BNA, INC.

DIGITAL DISCOVERY & E-EVIDENCE

VOL. 9, NO. 6 | **REPORT** | **JUNE 1, 2009**

Reproduced with permission from Digital Discovery & e-Evidence, 9 DDEE 6, 06/01/2009. Copyright © 2009 by The Bureau of National Affairs, Inc. (800-372-1033) http://www.bna.com

GUEST ANALYSIS

The authors argue that businesses and other large data producing entities—already struggling with the challenges of managing exploding volumes of electronically stored information (ESI) and, if they are regular litigants, the American philosophy of full pretrial disclosure—might now have a new cause for concern. A federal court decision out of the District of Utah will, if followed by other courts, vastly expand their duties to manage their data and preserve it for possible future litigation.

Outlier or Harbinger? Recent Case Invents New Preservation And Information Management Duties for Corporations

BY DAVID J. KESSLER AND ROBERT D. OWEN

The U. S. District Court for the District of Utah March 30 (i) found that companies have a common law obligation to third parties to manage their information in certain ways, (ii) expanded the preservation trigger far beyond the well-accepted ''reasonable anticipation of litigation,'' and (iii) criticized the defendant's reliance on line employees as the primary people responsible for giving effect to litigation holds (*Phillip M. Adams & Assocs. LLC v. Dell Inc.*, D. Utah, Case No. 1:05-CV-64 TS, 3/30/09 (2009 WL 91080)).

Apparently convinced that a defendant had destroyed ESI and covered it up, the court has, in the process of punishing that defendant, made some statements that would turn universally accepted information management principles on their head.

Case History and Background. Plaintiff Adams alleged that a group of defendants, including ASUSTEK Computer Inc. and ASUS Computer International (''ASUS''), infringed a number of its patents related to fixing an alleged defect in a floppy disk controller (''FDC'') (p. *2.) Specifically, Adams claimed that starting in 2000, ASUS improperly obtained Adams' patented technology and used it to test and fix ASUS chips and motherboards. (Id.) Adams also claimed that ASUS required its chip vendor, Winbond, to modify its chips using Adams technology.

The alleged defect in FDCs first came to prominence in a series of class action suits against major computer manufacturers including Toshiba, HP, and Sony. They were commenced in the late 1990s. In late 1999, Toshiba paid $2.1 billion to settle its litigation.

David Kessler is a partner at Drinker Biddle & Reath in its Intellectual Property and Commercial Litigation groups. David was one of the founders of the firm's E-Discovery and Data Management Team and as national e-discovery counsel represents his clients regarding both strategic and tactical e-discovery issues as well as information management choices. David is also a member of both Working Groups 1 and 6 of the Sedona Conference®.

Robert D. Owen is head of Fulbright & Jaworski's New York litigation group and founding co-head of the firm's E-Discovery and Information Management practice group. His practice focuses on litigation and electronic discovery. Mr. Owen has litigated commercial matters in New York and throughout the United States since 1973. Mr. Owen's long experience with computers—in the 1960s he wrote computer code as an engineering student, and in the 1980s he tried numerous computer cases for Wang Labs—has facilitated his nationally recognized work in e-discovery matters.

For several of these cases, including the Toshiba case, Adams acted as an expert for the plaintiffs. These cases called attention to Adams' FDC technology and, according to Adams, led to an increase in both legitimate licensing and infringement by other computer manufacturers.

Pointing to several documents it received from Gateway Inc., Adams claimed that it learned that ASUS was also infringing and gave ASUS notice of its intention to file suit. The parties disagreed on the timing of Adams' notice; Adams claimed notice was given on October 4, 2004 while ASUS claimed it was no earlier than February 25, 2005.

Motion for Sanctions. During pretrial discovery, Adams moved for sanctions for spoliation against ASUS. Adams lacked direct proof of spoliation and instead argued inferentially that spoliation must have occurred because ASUS had produced, in Adams' opinion, so few documents of the kind ASUS must have possessed.

The documents Adams claimed ASUS should have had included source code of certain test programs that allegedly infringed Adams' patents, e-mails or other documents related to the development of the test programs, and correspondence with suppliers or customers regarding the test programs. As the court stated:

> ''Adams' stated factual basis for this motion is twofold: first, that ASUS has illegally used Adams' patented software; and second, that ASUS has destroyed evidence of that use. The first assertion is identical to the liability issue in this case. The second assertion is premised on the first: Assuming ASUS *used* Adams' software, ASUS' *failure to produce evidence* of that use is sanctionable spoliation. Adams has no direct proof of destruction of evidence but is inferring destruction or withholding of evidence. Since Adams is convinced that ASUS infringed, Adams is also convinced that failure to produce evidence of infringement is sanctionable.''(p. *2.)

The court found that there was ''no direct evidence that ASUS possessed or copied Adams' software or of 'infringement' by the ASUS programs'' (p. *4). Nonetheless, the court found that ASUS did spoliate documents (p. *16) and based its holding on three novel concepts: (1) ASUS owed a duty to third parties to establish an information management system that did not tend toward the loss of data; (2) ASUS' duty to preserve arose in 2000 when the computer industry was sensitized to the FDC defect problem; and (3) ASUS' use of employees as the primary means of preserving ESI was unreasonable.

Information Management: Are There Legal Obligations to Third-Parties? On the first point, the court made the following statement in the course of discussing what it called ASUS' ''questionable information management practices'':

> ''The culpability in this case appears at this time to be founded in ASUS' questionable information management practices. A court—and more importantly, a litigant—is not required to simply accept whatever information management practices a party may have. A practice may be unreasonable, *given responsibilities to third parties*. While a party may design its information management practices to suit its business purposes, *one of those business purposes must be accountability to third parties*.'' *Adams v. Dell*, at p.*14 (emphasis supplied).

The court added that ''ASUS' system architecture of questionable reliability which has evolved rather than been planned, operates to deny Adams access to evidence. This should not be excused.'' Id.

The opinion sets forth no examples of what ''responsibilities to third parties'' the court had in mind, nor does it explain the contours of the ''accountability to third parties'' that it references without citation.

The prevailing view among the courts and commentariat is that information management policies, a/k/a document destruction policies, are common and serve proper business purposes.[1] Of course businesses and individual citizens do have statutory and regulatory duties to retain certain well defined classes of documents or, nowadays, ESI.

Moreover, even without a statutory command, parties have duties to preserve specific categories of information once litigation is commenced or reasonably anticipated, or a duly issued subpoena is received or anticipated. But these statutory and common law duties are a far cry from what the *Adams* court has assumed in its opinion.

When litigation is commenced or a subpoena received, the recipient has a reasonably well defined idea of what it must preserve. But the *Adams* court's guidance would leave all corporations, individuals, and other citizens utterly at sea. What ''responsibilities to third parties'' mandate preservation, and exactly what are the boundaries of those ''responsibilities''? How could an *Adams*-compliant information management policy be designed?

The *Adams* court appears not to have considered these issues, and the cases it references do not support the breadth of its holding nor its reasoning.

---

[1] The Supreme Court agrees, and it recently implied that such policies are not improper even when their purpose is to ''keep certain information from getting into the hands of others, including the Government.'' *Arthur Andersen v. United States*, 544 U.S. 696, 704 (2005).

 COPYRIGHT © 2009 BY THE BUREAU OF NATIONAL AFFAIRS, INC. DDEE ISSN 1941-3882

Preservation Obligations: Now Triggered by Actions Against *Others*? Turning to the second curious aspect of *Adams*: if followed by other courts, the opinion would greatly expand a potential litigant's duty to preserve by reducing the threshold to trigger a duty to preserve from ''reasonable anticipation'' to mere sensitization to an issue that may spawn litigation. The court found:

> ''In late 1999, Toshiba paid billions of dollars in a class action settlement related to the floppy disk errors at issue and a class action lawsuit was filed against HP. In early 2000, [ASUS employee] Sam Yang was writing emails about his work on the software ASUS was using 'to verify the FDC write-data distortion.' In late 2001, a patent application was filed by Yang and ASUS. In April 2000 a class action lawsuit was filed against Sony based on this alleged defect. Throughout this entire time, *computer and component manufacturers were sensitized to the issue*. The time period was the technology equivalent of the *103 Investors'* building fire. The building owner may not have known that a defective wiring bus caused the fire, or that suit would be filed, but the owner had a duty to preserve immediately after the fire. In the 1999-2000 environment, ASUS should have been preserving evidence related to floppy disk controller errors. (p. *13 (emphasis supplied).)

The court cites no evidence that ASUS knew or should have known that Adams was reasonably likely to sue ASUS for patent infringement. The court does not even cite any evidence that ASUS knew or should have known about Adams' technology or that Adams even had a patent on his technology (yes, this information was in the public domain by 2000, but all information in the public domain is not automatically imputed to every corporation).

Rather, *because companies (other than ASUS) were being sued in 1999 and 2000 for damages allegedly caused by a defect in their FDC, the court held that as of then ASUS had a duty to preserve information related to its solution to the alleged defect.*

In other words, the court held that ASUS should have anticipated in 2000 that it would be sued four years later and should have preserved its ESI and documents then and there.

Implications. From a practical perspective, this standard is much too broad and impossible to implement. If the *Adams* court's analysis were to be adopted, any company in an industry that faced litigation on a regular basis would need to start preserving documents generally related to the topic at issue in these litigations, even if it had no concrete reason to believe it would be sued (in fact, ASUS was not sued in the late '90s because of a defect in its FDC) and would need to maintain these documents indefinitely or risk a claim of spoliation if a litigation arises that is tangentially related to the original lawsuits.

The court's approach to preservation is too amorphous and too vague; for many companies wishing to avoid spoliation claims it bleeds too easily into a requirement to preserve all records forever.[2]

The court cites *103 Investors I, L.P. v. Square D Co.*, 470 F.3d 985 (10th Cir. 2006), to support its conclusion that ASUS had a duty to preserve (p. *12), but the citation is misplaced. In *103 Investors*, a building the plaintiffs owned was destroyed by fire which the plaintiffs ultimately blamed on a malfunction of a busway (a system of four electricity-carrying, insulated aluminum bars in aluminum casing). Id. at 987.

Prior to filing its complaint against the manufacturer of the busway, the plaintiff destroyed all but a small amount of the busway. Id. at 988. The court found that a sanction was proper because the plaintiff ''knew or should have known that litigation was imminent.'' Id. at 989.

These facts are not similar to the ones confronting the court in *Adams*. In *103 Investors*, the plaintiff had a particularized anticipation of a specific lawsuit with identifiable parties that concerned very specific evidence. By contrast, ASUS knew only that certain computer companies were being sued for defects in their floppy disk controllers under consumer protection laws.

The opinion does not state that there was any evidence that ASUS even suspected that Adams held a patent, much less that it felt any threat of litigation.

This is the difference between a credible threat of litigation, *see The Sedona Conference® Commentary on Legal Holds*: *The Trigger & The Process* (August 2007), p. 5 (''Guideline 1: Reasonable anticipation of litigation arises when an organization is on notice of a credible threat it will become involved in litigation or anticipates taking action to initiate litigation.''), a mere possibility of litigation, or the probability of suit by someone at sometime about something.

As the court in *Cache La Poudre Feeds, LLC v. Land O'Lakes Farmland Feed, LLC*, 244 F.R.D. 614 (D. Col. 2007), stated while evaluating whether a *demand letter* triggered the duty to preserve:

> However, a party's duty to preserve evidence in advance of litigation must be predicated on something more than an equivocal statement of discontent, particularly when that discontent does not crystallize into litigation for nearly two years. *Any other conclusion would confront a putative litigant with an intractable dilemma: either preserve voluminous records for an indefinite period at potentially great expense, or continue routine document management practices and risk a spoliation claim at some point in the future.* Id. at 623 (emphasis supplied).

Litigation Preservation: Can Companies No Longer Rely on Line Employees? The final surprising aspect of the *Adams* decision is its criticism of ASUS for relying on its front line employees to implement its preservation holds. Given that prior case law and commentary has long accepted the obvious necessity of relying on individual employees to segregate material for preservation, this criticism bears some scrutiny.

In *Adams* the court deployed heavy criticism at ASUS' failure to have a formal document retention policy.

> ''Neither the expert nor ASUS speak of archiving 'policies;' they speak of archiving 'practices.' Apart from archiving, neither the expert nor the employees describe any sort of backup system or data backup policy, past or present. Presumably ASUS' current data is at the mercy of individual employees' backup practices.'' (*Adams* at p.*13.)

---

[2] *See U.S. v. Maxxam Inc.*, 2009 WL 817264 (N.D. Cal. Mar. 27, 2009) (holding that destruction before reasonable anticipation of litigation was not spoliation as there was no duty to preserve); *Zubulake v. UBS Warburg LLC*, 220 F.R.D. 212, 217 (S.D. N.Y. 2003) (''*Zubulake IV*'') (parties must retain all relevant documents in existence or created after the duty to preserve attaches, but organizations need not preserve ''every shred of paper, every email or electronic document and every back-up tape'').

Without citing any evidence to support its conclusions, and apparently unaware of the standard operating procedure in the vast majority of American businesses, the court merely assumed that ''ASUS' practices invite the abuse of rights of others, because the practices tend toward loss of data.'' (Note the reference to the unspecified ''rights of others'' as a reason, presumably, to save everything.)

After a lengthy recitation of the e-mail and data practices of ASUS, the *Adams* court offers that while these practices ''may explain why ASUS has not produced certain emails'' it ''does not establish the good-faith nature of ASUS data management practices'' (Id. at p. *6). It is quite a leap to suggest that because ASUS, prior to 2004, had not instituted formal information management policies to the court's liking that it was necessarily operating in bad faith.

Note that the court does not find that ASUS failed to notify its employees of the need to preserve material, nor does it find that ASUS or its counsel failed to monitor the employees' compliance. It simply reasons from certain facts that ASUS must be sanctioned.

It may be that the court's discomfort was related to ASUS' failure to have a centrally determined document retention policy. The description of what ASUS did between 2000 and 2004 sounds not too dissimilar from what many companies did—allow their employees to determine what to save and what to delete, using their good faith, best judgment. It was common for the largest companies to have sophisticated document management policies, but for newer and smaller companies during that time, it was not.

ASUS got unlucky, because it was put under scrutiny in 2009 for its practices five and more years earlier, and the intervening time had seen a lot of change and evolution in conventional thinking about what was required. From this perspective, perhaps the court's criticism is at least understandable if ill-advised.

However, it is not yet mainstream thinking that in preserving materials in anticipation of litigation or investigations companies may not rely on their line employees. It's hard to see how they could do otherwise, short of saving everything.

There are hints in this opinion that the court believes litigants do or should have a ''save everything'' obligation, but fortunately that is not the law.

An Ill-Conceived Precedent? In three significant ways, the court in *Adams v. Dell* departs from established e-discovery precedent and thoughtful, well considered commentary, and creates new duties heretofore unknown in American jurisprudence. Part of the problem with this case's reasoning may be the result of judging 2004 decisions and actions by 2009 standards in this quickly evolving area of the law, but nonetheless, courts and practitioners would be well advised to avoid reliance on *Adams* for guidance in these areas. *Adams* is a classic example of the aphorism that cases with bad facts make bad law.

 COPYRIGHT © 2009 BY THE BUREAU OF NATIONAL AFFAIRS, INC. ISSN 1941-3882