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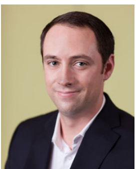
Proposed E-Discovery Rule To Test Document Retention Policies



by Matthew J. Peck

The management of electronically stored information ("ESI") is becoming an increasingly prominent concern for companies, large and small, and their attorneys tasked with managing litigation. Given the exponential growth in the volume of ESI over the past two decades, it should come as no surprise that there has been a parallel increase in the amount of litigation related to the management (and mismanagement) of ESI under the Federal Rules of Civil Procedure ("Rule(s)").

This article provides a general outline of best practices for companies and their attorneys related to the identification and preservation of relevant ESI through internal document retention policies and the issuance of litigation hold letters. The article first highlights some recent case law that illustrates the potential scope and severity of sanctions imposed on parties who fail to adequately identify, collect and preserve relevant ESI under the Rules. The article then discusses the proposed amendments to Rule 37(e), which, if adopted would provide a uniform process for the courts to analyze spoliation in the ESI-context and resolve the existing split of authority regarding the culpability required to impose the harshest, case-dispositive sanctions under the current Rules.

I. ESI PRESERVATION – LITIGATION HOLD LETTERS AND DOCUMENT RETENTION POLICIES

A litigation hold letter is broadly defined as a written directive to all potentially relevant personnel of a company that they are obligated to preserve relevant documents and ESI in anticipation of future litigation.[1] The affirmative obligation to institute litigation holds stems from a party's common law duty to avoid spoliation, which is broadly defined as the destruction or significant alteration of evidence or the failure to preserve property for another's use as evidence in pending or reasonably foreseeable litigation.[2]

Once a company reasonably anticipates litigation, it must suspend its routine document retention and destruction policy and put in place a litigation hold to ensure that relevant evidence, including ESI, is preserved.[3] That said, a company's obligation to preserve relevant evidence exists whether or not an opposing party has requested that party to issue a litigation hold.[4]

Companies and their attorneys should be aware that the events which provide notice of impending litigation and "trigger" a company's preservation obligations take many forms. Sometimes the event "triggering" the obligation to issue a litigation hold is obvious, such as a letter threatening litigation. Other times, however, the "triggering" event is more subtle.[5]

Attorneys preparing litigation hold letters should keep in mind the following general principles when doing so:

- **Put It In Writing –** Although it is permissible to issue litigation holds orally, it is better to issue a litigation hold letter in writing. If disputes arise regarding the adequacy of the preservation efforts undertaken, a written litigation hold letter provides a clear record of the steps taken to preserve relevant evidence.
- **Identify What is Relevant –** The scope and parameters of the litigation hold must be driven by the documents, including ESI, which are relevant to the facts and circumstances likely to be at issue. That said, attorneys should ***not*** simply advise the custodians of the records to preserve "all relevant evidence" without providing any guidance on what this means in the context of the litigation.[6]
- **Assume It Is Discoverable –** Although litigation holds are generally not discoverable, some jurisdictions have ordered their discovery where the party was able to show that spoliation of evidence was likely.[7] Therefore, attorneys should prepare the litigation hold letter keeping in mind that it may be viewed by opposing counsel or a judge.
- **Understandable to Non-Attorneys –** Because the litigation hold letter outlines steps that non-attorneys must take to preserve relevant ESI, it should be understandable to non-attorneys and should not be written in "legalese."
- **Proportionate to Size of Litigation –** The scope of the litigation hold letter should be proportionate to the scope of the anticipated or pending litigation.
- **Identify Litigation Holds Already in Place –** Be aware that pre-existing holds in related litigation may trigger greater preservation obligations. For example, if a company issued a hold related to litigation involving one of the company's products in 2002 and that litigation hold was still in place when additional litigation on the same product began, the court may use the 2002 date as the relevant date for when that company's preservation obligation was "triggered" for the later litigation.[8]
- **Review Periodically –** Attorneys should review the scope of the litigation hold letter periodically to determine whether the preservation efforts outlined are too broad or too narrow in light of later developments with the litigation.
- **Follow-Up To Ensure Compliance –** Attorneys should follow-up with the relevant custodians, discovery vendor and other persons charged with implementing the hold to ensure that it is being implemented properly.
- **Identify Who The Internal (or External) Experts Are –** Prior to, or during the preparation of the litigation hold letter, the attorney should identify the person(s) with the most knowledge of the company's internal document retention policies. If spoliation issues do arise and the court requires expert testimony on the issue, whether or not this person is an employee of the company or a third-party expert is an important decision that could have a material impact on the litigation.[9]

Aside from the above-mentioned points, the directives contained in a litigation hold letter ***must*** take into account the company's internal document retention policies ("retention policies"). Although some government agency regulations and federal and state laws require companies to maintain specific types of documents for a period of time, companies are generally not otherwise required to implement retention policies.[10] It is advisable, however, that companies implement clear retention policies that outline the company's maintenance, retention and destruction policies related to company records, including ESI. This is because companies cannot destroy documents in their possession, custody or control that are relevant to

litigation, or potential litigation, or are reasonably calculated to lead to the discovery of admissible evidence, are reasonably likely to be requested during discovery, and/or the subject of a pending discovery request. [11] Clear retention policies enable a company to better maintain records in accordance with their preservation obligations under the Rules and the common law. Absent that, a company's retention policy is free to define what it considers a business record, including with respect to ESI, the value of that record over time and when that record is no longer of value and can be deleted. In other words, while retention policies provide internal guidelines on record maintenance, implicit in the idea of the retention policy is that anything *not retained* can be deleted.[12]

That said, the attorney charged with drafting the litigation hold letter will not be able to completely outline the company's preservation obligations without a full understanding of the company's retention policies. Companies and their attorneys should assume that their retention policies are discoverable in litigation. The scope and parameters of retention policies must take into account a variety of factors, including, the costs associated with complying with the policy, the frequency of litigation involving the company, applicable laws and regulations, and the size, type, and customer-base of the company.

Retention policies, like litigation hold letters, should be reviewed periodically and updated to address new developments in technology or changes in the company's business. Although short-duration or limited scope retention policies are not *per se* inadvisable, a company needs to have a justifiable basis for having such a policy that is reasonable in light of the above-mentioned concerns. For example, companies frequently involved in litigation will have a difficult time justifying short-duration or limited scope retention policies for their business records and ESI solely on the basis of the costs associated with implementing longer-duration or broader retention policies.

In sum, companies and their attorneys should work together to develop a litigation readiness plan so that a litigation hold can be effectively implemented, including the sequestering of back-up tapes, suspension of routine data destruction policies, and implementation of collection procedures for ESI. It is imperative that all of the parties involved in the identification and preservation of ESI have an accurate picture of where relevant ESI is stored, whether that be in active systems, backup or archival systems, mobile devices, or in other locations so that the company's "data map" is fully understood at the outset of litigation.

II. SPOLIATION AND SANCTIONS UNDER THE CURRENT RULES AND COMMON LAW

Not until the 2006 amendments, did the Rules explicitly address the treatment of ESI or electronic discovery. Following those amendments, there has been a proliferation of case law involving discovery in the ESI-context. Many of these cases have dealt with whether a party's mismanagement or failure to adequately preserve ESI that resulted in the spoliation of potentially relevant evidence warranted sanctions. Courts have derived their authority to sanction parties for failing to satisfy their obligation to preserve relevant ESI under a variety of Rules and through the court's "inherent authority."[13]

Most frequently, however, courts have imposed sanctions pursuant to Rule 37, as well as the court's "inherent authority," both of which require "clear and convincing evidence" of the sanctionable behavior.[14] The most severe sanctions available to the court, under either alternative, require a finding of "bad faith" and include the striking of pleadings, drawing an adverse inference and entering a default judgment.[15] Less severe sanctions, which do not require a finding of "bad faith," include permissible inference charges, which create a rebuttable presumption that the evidence is favorable to the innocent party, evidentiary limitations on the guilty party, the payment of attorney fees and monetary sanctions for the offending party.

Notably, Subdivision (e) of Rule 37 provides a "safe harbor" to the imposition of sanctions for ESI-related

discovery failures:

(e) Failure to Provide Electronically Stored Information. Absent exceptional circumstances, a court may not impose sanctions under these rules on a party for failing to provide electronically stored information lost as a result of the routine, good-faith operation of an electronic information system.

Although the "safe harbor" described in Rule 37(e) seems straightforward enough, most courts have declined to use it. Further, the courts have not been consistent or uniform with respect to their interpretations of the culpability required as the prerequisite to a finding of "bad faith" in the spoliation context. For example, the Second Circuit has held that a party's "negligent or grossly negligent" deletion of electronic data prior to litigation when the party did, or should have, "reasonably anticipated" litigation constituted "bad faith" for purposes of imposing the harshest, case-dispositive sanctions.[16] Within the Ninth and Tenth Circuits, however, the courts will not impose the harshest sanctions upon a finding of negligence or gross negligence, but instead require proof of actual "bad faith."[17] By contrast, even in cases of intentional spoliation, courts within the Fifth Circuit have declined to impose terminating sanctions in the absence of “incurable prejudice.”[18]

The obvious import of this clear split-of-authority is that whether a party will suffer harsh, case-dispositive sanctions for spoliation may well depend on the jurisdiction where the motion for sanctions is brought. Given the conflicting case law, companies should be pleased to learn that the 2014 amendments to the Rules include a Proposed Rule 37(e), which would entirely replace the current Rule and create a uniform approach to the spoliation/sanctions analysis.

III. SPOLIATION AND SANCTIONS ANALYSIS UNDER PROPOSED RULE 37(e)

On May 1, 2015, the Supreme Court adopted the proposed amendments to the Rules, including Proposed Rule 37(e) (the “Proposed Rule”). The amendments will become effective December 1, 2015.[19]

As background, it is important to note the Committees' proposed changes to a related Rule – Rule 26(b)(1), which currently defines the scope of discovery as follows: “Parties may obtain discovery regarding any non-privileged matter that is relevant to any party’s claim or defense – including the existence, description, nature, custody, condition, and location of any documents or other tangible things and the identity and location of persons who know of any discoverable matter." As drafted, the removal of the underlined language from the present iteration of Rule 26(b)(1) will essentially eliminate opportunistic "discovery about discovery" by removing a parties' identification, hold, and collection efforts from the scope of discoverable matters, thereby making it harder for a requesting party to establish a failure to preserve in the first instance.

Importantly, the Proposed Rule applies explicitly (and exclusively) to ESI; it does *not* apply to the loss of paper documents or physical evidence. As drafted, the Proposed Rule will resolve the existing split-of-authority regarding the level of culpability required to impose case-dispositive sanctions and will provide a clear process for analyzing spoliation in the ESI.[20] Proposed Rule 37(e) reads as follows:

(e) Failure to Provide Electronically Stored Information. If electronically stored information that should have been preserved in the anticipation or conduct of litigation is lost because a party failed to take reasonable steps to preserve the information, and the information cannot be restored or replaced through additional discovery, the court may:

(1) Upon a finding of prejudice to another party from loss of the information, order measures no

greater than necessary to cure the prejudice;

(2) Only upon a finding that the party acted with the intent to deprive another party of the information's use in the litigation,

(A) presume that the lost information was unfavorable to the party;

(B) instruct the jury that it may or must presume the information

was unfavorable to the party; or
(C) dismiss the action or enter a default judgment.

The Proposed Rule is composed of three distinct parts: (1) a three-factor test for determining when the Proposed Rule will apply; (2)"prejudice" and curative remedies where there is no "intent to deprive"; and (3)"intent to deprive" as the only route to case-dispositive sanctions.

a. When Does Proposed Rule 37(e) Apply?

Whether the Proposed Rule applies depends on the application of a three-factor test. As drafted, the Proposed Rule will only apply if the court finds that: (1) ESI that "should have been preserved in the anticipation or conduct of litigation is lost"; (2) the loss of the ESI resulted from the party's failure to take "reasonable steps to preserve", the ESI; and (3) the lost ESI "cannot be restored or replaced through additional discovery."

The first part of the three-factor test is a direct reference to a party's common law duty to preserve relevant ESI when litigation is reasonably anticipated or reasonably foreseeable. The Committee Notes confirm that the Proposed Rule does not apply if ESI was lost ***prior to*** the date a party's duty to preserve arose and, instead, only applies if relevant ESI was lost ***after litigation*** was reasonably anticipated or reasonably foreseeable – *i.e.,* after a party's duty to preserve has arisen.[21]

The second part of the three-factor test limits the application of the Proposed Rule to the situation where a party has "failed to take reasonable steps to preserve the information". Where a party can establish that it took "reasonable steps to preserve" relevant ESI, the party will not be subject to sanctions under the Proposed Rule; which stands in stark contrast to the illusory "safe harbor" available under Current Rule 37 (e). The Committee Notes also explain that "reasonable steps" should be viewed in light of the "proportionality" of the party's preservations efforts relative to the size of the litigation and the party's "sophistication."

The third, and final, factor asks whether lost ESI can be "restored or replaced through additional discovery." The Committee Notes to the Proposed Rule posits that if the lost ESI can be restored or replaced, the court should end its inquiry under the Proposed Rule and order the restoration of the lost ESI. In other words, before a court may undertake the spoliation, remedy and sanction analysis under Subdivisions (e)(1) and (e)(2) of the Proposed Rule, the court must consider the possibility that the lost ESI can be restored or replaced.

b. What Sanctions Are Available Under Proposed Rule 37(e)?

Only if the three-factor test is met – *i.e.,* a court has determined that relevant ESI, that should have been preserved, has been lost and cannot be restored, may a court undertake the spoliation, remedy and

sanction analysis under Subdivisions (e)(1) and (e)(2) of the Proposed Rule. Subdivision (e)(1) provides a court with broad discretion to define the curative measures that may be undertaken to remedy any prejudice caused by the loss of relevant ESI. By contrast, Subdivision (e)(2) limits a court's discretion to impose case-dispositive sanctions to situations where the guilty party has acted with the "intent to deprive."

Subdivision (e)(1) provides that "upon a finding of prejudice" a court may order "measures no greater than necessary to cure the prejudice." Notably, the remedies available under Subdivision (e)(1) do not include the most serious case-dispositive sanctions available under Subdivision (e)(2). The Committee Notes emphasizes that the Proposed Rule is "purposefully vague" on who has the burden of "proving or disproving prejudice" and leaves "judges with discretion to determine how best to assess prejudice in particular cases." Although Subdivision (e)(1) does not enumerate all of the possible remedies, existing case law identifies financial penalties, evidentiary limitations, and the payment of attorney fees as appropriate sanctions.

By contrast, where a court finds that a party acted with the "intent to deprive", Subdivision (e)(2) authorizes the court to impose adverse inference instructions, to dismiss the action, or to enter a default judgment – *i.e.,* the most severe case-dispositive sanctions available.[22] The Committee Notes are similarly explicit and provide that Subdivision (e)(2) permits courts to "draw adverse inferences . . . [***only***] when a court finds that the information was lost with the intent to prevent its use in litigation."

c. *Vicente v. City of Prescott* – A Preview of Things to Come?

Although Proposed Rule 37(e) has yet to be adopted or applied by a Court, a recent decision by Judge Campbell of the District Court of Arizona may be instructive of what is to come.[23]

In *Vicente v. City of Prescott*, the Court addressed whether sanctions could be imposed for "inadequate" preservation of ESI.[24] There, the plaintiff alleged First Amendment violations after his employer took disciplinary actions against him. During discovery, the plaintiff presented evidence that at least one relevant email was lost after the defendant's duty to preserve such ESI had arisen. The Court found that the defendant's ESI preservation and retention policies were inadequate. Notably, the defendant neglected to involve their information technology department in responding to the plaintiff's document requests, and as a result, a number of deleted emails were lost. The Court, however, refused to impose sanctions, because the plaintiff failed to present evidence that either the emails were lost as a result of the defendant's "bad faith" ***or*** that the plaintiff was prejudiced by the loss of the emails. The Court concluded that it was improper to impose significant sanctions without evidence that the plaintiff was prejudiced by the defendant's "bad faith" failure to preserve.

Although decided prior to the adoption of the Proposed Rule, the *Vicente* decision provides an example of the type of analysis that courts will likely undertake in the ESI-spoliation/failure to preserve context. That is, assuming the Proposed Rule is adopted, it is unlikely that courts will be inclined (have the authority to) impose the harshest, case-dispositive sanctions, in the absence of clear and convincing evidence that the guilty party intended to deprive the non-guilty party of relevant ESI.

IV. CONCLUSION

The proper management and preservation of ESI is a dynamic process that is becoming more complex as the volume of ESI generated by companies grows exponentially year-over-year. Although the Proposed Rule is helpful in that it clarifies the split-of-authority regarding the culpability required to levy the most severe sanctions against companies that fail to adequately manage and preserve ESI, companies and their

attorneys should proactively review their document retention policies, litigation readiness plans and "data maps" to ensure they can successfully preserve relevant ESI should litigation become a reality. Taking the right steps on the front-end will ensure that your company does not fall victim to expensive or case-dispositive sanctions.

Hanson Bridgett has extensive experience with helping client's develop and implement sound and defensible document retention policies and litigation readiness plans that successfully balance our client's business objectives with their business, compliance and litigation-readiness needs. Our firm works with each client to develop a tailored, cost-efficient and defensible plan to respond to the discovery needs of each matter through the efficient use of technology tools and project management principles to efficiently perform both electronic and hard copy reviews. Hanson Bridgett also has extensive experience in all phases of discovery and case preparation, ranging from initial party and court conferences, to written discovery, motions practice, depositions and trial.

[1] Timothy J. Hogan, *The International and Domestic Implications of Electronic Discovery on Litigation and Business Practices*, International Legal News, vol. 2, at 7 (June 10, 2005).

[2] *Zubalake v. UBS Warburg LLC ("Zubalake IV")*, 220 F.R.D. 212, 218 (S.D.N.Y. 2003).

[3] *Zubalake IV*, *supra,* 220 F.R.D. at 218; *See also, Apple Inc. v. Samsung Elecs. Co.*, 888 F. Supp. 2d 976, 991 (N.D. Cal. 2012).

[4] *Kemper Mort. Inc. v. Russell,* 2006 U.S. Dist. LEXIS 20729, at *3 (S.D. Ohio Apr. 18, 2006); *See also*, *Small v. Univ. Med. Ctr. of S. Nev.*, 2014 U.S. Dist. LEXIS 114406, 48 (D. Nev. Aug. 18, 2014).

[5] *See*, *e.g.*, *Doe v. Norwalk Comm. College*, 248 F.R.D. 372 (D. Conn. 2007) [In light of discussions by supervisors regarding employee reports of harassment, the college should have reasonably anticipated the prospect of litigation notwithstanding the lack of a formal preservation demand].

[6] *Samsung Electronics Co., Ltd. v. Rambus, Inc.,* 439 F.Supp.2d 524, 565-66 (E.D. Va. 2006) [The court held that a company "must inform its officers and employees of the actual or anticipated litigation, and identify for them the kinds of documents that are thought to be relevant to it." Simply, instructing employees to "look for things to keep" and to not to destroy "relevant documents" is insufficient.].

[7] *Major Tours v. Colorel*, 2009 U.S. Dist. LEXIS 68128 (D. N.J. Aug. 4, 2009) [authorizing discovery of litigation hold letter upon a preliminary showing that spoliation likely occurred]; *See also*, *Cannata v. Wyndham Worldwide Corp.,* 2011 U.S. Dist. LEXIS 88977, *6-7 (D. Nev. Aug. 10, 2011) [holding that disclosure of broad parameters of litigation hold letter for purposes of Rule 30(b)(6) Deposition was permissible in light of spoliation concerns].

[8] *In re Actos (Pioglitazone) Prods. Liab. Litig.*, 2014 U.S. Dist. LEXIS 86101, *42 (W.D. La. June 23, 2014).

[9] *Id.* at *66 [holding that defendant's choice to hire a third-party expert to testify regarding spoliation prevented defendant from adequately defending preservation techniques and resulted in sanctions].

[10] Companies and their attorneys should research federal and state laws and regulations to ensure that their existing retention policies are in compliance with applicable laws or regulations.

[11] *William T. Thompson Co. v. General Nutrition Corp.,* 593 F.Supp. 1443, 1455 (C.D. Cal. 1984); *See also*, *Rensel v. Fluidmaster, Inc.*, 2014 U.S. Dist. LEXIS 162692, 5 (C.D. Cal. Nov. 12, 2014).

[12] *Arthur Andersen LLP v. United States*, 544 U.S. 696 (U.S. 2005) ["Under ordinary circumstances, it is not wrongful for a manager to instruct his employees to comply with a valid document retention policy, even though the policy, in part, is created to keep certain information from others, including the Government."]

[13] *See, e.g.,* Fed. R. Civ. P. §§ 26(g), 37(b), (c), (d) and (e); 28 U.S.C. § 1927.

[14] *Danis v. USN Communs., Inc.,* 2000 U.S. Dist. LEXIS 16900 at *103 (N.D. Ill. Oct. 20, 2000); *See also*, *Lahiri v. Univ. Music & Video Distrib. Corp*., 606 F.3d 1216, 1219 (9th Cir. 2010) [declining to resolve burden of proof issue because clear and convincing evidence supported the court's bad faith finding]; *In re Lehtinen* 564 F.3d 1052, 1061 n.4 (9th Cir.2009) [accord].

[15] *Pension Comm. of the Univ. of Montreal Pension Plan v. Banc of Am. Sec., LLC*, 685 F. Supp. 2d 456, 468-69 (S.D.N.Y. 2010).

[16] *Residential Funding Corp. v. DeGeorge Financial Corp.,* 306 F.3d 99 (2d Cir. 2002).

[17] *Leon v. IDX Sys. Corp.,* 464 F.3d 951, 961 (9th Cir. 2006); *See also*, *Aramburu v. Boeing Co.,* 112 F.3d 1398, 1407 (10th Cir. 1997) ["The adverse inference must be predicated on the bad faith of the party destroying the records. Mere negligence in losing or destroying records is not enough because it does not support an inference of consciousness of a weak case."].

[18] *See, e.g., Rimkus Consulting Group, Inc. v. Cammarata,* 688 F.Supp.2d 598, 644 (S.D. Texas 2010) [ordering an adverse inference instruction rather than terminating sanctions where plaintiff had obtained some of the deleted evidence from other sources and where some of the deleted evidence was favorable to the guilty party; "the sanction of dismissal or default judgment is appropriate only if the spoliation or destruction of evidence resulted in irreparable prejudice and no lesser sanction would suffice"].

[19] Proposed Fed. R. Civ. P. § 37(e).

[20] See, Committee Note to Proposed Fed. R. Civ. P. § 37(e): "forecloses reliance on inherent authority or state law to determine when certain measures should be used" such as the imposition of case-dispositive sanctions upon a finding of "negligence" or "gross negligence" under the existing case law.

[21] See, Section I, *supra.*

[22] Proposed Fed. R. Civ. P. §§ 37(e)(2)(A), (B) and (C).

[23] *Vicente v. City of Prescott*, No. CV–11–08204–PCT–DGC (D. Ariz. Aug. 8, 2014).

[24] *Id.* at *8.

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