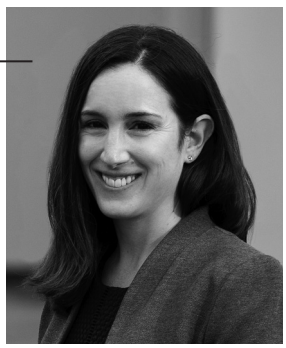
UNDERSTANDING KEY DISTINCTIONS IN CALIFORNIA STATE AND FEDERAL PRIVILEGE LAW

Written by Rachel Naor* & Michael Lundholm*



Rachel Naor

Michael Lundholm

Litigants often propound discovery requests seeking production of attorney invoices, retainer agreements, and client tax returns. Whether or not these sensitive documents must be produced — or whether they can be withheld as privileged — depends on the forum and whether state or federal privilege law applies. This article seeks to assist attorneys who litigate in California state and federal courts by identifying the key differences in how state and federal privilege law applies to these types of documents.

LEGAL INVOICES

In the Ninth Circuit, invoices from an attorney to a client containing "information on the identity of the client, the case name for which payment was made, the amount of the fee, and the general nature of the services performed" are not privileged and are thus subject to disclosure. (*Clarke v. Am. Com. Nat. Bank* (9th Cir. 1992) 974 F.2d 127, 130.) But invoices can be privileged if the entries provide information beyond the general nature of the services performed and include descriptions that reveal specific research, client motive, or litigation strategy, such as billing entries revealing that an attorney researched particular areas of law. (*Ibid.*)

Meanwhile, the California Supreme Court in *Los Angeles County Board of Supervisors v. Superior Court* (2016) 2 Cal.5th 282, 300 concluded that invoices as a whole are not categorically privileged, but they are privileged if they are sought in an active matter. The court reasoned that invoices for active and ongoing litigation are categorically privileged because of the risk that information in those invoices could expose legal consultation and strategy. (*Id.* at p. 297.) In reaching this conclusion, the court noted that the entire invoice is privileged — rather than just the billing descriptions — because fee totals in ongoing matters could reveal swings in spending, and such swings could expose legal strategy. (*Ibid.*) On the other hand, the court found that invoices for dormant or closed matters are only privileged where those invoices reveal the substance of legal consultation or strategy. (*Id.* at p. 298.) The court noted that the significance of information that was once privileged may lose its privileged status after the conclusion of the case because it no longer provides insight into litigation strategy or legal consultation. (*Ibid.*) For example, the court noted that a cumulative fee total for a long-completed matter would likely not reveal the substance of legal consultation in the same way it would for an ongoing legal matter.

RETAINER AGREEMENTS

California and federal law diverge in their treatment of retainer agreements. The Ninth Circuit has repeatedly held that under federal law, retainer agreements are not protected by the attorney-client privilege or work product doctrine. (See, e.g., *United States v. Blackman* (9th Cir. 1995) 72 F.3d 1418, 1424 ["As a general rule, client identity and the nature of the fee arrangement between attorney and client are not protected from disclosure by the attorney-client privilege."].) An exception to this general rule exists, however, where a retainer agreement contains privileged information, such as a party's motive in bringing suit or litigation strategy, beyond the typical scope of what is included in a retainer agreement. (See, e.g., *Stanley v. Bayer Healthcare LLC* (S.D.Cal. Nov. 16, 2011) No. 11cv862–IEG (BLM)) 2011 WL 5569761 at p. *4 [conducting in camera review in light of plaintiff's claim that the retainer agreement contained privileged communications including information pertaining to the scope and nature of the representation].)

On the other hand, California courts treat retainer agreements as protected by the attorney-client privilege. Under Business and Professions Code section 6149, a "written fee contract shall be deemed to be a confidential communication" as set forth in Evidence Code section 952. (See also *Dietz v. Meisenheimer & Herron* (2009) 177 Cal.App.4th 771, 786 ["Among those communications subject to the duty of confidentiality and the attorney-client privilege, is a written fee contract between an attorney and a client."].)

TAX RETURNS

In federal court, tax returns "do not enjoy an absolute privilege from discovery." (*Premium Serv. Corp. v. Sperry & Hutchinson Co.* (9th Cir. 1975) 511 F.2d 225, 229.) But the Ninth Circuit recognizes a public policy against unnecessary disclosure of tax returns, which arises from the need to encourage taxpayers to file complete and accurate returns. (*Ibid.*) Thus, federal courts generally apply a two-pronged test designed to balance the liberal scope of discovery and the policy favoring the confidentiality of tax returns. Under this test, "[f]irst, the court must find that the returns are relevant to the subject matter of the action. Second, the court must find that there is a compelling need for the returns because the information contained therein is not otherwise readily obtainable." (*Farber & Partners, Inc. v. Garber* (C.D.Cal. 2006) 234 F.R.D. 186, 190-191.) Under this test, courts deny access to tax returns where the party seeking the returns can obtain the information from less intrusive means. (See, e.g., *Aliotti v. Vessel SENORA* (N.D.Cal. 2003) 217 F.R.D. 496, 498 [holding that although plaintiff's tax returns were relevant to assess lost earnings (among other things), defendant failed to meet its burden of establishing a compelling need as defendant could use interrogatories and other means of discovery to obtain the information].)

On the other hand, California courts treat tax records, both state and federal, as privileged. (*Schnabel v. Superior Court* (1993) 5 Cal.4th 704, 718-721.) The privilege applies broadly to all types of tax records, including income taxes, employment taxes, sales taxes, and estate taxes, and thus it is generally difficult for a litigant to obtain the opposing party's tax returns in litigation. (*Sav-on Drugs, Inc. v. Superior Court* (1975) 15 Cal.3d 1, 6.) But the privilege is not absolute, as the California Supreme Court has recognized three narrow exceptions: (1) When there is an intentional waiver of the privilege; (2) when the gravamen of the lawsuit is so inconsistent with the continued assertion of the taxpayer's privilege as to compel the conclusion that the privilege has in fact been waived; or (3) where a public policy greater than that of confidentiality of tax returns is involved. (*Weingarten v. Superior Court* (2002) 102 Cal.App.4th 268, 274.) The scope of each exception is beyond the scope of this article, but can be reviewed in the following cases: *Fortunato v. Superior Court* (2003) 114 Cal.App.4th 475, 479 (discussing intentional waiver and public policy exceptions); *Wilson v. Superior Court* (1976) 63 Cal. App.3d 825, 830 (discussing second exception).

WHETHER STATE OR FEDERAL LAW APPLIES

Given the differences in state and federal law, litigants must be able to determine which law applies to the discovery in their case. For cases in California state court, the application is straightforward, as California state law applies. But federal cases are more complicated. While federal law governs a case venued in federal court based on federal subject matter jurisdiction, when a case is in federal court on diversity grounds and the evidence goes to state law causes of action, California state law applies to privilege issues. (See Fed. Rules Evid., rule 501; see also *Bozzuto v. Cox, Castle & Nicholson, LLP* (C.D.Cal. 2009) 255 F.R.D. 673, 676 [state law applies to privilege claims to cases in

federal court based purely on diversity of citizenship where only state law causes of action are raised].)

What if the case is in federal court, but there are both state law and federal claims? Then the court must determine whether the evidence sought is relevant to both the state and federal claims. If it is, federal law will apply. (*In re TFT-LCD (Flat Panel) Antitrust Litig.* (9th Cir. 2016) 835 F.3d 1155, 1159 [determining that federal law applied because the evidence sought related to both federal and state law claims].) If, on the other hand, the evidence sought is only relevant to the state law claims, the court will still apply state law. (See, e.g., *Platypus Wear, Inc. v. K.D. Co., Inc.* (S.D.Cal. 1995) 905 F.Supp. 808, 812 [determining that state law applied to privilege claims where the case was "primarily a diversity case, despite the existence of one federal law claim in Defendants' counterclaim," and the disputed evidence went only to state law issues].)

CONCLUSION

If you litigate in California, there is a good chance you will encounter discovery requests for the documents described in this article. Understanding the nuances of California and federal privilege law and how they apply to these types of requests will be helpful in navigating discovery in both your state and federal cases.

**Rachel Naor is a shareholder and Michael Lundholm is an associate at London & Stout P.C., a litigation boutique in Oakland.*

THE NEW ETHICS COMMITTEE OF THE CALIFORNIA LAWYERS ASSOCIATION

The California Lawyers Association has created a new Ethics Committee to help ensure CLA members stay up-to-date with their ethical obligations. This new advisory group will create educational content, comment on proposed rule changes, write advisory opinions on emerging ethical issues, and issue ethics alerts and reminders to CLA members.