Implementing a Litigation Hold

Nicholas Panarella and Wook Kim, Kelley Drye LLP

A Practice Note discussing the key issues that companies should consider when instituting a litigation hold and the potential consequences of failing to implement one appropriately.

When faced with litigation or a regulatory investigation in the US, companies must implement and maintain litigation holds (also called document holds) designed to identify and preserve relevant evidence. Companies that fail to properly implement litigation holds risk severe legal repercussions, including monetary penalties and adverse jury instructions.

This Note discusses how to institute and enforce a litigation hold. Specifically, it addresses:

- What a litigation hold is.
- The consequences of failing to implement a litigation hold.
- The events that may trigger the duty to implement a litigation hold.
- How to set up, communicate and supervise a litigation hold.

WHAT IS A LITIGATION HOLD?

Although companies doing business in the US generally are not required to indefinitely preserve business records and information, companies must preserve relevant information when a lawsuit or an investigation is reasonably anticipated. This duty stems from both the common law duty to prevent spoliation of evidence and certain statutes and regulations, including the Sarbanes-Oxley Act of 2002 (*Pub. L. No. 107-204, 116 Stat. 745*).

A litigation hold is an instruction within a business organization directing employees to preserve (and refrain from destroying or modifying) certain records and information (both paper and electronic) that may be relevant to the subject matter of a pending or anticipated lawsuit or investigation. The ultimate purpose of a litigation hold is to ensure that the company complies with its duty to preserve and produce relevant information, including electronically stored information (ESI), in litigation or to a regulator.

CONSEQUENCES OF FAILING TO IMPLEMENT A LITIGATION HOLD

Failure to timely institute and maintain a litigation hold can have serious consequences for a company. US courts sanction companies for failing to adequately implement litigation holds. These sanctions can include:

- Monetary penalties, such as payment of the adversary's legal fees and costs.
- Adverse inference instruction(s) to the jury relating to the information lost or destroyed.
- Preclusion of evidence to support a claim or defense.
- In extreme cases, default judgment or dismissal.

(*Pension Committee of the University of Montreal Pension Plan v. Banc of America Securities, 685 F. Supp. 2d 456, 469 (S.D.N.Y. 2010).*)

Recent Examples of Sanctions

Several recent court decisions demonstrate the types of sanctions companies face for failing to properly implement a litigation hold. In several instances, companies that had issued a hold were still sanctioned because the hold was not complete or timely.

For example, in *Pension Committee*, the court ordered several plaintiffs who were negligent in their efforts to implement and enforce a litigation hold to pay the defendants' costs and attorneys' fees. In addition, the court instructed the jury to take an adverse inference against several other plaintiffs who were grossly negligent in their failure to properly implement and enforce a litigation hold. The adverse jury instruction would permit the jury to consider evidence regarding the plaintiffs' spoliation of evidence, as well as consider whether the lost evidence would have helped the defendants.

A New York state appellate court recently upheld the imposition of an adverse inference against a company that had put a litigation hold in place but failed to suspend the automatic deletion of emails until four months after it had been sued (*Voom HD Holdings v. EchoStar Satellite LLC, 93 A.D.3d 33 (N.Y. App. Div. 2012)*). The appellate court agreed with the trial court that the hold should have been implemented at least 8 months before the suit was filed when the company's corporate counsel sent a demand letter to the adversary.

In another case, a court identified several failures to preserve relevant ESI, which resulted in the permanent destruction of data, including:

- The deletion of ESI after the lawsuit was filed.
- Attempts to permanently erase deleted ESI.
- Failure to preserve an external hard drive containing key information.

(*Victor Stanley, Inc. v. Creative Pipe, Inc., 269 F.R.D. 497, 501 (D. Md. 2010)*).

The court, among other things, ordered that a default judgment be granted against the defendant on the plaintiff's primary claim.

Another court ordered an adverse jury instruction and monetary sanctions, including the payment of plaintiff's attorneys' fees and costs, against a defendant for failure to include in its litigation hold a key employee that was rehired for purposes of investigating a crash that was the subject of the lawsuit (*Yelton v. PHI, Inc., No. 09-3144C, 2011 WL 6100445 (E.D. La. Dec. 7, 2011)*). The court's sanctions were despite the fact that the litigation hold was otherwise timely implemented to cover all other custodians.

Likewise, a court imposed monetary sanctions on in-house counsel for his destruction of and failure to preserve evidence, despite the fact that he was neither a named party to the action nor an attorney of record (*Swofford v. Eslinger, 671 F. Supp. 2d 1274, 1287-88 (M.D. Fla. 2009)*).

WHEN TO IMPLEMENT A LITIGATION HOLD

The duty to preserve electronic and paper records arises once a company:

- Receives a complaint or is otherwise put on notice of a lawsuit against it.
- Receives a subpoena for information as a third party to an existing lawsuit.
- Receives a formal order of investigation from a US regulatory body.
- Becomes, or should reasonably become, aware of a potential legal claim against it.

US courts consistently rule that the duty to preserve may begin whenever litigation or an investigation is reasonably anticipated, which may well happen before a complaint is filed against the company. At that time, companies must issue a hold and suspend their routine document destruction under their normal document retention policies to prevent the loss of information that may be relevant to the subject matter of the proceeding.

Determining when litigation or an investigation is reasonably anticipated is a fact-specific inquiry and not always an easy task. The question of when and how broadly a litigation hold must be issued is not perfectly clarified by case law. However, a reasonable anticipation of litigation generally arises when a company is on notice of a credible threat that it will become involved in litigation or subject to an investigation, such as when it is involved in a pre-litigation dispute (having received cease and desist letters, for example).

Likewise, when a company decides to initiate a lawsuit, it is almost always under a duty to preserve. In these types of situations, a written litigation hold notice should be issued quickly (see *Standard Document, Document Preservation Notice (www.practicallaw.com/0-501-1545)*).

Other possible triggering events include:

- Management discussions about a complaint that can lead to litigation (see *Doe v. Norwalk Community College, 248 F.R.D. 372, 377 (D. Conn. 2007)*).
- A whistleblower's complaint to management.
- Any other particular event that in the company's experience has typically resulted in litigation or a government investigation.

Rumors and Verbal Threats

In situations involving rumors and verbal threats of litigation, the court's determination of whether a party should have reasonably anticipated litigation is based on that party's good faith. Courts examine the circumstances to judge whether there is a frivolous attempt from a pro se litigant to extort a settlement from the company, for example, or a warning letter from a reputable law firm representing a credible plaintiff. The latter example often triggers a duty to preserve, while the former does not. The test is whether the party reasonably evaluated the totality of facts and circumstances known to it at the time the litigation hold decision was made.

WHAT THE LITIGATION HOLD SHOULD INCLUDE

A litigation hold should inform employees of their duty to identify, locate and preserve information that may be relevant to an ongoing (or anticipated) litigation or investigation. Information is relevant to a lawsuit or an investigation if:

- It relates to the claims or defenses alleged in the lawsuit or the subject matter of the investigation (see *Fed. R. Civ. P. 26(b)(1)*).
- It is reasonably likely to lead to the discovery of admissible evidence (see *Fed. R. Civ. P. 26(b)(1)*).
- A company "knows or reasonably should know" an opposing party will likely request this information in "reasonably foreseeable litigation" (*Mosaid v. Samsung, 348 F. Supp. 2d 332, 336 (D.N.J. 2004)*).

Relevant evidence may exist in paper or electronic form and companies must preserve this evidence regardless of the media in which it exists. Relevant information may therefore be located in several places, including:

- Employee files and workspaces.
- Document warehouses.
- E-mails.
- Voicemails.
- Computer hard drives.
- External hard drives (including "memory sticks" or universal serial bus (USB) drives).
- Back-up tapes.
- Digital copiers.

- Databases.
- Outsourced locations.
- Hand-held digital devices and personal digital assistants, such as Blackberries, iPhones and tablet computers.

Companies should therefore create a list of places to look for responsive information.

PRACTICAL TIPS FOR INSTITUTING AND MANAGING A LITIGATION HOLD

Effectively instituting and managing a litigation hold involves preparation and requires several steps, including:

- Assembling a team to oversee the hold (see *Identify a Litigation Hold Team*).
- Developing a plan to implement the hold (see *Develop a Reasonable Litigation Hold Plan*).
- Issuing the hold (see *Issue the Litigation Hold Notice in Writing*).
- Properly distributing the hold (see *Communicate and Distribute the Written Litigation Hold Notice*).
- Ensuring compliance with the hold (see *Monitor and Enforce Compliance*).
- Modifying the hold as necessary (see *Modify or Remove the Hold When Necessary*).
- Removing the hold when no longer required (see *Modify or Remove the Hold When Necessary*).

Identify a Litigation Hold Team

This team oversees the litigation hold and document preservation processes. Because of the legal and technological issues involved in implementing a litigation hold, as well as the possible effects of a hold on the company's business, the team should include:

- Key employees from the business units affected by the litigation or investigation.
- An employee from the information technology and records departments.
- In-house counsel.
- Outside US counsel.

This team should coordinate to determine:

- What information (electronic and otherwise) is available.
- The form in which it is available.
- How it can be preserved cost-efficiently.

Small companies without in-house counsel may want to appoint a high-level executive (the chief information officer or chief financial officer, for example) to be in charge of implementing and monitoring a litigation hold, as well as liaising with outside counsel.

Develop a Reasonable Litigation Hold Plan

The company's litigation hold plan should define the scope of the company's efforts to identify and preserve relevant information. At a minimum, the plan should:

- Identify the key players and custodians of relevant records associated with the litigation's or investigation's subject matter, including potential witnesses, support staff and former employees.
- Identify other employees who may have records relevant to the dispute.
- Identify the relevant time period to which the preservation obligation applies.
- Identify the types of records and materials, including ESI and paper documents, that must be preserved.
- Outline the company's data storage architecture and identify where the relevant information may reside (for example, on network servers, digital copiers and back-up tapes and in employee offices and e-mail folders).
- Determine whether the company has possession, custody or control of potentially relevant information and data, after understanding the company's data storage procedures.

The litigation hold notice should be issued as soon as a lawsuit or a regulatory investigation is reasonably anticipated. If the company decides against issuing a litigation hold, the company, through counsel, should document that decision and the reasons behind it.

Issue the Litigation Hold Notice in Writing

The written notice should include:

- A clear description of the subject matter of the litigation or investigation, to help the recipient determine if he possesses relevant information.
- Explicit instructions not to destroy or modify records, with examples of the records that should be preserved and their sources, such as:
  - work and home computers;
  - cell phones;
  - flash drives and USB keys;
  - office and personal voicemail systems; and
  - back-up tapes.
- Warnings to the recipient regarding the importance of preserving potentially relevant materials and the possible consequences of not complying with the notice.
- Detailed guidelines that set out the date ranges for and types of documents and materials that should be preserved.
- An explanation to the recipient that the duty to preserve is continuing and does not end until further notice.
- Contact details for corporate counsel in charge of issuing and enforcing the litigation hold, or another internal point person who is responsible for answering questions about the hold and receiving relevant information collected by company employees.

Although outside counsel may draft the notice, it should be issued in the name of an individual recognized as having authority within the organization for it to be effective. The hold notice should be in writing to preserve a record of the company's efforts to safeguard documents, in case a later dispute arises over the company's document preservation efforts (see *Standard Document, Document Preservation Notice) (www.practicallaw.com/0-501-1545)*. The hold notice and its instructions must be tailored to the specific matter. It should state what categories of records the recipient should preserve and what to do with those preserved records. After reading the notice, the employee should have a concrete idea on what must be preserved and not feel that he has to preserve absolutely everything.

Communicate and Distribute the Written Litigation Hold Notice

The hold notice must be communicated to all key players and anyone in the company with relevant materials, including departing and re-hired employees. The head(s) of the business unit(s) affected by the proceeding should be consulted for the identities of the key players. Counsel may need to add more employees to the litigation hold list as it conducts further investigation into the facts and reviews additional documents. For a litigation hold to be distributed effectively, it may not be sufficient to simply e-mail it company-wide. Instead, counsel should determine the types of information the key players are likely to possess and where they keep it. It may be necessary to meet with some or all of these key players to ensure they understand the gravity of the duty to preserve and their obligation to help the company avoid sanctions.

Moreover, counsel should provide the litigation hold notice to information technology (IT) personnel (internal and outsourced) so that they may execute the critical step of suspending any of the company systems' auto-delete features that could lead to the destruction of relevant data. This may include issuing instructions to IT personnel and managers to keep the files, e-mails and any records in the custody of any departing employees (including temporary staff and interns) until the litigation hold team has reviewed them and determined whether any must be retained.

Meet with IT personnel before and after issuing the litigation hold to better understand:

- Where various categories of information are stored.
- How accessible the different types of information are.
- Who in the company has had access to which type of information.

Monitor and Enforce Compliance

The company should initially require a certification or other type of written confirmation from each recipient of the litigation hold notice acknowledging that he has read, understands and will comply with the hold. In-house or outside counsel (or another individual in the company with authority to oversee the hold process) should track who received the notice and who has returned a confirmation receipt, as well as the dates any changes were made to the notice. The company should also track the costs related to implementing and enforcing the litigation hold and maintain the contact information of any departing employees identified as having had access to or custody of relevant documents.

To help in capturing all of the potentially relevant documents and records, consider copying and storing certain users' hard drives and paper files for future review by the legal team. Doing this before formally issuing the written hold notice can reduce the risk that certain employees will delete relevant material they think endangers their employment.

In addition, counsel should:

- Periodically issue reminder notices.
- Monitor compliance with the hold by examining its effectiveness weeks and months after it is instituted.
- Keep the hold in place at least until the matter is concluded.

Effective implementation of these litigation hold steps can help companies comply with the law, uncover relevant facts, appear responsible to the court and/or regulatory agency and avoid costly sanctions.

Modify or Remove the Litigation Hold When Necessary

The company must supplement the litigation hold notice immediately after any event that changes the scope of the original hold, such as when new:

- Issues arise in the course of the proceeding.
- Locations of additional relevant information are found.
- Additional employees are identified (possibly after a deposition) with potentially relevant information.

When any of these happen, it may be necessary to determine whether new preservation efforts are necessary and whether there are additional key custodians that counsel should interview. It may also be necessary to meet with IT to examine the results of their preservation activities and discuss any helpful changes. These efforts may help the company respond to arguments that its document preservation efforts were insufficient, especially in situations where an employee does not follow the company's document preservation directives.

The modified hold notice can serve as a reminder of the original obligation to retain documents and in addition include:

- Descriptions of the information that employees must retain.
- A list of places they must search.
- Any additional points they must know to properly preserve any resources relevant to the litigation.

Counsel should also set up an automatic reminder tool that periodically (quarterly, for example) sends all of the original litigation hold recipients (and any new ones) an updated litigation hold notice. The litigation hold team should re-evaluate the hold's scope and the notice's language before sending the reminder,

being careful to include any additional necessary locations and types of documents potentially relevant to the dispute. This also is the right time for the litigation hold team to update its recipients list, remove custodians no longer with the company if necessary and add new employees who were not with the company at the time the last reminder was distributed. Counsel may want to meet with any new employees to explain their obligations under the hold and answer their questions.

Modifying the litigation hold can also mean reducing the amount of people from whom counsel must collect documents, or removing certain types of information from the hold.

Counsel should ensure that any changes made to the hold are documented, including the reasons for the changes and the names of people consulted about these changes.

Terminating the litigation hold is a necessary final step in the process. It provides for the company's return to its normal document retention policy and ends the costs incurred with locating, reviewing and storing electronic and paper documents.