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FEDERAL E-DISCOVERY

'Pippins' Order Highlights Preservation Burdens

By **H. Christopher Boehning**
And **Daniel J. Toal**

Preservation of electronically stored information (ESI) continues to be a vexing topic for attorneys and their clients. Judicial expectations vary widely, existing precedent is often unhelpful, and the Federal Rules of Civil Procedure (Federal Rules) do not give guidance on the issue. The lack of guidance, coupled with conflicting judicial standards, often causes parties—mindful that one misstep could lead to sanctions—to over-preserve.

Acknowledging the growing cry for guidance on the topic of preservation in the Federal Rules, the Discovery Subcommittee of the Advisory Committee on Civil Rules held a mini-conference on preservation and sanctions on Sept. 9, 2011. The subcommittee, chaired by Judge David Campbell, proposed three wide-ranging, alternative rulemaking proposals: a rule setting forth a detailed list of preservation duties with specific guidance on triggers, scope, and sanctions; a rule providing a more general list of such duties without specific guidance; and a rule focusing only on sanctions in the absence of reasonable preservation-related behavior.[1] It is unclear what, if anything, will come from the subcommittee's initial work.

So, in the absence of guidance, what is a party to do? In *Pippins v. KPMG, LLP*,[2] KPMG thought it had the right approach. Unable to agree with plaintiffs on the scope of preservation, KPMG moved for a protective order to limit the scope of preservation of computer hard drives or to shift the preservation costs to plaintiffs.

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Instead, Magistrate Judge James L. Cott of the Southern District of New York issued a Memorandum and Order requiring KPMG to "preserve the hard drives of thousands of former employees" who could fall within an as yet uncertified nationwide FLSA collective and/or a New York state class at a potential cost of millions of dollars to KPMG. KPMG, supported by an amicus brief filed by the U.S. Chamber of Commerce, has since asked U.S. District Judge Colleen McMahon of the Southern District of New York to set aside the Memorandum and Order.[3] Judge McMahon's opinion will be of keen interest to those who are struggling to contain the significant costs associated with e-discovery and eager for guidance.

Background

In *Pippins*, the plaintiffs allege that KPMG violated the Fair Labor Standards Act (FLSA) and New York state Labor Law by depriving audit associates of overtime wages.[4] The FLSA suit was filed by two former KPMG audit associates on Jan. 19, 2011 as a collective action on behalf of themselves and similarly situated KPMG audit associates. On March 9, 2011, Edward Lambert, another former KPMG audit associate, filed a separate putative class action, alleging that KPMG violated New York state Labor Law.

On April 25, 2011, the *Pippins* plaintiffs filed the First Amended Complaint, adding Lambert as a named plaintiff, and incorporating Lambert's New York state Labor Law claims.[5] The plaintiffs then moved for conditional certification pursuant to the FSLA (motion to certify). There are more than 7,500 potential opt-in FLSA plaintiffs, and more than 1,500 members of the putative New York class.[6] Judge McMahon stayed discovery pending the outcome of the motion to certify.[7]

> The 'Pippins' court denied KPMG's motion for a protective order and held that it must preserve hard drives of former and departing associates who could be members of the FLSA collective or putative New York class.

As the case progressed, the parties began to discuss ESI and preservation protocol.[8] For this and other related actions, KPMG had preserved material relevant to the plaintiffs' complaint, including

H. CHRISTOPHER BOEHNING *and* DANIEL J. TOAL *are litigation partners at Paul, Weiss, Rifkind, Wharton & Garrison LLP.* MAXWELL KOSMAN, *a law clerk at the firm, assisted in the preparation of this article.*

"time records showing their hours recorded, and payroll records showing their compensation."[9] KPMG also represented that it had preserved more than 2,500 hard drives of departing employees who are part of the putative New York class.[10]

During the negotiations, KPMG argued that, because it had already preserved numerous hard drives, going forward it should only be obligated to preserve a sampling of those hard drives against which search terms could be run.[11] Plaintiffs agreed in principle to the sampling method, but despite efforts by the court to mediate, the parties were unable to agree to a preservation approach.[12]

On Aug. 22, 2011, after negotiations with the plaintiffs failed, KPMG filed a motion for a protective order, asking the court to direct that KPMG be required to preserve only 100 hard drives against which search terms could be run, or, in the alternative, to shift the cost of preserving additional hard drives to the plaintiffs.[13] Plaintiffs, for their part, asked the court to require KPMG to provide five drives to be sampled, to preserve the hard drives until the parties could agree on a sampling methodology, and for "guidance about how to proceed."[14]

The Parties' Arguments

KPMG. Rule 26(b)(2)(C) of the Federal Rules states that

> on motion or on its own, the court must limit the frequency or extent of discovery otherwise allowed by these rules…if it determines that: …the burden or expense of the proposed discovery outweighs its likely benefit….[15]

Rule 26(c)(1) provides that a court "may, for good cause, issue an order to protect a party or person from annoyance, embarrassment, oppression, or undue burden or expense…."[16] Based on these rules, KPMG argued that the court should issue a protective order because the cost of preserving the hard drives of all potential collective and class members would outweigh the benefit.[17]

As to the benefit provided by wholesale hard drive preservation, KPMG first asserted that the best sources of information for plaintiffs' allegations could be found not on these hard drives, but rather in sources such as KPMG's time and payroll records, which had been preserved.[18] Further, KPMG noted that it was "already preserving complete and accurate records of the hours worked by its Audit Associates through its TIMEnX system."[19]

KPMG continued that even to the extent that some relevant information could be found on some of the hard drives, the duty of preservation is limited to "key players"—in this case, the named plaintiffs and possibly their supervisors—not every putative member of the class or collective action. Rather than preserving every hard drive, "representative discovery" could be obtained from the hard drives of the key players and from other hard drives that KPMG had already preserved.[20]

Finally, KPMG argued that the named plaintiffs' demand that KPMG preserve every hard drive due to their supposed relevance would be antithetical to plaintiffs seeking certification of a class and collective action, which presupposes "that their claims are representative of the proposed class or collective."[21]

As to cost, KPMG asserted that preserving every hard drive at issue would be inordinately expensive. It estimated the cost of preserving each hard drive at $600. By the time of the motion, KPMG estimated it had already spent roughly $1,500,000 on the collection and storage of 2,500 hard drives.[22] KPMG claimed that the cost to preserve and produce the ESI the plaintiffs have demanded would exceed $100,000,000.[23]

Judge McMahon's determination of the scope of the term "key players" could have a significant effect on the scope of preservation obligations going forward.

The Plaintiffs' Reply. In opposition to KPMG's motion, the plaintiffs first argued that the proportionality test does not appy to preservation, but rather is expressly limited to "*production* of discovery,"[24] observing that "KPMG cites not *one* case where a court excused a party of its prediscovery duty of preservation…."[25] Second, the plaintiffs argued that KPMG's motion was premature because there had been no opportunity to cross-examine KPMG on its claims of excessive cost, nor to investigate sample hard drives to determine their content.[26]

Third, the plaintiffs contested KPMG's claim that an examination of the hard drives was unlikely to lead to discovery of admissible evidence. Plaintiffs argued that the hard drives could contain material distinct from that stored on KPMG's servers and, in any event, the mere fact that some of the information could be obtained by other means did not make the hard drives any less relevant.[27] Finally, the plaintiffs disputed KPMG's claims about the costs of preserving the hard drives, and asserted that keyword searches—which KPMG proposed as a manner to limit preservation costs—are "completely useless for the type of information [the] Plaintiffs seek to obtain from the hard drives."[28]

The Court's Decision

The court denied KPMG's motion for a protective order, and held that KPMG must preserve the hard drives of former and departing associates who are potential members of the FLSA collective or putative New York class, at least until Judge McMahon has resolved the plaintiffs' motion to certify.[29]

KPMG's Discovery Obligations. Judge Cott held that KPMG failed to prove "the absence of a duty to preserve the hard drives."[30] In so holding, he observed that because the contents of the disputed hard drives are largely unknown, KPMG had not established that they do not contain relevant information.[31] As to the key player argument, he noted that:

> until the pending Motion to Certify is resolved, each and every Audit Associate whom the company deemed was exempt from overtime payments under the FLSA is a potential plaintiff and thus could be found to be a "key player."[32]

Indeed, he also observed that even if Judge McMahon were to deny the motion to certify, KPMG would *still* be obligated to preserve the hard drives because it is now on notice that the drives may contain material relevant to potential litigation—i.e., potential individual actions filed by the thousands of possible class or collective members. Finally, Judge Cott held that KPMG had failed to establish that the material on the hard drives was duplicative of other discoverable information.[33]

The Proportionality Test. Judge Cott also held that the proportionality test did not limit KPMG's preservation obligations. He noted that protective orders are generally issued in the context of production, and that "courts…have cautioned against the application of a proportionality test as it relates to preservation."[34] Judge Cott reasoned that, in the early stages of litigation, "it is unclear whether an application of a proportionality test would weigh in favor of a protective order."[35] Judge Cott thus concluded that:

> [u]ntil discovery proceeds and the parties can resolve what materials are contained on the hard drives and whether those materials are responsive to the plaintiffs' document requests, it would be premature to permit the destruction of any hard drives.[36]

The court also held that KPMG failed to establish that the plaintiffs should bear the cost of preservation "[f]or the same reasons that KPMG…failed to establish that it has no duty to preserve the hard drives."[37]

The Issues at Stake

KPMG has asked Judge McMahon to set aside Judge Cott's decision under Rule 72(a) of the Federal Rules and 28 U.S.C. §636(b)(1)(A).[38] The issues raised in this case—and highlighted in KPMG's memorandum and the Chamber of Commerce's supporting amicus brief—are significant. Judge

McMahon's decision will have a substantial effect on parties and attorneys alike.

How Is a "Key Player" Defined? Judge McMahon's determination of the scope of the term "key players" could have a significant effect on the scope of preservation obligations going forward. Judge Cott found that "[t]he scope of…preservation duty extends to the 'key players' in a lawsuit…."[39] But, in so holding, Judge Cott adopted a definition that would render any potential class member a key player. In moving to vacate Judge Cott's order, KPMG has thus argued that, by broadly construing the term "key players" to include all putative class or proposed FLSA collective members, the order may come into conflict with the well-established principle "that a defendant, in recognizing the threat of litigation, is not required to preserve every shred of paper, email or electronic document or backup tape."[40]

KPMG has also raised questions about the implications of Judge Cott's assertion that "the potential FLSA opt-ins and the putative class members are at the very least, key players in one of the many *potential* actions that could result if no class collective is certified."[41] Under this reasoning, were Judge McMahon to refuse to certify the class or collective action, KPMG would still be required to preserve the hard drives because of the incredibly remote possibility that thousands of individual claims might be filed. KPMG has urged Judge McMahon to reject this holding, arguing that it "would effectively face a perpetual duty to preserve and thus would be unable to implement document-retention policies, despite the important and legitimate purposes…they serve."[42]

Does Proportionality Have a Role? The Chamber of Commerce's amicus brief takes aim at Judge Cott's refusal to consider proportionality in the context of a preservation dispute. The Chamber notes that "the amount of electronic information that accumulates in modern enterprises is immense,"[43] and argues that without proportional limits on parties' preservation obligations, "transaction costs due to electronic discovery will overwhelm the ability to resolve disputes fairly in litigation."[44] Indeed, as the Chamber of Commerce notes, the "Manual for Complex Litigation (Fourth)" advises courts to consider proportionality in determining the scope of preservation required.

What Is the Court's Role? More broadly, this case will require Judge McMahon to determine the appropriate judicial role in preservation disputes. Judge Cott appeared to place significant weight on the fact that KPMG was unable to reach a preservation agreement with the plaintiffs. He noted, for instance, that "KPMG's ongoing burden [was] self-inflicted to a large extent."[45] For its part, KPMG noted that:

> in filing its motion for protective order when the parties could not resolve the preservation dispute, [it] followed the procedure recommended by courts and commentators alike.[46]

And although courts understandably prefer to have parties reach an agreement about the appropriate scope of ESI preservation, it seems highly questionable to suggest that KPMG's inability to do so with its adversary meant that KPMG's preservation burden was a problem of its own creation. After all, a party seeking to impose maximum burden on its adversary may have little incentive to reach an agreement clarifying and limiting the adversary's preservation obligations.

Moreover, if the consequence of the inability of the parties to reach an agreement is that all conceivably relevant data must be preserved, a litigant behaving strategically will be less, rather than more, likely to agree on a preservation protocol since the absence of an agreement may be held against the party who has more to preserve.

Conclusion

As evidenced by the fact that the Chamber of Commerce saw fit to submit an amicus brief regarding a discovery dispute, the resolution of KPMG's motion for a protective order has potentially far-reaching implications and threatens to radically alter the scope of ESI preservation obligations. Preservation obligations as broad as those Judge Cott was prepared to impose on KPMG threaten to exponentially increase the already crushing costs of discovery and heighten the risk that, absent prevailing on a dispositive motion, resolution of disputes on the merits may become cost prohibitive in a large percentage of cases. In view of the stakes, rest assured that the bar will be following Judge McMahon's resolution of this motion with an interest rarely seen in the typically mundane world of discovery motions.

1. Materials related to this mini-conference are available at http://www.uscourts.gov/RulesAndPolicies/FederalRulemaking/Overview/DallasMiniConfSept2011.aspx.
2. *Pippins v. KPMG LLP*, No. 11 Civ. 0377 (CM) (JLC), 2011 WL 4701849, at *1 (S.D.N.Y. Oct. 11, 2011).
3. Notice of Motion, at 1, *Pippins*, 2011 WL 4701849.
4. *Pippins*, 2011 WL 4701849, at *1.
5. Id. at **1-2.
6. Id. at *3.
7. Id. at *2.
8. Id.
9. Memorandum of Law in Support of Defendant's Motion for a Protective Order (Memorandum in Support), at 4, *Pippins*, 2011 WL 4701849.
10. Id.
11. Id. at 5.
12. *Pippins*, 2011 WL 4701849, at *2.
13. Id.
14. Id. at *4.
15. Fed. R. Civ. P. 26(b)(2)(C).
16. Fed. R. Civ. P. 26(c)(1).
17. Memorandum in Support, at 6 (citing *Zubulake v. UBS Warburg LLC*, 217 F.R.D. 309, 316 (S.D.N.Y. 2003)).
18. Id. at 8.
19. Reply Memorandum of Law in Further Support of Defendant's Motion for a Protective Order, at 8, *Pippins*, 2011 WL 4701849.
20. Memorandum in Support, at 11.
21. Id. at 10.
22. Id. at 12.
23. Id. at 14.
24. Plaintiffs' Memorandum of Law in Opposition to Defendant's Motion for Protective Order at 10, *Pippins*, 2011 WL 4701849 (emphasis in original).
25. Id. at 11 (emphasis in original).
26. Id.at 13.
27. Id.
28. Id. at 15-16.
29. *Pippins*, 2011 WL 4701849, at *10.
30. Id. at *8
31. Id. at *6.
32. Id.
33. Id. at *7-*8.
34. Id. at *8.
35. Id.
36. Id.
37. Id. at *10.
38. Notice of Motion, at 1, *Pippins*, 2011 WL 4701849.
39. *Pippins*, 2011 WL 4701849, at *5.
40. Defendant's Objections to the Magistrate Judge's Memorandum and Order, Entered and Served on Oct. 11, 2011, Concerning Preservation of Computer Hard Drives of Potential Members of the Putative Class or Collective Action (Defendant's Objections), at 8, *Pippins*, 2011 WL 4701849 (citing *Zubulake v. UBS Warburg, LLC*, 220 F.R.D. 212, 217 (S.D.N.Y. 2003)).
41. Id. at 10 (internal citations omitted) (emphasis in original).
42. Id. at 11 (citing *Arthur Anderson LLP v. United States*, 544 U.S. 696, 704 (2005)).
43. Brief for Chamber of Commerce of the United States of America as Amicus Curiae In Support of Defendant's Objections to the Magistrate Judge's Oct. 11 , 2011 Order, at 3.
44. Id. at 6 (quoting "The Sedona Principles: Second Edition, Best Practices Recommendations & Principles for Addressing Electronic Document Production," 17 cmt. 2.b. (2007).
45. *Pippins*, 2011 WL 4701849, at *9.
46. Defendant's Objections, at 16, *Pippins*, 2011 WL 4701849.