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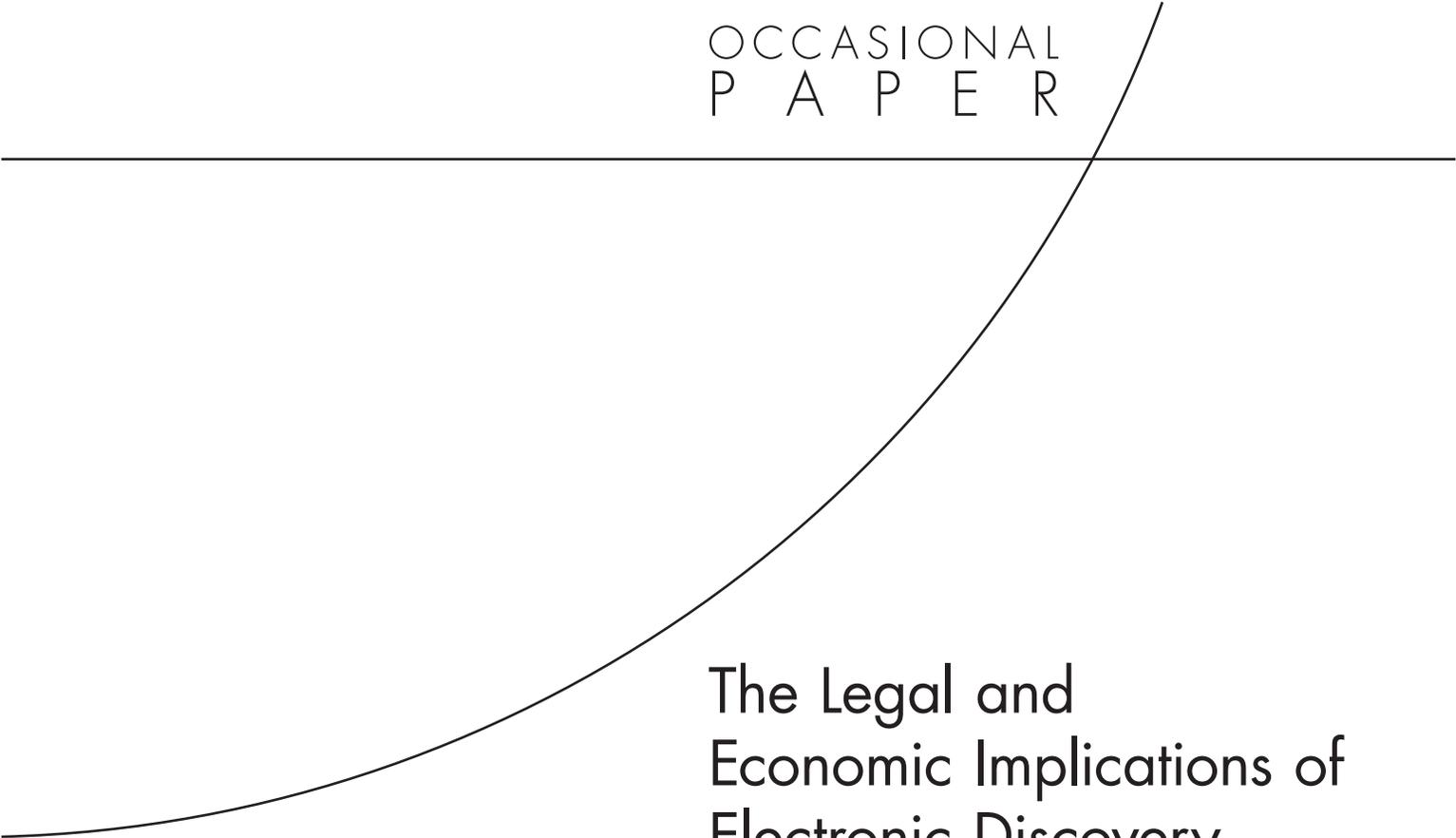
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OCCASIONAL
P A P E R



The Legal and Economic Implications of Electronic Discovery

Options for Future Research

James N. Dertouzos, Nicholas M. Pace,
Robert H. Anderson



RAND INSTITUTE FOR CIVIL JUSTICE

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1776 Main Street, P.O. Box 2138, Santa Monica, CA 90407-2138
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Summary

Pretrial discovery, involving the exchange of relevant information between litigants, is central to the American civil legal process. With the development of computer technologies, most information that is produced, distributed, and stored by business now exists in electronic form. Based on a review of the literature, interviews with practitioners (corporate counsel, information technology [IT] directors, and independent law firms) and a preliminary modeling effort, this paper identifies several salient legal and economic issues raised by e-discovery and proposes an agenda of research designed to improve future policy.

New technology can promote the efficient flow of information, thereby improving the civil justice system. However, if not managed properly, it is also possible that the sheer volume and complexity of electronically stored information (ESI) can increase litigation costs, impose new risks on lawyers and their clients, and alter expectations about likely court outcomes. Such changes could influence litigation patterns such as the propensity to file suits, the amounts of settlements, and the frequency of trials. In addition, businesses could face higher operational costs as they adopt technologies and IT practices in response to the likelihood of e-discovery requests. These costs could well increase dramatically with the size, scope, and complexity of business functions. On the other hand, smaller businesses, with less sophisticated technologies and methods for responding to e-discovery requirements, may face a disadvantage in the competitive world of litigation.

In response to concerns raised about these issues, there have been recent changes in the Federal Rules of Civil Procedure that focus on electronic discovery. However, many questions remain about their implementation, likely impact, and whether similar rules should be adopted at the state level. Furthermore, anticipated changes in technology, such as new communications platforms, improved search tools, and increased storage capacity, are likely to alter the future landscape significantly. Thus, e-discovery will be a topic of considerable policy importance for many years.

Given the importance of these issues, the RAND Institute for Civil Justice is supporting new research on e-discovery. This paper presents the results of an exploratory study to identify the most important legal and economic implications of e-discovery and to develop a plan of research to be conducted over the next several years. Our approach involved four tasks: We conducted multiple interviews with plaintiff and defense attorneys as well as IT personnel and in-house counsel for a number of large corporations; we reviewed the current state of e-discovery law and practices, including the main features of the new Federal Rules of Civil Procedure; we conducted an initial modeling effort to simulate the range of plausible effects of e-discovery on case outcomes; and we analyzed the implications of our results for future research.

Results of Interviews

Our interviews highlighted a number of concerns about the effects of e-discovery on the legal system. First, the most frequent point mentioned in interviews was the rising costs of reviewing information produced in e-discovery. Interviewees claimed that as much as 75 to 90 percent of cost increases come from the additional time it takes attorneys to conduct an “eyes-on” review of electronic documents. Although interviewees acknowledged that certain types of litigation may be less affected by these trends, it is likely that, in many areas of litigation, increasing costs are changing perceptions about case value and influencing incentives to file suits, settle cases, and go to trial.

Second, interviewees expressed concern about the vulnerability of electronic evidence: Those requesting evidence emphasized the risk of willful tampering or destruction of evidence, and those producing evidence emphasized the potential for significant sanctions for inadvertent failure to preserve information.

Third, interview results were mixed concerning the new federal rules on e-discovery. Although many interviewees were optimistic that the new rules would reduce inconsistencies among states in handling electronic evidence, they felt that the regulations did not go far enough to clarify the steps that should be taken with potential evidence in advance of and during litigation.

Current State of E-Discovery Law

Despite all the concern about e-discovery, there have been very few judicial rulings at either the federal or state level to help litigants make decisions about such evidence. Because only a handful of states have had formal rules of discovery tailored to electronic data and because appellate cases are silent on the subject, typically existing laws that govern paper-based discovery have been applied to electronic data. The few trial court decisions that have explored e-discovery issues have provided some guidance to the legal community. Besides those, until the Federal Rules of Civil Procedure were enacted in December 2006, two other sources have been used to define certain parameters: the Sedona Conference guidelines and the American Bar Association’s *Civil Discovery Standards*.

The new federal rules are expected to influence the way electronic evidence is understood and handled in many states. They define with more specificity what e-discovery includes and they clarify how it should be produced. For example, the rules distinguish between relevant data that are “reasonably accessible” and must be produced without complaint and data that would impose an undue burden or expense to retrieve and therefore must be identified and preserved but need not be produced unless requested by the judge. The new rules also offer guidance about the format for production, what to do when privileged information is inadvertently shared, and what restrictions apply to sanctions for data lost in circumstances that were clearly unintended.

However, the new rules leave a number of key questions unresolved: For example, what constitutes “reasonably accessible” data? What steps should be taken to preserve electronic information that might be sought as evidence? And what are the potential legal ramifications of adopting different business practices?

Results of Exploratory Modeling

To explore the potential impact of e-discovery on litigation outcomes, we developed an illustrative model of legal decisionmaking. Although the work is preliminary, it indicates that a theoretical model can lead to testable empirical results developed in future studies. The simulations produced by the preliminary model identify a range of plausible effects of e-discovery on litigation, depending on certain case characteristics.

The model assumes that plaintiffs and defendants form expectations of litigation costs and benefits based on the information they receive about likely legal outcomes. The expected value of a case to plaintiffs, for example, is their estimate of the probability of a range of possible awards, including the chance that they will lose the case. For defendants, the value of a case represents a risk-adjusted expected liability based on a perceived range of plausible case outcomes and their probabilities. Given their expectations, the parties in a case have incentives either to settle or to move to the next phase of the legal process.

The influence of e-discovery on outcomes depends on whether the e-discovery process adds information that changes perceptions about either case value or costs. For example, e-discovery can provide information that changes perceptions of expected case values. Before discovery, an assessment of case value depends on a range of expected case outcomes based on closely held information. But after e-discovery, these expectations are modified. If the plaintiff discovers information that strengthens his or her case, for example, then settlement demands will increase.

E-discovery could also increase or decrease production costs. Clearly, the higher volume of information requires a higher level of attorney review. E-discovery also increases certain risks, such as the potential for severe sanctions or loss of attorney-client privilege. On the other hand, improved technologies for storage, reproduction, and transmission of data could significantly decrease some costs. It could also make it easier to identify relevant information and thereby reduce the need for “eyes-on” attorney review.

In general, this theoretical model of litigant behavior suggests a number of effects of e-discovery on case outcomes, depending on case characteristics. For example:

An increase in costs for both parties will increase the probability of settlement. A decrease in costs will have the opposite effect.

An increase in defense costs will increase settlement amounts, while an increase in plaintiff costs will have the opposite effect. Again, these effects are reversed if costs decline.

Increased information exchange will tend to diminish the gap in expectations about trial outcomes and increase the number of early settlements.

E-discovery, to the extent that it increases perceived risks for either party early in the process, will encourage early settlement.

This model suggests that e-discovery will have different levels of effects on different types of cases, such as employment cases, business-versus-business cases, regulatory cases, and class-action cases. We offer illustrative examples of these effects in this paper, which we propose to examine more closely through econometric analysis of actual case outcomes obtained from a survey of law firms, as described below.

Proposed Research Agenda

Because e-discovery will affect litigation outcomes within a complex and interactive system that includes technology, business practices, and public policy, the independent effects of one component must be evaluated in terms of the others. Federal and state rules and case law, for example, will be influenced by the evolution of technology and prevailing business practices. Such policies will have a direct effect on legal outcomes as well as business practices. We propose five studies that focus on particular elements of this system, but our ultimate goal is to integrate what we learn so that we can maintain a full system perspective on the issue.

Impact of E-Discovery on Litigation Outcomes

Based on a new model of litigant decisionmaking and econometric analysis of survey data on actual case outcomes, this project will evaluate the impact of new technology and e-discovery rulemaking and judicial decisions on litigation patterns such as propensities to file cases, litigation costs, propensity to settle, settlement amounts, and probability of going to trial. In conducting this research, we will consider impacts on both plaintiffs and defendants.

The Costs of E-Discovery

This research will develop a cost model, based on technical information and analysis of survey data, that links discovery costs with several observable characteristics, including company size, industry, IT structure, data location, case type, and regulatory retention requirements. One product from this task will be a cost guidebook that would enable courts to evaluate the likely burden of discovery requests.¹

Forward-Looking Review of Emerging Technologies

With anticipated changes in information technologies, present rules may not be effective or even meaningful in the future. This project will involve a forward-looking review of emerging technologies likely to affect the e-discovery cost-benefit calculus, and it will evaluate the implications for the relative efficacy of alternative legal requirements.

Evaluation of Federal Rules

Although evaluating the impact of the federal rules will be difficult until well after their implementation (December 2006), the project will conduct an initial evaluation based on theory, available cost data, and an evaluation of early indicators such as numbers of sanctions and the form of e-discovery requests and required productions.

Assessment of Effects of E-Discovery on Business Practices

In assessing the potential burdens of e-discovery, one has to consider the effects on business operations. To quantify these potential impacts, we intend to gather and analyze information on prevailing IT practices and technologies as well as the extent to which they may have been altered in response to e-discovery concerns.

¹ Of course, it may be that costs vary significantly on the basis of factors that cannot easily be identified and accounted for *ex ante*. In such a case, the guidebook's value will be based on establishing a feasible range of estimates that will require additional analysis on a case-by-case basis.