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KEY IDEAS:

NOT SO FAST ...
THIRD CIRCUIT LEAVES SKID MARKS ON ESI "COSTS"

The brakes may have been applied to recovering all litigation expenses associated with electronically stored information (ESI) as "taxable costs," with the Third Circuit forcing the prevailing party to absorb non-statutory expenses.

Making ESI lawsuit-ready is a tedious, time-consuming and expensive job, yet it is central to modern patent infringement litigation. This database arms race demands "perfect knowledge" of relevant documents that only a sophisticated document system provides. Fees for this technology can skyrocket into hundreds of thousands or even millions of dollars, playing a significant role in the upward spiral in patent litigation cost.

Historically, some courts have allowed prevailing parties to recover all expenses associated with ESI as part of taxable costs. But this speeding car may have been pulled over. In its watershed 2012 decision, *Race Tires America, Inc. v. Hoosier Racing Tire Corp.*,[1] the Third Circuit severely limited a prevailing party's ability to recover ESI-related expenses as taxable costs. Subsequent cases are following the court's in-depth analysis and are also restricting recoverable costs.

Ground Rules for Recovering Litigation Costs

Rule 54(d)(1)

Federal Rule of Civil Procedure 54(d)(1) provides, "Unless a federal statute, these rules [of Civil Procedure], or a court order provides otherwise, costs – other than attorneys' fees – should be allowed to the prevailing party." Given this rule, there is a strong presumption that the prevailing party in a lawsuit will be awarded costs.[2]

Under Rule 54(d), "district courts enjoy wide discretion in determining and awarding reasonable costs."[3] But, judges do not have "unrestrained discretion to tax costs to reimburse the winning litigant for every expense he has seen fit to incur in the conduct of his case."[4] The court's ability to tax litigation costs is limited to those explicitly authorized by statute.[5]

28 U.S.C. § 1920

Title 28 U.S.C. § 1920 "defines the term 'costs' as used in Rule 54(d),"[6] thus proscribing "the *full extent* of a federal court's power to shift litigation costs absent express statutory authority."[7] That statute provides

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1 674 F.3d 158, 166 (3d Cir. 2012).

2 *Kellogg Brown & Root Int'l, Inc. v. Altanmia Commeercial Mktg. Co. W.L.L.*, No. H-07-2684, 2009 WL 1457632, at *2 (S.D. Tex. 2009) (citing *Cheatham v. Allstate Ins. Co.*, 465 F.3d 578, 586 (5th Cir. 2006); *Cefalu v. Vill. of Elk Grove*, 211 F.3d 416, 427 (7th Cir. 2000)).

3 *Northbrook Excess & Surplus Ins. Co. v. Procter & Gamble Co.*, 924 F.2d 633, 642 (7th Cir. 1991).

4 *Farmer v. Arabian Am. Oil Co.*, 379 U.S. 227, 235 (1964).

5 *Crawford Fitting Co. v. J.T. Gibbons, Inc.*, 482 U.S. 437, 445 (1987).

6 *Crawford Fitting Co. v. J.T. Gibbons, Inc.*, 482 U.S. 437, 441 (1987).

7 *W. Va. Univ. Hosps., Inc. v. Casey*, 499 U.S. 83, 86 (1991) (citing *Crawford Fitting Co.*, 482 U.S. at 439 (1987)) (emphasis added).

a list of six litigation-related categories of expenses that may be taxed as costs and "embodies Congress's considered choice as to the kinds of expenses that a federal court may tax as costs against the losing party."[8] The Federal Circuit applies regional circuit law when interpreting § 1920.[9]

Section 1920(4), our focus here, entitles a prevailing party to recover "(f)ees for *exemplification* and costs of *making copies* of any material where the copies were necessarily obtained for use in the case."[10]

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As one circuit court noted, the "[U.S.] Supreme Court did not 'prevent courts from interpreting the meaning of the phrases used in § 1920.'"[11] The circuits have split over the meaning of "exemplification."[12] The Seventh Circuit has adopted a broad definition, concluding that exemplification "signifies the act of illustration by example, a connotation broad enough to include a wide variety of exhibits and demonstrative aids . . ."[13] Other circuit courts read the term narrowly as "[a]n official transcript of a public record, authenticated as a true copy for use as evidence."[14]

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Similarly, no uniform definition applies to costs. Given this, courts have developed a hodge-podge of standards for determining whether ESI-related expenses are taxable litigation costs.

Courts adopting a broader reading of § 1920(4) have approved a wide range of ESI-related expenses as taxable costs, including:

- Expenses related to a third-party electronic database service and producing documents electronically recoverable as costs under Ninth Circuit law.[15]
- Costs awarded for litigation database creation, data storage, hard-drive imaging, keyword searches, deduplication, data extraction and processing awarded based on complexity and cost savings compared to manually completing those tasks.[16]
- Appropriate to take into account costs associated with producing ESI in assessing costs for exemplification and copying.[17]
- Costs for electronic database prepared in lieu of more expensive fees for printing allowed.[18]
- Costs for e-discovery vendor's work collecting, searching and assisting in the production of ESI recoverable as "the 21st Century equivalent of making copies."[19]
- Costs for database allowed due to complexity of a case and immense time savings.[20]

8 *Crawford Fitting Co.*, 482 U.S. at 440.

9 *In re Ricoh Co., Ltd. Patent Litig.*, 661 F.3d 1361, 1364 (Fed. Cir. 2011) (citing *Summit Techs., Inc. v. Nidek Co.*, 435 F.3d 1371, 1374 (Fed. Cir. 2006)).

10 28 U.S.C. § 1920(4) (emphasis added).

11 *Northbrook Excess & Surplus Ins. Co. v. Procter & Gamble Co.*, 924 F.2d 633, 643 (7th Cir. 1991).

12 *Kellogg Brown & Root Int'l, Inc. v. Altanmia Commercial Mktg. Co. W.L.L.*, No. H-07-2684, 2009 WL 1457632, at *4 (S.D. Tex. 2009); *Mann v. Heckler & Koch Def., Inc.*, No. 1:08-cv-611, 2011 U.S. Dist. LEXIS 46045, at *6 n.2 (E.D. Va. Apr. 8, 2011).

13 *Cefalu v. Vill. of Elk Grove*, 211 F.3d 416, 427 (7th Cir. 2000).

14 *Arcadian Fertilizer, L.P. v. MPW Indus. Servs., Inc.*, 249 F.3d 1293, 1296 (11th Cir. 2001); *Summit Tech., Inc. v. Nidek Co.*, 435 F.3d 1371, 1375 (Fed. Cir. 2006).

15 *In re Ricoh Co. Ltd. Patent Litig.*, 661 F.3d 1361, 1364-65 (Fed. Cir. 2011) (applying Ninth Circuit law, but ultimately holding costs not recoverable due to a cost-sharing agreement between the parties).

16 *In re Aspartame Antitrust Litig.*, 817 F. Supp. 2d 608, 615-16 (E.D. Pa. 2011).

17 *In re Scientific-Atlanta, Inc. Securities Litig.*, No. 1:01-cv-1950-RWS, 2011 U.S. Dist. LEXIS 73688, 2011 WL 2671296, at *1 (N.D. Ga. July 6, 2011).

18 *Chenault v. Dorel Indus., Inc.*, No. A-08-CV-354-SS, 2010 U.S. Dist. LEXIS 78096, 2010 WL 3064007, at *4 (W.D. Tex. Aug. 2, 2010).

19 *CBT Flint Partners, LLC v. Return Path, Inc.*, 676 F. Supp. 2d 1376, 1381 (N.D. Ga. 2009).

20 *Lockheed Martin Idaho Techs. Co. v. Lockheed Martin Advanced Envtl. Sys., Inc.*, No. CV-98-316, 2006 U.S.

Courts adopting a narrow reading of § 1920(4) have taken a more restrictive view of whether ESI-related costs are taxable under the statute, including:

- Finding that the creation of a native file database did not qualify as "copying" as recoverable under § 1920(4).[21]
- Disallowing costs for collecting and processing more than 2,100 gigabytes of ESI. [22]
- Vacating costs awarded for the preparation and entry of a computerized litigation database.[23]

Race Tires America, Inc. v. Hoosier Tire Corp.

In its 2012 decision, *Race Tires America, Inc. v. Hoosier Racing Tire Corp.*,[24] the Third Circuit conducted a detailed analysis of § 1920(4) in the ESI context.

In *Race Tires America,* the two defendants in an antitrust case retained separate vendors to assist them with ESI production.[25] Tasks the parties' vendors performed included:

> (1) preservation and collection of ESI; (2) processing collected ESI; (3) keyword searching; (4) culling privileged material; (5) scanning and TIFF conversion; (6) optical character recognition ("OCR") conversion; and (7) conversion of racing videos from VHS format to DVD format.[26]

After prevailing on their motions for summary judgment, defendants sought reimbursement of more than $350,000 that they paid to ESI vendors under § 1920(4).[27] The district court awarded the ESI-related expenses as costs, and an appeal followed. The issue on appeal was whether the vendors' charges for assisting in the collection, preservation, searching, culling, conversion, and production of ESI fell under § 1920(4) as fees for "exemplification" or the cost of "making copies."[28]

After reviewing statutory history, the Third Circuit concluded that the award of costs under § 1920 is a matter of statutory construction.[29] Thus, recoverable ESI-related expenses had to be either for "exemplification" or "making copies."[30] Adopting the narrower construction, the court decided that none of the expenses sought involved "exemplification" because they were not costs associated with producing illustrative evidence or authentication of public records.[31] Further, the court said that statutory "making copies" included only scanning files to create digital duplicates, the conversion of files for production, and the transfer of VHS recordings to DVD format.[32] Therefore, only those expenses were taxable.

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The Third Circuit rejected arguments based on cases where costs were allowed when courts said that ESI vendor services (1) are indispensable because they are highly technical and beyond counsel's expertise, and (2) promote efficiencies and cost savings.[33] Ultimately, the Third Circuit described decisions allowing costs based on these factors as "untethered from the statutory mooring" of § 1920[34], observing,

Dist. LEXIS 52242, 2006 WL 2095876, at *2 (D. Idaho July 27, 2006).

21 *Mann v. Heckler & Koch Def., Inc.*, No. 1:08-cv-611, 2011 U.S. Dist. LEXIS 46045, at *9 (E.D. Va. Apr. 8, 2011).

22 *In re Fast Memory Erase v. Spansion, Inc.*, No. 3-10-cv-0481-M-BD, 2010 U.S. Dist. LEXIS 132025, at *4 (N.D. Tex. Feb. 2, 2010).

23 *Northbrook Excess & Surplus Ins. Co. v. Procter & Gamble Co.*, 924 F.2d 633, 643 (7th Cir. 1991).

24 674 F.3d 158 (3d Cir. 2012).

25 *Id.* at 161.

26 *Id.* at 161-62, 167.

27 *Id.* at 162.

28 *Id.* at 164-65.

29 *Id.* at 164.

30 *Id.* at 165.

31 *Id.* at 166.

32 *Id.* at 167.

33 *Id.* at 168-69.

34 *Id.* at 169.

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Shook, Hardy & Bacon offers expert, efficient and innovative representation to our clients. We know that the successful resolution of intellectual property issues requires a comprehensive strategy developed in partnership with our clients.

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> Section 1920(4) does not state that all steps that lead up to the production of copies of materials are taxable. It does not authorize taxation merely because today's technology requires technical expertise not ordinarily possessed by the typical legal professional. It does not say that activities that encourage cost savings may be taxed. Section 1920(4) authorizes awarding only the cost of making copies.[35]

The court concluded, "neither the language of § 1920(4), nor its history, suggests that Congress intended to shift all the expenses of a particular form of discovery – production of ESI – to the losing party."[36]

Race Tires America distinguished and harmonized the Federal Circuit's opinion in *In re Ricoh Patent Litigation* with its own because the parties in *Ricoh* jointly agreed to the creation of a specific document review database by a single vendor for document production purposes, unlike *Race Tires* where the defendants engaged their own vendors.[37]

Post-*Race Tires America* Cases

Since the *Race Tires America* decision in March 2012, district courts considering the issue have frequently rejected the costs of creating and maintaining an electronic discovery database as not recoverable under § 1920. For example, courts have:

- Refused to award the costs of an electronic database that was created solely for convenience.[38]
- Refused to award costs for litigation database creation, ESI processing, extraction of meta-data extraction, deduplication, electronic data hosting, or preparation for ESI production, but awarding costs for converting documents into a word-searchable format, and creation of TIFF images, hard-copy productions, graphics, and deposition transcripts.[39]
- Stated that "Under the *Race Tires America* approach, the only compensable costs are (a) the conversion of native digital files to the agreed-upon production format and (b) the scanning of paper documents to create digital duplicates for production in discovery."[40]
- Refused to permit recovery of costs for the maintenance of an electronic discovery database, but allowed fees for processing of electronic documents, including conversion of native files to "TIFF" format for production or from "TIFF" format to a searchable format; importing and loading of documents to an electronic database; production of electronic documents; and the associated project and technical support.[41]

Conclusions

Because this area of the law is not firm by any means, you should keep three things in mind when determining how best to recover ballooning ESI costs:

1. Before giving–or receiving–advice on the potential recoverability of ESI-related costs, know the rules in your jurisdiction. The Federal Circuit will apply the law of the relevant circuit, not its own.
2. ESI-related costs, particularly those costs related to expensive customized litigation databases, are likely not recoverable.
3. Some costs for processing and producing ESI, however, may be recoverable when properly presented to the court as "making copies."

35 *Id.*
36 *Id.* at 171.
37 *Id.* at 171 n.11.
38 *Finnerty v. Stiefel Labs., Inc.*, 2012 WL 4933863, at *2-5 (S.D. Fla. Oct. 16, 2012).
39 *Johnson v. Allstate Ins. Co.*, No. 07-cv-0781-SCW, 2012 WL 4936598, at *6 (S.D. Ill. Oct. 16, 2012).
40 *El Camino Res., Ltd. v. Huntington Nat'l Bank*, No. 1:07-cv-598, 2012 WL 4808741, at *7 (W.D. Mich. May 3, 2012).
41 *Abbott Point of Care, Inc. v. Epocal, Inc.*, No. CV-08-S-543-NE, 2012 U.S. Dist. Lexis 159042, at *3-5.