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SPECIAL TO IN-HOUSE COUNSEL

Buy or Build: The Impact of the New Federal Rules on the Corporate Law Department's Management of E-Discovery Part I

By Jeffrey Ritter

Corporate law departments are continuing to feel enormous pressure as the digital 21st century accelerates. The pressure is largely economic, but also structural, since an entire company's operations often must stop to respond to law department requests. Indeed, every law-driven request to identify, collect and preserve business records—notably electronically stored information (ESI)—diverts people, systems, and resources from their primary functions. As a result, corporate counsel find themselves targeted by CEOs, CFOs and internal auditors (“Again!” many would say) to apply proven business methods to establish process control, automate functions, and eliminate spending on external assets, including outside law firms.

With nearly \$2 billion in e-discovery expenditures projected to be spent on e-discovery in 2006 alone (with growth projected at a 35 per cent compound rate¹¹), companies and their law firms must expect that all of the discovery services performed by law firms are going to be examined against the essential standard of “buy or build”—will the company achieve better overall outcomes by shifting the service internally, automating the service, or engaging outside resources other than those of a law firm? In nearly every instance, the analysis will be heavily dependent on issues of technology, ESI, and a determination of which organization will be a superior manager of the systems and business infrastructure required for the job.

This article is the first in a series that examines specific services within the discovery process lifecycle that companies are most likely to prioritize for change, and for which law firms can (and should) develop innovative responses in order to remain relevant and competitive. For each service, the applicable legal standards are summarized, and the re-

lated procedures evaluated to more carefully determine the suitability of “buy or build” decisions.

The need for this analysis is inevitable—the simple reality is that 21st century corporate governance requires every aspect of a business to be improved by applying measurable controls that enable continuous improvement and reduce recognized risks. The pressing economic and operational disruption caused by e-discovery will not be tolerated for very long before auditors, controllers, and boards of directors ask the difficult questions. Ostrich-like refusals to address the issues now can only provoke the potential for more dramatic calls for change. Instead, responsible, informed dialogue between in-house counsel and their outside law firms today will assure a more orderly transition.

Initiating the Preservation of Evidence: Legal Issues

What are the responsibilities of outside counsel in connection with establishing the scope of preservation? What steps should outside counsel execute to discharge their duties, including as officers of the court?

Even prior to the final version of the new Federal Rules, judges made clear that lawyers could not ignore the impact of electronic business practices on the discovery and preservation process. See *G.T.F.M., Inc. v. Wal-Mart Stores, Inc.*, 2002 WL 335558, 49 Fed.R.Serv. 3d 219(S.D.N.Y. 2000). Several federal courts have adopted local rules (which do not appear to be superseded by the new Federal Rules) which impose the duty on counsel to review the relevant computer systems of their clients and understand how information is stored and can be retrieved. See, e.g., New Jersey Local Court Rule 26.1(d), District of Wyoming

Local Civil Rule 26.1(d), and others, set out in their entirety on the *DDEE* Web Reference service, under “Proposed & Enacted Rules.”

The new Federal Rules reinforce the need for competency with a client’s IT systems. The Rules require trial counsel to be responsible for discussing electronic information early in any civil case, both to avoid the destruction of potential evidence and to ensure suitable production occurs. Rule 26(f) requires parties to confer on issues relating to discoverable information prior to a Rule 16 scheduling conference and to specifically discuss “issues relating to disclosure or discovery of electronically stored information.” The resulting Rule 16 court orders may include provisions for the disclosure or discovery of ESI; thus, the judge is entitled to raise the issues directly. One recent commentator observed that the new Rules put an end to “. . . the era of ‘mutually assured destruction’ in which the parties could mutually choose to tacitly ignore electronic data issues.”²

In order to initiate the preservation of relevant evidence, particularly for defendant litigants, the first action taken is to transmit a notice to potential custodians of relevant evidence (often described as a “records hold notice”). To be legally sufficient, among other requirements (creating the actual content of a records hold notice will be analyzed in *Buy or Build—Part II*, to be published in the January 2007 issue of *DDEE*), the notice must sufficiently describe the kinds of information to be preserved so the affected custodians can segregate and preserve the identified files, including ESI. See *Wiginton v. CB Richard Ellis, Inc.*, 2003 WL 22439865, at *5 (N.D. Ill., Oct. 27, 2003). Moreover, the notice must be timely. See *Broccoli v. EchoStar Communications Corp.*, 229 F.R.D. 506 (D. Md. 2005).

Basic Considerations

Any “buy or build” decision first involves defining what services are in play—for those services, the options are weighed by resource availability, cost, and the contingent risks associated with rejecting the alternatives. Companies with persistent litigation portfolios have different variables to consider than companies who only face the occasional lawsuit. Similarly, companies under ongoing regulatory review usually have ongoing production and inspection requirements that can be more pervasive than production requests in litigation. There is no magic formula—for each company, the “buy or build” analysis involves different calculations.

An overview of the alternatives available for many e-discovery services reveals that law firms and law departments often have an equal opportunity to acquire and use tools or resources that improve efficiency or lower risk. These tools can include software applications employed to automate the identification and capture of relevant electronic records, practice tools that provide consistent

structure (such as systems maps, checklists or published protocols for specific procedures), or third-party service providers (such as digital forensic specialists). Thus, for many e-discovery “buy or build” decisions, the corporate law department is not merely making a choice between in-house or outside counsel, but also determining which group can make the most productive (and cost-effective) use of the service tools available in the marketplace.

Initiating Preservation

What services should be activated to initiate the preservation of relevant evidence, notably ESI? Most of them (described below) should occur long before notice of specific litigation, particularly within companies regularly facing litigation. In the absence of this course of action, companies face substantial challenges demonstrating they exercised due care in initiating preservation. The recommended actions include:

- Produce a technically sound inventory of the IT assets operated or controlled by a company. The inventory process can involve contributions by many different actors; for example:
 - The CIO/CTO staff should provide the IT systems architecture, detailing the machines, applications and storage facilities.
 - Those responsible for information security should account for the access logs, audit records and similar ESI that often influence the reliability and weight of ESI.
 - Managers that interact with third-party service providers (such as outsourced operations that duplicate or maintain corporate records) should inventory the records maintained outside the company’s normal IT systems.
- Produce a matching inventory of the applicable records management policies and procedures. This service is particularly important since a negligent accounting of the policies can result in potential evidence being overlooked, or disposed of in the ordinary course. As with the IT asset inventory, different actors are involved; for example:
 - Compliance managers should identify the policies and procedures that align to external legal requirements for preserving and managing specific records.
 - Records managers should produce all relevant policies and procedures, including the procedures in place to initiate and execute records hold notices.
 - IT systems administrators should account for the settings within specific systems and software applications that influence the storage of ESI (such as auto-delete rules within e-mail programs).

- Develop a “records-hold notice” program that can be implemented by the company. A good program should include the policies, procedures, and tools (such as model notices, checklists, protocols) for organizing the preceding inventories and records for analysis, creating a plan for case-specific preservation activities and developing, communicating and managing the records-hold notices. Various software applications are also on the market that can be a foundation around which these programs are developed.
- Create a means within the records-hold notice program to document the time at which the company believes the duty to preserve evidence arose (e.g., receipt of notice of the complaint). That time, of course, becomes the trigger event for initiating preservation.
- Organize the preceding inventories, programs, and information in a manner that enables trial counsel to access the knowledge in order to discharge effectively its responsibilities to be familiar with the company’s IT systems and methods for identifying and preserving relevant evidence.

During the last year, as the new Federal Rules moved toward final approval, many companies invested in services to enable them to perform in this arena. But, in doing so, law firms may have been excluded from the equation, in favor of IT and management consulting firms, records management consultants, e-discovery service vendors, and other non-law firm professionals engaged to assist a company’s internal teams. Businesses have also been making “buy or build” decisions to contract with e-discovery service vendors (not law firms) to perform the subsequent steps of identifying and collecting relevant ESI; in doing so, some vendors include the inventory and planning services described above and offer more complete solutions.

Ultimately, however, outside counsel must respond to the courts regarding the adequacy of these services. If counsel is not properly informed, or if inventories and records policies have not been properly prepared, counsel will be limited in their effectiveness in Rule 16 and Rule 27 conferences and related communications. This involves risks both for the lawyer and the corporate client; courts have specifically faulted outside counsel for their failures in this regard, even before the new Federal Rules become effective. *See Wachtel v. Guardian Life Insurance Company*, 2006 WL 1286189 (D. N.J., 2006); *Zubulake v. UBS Warburg LLC*, 229 F.R.D. 42 (S.D. N.Y., 2004); *Metropolitan Opera v. Local 100, Hotel Employees*, 212 F.R.D. 178 (S.D. N.Y., 2003). Thus, a corporate litigant cannot avoid outside counsel involvement—the critical variable is timing and the critical question is when should outside counsel be brought in.

Law Firm Qualifications

For earlier involvement in the planning to initiate preservation, outside law firms must be able to demonstrate they have an informed understanding of the intersection between corporate information systems and the prevailing legal requirements. They must be able to demonstrate that, within the law firm, they have invested in training their teams to navigate the realities of 21st-century business practices and have organized efficient means for working with their clients. For this component of litigation, companies are proving to be particularly resistant to paying the billable hour to educate outside counsel in essential IT knowledge.

Law firms should also evaluate the value of creating ongoing relationships (consistent with ethical constraints on the sharing of revenue) with e-discovery service vendors that, together with the law firm, can produce a more seamless delivery of the overall services needed by the corporate client.

Whether with others or on its own, trial counsel should be able to conduct efficient reviews of a client’s IT systems information; counsel should develop and employ consistent, defined procedures for reviewing the inventories and knowledge available and integrating that knowledge into what is required to advocate effectively for the client in the initial preservation and discovery proceedings.

Creating these types of resources and services can enable a law firm to compete more effectively in the “buy or build” decisions their clients need to make in order to better navigate the impact of the new Federal Rules.

*Jeffrey Ritter is co-founder and director of Waters Edge Consulting (www.wec-llc.com), assisting companies to implement competitive strategies in the rule-based management of information across complex systems, including cost-effective methods for records management and e-discovery production. He and Karen Worstell have co-authored the recently released Pike & Fischer title, **Evaluating the Electronic Discovery Capabilities of Outside Law Firms: A Model Request for Information and Analysis**. For more information or to place your order for this innovative publication, visit <http://www.pf.com/evalEDCofLawFirmsPD.asp> or call 800-255-8131 ext 248.*

Endnotes

1 Vol. 5, Issue 10 *Corporate Counsel* 104 (Oct. 2005).

2 Laura E. Ellsworth, Irene Savanis Fiorentinos, and Cecilia R. Dickson, *E-Discovery-Related Changes to the Federal Rules of Civil Procedure*, http://www1.jonesday.com/pubs/pubs_detail.aspx?pubID=S3599 (visited October 23, 2006).