

# Forewarned is forearmed: E-discovery challenges in the context of an insolvency

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**In an insolvency situation, a company's data is critical to unlocking greater value for creditors. Consequently, being able to locate and review a company's documents efficiently can be crucial to asset recoveries and successful defences of claims.**

When the western world last found itself in a major recession in the early 1990s, business was still to a large degree conducted in a paper-based world. Although computers were in common use, most company records were created and stored in paper form and electronic means of communication such as emails and text messaging were in their infancy. These days, it's different. Globalisation has accelerated so rapidly that complex multi-national entities with data in various countries is now the norm rather than the exception.

The increased use and declining cost of electronic media systems and storage and the adoption of email as the primary means of business communication have led to an explosion in the number of documents that companies generate and store. In the past, reviewing 50,000 documents would have been considered a large project. Now, it is common for that number of documents to run into the millions. Electronic discovery (also known as 'e-discovery' or 'e-disclosure'), which is the process of finding, securing, processing, and producing electronic data as evidence in, among other things, legal and other governmental proceedings, has emerged in at least the past five years as a common consideration and obligation in litigation and investigatory (among other) matters. However, there is a rapidly growing body of precedent directing its use to specific issues encountered by companies experiencing financial difficulty.

This has important implications for businesses that are either restructuring or in the 'zone of insolvency' because a company's data is very often the road map to unlocking value for creditors. Consequently, a company - or an administrator, trustee, or debtor in possession - needs to locate and preserve data quickly to find assets and defend against claims. That data also constitutes property of the estate in a chapter 11 bankruptcy. Therefore, it is critical that an administrator take immediate steps to assess data issues at the beginning of a case or matter.

## Data preservation

The rules that govern how long electronic data should be retained vary by country and regulator. A company

that fails to abide by these rules in a litigation or regulatory investigation usually suffers adverse consequences – and insolvency is no different.

Typically, companies have a business continuity programme, or data retention programme, in which documents such as emails are routinely disposed of after six months or some other predetermined period of time. However, in the event of a formal insolvency, the laws of a particular country may require that some types of documents be kept for a longer period.

What is often less appreciated in this respect is the importance – and fragility – of the invisible 'metadata' contained in electronic documents. Much of the value of electronic evidence is often contained in its 'metadata', the invisible record of who has read a document, for example, or when or how it was amended.

This can be damaged irrevocably by the careless handling of electronic documents. In some instances, metadata can be destroyed or altered simply by copying files from one medium to another or just by turning a computer off and then on again, as its internal processes constantly update the metadata. Failing to properly protect or select electronic evidence, including metadata, can lead to negative inferences by regulators or the courts. While the case law around the 'spoliation' of electronic evidence is evolving rapidly in the US, it remains largely untested in many other countries' courts. However, this is expected to change.

Many insolvency practitioners and certain US judges recommend that companies institute an immediate 'litigation hold' at the onset of a bankruptcy or insolvency proceeding. This initiates an immediate suspension of policies and practices that might potentially result in data being altered after a certain date. Data can be extracted and held in a stable environment to allow administrators to develop a complete inventory as they begin the process of identifying potential assets and litigation. Such action insures that the integrity of electronic evidence is maintained.

E-discovery systems can help in this respect by

'harvesting' electronic evidence, e.g. making a non-invasive 'mirror' image through bit-by-bit and sector-by-sector copying of a memory device onto an external hard drive. This will include information on file creation and modification dates, and deleted and partially deleted files, thereby ensuring that the integrity of electronic evidence is preserved.

'Harvesting' electronic data in this way is one of a number of forensic e-discovery techniques that are becoming more useful, especially in cases where fraud or the deliberate concealment of evidence is suspected.

Allegations of fraud frequently accompany an insolvency matter; however, using forensic techniques to harvest electronic evidence will frequently expose any attempts to destroy or alter electronic evidence. Another useful electronic review tool is email threading, which identifies related emails and alerts reviewers if messages in a chain are missing. Again, this saves reviewer time by automatically grouping related documents together. It also enables lawyers and investigators to spot wrongdoers attempting to hide or disguise their trails.

## Speed is of the essence

Once a company's data has been preserved, it is essential to search it quickly and, especially, efficiently. This is likely to be particularly important during an insolvency event as multiple, concurrent processes and data searches may be required. Even though the insolvency procedure in most countries allows a company some breathing space from its creditors, the company will still face multiple claims from employees, secured creditors and counter-parties. Additionally, the need to interrogate a company's data set efficiently will be highly important when insolvency is in the offing because failing companies frequently find themselves embroiled in regulatory or criminal investigations.

One response to the financial and corporate failings that led to the credit crunch has been to give regulators considerably enhanced investigatory powers and the official encouragement to use them. In practice, this has led to a sharp rise in the number of dawn raids and information requests.

These can present a particular challenge for companies due to the tight timetables that regulators usually impose on their targets. For many companies, document retention and discovery policies have generally been formulated in anticipation of litigation rather than regulatory interventions. However, where the timescale for discovery in litigation can be measured in months, sometimes years, regulators commonly expect to receive the evidence they require within 30 days. Moreover, regulatory investigations are very often much wider in scope and

as a result, involve many more documents, which may come in a variety of formats.

Finding the important and relevant information amongst gigabytes, or even terabytes, of data is a daunting job. While lawyers and their litigation support teams are normally now in possession of some reasonably advanced tools with which to tackle that job, many of the ways in which they are utilised are still stuck in the paper age.

Some litigation support teams approach the task with a linear mindset developed in the days when the dominant business media was still paper and each document was read, coded and classified. Attempts are made to circumvent some of this process by conducting an electronic search of the documents, but it is usually done through identifying and search for key words. This method has some serious limitations, however, and keyword searches can often exclude some crucial documents.

This 'linear' approach to document review can have some severe drawbacks when time is tight and speed and accuracy are paramount. One of the many advantages of the digital world is that we no longer need to proceed in a linear, analogue way. Using linear methods to review electronic evidence is like using your iPod in the same way as your old Walkman. You wouldn't fast forward through your whole record collection to find your favourite songs – the digitalisation of music means that we can play what music we want, when we want, and when it comes to finding electronic information, the same principle applies to modern discovery tools.

Advanced review tools allow the review team to achieve higher levels of precision and, in fact, to change their whole review strategy. It is possible to analyse and use attachment relationships, email threads and near-duplicate document comparison analysis to speed up a review exercise. More fundamentally, these tools can change the basis on which reviewers retrieve relevant documents and exclude irrelevant ones.

The most advanced tools use 'meaning based' or 'concept' searching. Specifically, they use linguistic algorithms to identify the 'meaning' of a document by comparing it with a set of specimen documents. So, for example, if a reviewer finds a particularly relevant document, rather than looking for similar documents by running keyword searches, it is possible to use the document itself as a basis to find others like it even if they don't contain the same keywords.

Additionally, modern discovery applications can significantly reduce the size of the document set for manual review through a number of processes. From simple keyword searches and de-duplication processes at one end of the spectrum through to language and

format identification, data imaging and concept searches at the other, the range of tools at the disposal of reviewers is increasingly vast and sophisticated.

## Getting it in proportion

Being able to search a document set quickly is only part of the story, however. In the event of an information request, significant amounts of time can be saved by defining exactly what it is that the enquirer is asking for. While the scope of regulatory information requests is often wider than that for the discovery phase of litigation, companies very often waste time in recovering every document.

It is becoming increasingly common and required on both sides of the Atlantic for the parties to meet ahead of the discovery process to define the scope of the exercise. This 'meet and confer' process can save serious amounts of time – and money – by reducing the search down to a specific set of documents or a particular time frame.

One of the first questions should be: in what sort of documents is the information likely to be contained? Word documents stored on centralised servers are much easier to search than emails stored on PDAs or text messages held on mobile phones, so if particular types of documents can be excluded from a search, considerable review time and expense can be saved.

## Tracking down the data

Companies have increasingly globalised since the last major recession. Insolvencies like Parmalat, Maxwell, Enron, Lehman Brothers are recent examples of insolvencies and bankruptcies that involve entities with massive dealings in multiple countries. In the e-discovery context, many companies' data will be stored in many different locations around the world. This situation is often compounded by the use of outsourced data storage or application service providers, whose servers can often be located a long way from the source of the data.

Although many businesses have 'gone global,' the law has not kept up. Not only is insolvency law, one of the least harmonised of all business laws, different countries have different data protection, security, and data retention rules. As a result, companies may find themselves in breach of another country's rules simply because their data is located on a server in that country.

In litigation, companies may also find that information presumed to be confidential is discoverable by their opponents or by regulatory or fiscal investigators because it is stored on a server in a country with different data protection laws. In some

cases, it has even led to the courts or regulators of one country claiming jurisdiction over a case simply because a company's data was stored in that country, or was accessible from that country. Data protection and privacy laws can also make accessing that data more difficult in some countries; therefore, court orders may be required to access some types of documents.

Another complication of the spread of companies and their data around the world is the multiplicity of languages in which documents are written. Given the inter-connectivity of multi-national companies' IT systems, the repository of an organisation's documents can be, in theory, anywhere in the world. The geographic locus of a particular server may have no relationship to the language of the documents stored on it. Documents held in one country can often originate from many different places and are written in a variety of languages.

In recent times, e-discovery systems have developed to include language search facilities. These use software to quickly scan and identify the language of individual documents. By first identifying the language of documents, those of the same language can be collected together and sent to the appropriate lawyers or paralegals for review. Alternative is for reviewers to remove each foreign language document they come across from the main body of documents, collecting them together and then re-sorting them by language for review by native speakers. When this occurs in the course of a search process, large amounts of time can be lost during a review process by extracted documents not being in the expected language. Running a language search at an early stage can quickly flag this issue before valuable time is wasted by reviewers ploughing through documents they cannot understand.

## Hope for the best, but prepare for the worst

Insolvent companies are not likely to have adopted consistent email and management policies across all of their locations. A recent survey by Legal Week magazine in the UK found that only 41% of general counsel thought that their boards had a 'reasonable appreciation of the risks' of failing to robustly manage their electronic data. As a result, an administrator will need to determine what documents the company generates and where are they located.

In addition, the administrator will need to determine the existing document destruction policies. For many companies, an administrator will also need to consider the policies and practices of any third party data storage contractor the company employed to assess that third party's retention and destruction

policies. An inadequate back-up system may lead to the loss of key documents, especially emails, and the failure to produce important pieces of evidence will almost always be viewed adversely by courts, tribunals or regulators. If your data is stored in multiple jurisdictions, an administrator will need to assess their respective laws.

The current economic down cycle will generate tremendous numbers of insolvencies where data will play a meaningful difference in the recovery for creditors. Assessing issues and preserving data at the outset of any matter, or preferably before, will dramatically enhance the recovery of assets and enhance the ability to defend certain claims. Additionally, developing a thorough strategy and plan related to e-discovery review will significantly speed up the process and significantly reduce administrative expenses.

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