative of *Hickman*'s reasoning and should be the key language applied to the present case.²¹ In dissecting this language, the court emphasized that historical English privilege guided *Hickman* and the development of Rule 26(b)(3).²² The court found that, historically, the focus of work-product protection has been on materials prepared for use in litigation and that the English privilege invoked by *Hickman* protects documents that assist in litigation.²³ The court also relied in part on English precedent to argue that the decisive phrase used in Rule 26(b)(3)—"prepared in anticipation of litigation or for trial"—refers only to material prepared for and with the purpose of assisting in litigation.²⁴ The court reasoned that Textron's primary and only purpose in preparing the tax accrual work papers was to establish reserves for its financial statements and not for use in possible litigation; thus, the papers were not entitled to work-product protection.²⁵ To bolster this finding, the court relied on the theory that "any experienced litigator" would concede that tax accrual work papers are not case preparation material.²⁶

Turning next to direct precedent, the First Circuit indicated that *Maine* "straightforwardly" explained that Textron's tax accrual work papers were not entitled to protection because they were "documents that are prepared in the ordinary course of business or would have been created in essentially similar form irrespective of the litigation."²⁷ The court also drew a parallel with the Fifth Circuit's decision in *United States v. El Paso Co.*, which denied protection for work papers based on a "primary purpose" test, by highlighting that the work papers' "sole function" in *El Paso* was to support financial statements and finding that this, too, was

18. *Id.* at 30-32.

19. *Id.* at 28.

20. *Id.* at 29-32.

21. *Id.* at 27.

22. *Id.* at 29 (citing *Hickman v. Taylor*, 329 U.S. 495, 510 n.9 (1947)).

23. *Id.* at 29-30; see *Hickman*, 329 U.S. at 510-11.

24. *Textron*, 577 F.3d at 29.

25. *Id.* at 27.

26. *Id.* at 28.

27. *Id.* at 30 (quoting *Maine v. Dep't of the Interior*, 298 F.3d 60, 70 (1st Cir. 2002)).

the only purpose of Textron's papers.²⁸ Finally, relying heavily on prudential concerns, the First Circuit supported granting the IRS's summons because of the important function of detecting and disallowing abusive tax shelters, the threat involved in underpaying taxes, and the public interest in collecting revenue.²⁹ The First Circuit stated that "tax collection is not a game" and suggested that the practical problems confronting the IRS in discovering tax reporting errors outweighed any unfairness to Textron.³⁰

In dissent, Judges Torruella and Lipez protested that the majority's decision blatantly ignored and abandoned *Maine's* "because of" test and formulated a new "prepared for use in" test that is contrary to *Maine, United States v. Adlman*, which first articulated the "because of" test, and the text and policy of Rule 26(b)(3).³¹ Referencing *Adlman*, which the *Maine* court followed, the dissent argued that the intentional inclusion of the phrase "in anticipation of" in the text of Rule 26(b)(3) sweeps broadly and does not limit work-product protection to documents prepared to aid in, use in, or assist in litigation.³² The dissent also criticized the majority's policy analysis because it focused on the IRS's arduous and important task of revenue collection, but it ignored that the information accompanying the work papers would enable the IRS to identify the exact amount Textron would be willing to spend in litigation on each disputed item.³³ This, according to the dissent, was contrary to the underlying policy of the work-product doctrine stated in *Hickman*, which, as explained in *Adlman*, protects the attorney's litigation strategies, appraisal of likely success, and feasibility of settlement.³⁴ The dissent concluded that not only did the majority err in its interpretation, analysis, and application of the law, but under the "because of" test, the proper conclusion is that Textron's work papers are protected by the work-product doctrine.³⁵

The First Circuit's decision in *Textron* misuses the court's decision in *Maine* and misinterprets the language and intent of Rule 26(b)(3). The majority misconstrues language from *Hickman, Maine*, and Rule 26(b)(3) to develop a new "prepared for use in litigation" test while departing from the inherent purpose and broad scope of the precedential "because of" test. Moreover, the opinion offers biased public policy arguments to support the IRS's position without addressing the underlying intent and policy of the work-product privilege doctrine. Furthermore, the First Cir-

28. *Id.* (quoting *United States v. El Paso Co.*, 682 F.2d 530, 543-44 (5th Cir. 1982)).

29. *Id.* at 31-32.

30. *Id.* at 31.

31. *Id.* at 32 (Torruella, J., dissenting) (citing *United States v. Adlman*, 134 F.3d 1194, 1202 (2d Cir. 1998)).

32. *Id.* at 34 (citing *Adlman*, 134 F.3d at 1198-99).

33. *Id.* at 36-37.

34. *Id.* at 36 (citing *Adlman*, 134 F.3d at 1200); *see also Hickman v. Taylor*, 329 U.S. 495, 510-11(1947) (stating that it is essential that a lawyer be free to prepare his legal theories and strategies without undue interference).

35. *Textron*, 577 F.3d at 32, 38.

cuit disregards the future consequences of this ruling, its impact on a variety of practices and lawyers, and the additional split it has created in the interpretation of a well-established and important evidentiary doctrine.

As the dissent correctly points out, the majority's fatal flaw is in its reasoning and its deceptive reliance on the *Maine* opinion and the text of Rule 26(b)(3) in concluding that the tax accrual work papers are not entitled to work-product protection.³⁶ *Maine* rejected the "primary purpose" test, which stated that dual-purpose documents must be "prepared primarily for litigation purposes" to be entitled to work-product protection.³⁷ Instead, the First Circuit in *Maine* relied on the Second Circuit's rationale in *Adlman* and adopted the "because of" test for determining work-product protection for dual-purpose documents because it is a broader formula and is more consistent with the text and purpose of Rule 26(b)(3).³⁸ In *Textron*, the majority failed to even acknowledge *Maine*'s adoption of the "because of" test or the purpose behind endorsing it and, instead, highlighted a more discrete finding: that there is no work-product protection for "documents that are prepared in the ordinary course of business or . . . created in essentially similar form irrespective of the litigation."³⁹ Then the court deceptively stated that *Maine* "applies straightforwardly" because the work papers were prepared in the "ordinary course of business," disregarding the essential "because of" test and the critical district court evidence attesting that the work papers were only prepared *because of* possible litigation and would not have been prepared *but for* litigation.⁴⁰ In bypassing the "because of" test, the court subtly adopted a use-related test, which is comparable to the Fifth Circuit's "primary purpose" test specifically repudiated by the First Circuit.⁴¹ The First Circuit held that the tax accrual work papers were not afforded protection because their "only purpose" was to prepare financial statements and there was no evidence that the papers were "prepared for use in" or served a useful purpose in conducting litigation.⁴² To discredit district court testimony and enforce this novel "use" standard, the court boldly purported that "every lawyer" knows the "touch and feel" of documents used in preparation for a lawsuit and that "any experienced litigator" would know the work papers were not for use as case preparation.⁴³ The most troubling aspect of the majority's reasoning—aside from the fact that *Maine* does not reference any use-related test—is that it plainly con-

36. See *id.* at 32-34.

37. *Maine v. U.S. Dep't of the Interior*, 298 F.3d 60, 66-68 (1st Cir. 2002).

38. *Id.* at 68 (citing *Adlman*, 134 F.3d at 1197-99) (holding that the policies underlying the work-product doctrine suggest that protection should not be denied to a dual-purpose document that "analyzes expected litigation merely because it is prepared to assist in a business decision").

39. See *Textron*, 577 F.3d at 30 (majority opinion) (quoting *Maine*, 298 F.3d at 70) (internal quotation marks omitted).

40. See *id.*; *United States v. Textron Inc.*, 507 F. Supp. 2d 138, 150 (D.R.I. 2007).

41. See *Textron*, 577 F.3d at 26-30.

42. *Id.* at 30.

43. See *id.* at 28-30.

flicts with *Maine*, which explicitly comports with the *Adlman* decision that documents are protected if they have been prepared “because of the prospect of litigation” and not because they might “assist in” or be used in litigation.⁴⁴

Furthermore, the majority’s reliance on the English roots of the work-product doctrine seems archaic, and its resulting interpretation of the language and intent in Rule 26(b)(3) is distorted. The majority cites English privilege referenced in *Hickman* to argue that documents must serve the purpose of assisting in any actual or anticipated litigation to be afforded work-product protection.⁴⁵ Nearly twenty-five years after *Hickman* and decades later than the earliest English privilege, however, the work-product doctrine was codified in Rule 26(b)(3) with the intent to preserve the privacy of an attorney’s work, a concern essential to adversarial legal process.⁴⁶ Rule 26(b)(3) contains the intentional phrase “in anticipation of litigation,” which sweeps broadly to uphold the policies and principles behind its codification and is alone sufficient to afford *Textron*’s work papers protection.⁴⁷ The text of Rule 26(b)(3) does not limit its scope of protection to documents prepared strictly for use in or to assist in litigation.⁴⁸ To hold otherwise would jeopardize a lawyer’s ability to “prepare his legal theories and plan his strategy,”⁴⁹ which the dissent correctly points out is at stake in this case because of the explicit litigation strategies and statistics listed in the work papers.⁵⁰

The problems inherent in the court’s interpretation of Rule 26(b)(3) and its reliance (or lack thereof) on *Maine* pale in comparison to the sweeping consequences that this case has for tax litigation, discovery disputes, and corporate attorneys. The First Circuit’s new “prepared for use in litigation” test further compounds the issues created by the existing circuit split regarding the interpretation of “in anticipation of litigation” through the use of the “primary purpose” test or the “because of” test. The dissent accurately stated that in “straining to craft a rule favorable to the IRS . . . the majority has thrown the law of work-product protection into disarray.”⁵¹ The First Circuit’s narrow reading of the work-product doctrine will likely have implications beyond tax accrual work papers. Dual-purpose documents are increasingly relied on not only in tax but in many other types of litigation. Under *Textron*, corporations may now

44. See *Maine*, 298 F.3d at 68 (citing *United States v. Adlman*, 134 F.3d 1194, 1197-98 (2d Cir. 1998)).

45. *Textron*, 577 F.3d at 29 (citing *Hickman v. Taylor*, 329 U.S. 495, 510 n.9 (1947)).

46. See *Adlman*, 134 F.3d at 1198-99; FED. R. CIV. P. 26(b)(3) advisory committee’s notes.

47. See *Adlman*, 134 F.3d at 1198-99.

48. *Id.* at 1198.

49. *Hickman*, 329 U.S. at 511.

50. See *Textron*, 577 F.3d at 36 (Torruella, J., dissenting); see also *United States v. Textron Inc.*, F. Supp. 2d 138, 142-43 (detailing the “hazards of litigation percentages” included in *Textron*’s work papers).

51. See *Textron*, 577 F.3d at 43.

hesitate to record any financial liability on the books for fear that it will be discoverable.

The problem with the First Circuit's opinion in *United States v. Textron Inc.* is not in its holding, but rather its flawed, incomplete, and misguided reasoning. The majority should have acknowledged the "because of" test embraced in *Maine* instead of adopting a new use-related test. Then the court should have applied the "because of" test to the facts and testimony of the case rather than relying on what "experienced lawyers" know and do.⁵² Moreover, the court mistakenly relied on antiquated English privilege and misinterpreted the intent and text of *Hickman* and Rule 26(b)(3). The court offered an unbalanced policy argument that solely supported the IRS's position and overlooked the purpose of the work-product doctrine and its foundation in our legal system. If allowed to stand, this ruling will further fragment the issue of work-product protection for dual-purpose documents in an already divided area of law.

52. *See id.* at 28-30 (majority opinion).

