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Critical Legal Issues: WORKING PAPER SERIES

CURBS FOR COSTLY DISCOVERY?: FEDERAL RULES REFORM AIMS AT ELECTRONIC DOCUMENT BURDENS

by
Tony Rospert and Rob Ware
Thompson Hine LLP

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TABLE OF CONTENTS

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ABOUT THE AUTHORS

Tony Rospert is a partner with the law firm Thompson Hine LLP in its Cleveland office. As a member of the firm's Business Litigation group, Mr. Rospert helps clients overcome legal obstacles in order to protect their assets and manage litigation risk in pursuit of their strategic goals. He focuses his practice on complex business and corporate litigation involving financial service institutions, commercial and contract disputes, indemnification claims, shareholder actions, business transactions, pre- and post-closing merger disputes, class actions, regulatory enforcement and tax controversies. Mr. Rospert has developed strategies to streamline litigation costs using technology to manage the efficient analysis of electronically stored information to assist clients in reducing the costs associated with the discovery process.

Rob Ware is a partner with Thompson Hine LLP in its Cleveland office. He is a member of the firm's Executive Committee and a member of the Antitrust, Competition & Distribution, Business Litigation and Intellectual Property practice groups. Mr. Ware has significant experience litigating trade secret, unfair competition, copyright infringement, civil antitrust, non-competition, false advertising and other complex business cases throughout the United States. In addition to his substantial trial and litigation experience, he regularly counsels clients in complex antitrust, intellectual property and competition issues. Among his many professional and community activities, Mr. Ware is a past president of the Ohio State Bar Association (2007-08).

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INTRODUCTION

For many years there has been "a steady chorus of complaints [] about the increasing costs and delays in federal litigation."[1] The chorus has now become a crescendo, as soaring discovery costs have transformed the litigation landscape and raised the stakes for litigants. Rising litigation costs are driven largely by the discovery—specifically, the collection, review, and production—of electronically stored information (ESI).[2] As a result, parties to a lawsuit inevitably face significant litigation costs due to the burden of responding to overly broad discovery requests and uncertain preservation obligations relating to ESI.

Because of the skyrocketing cost of litigation, many companies are deciding against participation in the judicial process to avoid getting sucked into the vortex of electronic discovery. Companies are declining to file meritorious cases because the

[1] Hon. Mark B. Kravitz, Examining the State of Civil Litigation, July 2010, available at http://www.uscourts.gov/News/TheThirdBranch/10-07-01/Examining_the_State_of_Civil_Litigation.aspx.

[2] ESI includes any data found in e-mail, voicemail, instant and text messages, databases, metadata, digital images, and any other types of electronic files stored on computers, mobile devices and in the cloud.

likely litigation costs would render those cases worthless, or they are settling at the inception of unmeritorious matters to avoid the discovery process and its prohibitive costs. When the force driving decisions to pursue litigation or to settle it is the cost of discovery—rather than the merit and value of the underlying claim—the need for fundamental changes to the federal system is obvious.

To address these concerns, in August 2013 the Advisory Committee on Rules of Practice and Procedure ("Advisory Committee") published proposed amendments to the Federal Rules of Civil Procedure (the "Federal Rules"). After considerable input received during the public comment period between August 2013 and February 2014, the Advisory Committee approved revised amendments at its April 10-11, 2014 meeting. It accepted most of the proposed rule changes and submitted them to the Committee on Rules of Practice and Procedure ("Standing Committee"), which in turn approved them at its meeting on May 29-30, 2014 with the recommendation that the United States Supreme Court accept the changes. If approved, the proposed amendments will go into effect on December 1, 2015.

The proposed amendments have the potential to reverse the trend of escalating costs and move litigation in a more cost-effective and efficient direction by limiting discovery of information relevant to the "subject matter involved in the action," inserting considerations of proportionality into Rule 26(b), and substantially revising preservation obligations under Rule 37(e). This WORKING PAPER will first outline the problems litigants are facing under the existing paradigm prescribed by

the Federal Rules. It will then describe the proposed amendments to the Federal Rules, more specifically address the proposed changes to Rules 26(b) and 37(e), and discuss their impact on electronic discovery. The paper argues that the proposed amendments to the Federal Rules are a critically important step in easing the burden of discovery and decreasing the litigation costs associated with the preservation of ESI.

I. THE NEED FOR CHANGE

Electronic data is growing exponentially. It is estimated that close to 100 billion emails are sent daily, resulting in an astounding 36.5 trillion annually total.[3] Faced with this growing volume of electronic data, the cost of producing electronic documents during the discovery phase of litigation far exceeds that of producing traditional paper documents. The routine storage of older electronic data on backup tapes, which can cost millions of dollars to restore and review, compounds the problem.[4] Furthermore, unlike paper documents, electronic data must be processed and loaded into a review platform before the documents can even be analyzed. Thus, the volume of electronic data and the costs to the parties of culling and reviewing ESI are critical considerations in any litigation, large or small.

The massive amounts of electronic data in the era of digital discovery, in some

[3] George L. Paul & Jason R. Baron, *Information Inflation: Can the Legal System Adapt?,* 13 RICH. J. L. & TECH. 10, 12 (2007), http://jolt.richmond.edu/v13i3/article10.pdf (noting that "[p]robably close to 100 billion emails are sent daily").

[4] *See, e.g.*, *Rowe Entm't, Inc. v. William Morris Agency, Inc.*, 205 F.R.D. 421, 425 (S.D.N.Y. 2002) ("If the emails on all of the back-up tapes were produced instead of a sample of eight sessions, the total cost would mushroom to almost $9,750,000.").

cases amounting to billions of pages of documents and thousands of gigabytes of information, have multiplied the costs of litigating disputes. These costs include retaining vendors to collect, process, house, and manage electronic documents, and hiring armies of staff attorneys and contract lawyers for the sole purpose of reviewing millions of documents (many of which are of little or no relevance to the actual issues involved in the litigation). Indeed, the Rand Institute for Civil Justice found that the total cost per gigabyte of documents reviewed was at least $18,000 per gigabyte, which does not include the costs of processing and collection.[5]

Many companies complain that electronic discovery costs, as well as the enormous internal and external resources required to manage the preservation, collection, and production of data, have placed untenable burdens on their businesses. In its comment letter to the Advisory Committee, Ford Motor Company provided its own case study to illustrate this point: *Stokes v. Ford Motor Company*.[6] There, the plaintiff sued Ford in a product liability action relating to a single-vehicle crash and propounded discovery seeking litigation information involving other personal injury cases and other vehicle models that did not share any components at issue.[7] Because the court found that "discovery shall be liberally granted," it ordered

[5] Nicholas M. Pace & Laura Zakaras, Rand Institute for Civil Justice, *Where the Money Goes: Understanding Litigant Expenditures for Producing Electronic Discovery* 20 (2012), available at http://www.rand.org/content/dam/rand/pubs/monographs/2012/RAND_MG1208.pdf.

[6] Comment from Doug Lampe, Ford Motor Company, to the Advisory Committee on Rules of Practice and Procedure, Doc. #343 Pt. 2, at 6, Nov. 22, 2013.

[7] *Stokes v. Ford Motor Co.*, No. 05-1236 (Mont. 13th Jud. Dist. Ct. 2011).

Ford to produce the requested material.[8] In complying with this order, Ford identified more than 1,300 lawsuits and 1,200 witness transcripts, which required the work of 60 law firms and numerous individuals from Ford's in-house legal team—and cost millions.[9] Ford ultimately "won" with a 12-0 defense jury verdict, but the victory was hollow thanks to the staggering costs it had been forced to incur.[10]

In Re Matter of Fannie Mae Securities Litigation provides another illustration.[11] During the course of discovery, the Office of Federal Housing Enterprise Oversight (OFHEO) was served with a third-party subpoena to produce emails.[12] OFHEO's in-house counsel voluntarily agreed to comply with the subpoena without fully comprehending the time and expense compliance would entail.[13] After missing several discovery deadlines, the district court held OFHEO in contempt and ordered the agency to produce all documents responsive to the subpoena, even those otherwise protected by privilege.[14] Since many emails were no longer reasonably accessible and the plaintiffs sought 80% of all of OFHEO's emails, the agency spent more than $6 million, more than one-ninth of the agency's entire annual budget, to comply with the subpoena.[15] The United States Court of Appeals for the District of

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[8] Comment from Doug Lampe at 6.

[9] *Id.* at 6-7.

[10] *Id.* at 8.

[11] *In re Fannie Mae Sec. Litig.*, 552 F. 3d 814 (D.C. Cir. 2008).

[12] *Id.* at 816.

[13] *Id.* at 818.

[14] *Ibid.*

[15] *Id.* at 817.

Columbia Circuit upheld the contempt citation, rejecting OFHEO's argument that it should not have been compelled to comply with the subpoena in light of the excessive costs involved.[16]

Unfortunately, the astonishing costs in the *Ford* and *Fannie Mae* matters—costs wholly disproportionate to the value of the underlying claims at issue—are not unusual in the current litigation landscape. Without changes to the Federal Rules that govern electronic discovery, the expenses and inefficiencies of such cases will continue to pose significant challenges. Electronic discovery costs often continue to exceed the value of the controversy.[17] That situation is exacerbated when discovery is asymmetrical (i.e., when one side has little discoverable information compared to the other), putting the possessor of the information at a disadvantage by making it bear a higher proportion of the costs associated with collecting, reviewing, and producing its ESI, while removing any incentive for the other party to temper its demands.

Another major challenge companies face in the digital era is the preservation of ESI in anticipation of litigation. The Preservation Costs Survey Final Report, submitted to the Standing Committee on February 18, 2014, estimated (conservatively) that the costs of preservation, using the largest companies as a

[16] *Ibid.*

[17] Phil J. Favro and the Honorable Judge Derek P. Pullan, *New Utah Rule 26: A Blueprint For Proportionality Under The Federal Rules Of Civil Procedure*, 2012 MICH. ST. L. REV. 933, 938 (2012).

sample, exceed $40 million per company per year.[18] Smaller businesses are also reporting similar preservation burdens.[19] Indeed, the data show that, although smaller companies face fewer lawsuits, they are also less equipped to handle the preservation challenges that arise and are less able to make large-scale investments in technology to control the costs of preservation.[20]

Companies also report that they are "over-preserving" to protect themselves against the potential risk of sanctions.[21] The over-preservation of data is a direct result of the ambiguity under the current case law and the Federal Rules regarding how much data must be preserved and for how long.[22] As a result, companies err on the side of preserving too much, wary of preserving too little and falling victim to sanctions. Hence, unpredictability under the current Federal Rules regarding preservation unnecessarily inflates litigation costs.

Additionally, since preservation must occur before the scope of discovery in a case is defined, and often occurs before a party files suit, it is common that companies will preserve more than is ultimately requested and produced in litigation.[23] In fact, one survey respondent reported that 44% of its legal holds did not involve active litigation, and another respondent reported that 77% of their

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[18] William H. J. Hubbard, *Preservation Costs Survey Final Report: Prepared for Civil Justice Reform Group* 20 (2014) (hereinafter "The Final Report Study").

[19] *Id.* at 8.

[20] *Id.* at 8, 20.

[21] *Id*. at 8.

[22] *Id*. at 20.

[23] *Id*. at 43.

litigation holds were issued without a suit being filed or a subpoena issued.[24] And yet, most of the data that is preserved is never collected, processed, and reviewed.[25] Thus, these costs add no value to any litigation matter.

Regardless of the true costs of discovery, companies perceive that preservation costs lead to unjust outcomes. Some survey respondents to the Final Report Study stated, "[t]he costs and burdens (*e.g.*, fear of sanctions despite efforts and extreme use of internal resources and cost of external resources) of discovery and preservation have become an important factor in whether to litigate or settle."[26] Thus, a more uniform standard regarding preservation and spoliation issues is long overdue; one that balances continuing obligations to identify and maintain materials related to potential claims against the costs of over-preservation.

II. THE PROPOSED AMENDMENTS TO THE FEDERAL RULES GOVERNING DISCOVERY

The Advisory Committee proposed a number of amendments to the Federal Rules that will directly impact the scope of electronic discovery. The most significant proposed amendments, and the ones that have caused the most debate in the legal community, are the amendments to Federal Rules 26(b) and 37(e).

A. Federal Rule 26: Proportionality and Scope of Discovery

The Advisory and Standing Committees approved significant changes to Rule

[24] *Ibid*.

[25] *Ibid*.

[26] *Id*. at 31.

26(b), which narrow the standard of discoverable information to "any nonprivileged matter that is relevant to any party's claim or defense and proportional to the needs of the case." The proposed amendments are intended to limit the scope of electronic discovery—the outcome of which would be fewer documents to collect, process, review, and produce, which will reduce costs. The changes to Rule 26(b) described below "will decrease the cost of resolving disputes in federal court without sacrificing fairness."[27]

The proposed changes to Rule 26(b) would require a two-prong analysis: (1) an initial relevancy analysis as to the information requested by the opposing party, and (2) a proportionality analysis requiring that costs in complying with the discovery request be proportional to the needs of the case.

1. Relevance Prong

One proposed amendment to Rule 26(b) eliminates the language under the current Federal Rules that permits discovery if it is reasonably calculated to lead to the discovery of admissible evidence. By deleting the phrase "reasonably calculated," the proposed amendment clarifies that the scope of discovery is defined by the claims and defenses found in the four corners of the pleadings rather than the general subject matter in dispute. This creates a balanced approach that should reduce the potential for discovery abuses while preserving the right to obtain

[27] Report to the Standing Committee Advisory Committee on Civil Rules, May 2, 2014, available at http://www.uscourts.gov/uscourts/RulesAndPolicies/rules/Agenda%20Books/Standing/ST2014-05.pdf, at 68.

information critical to the actual claims or defenses in the litigation.

Today, litigants and judges often cite the "reasonably calculated" language as a way to justify broad construction of the Federal Rules. Indeed, this language has been used to support overly broad discovery requests and "fishing expeditions" into areas that have no direct relevance on the issues in a particular case. This antiquated standard is no longer effective in our digital age. The proposed amendment to Rule 26(b) would ultimately reduce the amount of resources spent responding to unwarranted and irrelevant electronic discovery, with the added benefit of providing parties with more cost certainty in planning for and budgeting their discovery obligations.

2. Proportionality Prong

The proposed amendments move the proportionality limitation from Rule 26(b)(2)(c)(iii) into 26(b), which directly addresses the scope of discovery. The goal of these proposed changes is to limit the scope of discovery to that which is "proportional to the needs of the case." Under the "proportionality" prong, the Advisory Committee outlined five cost-benefit factors for courts to consider in determining whether a discovery request is proportional to the needs of the case: (1) the amount in controversy; (2) the importance of the issue at stake in the action; (3) the parties' resources; (4) the importance of discovery to resolve the issue; and (5) the expense versus benefit analysis. The new language allows courts and parties to apply a more commonsense approach to discovery with the goal of preventing a

party from spending more on discovery than the case is worth. Ultimately, the proportionality prong requires courts to conduct a cost-benefit analysis of the documents and electronic data being sought in discovery.

Thus, as approved by the Standing Committee, revised Rule 26(b) will permit a party to

> obtain discovery regarding any non-privileged matter that is relevant to any party's claim or defense and proportional to the needs of the case, considering the importance of the issues at stake in the action, the amount in controversy, the parties' relative access to relevant information, the parties' resources, the importance of the discovery in resolving the issues, and whether the burden or expense of the proposed discovery outweighs its likely benefit. Information within this scope of discovery need not be admissible in evidence to be discoverable.[28]

The proposed changes to Rule 26(b) strike the correct balance here, as this two-prong analysis will allow parties and the law firms that represent them to make and defend their decisions in placing limitations on broad discovery requests seeking ESI.

B. Federal Rule 37: Failure to Disclose or Cooperate in Discovery and Sanctions

Under the current Federal Rules, a party's preservation obligation, especially with respect to ESI, is fraught with uncertainty and potential pitfalls, even for diligent and sophisticated companies.

The current iteration of Rule 37 causes the phenomenon of "over-preservation." Companies over-preserve their electronic data for a number of

[28] Advisory Committee on Civil Rules Report to the Standing Committee May 2, 2014, at 20.

reasons. First, they face the risk and fear of sanctions. This causes many harmful effects within a company. For example, over-preservation leads to unpredictability in the management of information (*e.g.*, do you delete information that was once the subject of a litigation hold, or should you continue to preserve it?). It also creates additional costs for classifying and storing electronic data that may never be used again.

Second, companies over-preserve because of the uncertainty they face regarding the extent of the preservation obligations required by the Federal Rules. Preservation issues are currently decided on a case-by-case basis through *ad hoc* litigation hold procedures created by each individual court.[29] As a result, companies over-preserve data due to the disparate treatment of preservation and discovery obligations in various jurisdictions.[30] The proposed amendments to Rule 37(e) seek to bring clarity and provide a safe harbor to companies by setting a uniform standard.

The proposed amendments, as approved by the Standing Committee, to Rule 37(e) are limited to ESI and state:

> (e) FAILURE TO PRESERVE 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

[29] Public Comment to the Advisory Committee on Civil Rules by Lawyers for Civil Justice, *Reducing the Costs and Burdens of Modern Discovery: Why the Proposed Amendments to the Federal Rules of Civil Procedure Are Urgently Needed (With a Few Important Improvements)*, Aug. 30, 2013.

[30] Report to the Standing Committee Advisory Committee on Civil Rules, May 2, 2014, available at http://www.uscourts.gov/uscourts/RulesAndPolicies/rules/Agenda%20Books/Standing/ST2014-05.pdf, p. 306 ("The courts agree unanimously that a duty to preserve ESI arises when a party reasonably anticipates litigation. But they differ significantly in the approaches taken after finding a loss of ESI that should have been preserved.").

take reasonable steps to preserve it, and it cannot be restored or replaced through additional discovery, the court may:

(1) upon finding prejudice to another party from loss of the information, order measures no greater than necessary to cure the prejudice; or
(2) only upon 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.[31]

The Advisory Committee acknowledged that its "previously recommended approach of limiting virtually all forms of 'sanctions' to a showing of substantial prejudice and willfulness or bad faith is too restrictive." [32] As originally proposed in August 2013, Rule 37(e) would have allowed courts to issue sanctions where they found that a party's failure to preserve "(i) caused substantial prejudice in the litigation and were willful or in bad faith; or (ii) irreparably deprived a party of any meaningful opportunity to present or defend against the claims in the litigation."[33] The Advisory Committee recognized this version did not "afford trial courts the flexibility they will need to deal with the wide range of ESI issues they will confront in

[31] Report to the Standing Committee Advisory Committee on Civil Rules, May 2, 2014, available at http://www.uscourts.gov/uscourts/RulesAndPolicies/rules/Agenda%20Books/Standing/ST2014-05.pdf, at 318.

[32] Discovery Subcommittee Report Rule 37(e), April 10-11, 2014, available at http://www.uscourts.gov/uscourts/RulesAndPolicies/rules/Agenda%20Books/Civil/CV2014-04.pdf, at 371.

[33] *Id*. at 377.

the coming years."[34]

The proposed amendments to Rule 37(e) represent a positive step toward providing a uniform level of protection for parties that act in good faith regarding the preservation of ESI. As the Final Report Study found, reducing over-preservation would not affect the amount of relevant and useful data preserved in litigation.[35] A large bulk of the information preserved is not even used in litigation, as vastly more data is preserved than actually turned over in discovery, and only a fraction of preserved data is ever collected.[36] The proposed amendments' clarifying language rejects the Second Circuit rule from *Residential Funding Corp. v. DeGeorge Fin. Corp.*, 306 F.3d 99 (2d Cir. 2002) that mere negligence is sufficient to support discovery sanctions. This clarification offers companies a heightened level of protection and may alleviate the disparate results litigants currently face from federal courts.

The proposed amendments to Rule 37(e) provide both comfort to companies assessing their preservation obligations and additional guidance for balancing continuing obligations to preserve ESI with the costs of over-preservation. In addition, the changes provide clarity to the courts in determining the appropriate circumstances for imposing sanctions involving ESI. While not perfect, the proposed amendments should lower the costs for companies seeking to comply in good faith with their preservation obligations.

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[34] *Id*. at 371.

[35] Hubbard, *The Final Report Study*, at 49.

[36] *Id.* at 43.

CONCLUSION

The Advisory Committee's proposed amendments to the Federal Rules, as approved by the Standing Committee, provide a much-needed step toward decreasing the costs and delay of litigation for all parties. More importantly, the proposed amendments offer a practical approach to cost-effectively managing electronic discovery in our digital information age and establishing a more efficient and uniform federal judicial system. This approach will benefit not only the litigants by decreasing the costs of discovery, but also will improve judicial economy and the efficiency of litigation in the courts.

