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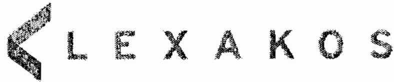

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December 28, 2006

By Electronic Mail (rules_comments@ao.uscourts.gov)
Peter G. McCabe, Secretary
Standing Committee on Rules of Practice and Procedure
of the Judicial Conference of the United States
Thurgood Marshall Federal Judiciary Building
Washington, D.C. 20544

Re: **Proposed Amendment to Federal Rules of Evidence**

Dear Mr. McCabe:

The Advisory Committee on Evidence Rules has proposed a new Rule 502 of the Federal Rules of Evidence, and the Standing Committee on Rules of Practice and Procedure of the Judicial Conference is holding public hearings and seeking comment before presenting recommendations to the Supreme Court and eventually Congress for adoption into law. The new rule would codify the conditions in which parties could waive protections afforded by the attorney-client privilege and work product doctrine. I would like the opportunity to appear at the hearings scheduled in New York, New York on January 29, 2007, and offer testimony at that time on the practical implications proposed new Rule 502 of the Federal Rules of Evidence would have on large organizations.

Background Information
Before founding the business advisory group of Lexakos LLC, I was global head of compliance for Cendant Corporation until its disaggregation in August 2006.[1] My decade

[1] I joined HFS Incorporated in 1996, and assumed roles of increasing responsibility over my 10 years with the company. During my tenure, I formed a new litigation group to handle conflict resolution for the largest franchise company in the world. I was centrally involved in the work to preserve electronically stored data in 1998, following the revelation of the CUC fraud and those efforts were instrumental in securing information needed by authorities investigating the expansive civil and criminal matters stemming from that situation. As Cendant grew to become a global corporation with over 90,000 employees across the world, in 2002 I designed and oversaw the organization's first compliance and ethics, and records management programs. When the company spun off into four separate entities in August 2006, I resigned from my role as senior vice president, corporate compliance officer and formed Lexakos, a legal consulting firm specializing in compliance, risk management and records management. Before my corporate career, I

of service in a corporate law department divide into three general areas, all of which pertain to proposed Rule 502 in some respect: (1) litigation and outside counsel management, (2) records and information management (including e-discovery, email and enterprise content management), and (3) corporate ethics and compliance. With respect to the latter areas, I reported to the board of directors and the audit committee of the board on a regular basis. In forming these corporate functions from their inception, I became familiar with best practices at other organizations and served various leadership roles over the years with the Corporate Executive Board, Association of Corporate Counsel, Ethics and Compliance Officer Association and the American Bar Association. The list below represents a sampling of my leadership roles in these organizations, in addition to my involvement in lectures, seminars and publications over the past several years.

- ABA – Chair, corporate counsel committee of Section of Administrative Law and Regulatory Practice (2000-), and liaison to the ABA Presidential Task Force on Attorney Client Privilege (2006-)
- ACC – Immediate-past president of the Greater New York Chapter (2006)
- CEB – Founding member of Compliance and Ethics Leadership Council, among select group of chief compliance officers from Fortune 100 companies (2004-)
- ECOA – Sponsoring member (2002-06) and nominee to the board of trustees (2006)[2]

Having now left corporate life, there are few constraints on my ability to give full and candid testimony of the current state of affairs inside corporations. Accordingly, I would appreciate the opportunity to participate in these proceedings and share the perspectives of a lawyer who represented corporations as inside and outside counsel, and a former senior executive who understands the challenges organizations face today in managing and producing information for legal and regulatory proceedings. While I recognize the Advisory Committee will be hearing testimony from many accomplished judges, lawyers and legal scholars, I respectfully submit that my unique experience could provide helpful, complementary perspectives on the practical implications of proposed new Rule of 502.

Overview of Proposed Testimony

If permitted to testify, I would address these three aspects of proposed new Rule 502: (1) inadvertent waiver, (2) claw-back and quick-peak agreements, and (3) selective waiver. The balance of this letter summarizes proposed testimony in these areas, with anticipation to develop these ideas in a more formal submission upon your request.

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practiced corporate litigation for 6 years at Pitney Hardin and LeBoeuf Lamb, following a one-year clerkship with Hon. Sylvia B. Pressler, Superior Court of New Jersey, Appellate Division in 1989.

[2] I could not accept nomination to serve on the ECOA board due to my decision no longer to serve as a corporate compliance and ethics officer. For the same reason, I tendered my resignation as president of the Greater New York Chapter of ACC, effective January 1, 2007. In December 2006, three members of the American Law Institute nominated me to become a member of ALI, subject to approval in February 2007.

Inadvertent Waiver -- Having uniform rules governing the doctrine of inadvertent waiver is an important development in the general protection of attorney-client privilege for all the reasons explained in the testimony taken on April 24, 2006, and aptly observed in the Advisory Committee's comments to proposed new Rule 502. I will not repeat the rationale here, but would testify about the significant complexity and expense involved in isolating privileged communications from the vast amounts of electronically stored information (ESI)[3] generated each day. In 2006, for instance, scholars estimate that organizations worldwide sent or received an estimated 85 billion emails each day. That figure is triple the number from just a few years ago and there is no end in sight.

Lawyers practicing today in corporate law departments have business clients who insist on receiving legal advice through email for all the reasons email has become the principal form of communication for business in general – email is expedient, efficient, convenient, and global. To compete in a global economy, organizations leverage email over the Internet to increase sales and productivity and need real-time legal advice to achieve demanding business goals. Of course, with the benefits email and the Internet bring to business come numerous detriments and liabilities. Studies show that enterprise content management has become, seemingly overnight, in the top three high-risk compliance areas for every organization. Organizations simply have not found ways to manage information with effective records retention policies that reduce overall storage through enforcement of information lifecycle management. Managing email traffic is a top priority in most all organizations polled in the last two years, but few, if any, have ESI under any semblance of control. Government is not immune from the information overload crisis, and Freedom of Information Act requests are creating significant burdens on key government agencies.

When you consider, then, the task of culling privileged communications from among all the others emails sent and received in a global organization, it begs a broader question regarding the ability of organizations to satisfy the standard of reasonableness envisioned in the proposed new rule. The current draft of Rule 502(b) (2) reads in pertinent part:

> (2) the disclosure is inadvertent and is made during discovery in federal or state litigation or administrative proceedings — and if the holder of the privilege or work product protection *took reasonable precautions to prevent disclosure and took reasonably prompt measures, once the holder knew or should have known of the disclosure, to rectify the error*, including (if applicable) following the procedures in Fed. R. Civ. P. 26(b) (5) (B) . . . . (emphasis added)

[3] "Electronically stored information" is the term used in the new Federal Rules of Civil Procedure, which became effective in all federal civil lawsuits filed after December 1, 2006. Rules 26, 33, 34, 37 and 45 of the Federal Rules of Civil Procedure, among others, bear close relation to the issues

Inasmuch as most organizations lack sound records management policy and procedures, few will be prepared to demonstrate "reasonable precautions to prevent disclosure" or "reasonably prompt measures ... to rectify errors." With the new Federal Rules of Civil Procedure, and the implied duty to preserve and express obligation to discuss and produce ESI in every civil case, organizations are finally ready to bring about meaningful change. Instituting the reforms needed to address records and information management in a large enterprise is a long-term proposition, however, leaving few if any organizations prepared to meet the threshold of inadvertency contemplated by the new proposed Rule 502. The vast majority of corporations would not be able to demonstrate having taken reasonable precautions to prevent disclosure of privileged information embedded in ESI. Accordingly, though promulgation of a rule for inadvertent waiver is a laudable means to protect the sanctity of attorney-client privilege, proposed Rule 502(b) (2), like the new Federal Rules of Civil Procedure, are highlighting a bigger problem.

Claw-back Agreements and Confidentiality Orders -- It is not cost effective to use traditional attorney review to cull privileged or confidential information from vast volumes of ESI. With the cost of searching and producing data so high, for general discovery and forensics, organizations are more frequently bypassing traditional search methods and are using new concept query technologies (not attorneys) to isolate relevant information for legal proceedings. The Adversary System will test those technologies over time for reliability and eventually we will recognize generally accepted methodologies, perhaps under a *Daubert* standard of analysis.

While there is no easy or clear answer to the question of when organizations will have reliable and effective records management programs, the use of stipulations and confidentiality orders, as envisioned under two sections of proposed Rule 502, is an excellent means to keep the flow of information moving in litigation. I am not convinced, however, there is a cost savings realized when producing information at the outset of proceedings under a claw-back agreement or confidentiality order. Though it might be cost effective in respect of expediency, the parties will need to incur the cost of culling ESI with expensive, new and largely untested technologies at one point or another.

Selective Waiver -- Understandably, there is mostly opposition to any rule that might lead to the erosion of the attorney-client privilege. For many, proposed Rule 502(c) is just that. I share the view that coerced waiver tactics violate the basic principles that underlie the attorney-client privilege. If intellectual honesty were to prevail, however, most would agree there are limited circumstances in which an organization might appropriately need to share the fruits of an investigation to advance the public interest and protect capital markets. The problem with the notion of selective waiver is the perception that such a rule would invite governmental abuses and open a floodgate of requests for waiver as a matter of convenience. The corporate and private bar, and most every other bar association that has spoken on the subject, argues that there has emerged a "culture of waiver" in the post-Enron years, where the government uses a target's decision to waive

privileges as a litmus test to show cooperation in an investigation and gain favor as a result.

The pressure of the bar, and perhaps the bill introduced by Senator Specter, ultimately led to the issuance of the "McNulty Memo," which, among other things, establishes procedures prosecutors must follow before asking an organization to waive privilege. For many critics, the McNulty Memo is not a departure from the practices followed under the Thompson Memo. The government plans to continue to ask for privilege waivers, but will not condition waiver on determinations of whether an organization is being "cooperative." It is unclear how anyone will know what ultimately influences prosecutorial discretion, notwithstanding the language in the McNulty Memo.

Those debating the issue of selective waiver may be missing a fundamental point I would like to review with the Advisory Committee as a reason that militates in favor of why selective waiver might be included in the proposed new rule. In short, the government and defense lawyers are fixated on the notion of privilege waiver as a means to gauge cooperation because they do not know how to measure the effectiveness of an organization's ethics compliance and compliance program.

Fortune 100 companies have spent and are spending millions of dollars each year maintaining and improving compliance programs modeled after the principles espoused in the Federal Sentencing Guidelines. Few, if any, compliance officers are involved when defense lawyers confer with prosecutors or regulators about a pending investigation or contemplated action. When discussion turns to cooperation in an investigation the dynamic of the discussion might not turn readily to privilege waiver if the person with day-to-day responsibility for ethics and compliance were present to explain all the positive actions a company takes to encourage an ethical culture and an organization that understands the importance of compliance with law. If able to demonstrate the effectiveness of a compliance program on the culture of an organization, there might be a higher degree of trust in the reliability of the nature and extent of a corporation's investigative efforts and scope of self-reporting, and waiver of privileges would be necessary, perhaps, as a last resort.

In 2005, participated in several meetings with chief compliance officers of some of the world's largest corporations, where we confidentially debated how best to measure effectiveness. The companies who participated in those meetings placed the initiative of measuring compliance program effectiveness atop their priority list for 2006. Remarkably, however, efforts at self-governance and improving corporate culture seem absent from the analysis of whether to charge a corporation. How to measure effectiveness is an admittedly difficult undertaking. There has been progress, however, and there needs to be a means through which to share the fruits of the labor of compliance programs. If prosecutors and the defense bar were better informed of these developments, I believe the emphasis on privilege waiver as a de facto litmus test for

cooperation would dissipate and ultimately deter requests for waiver from organizations able to demonstrate the effectiveness of its ethics and compliance program.

While these thoughts are not in a form of written testimony or talking points, if allowed to testify and submit comments, I would gladly provide more data and support for the points generally raised in this letter.

I appreciate your consideration of this request.

Respectfully submitted,

Richard J. Wolf

"Rick Wolf"
<rwolf@lexakos.com>
12/28/2006 07:10 PM

To <rules_comments@ao.uscourts.gov>
cc
bcc
Subject Letter of Rick Wolf to Advisory Committee on Evidence

Dear Mr. Secretary,

I attach for your consideration a letter in support of my request to testify with respect to the hearings upcoming on proposed new Rule 502 of the Federal Rules of Evidence.

Many thanks for considering my application.

Sincerely,

Rick Wolf
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RJW Letter to Advisory Committee on Evidence Rules.pdf

Testimony

STATEMENT OF
RICHARD J. WOLF*

Before the

ADVISORY COMMITTEE ON EVIDENCE RULES
OF THE
STANDING COMMITTEE ON RULES OF PRACTICE AND PROCEDURE
JUDICIAL CONFERENCE OF THE UNITED STATES

NEW YORK, NEW YORK
JANUARY 29, 2007

INTRODUCTION

Chairman Smith, Committee Members, and members of the Bench in attendance, I appreciate this opportunity to testify and share views for consideration on proposed new Rule 502 of the Federal Rules of Evidence. My name is Rick Wolf.

I offer my testimony from the perspective of a former senior executive who, from 2001 to 2006, put together and headed up the ethics and corporate compliance function of a Fortune 100 company. I also formed and managed a records management group within the compliance department, which included a cross-functional team to handle email and electronic document management. Ten years ago, with a company called HFS Incorporated, I designed a litigation management system to rationalize spending through early case evaluation and mediation, and settled or litigated hundreds of commercial cases in federal court over that period. For what we

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*(973) 324-0050, rwolf@lexakos.com. Before founding Lexakos LLC, a business advisory group specializing in compliance, records management, and conflict resolution, Mr. Wolf was head of global compliance and ethics at Cendant Corporation until its disaggregation in August 2006. During a decade serving as an executive in a corporate law department, he developed and ran litigation management, records management and compliance systems. Mr. Wolf was previously in private law practice, concentrating on corporate litigation, commercial law and appellate practice at the firms of Pitney Hardin and LeBoeuf Lamb. Mr. Wolf is immediate-past president of the Association of Corporate Counsel, Greater New York Chapter (2006), and holds leadership positions for the ABA, including chair of the corporate counsel committee of the Administrative Law and Regulatory Practice Section and that Section's liaison to the Presidential Task Force on Attorney-Client Privilege.

called the national counsel program, I established the business requirements for a customized matter management system used to collaborate with outside counsel and track litigation metrics.

While I recognize the Advisory Committee will hear testimony from many accomplished judges, lawyers and legal scholars on more nuanced legal implications of the proposed rule, I offer my blend of experience in compliance, records management, litigation and legal technology development, to help shed light on some practical implications of proposed new Rule of 502.

Like other members of the bar, I support these efforts to establish a clear standard for disclosures that would not lead to waiver of protections afforded by the attorney-client privilege and work product doctrine. I plan to address two principal exceptions to waiver by disclosure contemplated by the proposed new rule: (1) inadvertent disclosure, including a quick word on the effects on "claw-back" or "quick-peak" agreements, and (2) so-called selective waiver.

TESTIMONY OF RICHARD J. WOLF

Inadvertent Disclosure Exception

I support the adoption of proposed new Rule 502(b) and a uniform inadvertent disclosure exception. The Advisory Committee observed in its notice that the new rule should "reduce the risk of forfeiting the attorney-client privilege or work-product protection so that parties need not scrutinize production of documents to the same extent as they now do." In view of the challenge of managing electronically stored information ("ESI"), I would like to spend a few minutes exemplifying some of practical difficulties with applying an inadvertent disclosure exception in today's corporate environment.

Isolating privileged communications or attorney work product from the vast amounts of electronic information corporations amass and store is a complex and expensive undertaking.

Studies estimate that organizations collectively sent or received over 80 billion emails each day in 2006, more than tripling the figure estimated for 2002. Coupled with this information explosion, organizations do not practice information lifecycle management and keep data well past its useful life. One reason organizations over-retain information is simply that one cannot dispose data until they figure out how to find and preserve what is needed for legal purposes.

Commingled with the high volume of email generated and received each day is a much smaller universe of ESI containing privileged communications and attorney work product. Business representatives today expect to receive legal advice from in-house counsel through email for all the reasons that medium has become the principal form of communication for business in general – email is efficient, expedient and global. However, because organizations mix privileged email communications with the millions of other non-essential emails, it is difficult to cull privileged email from everything else.

It is not cost effective to search terabytes of data manually, so corporations have been turning to automated review technologies with concept search capabilities that isolate relevant information and reduce the overall volume of ESI subject to attorney review. The analysis for determining privilege is more subtle than looking for subject lines labeled "attorney-client privilege," however, and whether these new review technologies will withstand the scrutiny of the *Daubert* standard remains to be seen.

Organizations struggle to manage and control ESI due to fundamental issues of corporate governance and compliance. Over the last five years, IT departments answered the call and accommodated business needs by adding more email servers and bandwidth for global telecommunications. These infrastructures grew with little guidance from the law department and lacked compliance policies governing the management of content. When the law department

asked IT to retain email for discovery, the IT department used email server backup tapes intended disaster recovery as archives for litigation. Extracting email from these tapes requires computer forensic experts, and is a cumbersome and expensive process. Organizations accumulated thousands of these backup tapes with generally slack inventory controls. Morgan Stanley has become the poster child for poor email controls, but I suspect most would fare no better if their email retention practices were subject to scrutiny. Faced with the new federal procedures for e-discovery in civil litigation, organizations have finally started to bring order to the chaos of these sprawling IT infrastructures, but even the most basic request for ESI remains very expensive. For instance, it will be difficult to reduce tape inventories because your custody and control makes data on those tapes discoverable in new litigation, and retention is perpetual.

With the threat of spoliation claims and sanction motions looming, the new e-discovery rules have injected energy to records management compliance programs, but most companies are just starting down the road. The General Counsel Roundtable recently conducted a survey of chief legal officers and the results show that very few have records management controls. Eighty-five percent ranked records management as important or very important, and eighty percent ranked "Improving companywide records management policies, tools, and compliance" as important or very important. Eighty percent ranked "Improving electronic discovery policies and preparedness" as important or very important. Seventy-five percent ranked "Improving employee awareness of appropriate email use and tone" as important or very important. Generals counsel rank the task to "Improve consistency of enterprise-wide compliance with records management policies" as their second highest priority in 2007, behind plans for "Revising and streamlining preferred provider network of external law firms."

Findings at the Association of Corporate Counsel corroborate these figures. In a poll taken late last year, only seven percent of in-house counsel rated their company as prepared for the new Federal Rules of Civil Procedure and ninety-two percent said they are still taking steps to improve their organization's readiness for the new rules. In another ACC survey just released, chief legal officers cited records management and global expansion as the two most important areas of focus for 2007. Law departments have known the importance of having an effective records management policy for years, and unrestricted email traffic may be "clear and present danger" to the enterprise, but a combination of competing priorities and poor execution keeps efforts to improve records management compliance on the backburner.

In my experience, developing an effective records management program for a moderate-sized organization could take eighteen months and up to three years in a large company. To compound the challenge, email volume continues to grow unabated and lawyers are finding it difficult to influence the extent or use of technology in a corporation. The two functions that must coordinate closely to manage electronically stored information -- the law department and IT department – do not report into the same place in most companies and simply do not coordinate activity. While the law department tries to identify an individual to take on records management, make the business case for capital investment and align management behind a program that needs everyone's support to succeed, there remains a gaping hole in records management compliance. As questions of governance and accountability remain, few companies are ready to enforce a legal preservation policy or purge ESI that has no ongoing business or legal purpose.

When you consider, then, the task of culling privileged communications from among all the others emails sent and received in an organization, it begs a broader question of what is necessary to satisfy the standard of reasonableness in the proposed new rule. The current draft of

Rule 502(b) says a disclosure is inadvertent "if the holder * * * *took reasonable precautions to prevent disclosure and took reasonably prompt measures, once the holder knew or should have known of the disclosure, to rectify the error* . . . ." (Emphasis added). Without an enforceable records management policy, it is not clear what "reasonable precautions" organizations might take to "prevent disclosure" or how an organization could take "reasonably prompt measures ... to rectify errors." The standard is likely too high for most corporations to meet.

As noted, instituting the reforms needed to bring records and information management to a large enterprise is a long-term proposition, and that means few would be prepared to meet the threshold of inadvertency contemplated by the new proposed Rule 502. The test of reasonableness should take into account "whether an organization has followed the steps necessary to have an effective compliance program for records management," which should include an enforceable policy, adequate resources, training and awareness, regular monitoring, and proper remediation. Though an inadvertent disclosure exception to waiver is desirable, there is much to address before corporations would be able to meet the high standard of reasonableness contemplated by from Rule 502(b).

<u>Claw-back Agreements and Confidentiality Orders</u>

As noted, traditional attorney review is not a cost-effective or efficient way to cull privileged or confidential information from ESI. Proposed Rule 502(e) encourages the use of "claw back" or "sneak peek" agreements, supported by confidentiality orders under subsection (d) of the proposed rule, to facilitate discovery and "limit the costs of privilege review." Such stipulations and confidentiality orders allow parties to avoid the expense of pre-production review and recover privileged information inadvertently produced without fear of waiver. Aside from the question of enforceability as to non-parties, it is not clear to me how parties would

realize savings from avoiding pre-production review. The recipient of information under a claw-back agreement, for instance, would need to conduct the same review and incur the same costs, as the producing party. Although the claw-back agreement might achieve expediency, at some point in time parties will incur the expense of culling through ESI. There are also practical risks associated with the use of sneak-peak or information produced under the ambit of a confidentiality order, and reasons why organizations might not jump at this opportunity. Even if the parties agree that information shared under this procedure would remain privileged and not discoverable in the proceedings in which such an order is entered, once information gets out, particularly in electronic form, it is very difficult to contain dissemination and the producing party runs a significant risk of finding privileged communications republished notwithstanding stipulated confidentiality orders.

Selective Waiver

One would expect mostly opposition to any rule viewed as leading to the further erosion of the attorney-client privilege. Over the past few months, there has been much debate about the ethics and legality of asking an organization to waive privileges in a criminal investigation as a sign of cooperation. I share the view that coerced waiver tactics violate fundamental rights and the basic principles underlying the attorney-client privilege. Should intellectual honesty prevail, however, most would agree there *are* circumstances in which an organization should share the fruits of an investigation to advance the public interest, and protect capital markets and shareholder value. For instance, there is a legitimate need to share content with outside auditors or directors, who have common interests to the organization and need information in order to discharge oversight duties and regulatory obligations. Ideally, the rules should not view sharing information with outside auditors or directors as a disclosure of privileged information, but

recognize such communications or work product as subject to a cloak of protection under common interest principles.

A rule for selective waiver or "limited disclosure" does raise the concern that such a rule would invite governmental abuses and open a floodgate of requests for waiver as a matter of investigative convenience. The corporate and private bar, and most every other association that has spoken publicly on the subject, argues that there has emerged a "culture of waiver" in the post-Enron years, where the government uses a target's decision to waive privileges as a litmus test to show cooperation in an investigation and possibly gain favorable treatment as a result. I agree with this assessment, but only in part.

The pressure of the bar, and perhaps the bill introduced by Senator Specter at the end of the 109th Congress, and reintroduced earlier this month, ultimately led to the issuance of the "McNulty Memo" on December 12. 2006. The Specter bill, titled "The Attorney-Client Privilege Protection Act," among other things, would prohibit the government from conditioning civil or criminal charge decisions on whether an organization asserts privileges, defends employees with common interests, or fails to terminate employees implicated in an investigation. The McNulty Memo put one of these elements to rest when it denounced the policy against organizations advancing defense costs for employees, in response to the recent landmark decision of Judge Kaplan in the KPMG tax litigation.

The McNulty Memo also describes procedures prosecutors must follow before asking an organization to waive privilege, which varies based on the type of information sought, and says the government will not condition waiver on determinations of whether an organization is being "cooperative." What influences a prosecutor's decision is anyone's guess so, notwithstanding this new pronouncement, there is nothing to prevent the government from considering waiver an

important factor in measuring an organization's disposition, even if not expressly stated. For these reasons, in the eyes of most members of the bar, the McNulty Memo does not go far enough and they oppose, flatly, any rule that would encourage government to seek waiver of privileges in criminal or civil investigations.

I respectfully submit that any blanket opposition to proposed new Rule 502(c) is not representative of or consistent with corporate interests in general. Organizations have always wanted the type of protections envisioned under the proposed rule. Requests for limited disclosure should be the last resort, however, and the principal focus of prosecutors when considering whether to charge a corporation, initially, should be an assessment of the organization's culture and the effectiveness of its ethics and compliance program.

An organization should have the opportunity to demonstrate they have an ethical culture and an effective compliance program. The government and criminal defense bar seem fixated on the notion that privilege waiver is a means to gauge or demonstrate cooperation, and the over-reliance on waiver in this context is simply misplaced. Ironically, many of the most vocal critics of proposed new Rule 502(c) are the same lawyers who invoke the waiver approach in practice.

Companies have spent and are spending millions of dollars each year maintaining and improving ethics and compliance programs modeled after the principles espoused in the Federal Sentencing Guidelines, the Thompson Memo and the Seaboard Report. In 2005, I participated in several meetings with chief compliance officers from the world's largest corporations and we shared ideas on how best to measure effectiveness. The Compliance and Ethics Leadership Council, a sister division of the General Counsel Roundtable, hosted these meetings and the companies who participated unanimously named measuring compliance program effectiveness as the top priority.

Remarkably, these organizational efforts to self-govern and improve corporate culture seem absent from the analysis with prosecutors. How to measure the effectiveness of an ethics and compliance program is an admittedly difficult undertaking, but there has been progress over the last two years. Organizations should have meaningful opportunities to demonstrate the strength of their ethics and compliance program. If prosecutors and the defense bar better understood these developments and had an objective way to recognize a good culture from a corrupt one, I believe the emphasis on privilege waiver as a *de facto* litmus test for cooperation would dissipate.

There are few, if any, compliance officers involved in the conversations where defense lawyers and prosecutors discuss a pending investigation or contemplated action. In my view, the dynamic of those discussions would change if the person with day-to-day responsibility for the organization's ethics and compliance were present. If able to demonstrate the effectiveness of a compliance program on the culture of an organization, there might be a higher degree of trust in the reliability of the nature and extent of a corporation's investigative efforts and scope of self-reporting, and waiver of privileges would be necessary, perhaps, as a last resort.

In considering the proposed Rule 502(c), therefore, I respectfully suggest that the Advisory Committee take into account the prospect for prosecutorial abuses and coerced waivers by adding the word "proper" before the phrase "exercise of its, regulatory, investigative, or enforcement authority…." I also recommend that the Advisory Committee consider addressing in its comments to the proposed rule the importance of considering the totality of circumstances, including the effectiveness of an ethics and compliance program, before parties resort to extreme measures such as requesting waiver of attorney-client privileges or attorney work product.

06 - EV- 044
Final Comment

www.lexakos.com

February 15, 2007

Via Email to Rules_Comments@ao.uscourts.gov

The Honorable Peter G. McCabe
Secretary of the Committee on Rules of Practice and Procedure
Administrative Office of the United States Courts
Washington, D.C. 20544

Re: Proposed Federal Rule of Evidence 502

Dear Mr. McCabe:

I respectfully submit these comments on proposed Rule 502 of the Federal Rules of Evidence and would appreciate your sharing this letter with the rest of the Advisory Committee on Evidence Rules for its deliberations. Having had direct professional experience in compliance, records management, litigation management, legal technology applications, and business process development, I am familiar with the practical implications of proposed Rule 502 and trust the Advisory Committee will find my observations helpful in the rulemaking process. [1]

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[1] I was head of global compliance at Cendant Corporation until the company's disaggregation in 2006. During my decade of service in a public corporation, I developed and oversaw enterprise compliance, litigation and records management systems. Previously, I was in private practice, concentrating on corporate litigation, commercial law, and appellate practice and procedure. I am immediate-past president of the Association of Corporate Counsel, Greater New York Chapter. I chair the corporate counsel committee of the ABA Administrative Law and Regulatory Practice Section and am the Section's liaison to the ABA Presidential Task Force on Attorney-Client Privilege. I am a member of The American Law Institute. In 2006, I founded the business advisory firm, Lexakos LLC and the law practice, Wolf Associates LLC. The views expressed in this letter should be attributed only to me.

Like other members of the bar who have come before you to testify and comment on proposed Rule 502, I support and applaud the effort to establish standards for protecting attorney-client privilege and attorney work product. In this letter, I address three of the exceptions to waiver by disclosure contemplated by the proposed rule: (1) inadvertent disclosure, (2) "claw-back" and "quick-peek" agreements, and (3) selective waiver.

I. Inadvertent Disclosure Exception

I support the adoption of a uniform inadvertent disclosure exception, which is an amendment necessary to harmonize the procedural changes in amended Rule 26 of the Federal Rules of Civil Procedure. The Advisory Committee observed in its notice of rulemaking that the new rule should "reduce the risk of forfeiting the attorney-client privilege or work-product protection so that parties need not scrutinize production of documents to the same extent as they now do." While it is laudable to fashion a rule to protect against waiver for inadvertent disclosure, there are practical difficulties with applying such an exception using the current text of the proposed Rule 502(b).

A. *Corporate Governance Challenge: To Bring Order from the E-Chaos*

Studies estimate that organizations worldwide had sent or received over 60 billion emails each day in 2006, more than tripling the figure estimated for 2002. Organizations are struggling with information lifecycle management ("ILM") and most people keep data well past its useful life. The business doctrine of ILM relies on enterprise content management ("ECM") technologies and posits that to compete globally organizations must leverage and share knowledge through the use of

searchable, central repositories of business-critical information. ECM is the model to which all organizations should aspire, but a confluence of circumstances leads to retention of multiple instances of the same "electronically stored information." We over-retain out of fear we will not find *that* email attachment when we need it.

Notwithstanding the self-evident benefits of ECM, few companies have been able to utilize that practice. Instead, most organizations struggle to manage and control so-called ESI due to fundamental issues of corporate governance and compliance. As Table 1 in the Appendix shows, there was no consistent oversight structure for the records management area at the beginning of this ongoing period of information explosion. Without an executive function managing this area, ECM has not become standard operating procedure.

Deploying scalable ECM technologies is highly complex and expensive, and success largely depends on a willingness to carry out business process analysis and re-engineer work flow (*i.e.*, examining how one manages information today and changing processes to capitalize on new technologies). In contrast to ECM and centralization, over the last five years, information technology departments have been storage and infrastructure focused, as IT fulfilled requests to add more email servers and bandwidth for more expansive global telecommunications. These infrastructures grew with little guidance from law departments and mostly without policies governing content management.[2]

When the law department started to ask IT managers to retain email for discovery in the 1990s, companies used email server backup tapes intended disaster

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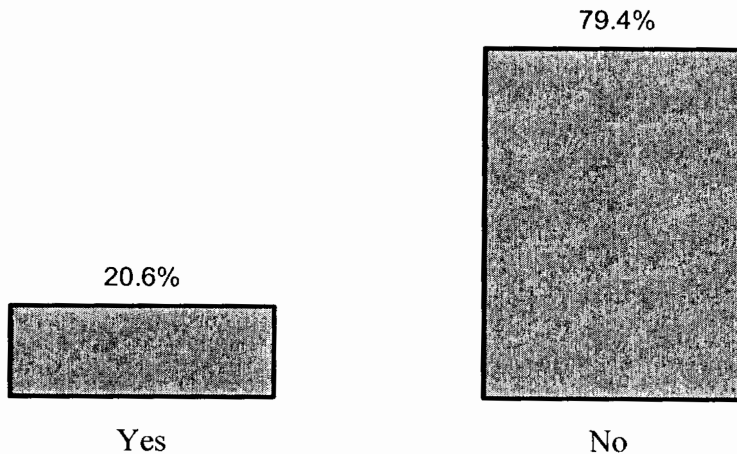
[2] The Brave New World of e-Discovery Rules, *Compliance Week Magazine* (Special Edition Jan. 2007).

recovery as archives for litigation. Many hundreds of thousands of those backup tapes with email dating back as far as ten years still exist, and the content of those archives continue to surface in damaging ways. Extracting email from backup tape requires forensic skill and careful restoration, an expensive and risky undertaking. To make matters worse, organizations accumulated these backup tape inventories with permissive controls. Faced with the amended procedures for e-discovery in federal civil litigation, companies have finally started to bring order to the chaos of these sprawling IT infrastructures, but even the most basic request for ESI remains very expensive. It is difficult to reduce these backup tape inventories. Possession of the tapes makes the data is discoverable in new litigation, and retention is seemingly perpetual.

Companies need to start imposing better policy and procedures. Developing an effective records management program for a moderate-sized organization takes between eighteen months to three years. To compound the challenge, email volume continues to grow unabated and lawyers have difficulty influencing the use of technology in a corporation. The two functions that must coordinate closely to manage electronically stored information -- the law department and IT department – do not report into the same person in most companies and do not coordinate their activity. While the law department struggles to identify an individual to champion records management, make the business case for capital investment and align management behind a program that needs everyone's support to succeed, there remains a gaping hole in records management compliance. As questions of governance and accountability remain, few companies are ready to enforce a legal preservation policy or purge ESI that has no ongoing business or legal purpose.

B. Complications with Culling Privileged Information Delivered in Email

Business people today expect to their legal advice from in-house counsel to come in email for all the reasons that medium has become the principal form of communication for business in general – email is efficient, expedient and global. Even so, only a fraction of the email generated and received contains privileged communications or attorney work product. If one accepts the premise that we receive and retain too much email, it follows that comingling privileged email with non-essential email makes it problematical to cull privileged email from everything else. In a recent poll taken in January 2007 during a webcast for Compliance Week, we asked in-house legal and compliance executives whether their company takes any measure to segregate privileged communications from general e-mail traffic as a standard operating procedure (i.e. before litigation)? Table 2 shows the results.[3]



Organizations can segregate privileged communications and attorney-work product from general email traffic and the other unstructured ESI stored on IT

[3] The poll took was conducted during a webcast on "New Federal Rules of Civil Procedure – E-Discovery and Records Management, *Compliance Week* (Jan. 11, 2007).

systems. This can be achieved with an approach combining (1) business process analysis and re-engineering, (2) uniform guidelines for litigation management, and (3) matter management technology that uses an extranet. Extranet systems allow outside counsel to collaborate with inside clients and lawyers through a secure and restricted internet connection. Such a process and system naturally separates privileged communications and work product information from everything else. If litigation ensues and the organization must produce relevant emails, some of that data might contain privileged communications, but most everything dealing with legal issues, litigation or an internal investigation relating to the problem, would be stored in a *structured* matter management database system.

C. *Emerging Search Technologies are Replacing Traditional Attorney Review*

When dealing with terabytes of data, it is not cost effective or practical to search manually for relevant or privileged information with traditional methods. Corporations are turning to emerging review technologies with term- and concept-search capabilities, which isolate relevant information and reduce amount of data subject to attorney review. The analysis required for determining privilege is often more subtle than searching metadata for in-house attorney names or subject-lines labeled "attorney-client privilege." At some level technology cannot replace manual, attorney review. Whether these new review technologies will withstand scrutiny under Federal Evidence Rules 702 and become reliable methodologies that satisfy *Daubert v. Merrell Dow Pharmaceuticals, Inc.,* 509 U.S. 579 (1993), remains to be seen. These new technologies will remain an integral part of the process and play an important role in the analysis under proposed Rule 502(b).

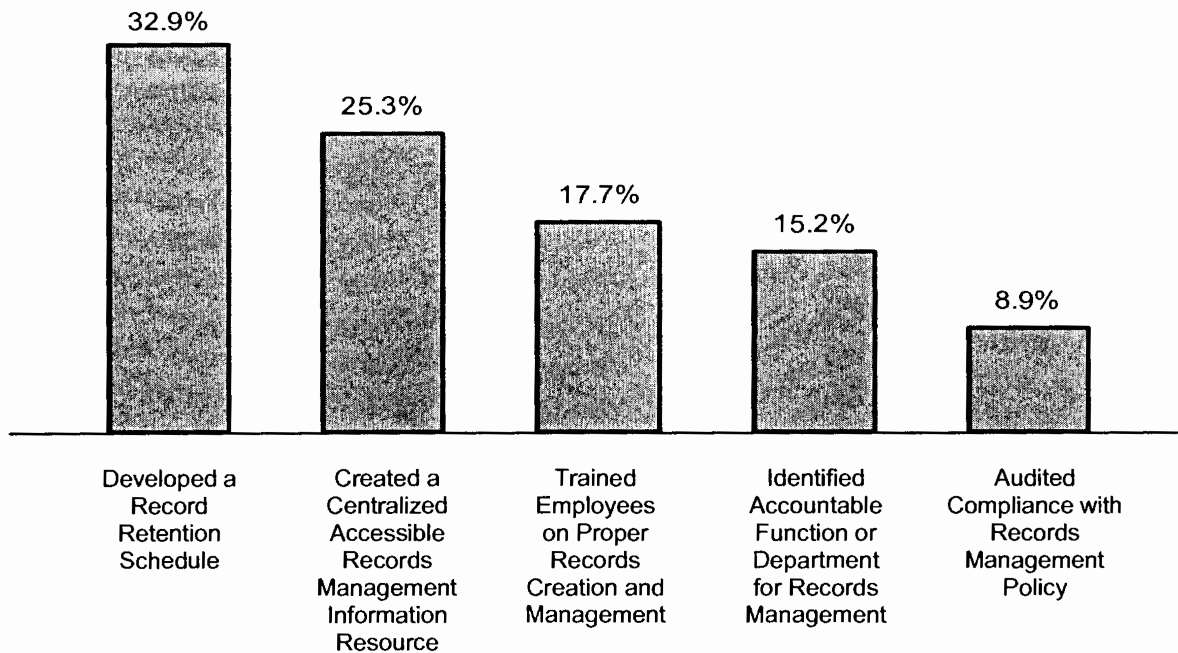
D. Records Management Policy Compliance

We would like to believe that what is needed for handling ESI is no more than extending records management policies used for managing paper documents. The preservation and disposition principles that apply to the content of paper records are no different from that which applies to the content of electronically stored information. It is simply a different medium. Exposure to spoliation claims and motions for sanctions under the amended Federal Rules of Civil Procedure have brought unprecedented attention to the need for records management compliance programs. Studies show companies are just starting to appreciate the need for effective records management compliance.

The General Counsel Roundtable conducted a survey of chief legal officers in late 2006, and the results show that few have effective records management. Eighty-five percent ranked records management as important or very important, and eighty percent ranked "Improving companywide records management policies, tools, and compliance" as important or very important. Eighty percent ranked "Improving electronic discovery policies and preparedness" as important or very important. Seventy-five percent ranked "Improving employee awareness of appropriate email use and tone" as important or very important. "Improv[ing] consistency of enterprise-wide compliance with records management policies" is the second highest priority for general counsel in 2007, behind "Revising and streamlining preferred provider network of external law firms."

Surveys of the Association of Corporate Counsel corroborate these figures. In 2006, seven percent of chief legal officers said their company was prepared for the new Federal Rules of Civil Procedure and ninety-two percent were taking steps to

improve their litigation readiness. Chief legal officers said improving records management was among the most important tasks to address in 2007. With these ACC polls in mind, during the Compliance Week webcast we asked legal and compliance executives what steps they have taken to create a records management program. Table 3 shows the results of that poll.



Although law departments know the importance of having an effective records management policy, and perhaps view unrestricted email traffic as "clear and present danger" to the enterprise, a combination of competing priorities, flawed governance, and poor execution keeps efforts to improve records management compliance on the backburner.

E. Difficulties Applying Rule 502(b) in Practice

When you consider, then, the task of culling privileged communications from among all the other email in an organization, it begs the question of what *is*

necessary to satisfy the standard of reasonableness in the proposed new rule. The current draft of Rule 502(b) says a disclosure is inadvertent "if the holder * * * *took reasonable precautions to prevent disclosure and took reasonably prompt measures, once the holder knew or should have known of the disclosure, to rectify the error. . . .*" (Emphasis added). If only a fraction of many millions emails have privilege content that needs protection, and most companies lack enforceable records management policies or practice ECM, it is unclear what "reasonable precautions" organizations might take to "prevent disclosure" or how one might take "reasonably prompt measures ... to rectify errors." It is respectfully submitted that the standard is too high for most corporations to meet in time for a pre-production document review.

As noted, instituting the reforms needed to have effective records management in a large enterprise is a long-term proposition, which means few are or will be prepared to meet the threshold of inadvertency contemplated by the new proposed Rule 502(b). The rule should apply a test of reasonableness based on subjective good faith and courts should consider "whether an organization is taking steps necessary to have an effective records management compliance program." Hence, the judgment of what is reasonable should take into account the totality of circumstances, including time, place and context. In other words, the analysis should include consideration of the size of the production, the amount of time needed to produce, and the care with which the organization handles information before litigation giving rise to the obligation to produce.

When there is a large production of ESI needed in a matter, there is little a producing party can do to prevent disclosing privileged communications. There should be some forgiveness, however, if the organization mitigates the risk of

inadvertent disclosure through an effective records management program with rules that govern the creation, use, retention, and ultimate disposal of ESI. Such a program would need a (1) high-level executive in place with authority over (2) the enforcement of records management policies with procedures, and that executive must have (3) adequate resources for (4) employee training and awareness programs, and (4) regular monitoring (5) to remediate gaps or deficiencies. Though an inadvertent disclosure exception to waiver is certainly desirable, there is much to address before corporations would be able to meet the high standard of reasonableness contemplated by from Rule 502(b).

Based on the forgoing recommendations, I respectfully suggest the Advisory Committee consider revising the proposed rule as follows:

> **(b) Inadvertent disclosure.** — A disclosure of a communication or information covered by the attorney-client privilege or work product protection does not operate as a waiver in a state or federal proceeding if the disclosure is inadvertent and is made in connection with federal litigation or federal administrative proceedings — and if the holder of the privilege or work product protection took reasonable precautions, <u>technological or *otherwise* through effective records management compliance practices,</u> to prevent disclosure and took reasonably prompt measures, once the holder knew or should have known of the disclosure, to rectify the error, including (if applicable) following the procedures in Fed. R. Civ. P. 26(b)(5)(B).

II. Claw-back Agreements and Confidentiality Orders

For the reasons discussed above, traditional attorney review is not a cost-effective, efficient or accurate method for culling privileged information from otherwise relevant ESI. Proposed Rule 502 encourages the use of "claw-back" or "sneak-peek" agreements, supported by confidentiality orders under the proposed rule, to facilitate discovery and "limit the costs of privilege review." Such stipulations and confidentiality orders allow parties to avoid the expense of pre-

production review and recover privileged information inadvertently produced without fear of waiver. Aside from the question of enforceability as to non-parties, it is unclear how parties will realize savings by using these procedures. The parties would be required to conduct the same review and presumably incur the same costs, but later in time. Although the claw-back agreement might achieve the goal of expediency, the parties invariable will incur the expense of culling for privileged communications.

There are practical risks associated with the use of stipulated agreements to produce potentially privileged material under the ambit of a protective order. Even if the parties agree that information shared through this procedure would remain privileged and not discoverable in the proceedings in which such an order is entered, once privileged information is produced, particularly in electronic form, it is very difficult to contain dissemination or reproduction and the producing party runs a significant risk of finding privileged communications republished notwithstanding stipulated confidentiality orders. While it is worthwhile to use claw-back and sneak-peek agreements in appropriate circumstances, these methods have limitations and certainly are not a substitute for good records management compliance.

III. Selective Waiver

Any rule that would lead to the erosion of the attorney-client privilege will be met with strenuous opposition. There surely has been vocal opposition to proposed Rule 502(c) and much debate about the ethics and legality of prosecutors asking an organization to waive privileges as a show of cooperation and to gain favor. I agree

coercive tactics that lead to the disclosure of privileged material violate fundamental rights and emasculate the basic principles underlying the attorney-client privilege.

Should intellectual honesty prevail, most would agree there *are* circumstances where organizations *choose* to share the fruits of an investigation to expedite proceedings and control collateral damage in the interests of capital markets and shareholder value. Indeed, each fiscal quarter public company lawyers share privileged information and work product with auditors when analyzing probable and estimable litigation exposure to ensure the proper setting of reserves pursuant to Statement of Financial Accounting Standard No. 5.[4] Seemingly any situation involving a meaningful internal investigation would require corporate counsel to share some privileged findings with auditors and independent directors. Outside auditors and directors share a common interest to protect the organization and need information to assess situations and discharge oversight duties. Arguably, there would never be a circumstance where a company would voluntarily share privileged information with prosecutors and not its auditors and board of directors. If anything, in the interest of self-governance and corporate responsibility, organizations should be able to disclose privileged information to auditors or outside directors when necessary to determine the need for self-reporting or other action, without fear of suffering broad, subject-matter waiver as to third parties.

Most who oppose proposed Rule 502(c) argue that the rule, if adopted, would encourage more requests for waivers and abuses by the government. A rule for

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[4] Statement of Financial Accounting Standards No. 5 requires that certain conditions exist before determining loss contingencies representing liabilities or asset impairments, and the reserve amount to accrue. The loss must be probable as of the balance sheet date and reasonably estimable; significantly, the loss must have occurred prior to the creation of the loss contingency and must not be in the future.

selective waiver or "limited disclosure" in this context does have potential to invite governmental abuses and waiver requests as a matter of investigative convenience. But if the legal system does not reward prosecutorial overreaching, those abuses can be checked. The Federal Rules of Evidence do not treat a coerced disclosure as a waiver. Without voluntary waiver, the holder of the privilege should still enjoy all protections recognized by law and third parties should be subjected to an exclusionary rule precluding the use of wrongfully obtained information.

The corporate and private bar, and most every other association that has spoken publicly on the subject, argues that there has emerged a "culture of waiver" in the post-Enron years, where the government uses a target's decision to waive privileges as a litmus test to show cooperation in an investigation and possibly gain favorable treatment as a result. I agree with this assessment, but only in part.

The pressure of the bar, and perhaps the bill introduced by Senator Specter at the end of the 109th Congress, and reintroduced at the start of the 110th Congress, ultimately led to the issuance of the "McNulty Memo" on December 12. 2006. The Specter bill, titled "The Attorney-Client Privilege Protection Act," among other things, would prohibit the government from conditioning civil or criminal charge decisions on whether an organization asserts privileges, defends employees with common interests, or fails to terminate employees implicated in an investigation. The McNulty Memo put one of these elements to rest when it denounced the policy against organizations advancing defense costs for employees, in response to the recent landmark decision of Judge Kaplan in the KPMG tax litigation.

The McNulty Memo describes procedures prosecutors must follow before asking an organization to waive privilege, which varies based on the type of

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information sought, and says the government will not condition waiver on determinations of whether an organization is being "cooperative." As a practical matter, there is nothing to prevent the government from considering waiver as a factor in measuring an organization's disposition, even if not expressly stated. The McNulty Memo probably does not go far enough and most oppose, flatly, any rule that might encourage more waiver requests in criminal or civil investigations.

I respectfully submit that a blanket opposition to proposed new Rule 502(c) is misplaced. Organizations have always wanted the type of protections envisioned under the proposed rule. Even assuming for sake of argument there have been more waiver requests than in the past, proposed Rule 502(c) would only improve the status quo and afford protections that do not exist today. Requests for limited disclosure should be the last resort, however, and the principal focus of prosecutors when considering whether to charge a corporation, initially, should be an assessment of organizational culture and effectiveness of compliance programs.

An organization should have the opportunity to demonstrate they have an ethical culture and an effective compliance program. The government and criminal defense bar have fixated on privilege waiver as a sole means to gauge or demonstrate cooperation, and the over-reliance on waiver in this context is troubling. Companies have spent and are spending millions of dollars each year maintaining and improving ethics and compliance programs modeled after the principles espoused in the Federal Sentencing Guidelines, the Thompson Memo and the Seaboard Report. An appreciation for organizational efforts to self-govern and improve corporate culture are strikingly absent from the analysis with prosecutors. How to measure the effectiveness of an ethics and compliance program is an

admittedly difficult undertaking, but there should be meaningful opportunities to demonstrate the strength of compliance programs. If prosecutors and the defense bar better understood these developments and had objective means to recognize a good culture from a corrupt one, the emphasis on privilege waiver as a *de facto* litmus test for cooperation would dissipate and proposed Rule 502(c) might be viewed in a different light.

There are few, if any, compliance officers involved in the conversations where defense lawyers and prosecutors discuss a pending internal investigation or contemplated action. In my view, the dynamic of those discussions would change if the person with day-to-day responsibility for the organization's ethics and compliance were present. If able to demonstrate the effectiveness of a compliance program on the culture of an organization, there might be a higher degree of trust in the reliability of the nature and extent of a corporation's investigative efforts and scope of self-reporting, and waiver of privileges would be necessary, perhaps, as a last resort.

In considering the proposed Rule 502(c), therefore, I respectfully suggest that the Advisory Committee take into account the prospect for prosecutorial abuses and coerced waivers by adding the word "proper" before the phrase "exercise of its, regulatory, investigative, or enforcement authority...." I further recommend the Advisory Committee consider addressing in its comments to the proposed rule the importance of considering the totality of circumstances, including the effectiveness of an ethics and compliance program, before prosecutors or regulators resort to extreme measures such as requesting the disclosure of attorney-client communications or attorney work product.

Based on these comments, it is respectfully submitted that Rule 502(c) should include the additional exception and be revised as follows:

> **(c) Selective waiver**. *(1)* In a federal or state proceeding, a disclosure of a communication or information covered by the attorney-client privilege or work product protection — when made to a federal public office or agency in the *proper* exercise of its regulatory, investigative, or enforcement authority — does not operate as a waiver of the privilege or protection in favor of non-governmental persons or entities. The effect of disclosure to a state or local government agency, with respect to non-governmental persons or entities, is governed by applicable state law. Nothing in this rule limits or expands the authority of a government agency to disclose communications or information to other government agencies or as otherwise authorized or required by law.
>
> *(2) A public corporation's disclosure of a communication or information covered by the attorney-client privilege or work product protection—when made to an outside auditor or director of the company in the exercise of their regulatory, investigative, or oversight authority—does not operate as a waiver of the privilege or protection in favor of other persons or entities, including government entities.*

Thank you for the opportunity to submit these comments and share my views on the important issues raised by proposed new Rule 502 of the Federal Rules of Evidence.

Respectfully submitted

Richard J. Wolf

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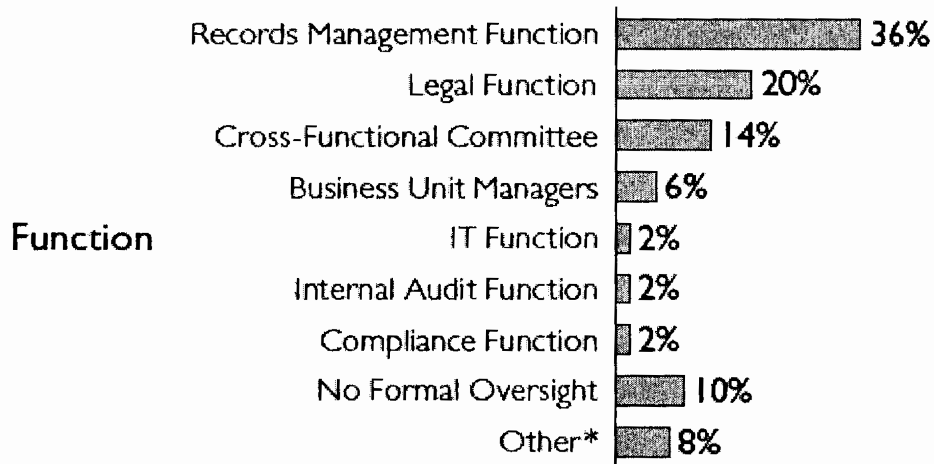
APPENDIX

Table 1[5]



[5] Provided with express permission of the General Counsel Roundtable 2003.

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