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tel +44 (0)20 7012 1380 fax +44 (0)20 7729 6093 info@e-comlaw.com
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California's e-discovery rules: US and non-US impact

California has implemented new rules designed to provide guidance on the collection, preservation and production of electronic documents, which must be produced by both parties to a lawsuit on pain of sanctions. Melinda F. Levitt and Leeann Habte, of Foley & Lardner LLP, examine the impact that the rules will have in both the US and abroad, as case law suggests that EU data protection legislation does not necessarily protect European companies from requests for electronic documents. They also highlight steps that companies and lawyers can take to protect themselves from the possibility of being sanctioned for non-production of electronic documents.

It is official - as of 29 June 2009, California entered the 'discovery' electronic age. That is, California's State court system now will be governed by newly adopted rules designed to provide guidance on the preservation, collection, and production of electronic documents (known as 'electronically stored information' or ESI) in litigation pending in the State court system. This is an important development because although the US federal court system has had a set of ESI discovery rules in place since December 2006, thus far, only 22 of the 50 State court systems have adopted their own rules for handling ESI, leaving parties in the States without ESI rules somewhat adrift in terms of navigating the complexities that arise when trying to deal with a party's emails and documents that are created and stored on computers and other electronic devices. With California - one of the largest and most populous States - taking this step, it is clear that more and more litigants will be confronting the difficulties and additional expense associated with those dreaded words - 'electronic discovery'.

Before examining the significance of the new California statute, it might be useful to briefly review the basics of 'discovery' in the United States, which is followed in both the federal and State court systems. Discovery is a fact-finding process that takes place during the pre-trial phase in a lawsuit. Both parties to the lawsuit are able to request documents and other evidence from other parties, or can compel the production of evidence by using a subpoena - and, for the most part, the party receiving a discovery request must provide responses. Although the courts can get involved if a dispute arises about what is or is not responsive to discovery requests, the basic idea is that the parties, through their lawyers, self-direct and self-control the process - and, again, participation is mandatory, with failure to provide the requested documents subjecting the party to a variety of court-ordered sanctions ranging from monetary fines to automatic adverse judgments.

While 'discovery' was difficult enough while the world continued to function almost exclusively as a paper society, it changed radically with the advent of the personal computer, in particular the business personal computer. Starting in the mid-1990s or so, when the use of office desktop or laptop computers became common and the 'world wide web' opened to the masses, fewer and fewer business records were created on paper, filed away in folders and placed neatly in file cabinets or desk drawers. Now, business documents very often are not ever transferred to actual paper, but simply are found 'living' in the emails or electronic memoranda, spreadsheets, presentations and other such 'documents' that are readily accessible each morning when an employee logs on to his or her computer. While the reduction in the use of paper has its advantages, the amount and level of electronic communication has sky-rocketed in terms of volume.

From a 'discovery' perspective, the challenges posed by this electronic world are daunting. How does one now respond to a discovery request seeking 'all documents' relating to subjects x, y, and z, which are immediately relevant to a claim in a lawsuit - and, it should be noted that requests for 'all' documents about a certain subject are quite common in US discovery. Where are 'all' these documents located - or on whose computer, on which server... and how can a search be crafted to identify and segregate

them? Who has the ability to find and preserve them? What if they have been deleted? Can they still truly be found again? Isn't that what the computer 'back-ups' are for? What about the so-called 'data fragments' found on a computer hard-drive - is that a 'document' within the meaning of 'discovery'? What about the emails of an ex-employee who played an active role in the controversy now playing out in court? Where are those emails? What about text messages sent via mobile phone that constitute a business communication? What about voice-mails...are they a 'document' too?

The limitations of this article do not allow for an extensive examination into all the myriad questions and possible answers to these questions. Some are too technical and some are simply too mind-numbing. Suffice to say, however, these are the very questions that litigants in the federal courts, as well as judges, have been grappling with for several years and they are recognizing more and more that to find answers, they must turn to outside computer or electronic forensic experts for help and advice. As for anyone having faced or who will face a document request that includes ESI - these questions will need to be confronted. In terms of litigants in the California State courts, what does this mean? Keep in mind that under the US system of legal disputes, the State courts, unlike the federal system, often see smaller and more localized disputes. Although the individual disputes may be smaller, these State court systems collectively handle a larger litigation caseload than federal courts. More than 97% of all civil cases are filed in State courts. State courts have jurisdiction over a wide variety of civil cases, including all kinds of commercial transactions, contract disputes, property/real estate disputes, insurance matters, product liability cases, and personal injury claims. For cases like these, the rules governing e-discovery have significant implications.

It is not yet clear whether various European data privacy acts, or the EU Privacy Directive, will suffice to protect a European company from being subject to a court order to produce ESI

The California State court system, the largest in the nation, has more than 2,000 judges sitting in courthouses in 450 different locations throughout the State. The system has 58 Superior Courts (sometimes referred to as Trial Courts), six Courts of Appeal and a Supreme Court. The State's Superior Courts handle more than 1.4 million civil filings per year. Even before the new rules, e-discovery has been an issue in complex commercial litigation and business disputes pending in the California State court system. However, these new rules open the door for attorneys to invoke e-discovery - even in small to mid-size cases. While large corporations and businesses generally have sophisticated computer networks and information policies, smaller businesses and other persons that are now subject to the civil e-discovery rules may well have to grapple with the technical limitations of their information systems.

Do non-US based businesses have any reason to be concerned about discovery, in particular electronic discovery in State courts? The answer is certainly yes, as smaller business disputes - for example, disputes over products shipped to a US purchaser or other contractual matters - could well find themselves proceeding in a State court rather than in federal court, which for commercial disputes not involving a federal statute, is limited to hearing cases exceeding a value of $75,000. Moreover, if the foreign company has a US-based subsidiary, the foreign parent could find that it is subject to discovery requests served on or through its subsidiary even though it is not directly involved in the dispute. The test for document production is control - not location. Documents may be within the control of a party even if they are located abroad[1]. Numerous courts have concluded that a parent corporation has a sufficient degree of ownership and control over a wholly-owned subsidiary that it must be deemed to have control over documents located with that subsidiary. In other words, if the foreign entity has documents - including ESI - relevant to a dispute pending in a US court involving its US-based affiliate, the foreign parent will be expected to produce materials in response to the discovery requests[2]. It is not yet clear whether various European data privacy acts, or the EU Privacy Directive, will suffice to protect a European company from being subject to a court order to produce ESI. At least one California federal case has found that requiring the production of electronic data stored on computer servers located in the Netherlands was proper and that the existence of the Netherlands Personal Data Protection Act did not alter that result[3]. This example may prove very persuasive for California State court judges facing similar issues under the new statute.

So, do the new rules adopted in California represent good news? Answer: Yes, in that the new statute recognizes what has become a reality in today's world - i.e., electronic documents have become a dominant part of how we communicate and conduct business worldwide. Therefore, it is better to have rules to help parties, their lawyers and the courts navigate how and under what circumstances ESI can be obtained.

Let's ask that again...is this good

news? Answer: Well, not necessarily. The discovery of ESI can be very expensive and filled with traps for the unwary. Lessons from the federal court experiences show that proper ESI discovery requires a sophisticated level of technical knowledge quite often beyond that of the typical lawyer, litigant, or - in fact - judges. One federal judge who is regarded as a maverick on the subject recently explained that the complexity of ESI discovery leads to where 'angels fear to tread' and 'is clearly beyond the ken of a layman,' or lay-lawyer, thereby requiring the assistance of persons qualified to testify as experts in the field[4]. Now, with a whole new set of rules and even with the federal court examples to provide some guidance, State court lawyers, their clients and the courts will have to struggle through a learning process that seeks to balance the needs of litigation against the often significant costs and burdens associated with electronic discovery. Thus, until a body of law develops about how to interpret the new rules and how to balance the parties' interests, almost everyone walking into a California State courthouse will be standing on shifting sands.

Does the new California law address these issues? Answer: Yes and no. What the new California statute does is recognize that ESI constitutes 'documents' subject to discovery, thereby eliminating any arguments about whether a party must produce relevant emails and other electronic documents along with any paper documents. In other words - no more pretending that the bits and bytes buried in the bowels of a computer are not really 'documents.'

The new statute also provides some protections. For example, for non-parties who receive a subpoena requiring the production of ESI, the statute states that the courts 'shall protect' a person subject to a subpoena 'from undue burden or expense resulting from compliance.' This provision may prove to be very significant given that the collection and production of ESI can quickly cost hundreds of thousands of dollars - or more. Where the California courts will strike the balance remains to be seen.

These new rules open the door for attorneys to invoke e-discovery

The statute also states that unless special circumstances exist, sanctions shall not be imposed if responsive ESI is 'lost, damaged, altered, or overwritten as a result of the routine, good faith operation of an electronic information system.' This is stronger language than that found in the rules governing federal court proceedings. But, how the California courts will interpret this provision is a key question given that over the course of the first half of 2009, the federal courts have seen a significant jump in the number of requests for monetary and other sanctions for failure to properly preserve and then produce responsive ESI - a failure that can occur when ESI is deleted unintentionally or 'back-up' recovery tapes are not preserved. As the California statute points out however, the statute's 'safe harbor' does not alter a party's obligation to preserve potentially discoverable ESI, an obligation that arises as soon as a party is aware the litigation is taking place or is likely to take place. And preservation must be taken seriously such that, for example, employees are instructed to cease deleting emails on relevant subjects and there is sufficient monitoring to ensure that they comply, the 'auto delete' or other automatic systems-wide 'janitorial' functions are disabled and, as a precaution, disaster recovery tapes are preserved and taken out of normal rotations - at least initially - to ensure that historically created electronic documents are preserved. The preservation of such back-up tapes takes on particular importance in California because unlike the federal rules which provide certain protections for ESI regarded as 'not reasonably accessible' - which very often means disaster recovery back-up tapes - under the California scheme, the protections are weakened and the rules require a party to obtain a court order to avoid having to preserve and produce this type of ESI.

Quite recently, a federal court in the State of George imposed sanctions of just over a million dollars on defendants for numerous failures to preserve and produce ESI[5]. In a California federal court case, the defendants were ultimately ordered through a series of court orders to pay over $650,000 in ESI discovery sanctions[6]. Even before the adoption of the new State court rules, a California State court of appeals upheld ESI discovery sanctions of $90,000[7]. Although there are numerous decisions awarding lesser sanctions or even declining to award sanctions despite ESI discovery failures, the existence of decisions awarding substantial fines provides ample precedents for the California courts to follow. The question will be where will they draw the line.

Another change that the new California law will most certainly bring - although it is not specifically addressed in the new legislation - is a need for much greater cooperation between the parties' attorneys in order to develop a reasonable mechanism for obtaining requested ESI. For parties and attorneys used to engaging in litigation 'war,' the advent of ESI discovery has altered the playing field. To avoid having to produce - and the requesting party having to review - literally millions of electronic documents

that technically may be responsive to a request for 'all documents, including ESI' on certain topics, the attorneys will need to first understand how their clients maintain ESI and how their computer systems operate and who are the employees most likely to have truly relevant information. Once, having grasped this information, the attorneys from both sides should meet, confer and work together to develop a search and production protocol that will seek to capture the truly relevant without overwhelming the whole process or bankrupting either side. One of the most common tools used today is a list of 'keyword' search terms to which both sides agree, such that only documents containing those words or phrases are required to be produced. Although experts readily recognize that the use of such terms is imperfect at best, no other readily acceptable method has yet emerged for capturing potentially responsive ESI. Thus, as one federal judge just recently has explained in issuing a 'wake-up' call to attorneys:

'This Opinion should serve as a 'wake-up' call...about the need for careful thought, quality control, testing and cooperation with opposing counsel...Electronic discovery requires cooperation between opposing counsel and transparency in all aspects of preservation and production of ESI. Moreover, where counsel are using keyword searches...they at a minimum must carefully craft the appropriate keywords, with input from the ESI's custodians as to the words and abbreviations they use, and the proposed methodology must be quality tested to assure accuracy in retrieval and elimination of 'false positives[8]'".

California litigants should expect similar rules and dictates to emerge as the State courts come to terms with the new ESI rules that will govern discovery throughout the State. In sum, change has come to California, with more surely to follow.

Melinda F. Levitt Partner
Leeann Habte Associate
Foley & Lardner LLP
mlevitt@foley.com
lhabte@foley.com

1. In re Flag Telecom Holdings, Ltd. Sec. Litig., 236 F.R.D. 179, 193 (S.D.N.Y. 2007).
2. Dietrich v. Bauer, 2000 WL 1171132 (S.D.N.Y. 2000).
3. See Columbia Pictures, Inc. v. Bunnell, 245 F.R.D. 443, 452-53 (C.D. Cal. 2007).
4. United States v. O'Keefe, 537 F.Supp.2d 14, 24 (D.D.C. 2008) (Facciola, J.).
5. See Kipperman v. Onex Corp., 2009 WL 1473708 (N.D. Ga. 2009).
6. See Keithley v. Homestore.com, Inc., 2009 WL 816429 (N.D. Cal. 2009).
7. See Oz Optics v. Kakimoglu, 2009 WL 1017042 (Cal. App. 1 Dist. 2009).
8. William A. Gross Const. Associates, Inc. v. American Mfrs. Mut. Ins. Co., 256 F.R.D. 134 (S.D.N.Y. 2009).

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