COMMENT

to
THE CIVIL RULES ADVISORY COMMITTEE
and the
DISCOVERY SUBCOMMITTEE

THE UN-AMERICAN RULE: HOW THE CURRENT "PRODUCER PAYS" DEFAULT RULE INCENTIVIZES INEFFICIENT DISCOVERY, INVITES ABUSIVE LITIGATION CONDUCT AND IMPEDES MERITS-BASED RESOLUTIONS OF DISPUTES

submitted by

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Lawyers for Civil Justice (LCJ) respectfully writes to engage the Civil Rules Advisory Committee ("Committee") and the Discovery Subcommittee on what we consider to be the "third pillar" of needed discovery reform: a "requestor pays" default rule requiring the party that asks for discovery to pay the costs of its requests.[1] Our current discovery scheme – which allows a party to request liberal discovery from an adversary and saddle that adversary with the cost – at best incentivizes inefficient discovery and at worst invites tactical abuse. The "producer pays" rule virtually guarantees the absence of any meaningful cost/benefit considerations to reign in the scope of discovery requests. Instead of incentivizing reasonably precise requests, the current system rewards the exact opposite, by licensing a party to fish for a relevant needle in haystacks of irrelevancy, while imposing all the costs and inefficiencies of such requests on its adversary and, in many respects, on the justice system itself.

LCJ believes that a common sense reform requiring each party to pay the costs of the discovery it requests will revolutionize discovery practice, for the better. A pay-as-you-go system would encourage each party to tailor its discovery requests to the needs of the case by placing the cost-benefit decision onto the requesting party – the party in the best position to control the scope of those demands. This simple and largely self-executing rule would also encourage substantive assessment of cases before they are filed, create more realistic incentives to settle meritorious cases and ease over-crowded court dockets. For these reasons, LCJ proposes that the Rules be amended to require that each party pay the costs of the discovery it seeks.

[1] LCJ believes the three pillars of discovery reform are: (1) preservation sanctions and triggers; (2) proportionality and the scope of discovery; and (3) an incentive-based cost default rule. No reform effort will succeed without addressing all three. We address the first two pillars in a separate Comment.

I. The De Facto "Producer Pays" Paradigm is an Accident of History and Inconsistent with the "American Rule."

The genesis of the "producer pays" presumption is largely an accident of history. Historically, certain practical limitations on discovery production costs existed simply due to the form of discovery sought. When records were kept on paper, and photocopying was unavailable, the cost of providing discovery was minor. There was no need for the Rules to address responsibility for the costs and, in the absence of any rule on this subject, an implicit assumption arose that the producing party pays. The economic merits of that assumption went unchallenged, even as a revolution in the means and methods of information storage occurred, and discovery compliance costs soared. Professor Martin H. Redish explains:

> The drafters of the Rules, of course, were only human, and humans make mistakes—especially in the process of revolutionizing an entire system. In the discovery process, their first mistake was their failure even to consider the question of to whom discovery costs were to be appropriately attributed in the first instance. Their second mistake was their flawed implicit assumption that the costs were properly to be attributed not to the party who is best able to economically internalize the costs and benefits of discovery, but to the party who has little or no control over those decisions. It is now time to correct their errors—and get ready to wish them a happy birthday.[2]

The accidental nature of "producer pays" is evidenced by its inconsistency with the "American Rule" – the principle that each party should bear its own litigation expenses regardless of which party ultimately prevails. Today a party pays the other side's discovery tab.[3] This goes even beyond "loser pays" because win or lose, a party still pays the other's bill. The result is particularly dramatic when a party that has made massive discovery requests loses the case and *still* the responder is left having paid the losing party's discovery expenses. The disconnect between this current system and the "American Rule" is difficult to understand as anything other

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[2] Martin H. Redish, *Allocation of Discovery Costs and the Foundation of Modern Procedure*, *in* THE AMERICAN ILLNESS (F.H. Buckley ed., forthcoming May 2013) (manuscript at 14).

[3] Even aside from its inconsistency with the "American Rule, " this cost allocation default rule is incompatible with established precepts of economic justice. Professors Redish and McNamara explain:

> If one strips away the long accepted assumption as to how the American system allocates costs among litigants, the actions of the parties to a lawsuit in the discovery process would be most appropriately seen as analogous to a quasi-contractual relationship between the adversary litigants. Under the theory of *quantum meruit*, a party to a quasi-contract is legally entitled, as a matter of fundamental principles of economic justice, to be reimbursed for any benefit he confers on another person at that person's expressed or implied request. . . . [I]t is [therefore] morally untenable to allow the requesting party to retain the benefit of its opponent's labor without, at the very least, reimbursing the costs of discovery incurred by the producing party.

Martin H. Redish & Colleen McNamara, *Back to the Future: Discovery Cost Allocation and Modern Theory*, 79 Geo. Wash. L. Rev. 773, 777 (2011).

than an unexamined historical practice outstripped by the realities of modern discovery. Professor Redish explains:

> "Yet at no point has anyone—including those who drafted the Federal Rules in the first place—even attempted to rationalize the respondent-centric model of cost allocation that has dominated federal court practice since the Rules' original promulgation. Were one actually to consider the issue afresh, it would be difficult to understand the assumptions inherent in a respondent-based allocation model."[4]

The Discovery Subcommittee should seize the opportunity to consider the current cost default assumptions afresh and to examine whether our "producer pays" system makes sense for the American civil justice system in the information age.

II. The "Producer Pays" Default Presumption Invites the Use of Overbroad Discovery as a Litigation Tactic.

Litigants report that discovery is too often used as a weapon to impact the outcome of a case irrespective of the merits, rather than as a tool to collect information to aid the fact finder. Parties request substantial volumes of information that is very expensive to collect and review in an effort to force opposing parties to consider settlement based primarily on the threat of excessive litigation costs. This tactic works. Many parties decide to settle cases to avoid expensive and protracted discovery instead of undertaking a fair and practical examination of the merits.

Expertise in economics is not required to acknowledge the reality that when the consumer does not have to pay for what he consumes, the consumer will demand more than is economically rational. This results in gross over-demand for resources that are by no means free, but which must be provided at a cost borne by someone else. As Professors Redish and McNamara have noted, this multiplies the incentive a party already has to consume that which is "free" by creating a "free" benefit to the requester on one side of the ledger, and a detriment to his opponent on the other side.[5]

As Professor Redish further explained, "the fact that a party's opponent will have to bear the financial burden of preparing the discovery response actually gives litigants an incentive to make discovery requests, and the bigger expense to be borne by the opponent, the bigger the incentive to make the request."[6] Accordingly, "[i]t is, then, all but inevitable that . . . the current cost allocation system will result in excessive and therefore inefficient discovery even where the discovering party does not consciously intend the discovery to be abusive."[7]

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[4] Redish, *supra* note 1, at 7.

[5] *See* Redish & McNamara, s*upra* note 2.

[6] Martin H. Redish, *Electronic Discovery and the Litigation Matrix*, 51 Duke L.J. 561, 603 (2001).

[7] *Id.*

While some may point to professional and ethical conduct as a limitation in such instances, the reality is otherwise. Indeed, some have argued that duties to one's client actually *demand* aggressive and overbroad discovery tactics, as long as there is some remote hope that expansive discovery might lead either to some relevant information, or more likely to a settlement forced by the opposing party's unwillingness or inability to bear the diversion of financial and human resources to respond to scorched-earth discovery tactics. This situation is particularly true in "asymmetric" cases[8] where one party holds most of the ESI and therefore bears a wildly disproportionate share of the burden, as explained by Professor Esenberg:

> In cases in which both parties are more or less equally subject to the costs and burdens of electronic discovery, each side can expect the other to be just as aggressive or reasonable as it has been. This form of mutually assured destruction may discipline the parties and temper the discovery "arms race." But, in cases of asymmetrical information, namely, those in which the bulk of information (particularly ESI) resides with one party, incentives diverge. Here the burden of responding to discovery is largely borne by one side, and there are fewer incentives to act with self discipline.[9]

Discovery rules should not provide weapons for parties to force settlements not justified by the merits. But that is what they do, and for the simple economic reason that the party who makes the request does so at the other party's expense. As Professors Redish and McNamara state: "Subsidization—through allocation of the total costs to the responding party—renders discovery costs a complete externality, and removes all incentives for litigants to limit the scope of their requests."[10] The result: "The externalization of discovery costs, accomplished through the *de facto* hidden litigation subsidy caused by our current model of cost allocation, incentivizes what can most appropriately be called excessive discovery."[11]

There is nothing the Federal Rules can do to prevent asymmetry of information. The Rules could eliminate, however, the ability of litigants to exploit asymmetry by the simple expedient of applying a common sense rule that litigants must pay for what they ask for. The Federal Rules should not encourage economically perverse litigation tactics, but rather should incentivize pursuit of discovery at the lowest cost and in the least burdensome manner possible to obtain the

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[8] In cases where the parties possess wildly asymmetrical amounts of discovery information, they thus face dramatically asymmetrical discovery burdens. Scott A. Moss, *Litigation Discovery Cannot Be Optimal But Could Be Better: The Economics of Improving Discovery Timing in a Digital Age*, 58 Duke L.J. 889, (2009). A government contractor expended over $6 million in e-discovery alone, amounting to more than nine percent of the agency's annual budget, but still failed to fully satisfy e-discovery requests for archived e-mail messages. Plaintiffs can similarly face daunting discovery costs, as shown by the federal government's lawsuit against the tobacco companies in which defendant Phillip Morris demanded the production of electronically stored information from over thirty federal agencies, "yielding [over] 200,000 e-mail 'hits,'" compliance with which "required a 'small army' of lawyers, law clerks and activists working full time for over six months," all costing millions of dollars. *United States v. Phillip Morris*, 449 F. Supp. 2d 1 (D.D.C. 2006), *aff'd in part and vacated in part*, 566 F.3d 1095 (D.C. Cir.2009).

[9] Richard Esenberg, *A Modest Proposal for Human Limitations on Cyberdiscovery*, 64 Fla. L. Rev. 965, 975 (2012).

[10] Redish & McNamara, *supra* note 2, at 800.

[11] *Id.* at 801.

evidence necessary for a merits-based resolution by the fact finder. This is not just a matter of economics, it is fundamental to whether the judicial system can deliver on Rule 1's guiding principle of just, speedy and inexpensive determination of civil actions.

III. Overbroad Discovery Damages the Integrity of the Judicial System, Harms the Economy, and Can Skew Enforcement of Substantive Law.

One result of perverse incentives in the judicial system is easily predictable: parties whose underlying behavior is perfectly acceptable, but who are forced to "buy peace" by settling cases only to avoid tremendous discovery burdens, lose faith in our judicial system and avoid any activity that risks an association with it. Professor Allen explains:

> In such cases, defendants will be deterred from productive activities not by the law but by litigation costs that increase the *in terrorem* value of even meritless suits that puts pressure on a defendant to settle and burden otherwise lawful conduct.[12]

Reform is needed when risks associated with of an out-of-control litigation process rationally hampers willingness to engage in productive activity.

Moreover, discovery burdens that are severe enough to cause inefficiencies in the judicial process can also skew the impact of substantive law, as Professor Redish explains:

> Designed to enable litigants to gather the information necessary to facilitate accurate decision-making and the effective vindication of substantive rights, the discovery process has a dark side that seems to have been largely undervalued at the time of the Rules' framing. At least in an important category of litigation—those cases in which significant amounts of discovery are likely to take place—the costs and burdens inherent in the discovery process threaten to give rise both to serious inefficiencies in the adjudicatory process and to a potentially pathological and coercive skewing of the applicable substantive law being enforced.[13]

In sum, when procedural rules, fueled by perverse economic incentives, influence not only decisions about whether to engage in productive economic activity, but also the enforcement of substantive law, it is time to reexamine the rules.

IV. Existing Rules Do Not Provide a Mechanism to Change the Incentives that Drive Overbroad Discovery.

The Federal Rules provide no meaningful recourse for a litigant to challenge the imposition of the de facto cost default burdens. Although much has been written and discussed about the role of judges in managing discovery, judges are asked to manage the scope of discovery, but are

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[12] Ronald J. Allen, *How to Think About Errors, Costs, and Their Allocation*, 64 Fla. L. Rev. 885, 888 (2012).

[13] Redish, *supra* note 1, at 2.

significantly hampered by institutional limitations on the courts.[14] Moreover, judges struggle to determine the proper scope of discovery without sufficient access to the underlying facts and with little or no knowledge about the costs involved. Even with the most effective judicial supervision, therefore, judges cannot counteract the strong economic forces driving the inefficient outcomes under the current "producer pays" paradigm.

Several ideas have been suggested as remedies. Some have recommended linking the parties' discovery entitlement to the amount in controversy and requiring a bond to ensure proportionality.[15] Others recommend that discovery be improved by changing its timing until after a claim has survived a motion for summary judgment.[16] Others would simply provide for equal cost-sharing – splitting discovery costs among the parties.[17] States have experimented with various cost allocation schemes as well. Each of these proposals has some merit, but none is simpler or more effective than a "requester pays" default rule, a self-executing solution that provides clarity to parties and does not rely on judicial intervention.

V. A "Requester Pays" Default Rule Would Increase Efficiency, Rationality and Fairness in Civil Discovery.

A rule requiring each party to pay the costs of the discovery it requests will encourage each party to manage its own discovery expenses and tailor its discovery requests to its needs by placing the cost-benefit decision onto the requesting party – the party in the best position to control the scope of those demands and, therefore, their cost. Such a Rule would also discourage parties from using discovery as a weapon to force settlements without regard to the merits of a case; a party that pays for discovery will have no incentive to make overly broad requests.

As Professor Allen has explained:

> If each side will have about the same amount of discovery costs, it makes perfect sense to let each side bear their own costs. That is identical to cost shifting, and any resources spent in shifting costs are simply wasted. Asymmetric costs, by contrast, cause skewed cost allocation and provide the opportunity for strategic exploitation. By contrast, placing the costs of discovery provisionally on the person asking for it, but allowing for judicial involvement to make adjustments,

[14] As the Supreme Court noted in *Twombly*, the Federal Rules were designed to allow liberal access to courts with weak claims being weeded out as litigation progressed. *Bell Atl. Corp. v. Twombly*, 550 U.S. 544 (2007). However, as discovery has grown increasingly expensive and complex, the Court noted that "[i]t is no answer to say that a claim just shy of a plausible entitlement to relief can, if groundless, be weeded out early in the discovery process through 'careful case management . . . given the common lament that the success of judicial supervision in checking discovery abuse has been on the modest side." *Id.* at 559.

[15] Peter B. Rutledge, *The Proportionality Principle and the (Amount in) Controversy*, *in* THE AMERICAN ILLNESS (F.H. Buckley ed., forthcoming May 2013) (manuscript at 3).

[16] Moss, *supra* note 7.

[17] Robert Hardaway, Dustin D. Berger, Andrea DeField, *E-Discovery's Threat to Civil Litigation: Reevaluating Rule 26 for the Digital Age*, 63 Rutgers L. Rev. 521 (2011).

> may both generally give incentives for the optimal production of information and permit a safety valve in the unusual case.[18]

A "requester pays" rule would achieve those results. A party who benefits by making a claim or raising a defense is in the best position to decide if information is worth the cost of obtaining it. A requester pays rule will encourage focused requests designed to obtain that information necessary for the just adjudication of the issues without the excessive costs currently experienced. It would encourage substantive assessment of cases before they are filed, create more realistic incentives to settle meritorious cases and ease over-crowded court dockets. It would do so while making trials more fair to both sides, as well as more likely to be resolved on the merits.

VI. Requestor Pays is Not a Penalty.

There is nothing unfair or "punitive" about the idea that a litigant must bear the costs of litigating his claim. Indeed, conventional economic theory on prices as a mechanism for efficient allocation of resources is adequate justification for a "requester pays" rule. Professor E. Donald Elliott explains:

> Judges should not confuse allocating costs to those who request discovery with penalties. There is nothing punitive about requiring an economic actor to pay for resources that are consumed in an activity that he undertakes to make a profit. On the contrary, the philosophy behind a market economy is that resources will be used most efficiently if those who decide to consume them pay the marginal costs of production. For the same reasons that electricity will be wasted and over-consumed if government requires it to be supplied at a price below the marginal cost of production, litigation will be oversupplied, wasting societal resources, if those who initiate litigation pay only a small fraction of its cost.[19]

Interestingly, the Rules provide one demonstrable example of the benefits of "requester pays." Fed. R. Civ. P. 26(b)(4)(C) already requires the requesting party to pay most of the other side's costs with regard to expert discovery. In practice, we know that each party often agrees to bear its own expert witness costs despite the rule-based ability to shift those costs because this is often a bi-lateral and roughly equivalent expense on both sides. What does this tell us about why parties almost never agree to pay for the other types of discovery they request? It says that costs in most claims by individuals against large entities are asymmetrical. When discovery costs are roughly (and reasonably) proportional, parties do in fact "work it out among themselves" by agreeing to divide costs in a fair way, without need for judicial intervention. But when costs are asymmetrical, the phenomenon described by Professor Allen prevails.

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[18] Allen, s*upra* note 11, at 894. *See also* Esenberg, *supra* note 9, at 975.

[19] E. Donald Elliott, *Twombly in Context: Or Why Federal Rule of Civil Procedure 4(b) is Unconstitutional*, 64 Fla. L. Rev. 895, 955-56 (2012) (footnotes omitted); *see also* E. Donald Elliott, *Managerial Judging and the Evolution of Procedure*, 53 U. Chi. L. Rev. 306 (1986); E. Donald Elliott, *Toward Incentive-Based Procedure: Three Approaches for Regulating Scientific Evidence*, 69 B.U. L. Rev. 487 (1989) (Because regulating by incentives is more efficient than by judicial command and control, incentive-based procedure is the first-best solution.)

Cost allocation based on common sense economics will not curb access to justice. Private, individual litigants rarely bear the expenses of initiating lawsuits under the contingency-fee systems that prevail in the U.S., despite the fact that anything beyond small-claims litigation can have massive costs apart from the discovery cost. One need only look to the steep, upfront expenses of employing expert witnesses, forensic accountants, investigators and the like to know that litigation is expensive. Despite this, few would argue that U.S. citizens are under-served in this regard. For example, while placing some of the costs of discovery on those requesting it "may be thought to burden the ability of less wealthy litigants to pursue a claim, the investment of substantial resources into litigation on behalf of non-wealthy parties thought by counsel to have a meritorious claim is quite common in a variety of contexts and has not materially impeded the pursuit of claims."[20]

Even so, adjustments can certainly be made in individual cases where access to justice is threatened. Professor Allen would "permit a safety valve in the unusual case"[21] and Professor Redish recommends that "Rule 26 should therefore be amended to state unambiguously that discovery costs are attributable to the requesting party, unless applicable substantive law provides to the contrary or the court finds that a compelling reason for shifting the costs to the responding party exists."[22]

Indeed, the notion of adjusting payment of court costs in individual cases already exists under the Rules. The Rules provide litigants to bypass the usual filing fee if they proceed *in forma pauperis*, with the consequence that such actions are subject to pre-service, threshold review of their lawsuits to weed out "frivolous or malicious" or otherwise defective claims. Thus, the Rules already recognize the truism that the ability to impose "free" litigation burdens on an adversary raises a potential for abuse that warrants additional judicial scrutiny.

Conclusion

LCJ respectfully asks the Committee and the Discovery Subcommittee to see the de facto "producer pays" paradigm for what it is: an accident of history that provides economic incentives for overbroad discovery that perverts the American civil justice system. The remedy is both simple and profound. Requiring requestors to pay the tab for what they order will curb overbroad discovery, end the use of discovery as a weapon and refocus attention on the merits of cases. Such a shift would accomplish more than any other single rule change to control the scope and costs of civil discovery effectively and fairly.

[20] Esenberg, *supra* note 8, at 980.

[21] Allen, *supra* note 11, at 894.

[22] Redish, *supra* note 1, at 12-13.