The Scope of Work Product in Massachusetts Tax Controversies

Posted on Mar. 28, 2011

By and

David J. Nagle and Sarah D. Wellings are Boston-based tax attorneys with Sullivan & Worcester LLP.

* * * * *

Massachusetts Democratic Gov. Deval Patrick's supplemental budget bill includes an apparently modest proposal authorizing the Department of Revenue to apply rules of criminal procedure when compelling testimony and the disclosure of books and records in civil tax examinations. The governor's proposal deserves attention because it could have far-reaching consequences for individual and business taxpayers that might otherwise rely on non-attorneys for assistance in weighing the pros and cons of various tax planning alternatives and their attendant litigation risks.

Background

Two years ago, the Massachusetts Supreme Judicial Court concluded that the work product doctrine protects from disclosure communications between in-house corporate counsel and the outside tax accountants whom counsel consulted regarding the structuring of a sale of stock mandated by an antitrust consent judgment.[1]

The case arose from U S WEST's 1996 purchase of Continental Cablevision. In response to the Department of Justice's civil antitrust action alleging that the acquisition would lessen competition in the telecommunications market, U S WEST agreed to divest its interest in a particular Continental subsidiary.[2] U S WEST expected the sale to have significant tax consequences, so its tax department director turned to in-house counsel in U S WEST's law department for advice regarding options for structuring the stock sale.[3]

In-house counsel considered various "planning opportunities" for the transaction, but being unfamiliar with Massachusetts tax law, and being concerned that the Massachusetts Department of Revenue might challenge the "appropriateness of the chosen vehicle" for the stock sale, he sought advice from two Arthur Andersen partners who had previously worked for the DOR.[4] In-house counsel discussed with the Andersen partners various options for structuring the stock sale and their associated risks of litigation.[5] He also asked the Andersen partners to prepare a memorandum discussing the "pros and cons of the various planning opportunities and the attendant litigation risks," which they did.[6]

Three years later, during the course of an audit of the stock sale, the DOR issued an administrative summons under a statute giving it broad authority to take testimony and require the production of books, papers, and records concerning any matter within its official purview.[7] U S WEST withheld the Andersen memorandum, arguing in part that it was protected from disclosure under the work product doctrine.[8] The DOR then filed a complaint to compel production of the Andersen memorandum, believing it would "reveal detailed information about why the transaction was structured as it was."[9]

The dispute eventually reached the Massachusetts Supreme Judicial Court, which concluded that the Andersen memorandum was protected from disclosure by the work product doctrine, although not by the attorney-client privilege.[10] The work product doctrine, the court said, enhances the vitality of an adversary system of litigation by establishing a "zone of privacy for strategic litigation planning . . . to prevent one party from piggybacking on the adversary's preparation."[11] In other words, the work product doctrine preserves the fairness of the adversary system by insulating a party's work in anticipation of litigation from intrusion, inference, or borrowing by other parties.[12]

In concluding that the Andersen memorandum was protected from disclosure under the work-product doctrine, the Supreme Judicial Court never considered the DOR's argument that the doctrine's "zone of privacy" is limited to work done by attorneys, and that the DOR was authorized to piggyback on the strategic planning of non-attorney consultants by compelling their testimony and the production of their papers. The commissioner waived that argument by raising it too late, the court concluded.[13] Now, however, the governor has proposed to revive the DOR's litigation position vis-à-vis all taxpayers by asking the legislature to enact it into law.

The Governor's Proposal

Tucked into the governor's supplemental budget bill is an amendment to the statute that authorizes the commissioner of revenue to take testimony and issue summonses regarding any matter within the official purview of the DOR. The statute currently provides as follows:

Such summonses shall be served in the same manner as summonses for witnesses in criminal cases issued on behalf on the commonwealth, and all provisions of law relative to summonses in such cases shall, so far as applicable, apply to summonses issued hereunder.[14]

The governor proposes to amend the second clause, so that "all laws relative to summonses in [criminal] cases, including but not limited to the attorney work product rules applicable under criminal procedure, [would] apply to summonses issued" by the commissioner.[15]

The commissioner may regard the governor's proposal as merely clarifying existing law, but the rule governing summonses to witnesses in criminal cases does not actually "include" the "work product rules applicable" to parties in the criminal discovery context.[16] The governor's proposal thus raises perplexing interpretive questions by conflating different rules of criminal procedure. As a practical matter, however, the commissioner's litigation position regarding the Andersen memorandum leaves no doubt concerning her interpretation of the governor's proposal and what any "clarification" could mean for taxpayers.

In her brief to the Supreme Judicial Court, the commissioner argued that the rules of criminal procedure applied not just to the service of summonses, but also their scope. Specifically, the commissioner argued that the statute giving her summons authority limits "work product to 'core' mental processes of opposing counsel but not reports of outside experts."[17] The Andersen memorandum was therefore not protected work product, the commissioner argued, because the criminal rules do "not shield from discovery reports prepared by non-attorneys, even when such reports are prepared with an eye toward litigation."[18] As the commissioner put it, the Andersen memorandum was "prepared by an outside accounting firm, not by an attorney or the attorney's legal staff," and therefore the memorandum did not contain the type of core work product that the criminal rules protect, namely, "the mental processes of an attorney."[19]

The governor's proposal could potentially strengthen the commissioner's litigation position and drive up litigation costs by purporting to circumscribe the work product protection available to taxpayers, and to authorize the commissioner to conduct civil tax examinations "on wits borrowed from the adversary."[20] The commissioner would presumably argue that the amendment limits the work-product protection available to taxpayers in Massachusetts solely to the core mental impressions of attorneys, whereas memorandums prepared by non-attorney tax experts do not qualify as protected work product.[21]

Observations

As a policy matter, the narrower definition of work product under the rules of criminal procedure is intended to promote a policy of liberal discovery in criminal cases.[22] Whatever the merits of this rule in a criminal discovery context, there is no good reason why summons enforcement actions in civil tax cases should be subject to a work product rule that represents such a substantial departure from the broader work product doctrine applied in federal courts and other state courts.[23] Circumscribing the work-product rule applicable to summons enforcement cases based on a criminal discovery rule makes particularly little sense because the traditional work product rule applies in tax cases that reach the Appellate Tax Board.[24]

The governor's proposed amendment could discourage taxpayers from seeking tax advice from tax experts who happen not to be attorneys. As the Supreme Judicial Court explained when rejecting U S WEST's argument that the Andersen memorandum was protected by the attorney-client privilege, taxpayers and their in-house counsel are "free to seek advice on Massachusetts tax law from a Massachusetts attorney, where the privilege would apply," but if in-house counsel instead puts a client "potentially at risk" by seeking "advice on Massachusetts tax law from Massachusetts accountants, where no privilege applies," that is simply the inevitable consequence of the absence of a privilege for accountants.[25] In the absence of a work product protection for accountants under the governor's proposal, taxpayers and in-house counsel who consult with outside accounting firms in anticipation of litigation could likewise put themselves "potentially at risk." Taxpayers and in-house counsel who have done so in connection with transactions during still-open years could even find themselves "potentially at risk" retroactively.

In the chorus of initiatives intended to speed the state's economic recovery and cultivate an attractive business environment, the governor's proposal to treat all taxpayers like criminal defendants is politically tone-deaf. The proposal also deserves greater transparency than the governor has invited by couching it as a modest proposal for an "administrative" or "technical" amendment within a supplemental budget bill for which he has requested prompt and favorable consideration by the Massachusetts Senate and House of Representatives.

Interestingly, the governor's supplemental budget bill would also give the commissioner an additional 60 days to identify and correct an abatement notice, if the commissioner discovers that she has abated a tax "improperly because of departmental clerical error or for any other reason."[26] This proposal also warrants attention, because the 60-day review period could effectively extend the statutory time period for making assessments, enabling the commissioner to resurrect assessments without regard to the procedural safeguards that usually precede them.[27] In effect, abatements would all become subject to a 60-day waiting period, and if the commissioner discovers a clerical error or changes her mind "for any other reason" during that period, then any prior abatement approval will be annulled.[28] Before this proposal becomes law, taxpayers who have no comparable opportunity to "take a mulligan" should understand why the commissioner should be held to a lower standard of care than they are.

FOOTNOTES

[1] *Comm'r of Revenue v. Comcast Corp.*, 453 Mass. 293 (2009). (For the decision, see *Doc 2009-5276* or *2009 STT 45-14*.)

[2] *Id.* at 296.

[3] *Id.*

[4] *Id.* at 296-299.

[5] *Id.* at 299.

[6] *Id.*

[7] *Id.* at 301. *See* G.L. c. 62C, section 70. ("The commissioner may take testimony and proofs under oath with reference to any matter within the official purview of the department of revenue, and in connection therewith may issue summonses and require the attendance and testimony of witnesses and the production of books, papers, records, and other data.")

[8] *Comcast*, 453 Mass. at 301.

[9] *Id.* at 300.

[10] *Id.* at 311 and 319.

[11] *Id.* at 311-312 (quoting *United States v. Adlman*, 68 F.3d 1495, 1501 (2d Cir. 1995)).

[12] *Id.* at 311 (quoting *Ward v. Peabody*, 380 Mass. 805, 817 (1980)).

[13] *Id.* at 312-313.

[14] G.L. c. 62C, section 70.

[15] *See* "An Act Making Appropriations for the Fiscal Year 2011 to Provide for Supplementing Certain Existing Appropriations and for Certain Other Activities and Projects," section 7(L), *available at* http://www.mass.gov/Agov3/docs/Legislation/01262011JanuarySuppBudget.pdf (the "bill"); HB 37, 187th Gen. Ct. section 7(L) (Mass. 2011), *available at* http://www.malegislature.gov/bills/187/house/h00037.

[16] *See* Mass. R. Crim. P. 17 (providing for summonses to witnesses) (Rule 17). *See also* Brief of The New England Cable & Telecommunications Association, Inc. as Amicus Curiae at 29, *Comm'r of Revenue v. Comcast Corp.*, 453 Mass. 293 (2009) (SJC-10209), *available at* http://ma-appellatecourts.org/?brief=SJC-10209_04_Amicus_New_England_Cable_Brief.pdf (NECTA amicus brief) (noting that the "'provisions of law' in the Rules of Criminal Procedure that actually deal with the summonsing of witnesses" are in Rule 17, which "says nothing at all about the work product doctrine").

[17] *See* Brief of the appellant at 2, *Comm'r of Revenue v. Comcast Corp.*, 453 Mass. 293 (2009) (SJC-10209), *available at* http://ma-appellatecourts.org/?brief=SJC-10209_01_Appellant_Comm_Of_Revenue_Brief.pdf (DOR brief). *See also Commonwealth v. Paszko*, 391 Mass. 164, 187-188 (1984) ("Rule 14 of the Massachusetts Rules of Criminal Procedure preserves the 'core' of the work product doctrine by 'shelter[ing] the mental processes of the attorney,' but, unlike the Federal doctrine, favors liberal discovery by excluding statements of witnesses other than the defendant and nonlegal reports from the definition of work product.")

[18] DOR brief at 34-35.

[19] *Id.* at 35.

[20] *Hickman v. Taylor*, 329 U.S. 495, 516 (1947) (Justice Robert H. Jackson, concurring) (explaining that the work product rule is intended to ensure that one side does not "perform its functions without wits or on wits borrowed from the adversary."). *See also Fleet National Bank v. Tonneson & Co.*, 150 F.R.D. 10, 14-15 (D. Mass. 1993) ("The substantive content of work product, particularly so-called opinion work product . . . is almost certainly of no legitimate use to an opponent. While it would no doubt provide a tremendous tactical advantage to an adversary to be able to pry into the 'mental impressions, conclusions, opinions, or legal theories of an attorney or other representative of a party concerning the litigation,' Fed.R.Civ.P. 26(b)(3), a competent adversary will never need access to such information in order to prepare and present his or her case effectively.") (citations and footnote omitted).

[21] DOR brief at 34-35 (arguing that "[t]he work product protection available under Mass. R. Crim. P. 14(a)(5) is 'more limited' than the work product protection applicable under Mass. R. Civ. P. 26(b)(3)" because the criminal rule "shields from discovery only 'those portions of records, reports, correspondence, memoranda, or internal documents . . . which are only the legal research, opinions, theories, or conclusions of the adverse party or its attorney and legal staff' [and] does *not* shield from discovery reports prepared by non-attorneys, even when such reports are prepared with an eye toward litigation.") (citations omitted) (emphasis in original).

[22] *Commonwealth v. Durham*, 446 Mass. 212, 221, 222 (2006), quoting *Commonwealth v. Paszko*, 391 Mass. at 188.

[23] DOR brief at 34 n.21 (acknowledging that Rule 14 of the Massachusetts Rules of Criminal Procedure "thus represents a substantial departure from the broader work product doctrine applied

in federal courts and other state courts."). *See also* Reply Brief of the Appellant at 8-9, *Comm'r of Revenue v. Comcast Corp*., 453 Mass. 293 (2009) (SJC-10209), *available at* http://ma-appellatecourts.org/?brief=SJC-10209_02_Appellant_Revenue_Reply_Brief.pdf (acknowledging that "the federal tax summons enforcement statute, 26 U.S.C. § 7602 . . . contains no similar incorporation of criminal standards.").

[24] G.L. c. 58A, section 11; 831 CMR sections 1.25, 1.37. *See also Commonwealth v. Lampron*, 441 Mass. 265, 269 (2004) (indicating that the Massachusetts rule of criminal procedure governing summonses for witnesses is "not a discovery tool" and "is reserved for evidentiary materials that are likely to be admissible at hearing or at trial."); NECTA amicus brief at 35-36. ("As the Commissioner's argument implicitly acknowledges, many, if not most, of her investigations will, if anything, lead to a proceeding before the Appellate Tax Board, not a criminal prosecution. The Commissioner would not have the same access to work product in such a proceeding that she would have in a criminal case, either in discovery or at a hearing. . . . It does not make sense to give the Commissioner access to materials that could not be used in such a proceeding and might well taint the proceeding at a stage where the end result of her investigation remains unknown.")

[25] *Comcast*, 453 Mass. at 311.

[26] *See* the bill, section 7(J) (proposing to amend G.L. c. 62C, section 37 by providing that "[i]f the commissioner determines that any tax has been abated improperly because of departmental clerical error or for any other reason, he may, in his discretion, correct such error within 60 days after the erroneous abatement notice. At his option, the commissioner shall either continue to consider the previously pending application or shall deny the application. In either case, the commissioner shall notify in writing the person to whom the abatement was issued of the erroneous abatement and shall state whether the commissioner is still considering the application or whether the application is denied. When the commissioner corrects an erroneous abatement by providing the notice described in this section, the assessment that was the subject of the erroneous abatement shall continue in effect as if the erroneous abatement had not occurred.").

[27] For a case in which the commissioner was prohibited from resurrecting an assessment after abating it, see *IDC Research, Inc. v. Comm'r of Revenue*, ATB 2009-399, 2009-504 (Docket C267868 et seq., Apr. 17, 2009), *available at* http://www.mass.gov/Eoaf/docs/atb/2009/09p399.doc.

[28] One can imagine the DOR's revocation notice: "On December 23, 2011, an Abatement Approval Notice was issued in response to your Application for Abatement filed for tax year 2008. Please be advised that said notice was issued prematurely and in error. Your Application for Abatement is denied. We apologize for any inconvenience or confusion that this error may have caused. Very truly yours, the Customer Service Bureau."

END OF FOOTNOTES