

# Arc Horizon

An Arc Partners, Inc. Publication

Arc Partners

## Special points of interest:

- The Federal Rules of Civil Procedure have changed; we discuss the effects on IT
- FRCP Rules changes; effect on Broker/Dealers
- Fred Post, Director, awarded CFA
- Narrowly avoiding disaster

— A feature for online readers —  
If you use Adobe Reader, you can navigate the newsletter by clicking on entries from 'Inside this Issue', 'Continued on... Continued from...' notations, or 'Special Points' above.

*“Although the legal community has been aware of the pending (Federal) rule changes for quite some time, the reality of their impact on IT... has yet to be fully appreciated.”*

## Featured Article

### FRCP Changes: What They Are and Why CIOs Should Care

**O**n December 1, 2006, changes to the *Federal Rules of Civil Procedure (FRCP)* regarding electronic discovery become official. These changes affect all U.S.-based organizations and some multi-nationals. The rules require more accountability within IT for preserving and producing electronic documents and may require the addition of IT infrastructure and capabilities.

The Federal Rules of Civil Procedure (FRCP), promulgated by the Supreme Court and approved by Congress, govern court procedures for all civil suits in Federal courts. The FRCP define the rules for initiating a lawsuit and provide 'rules of engagement,' especially with regard to the practice of *discovery*. Discovery is the pre-trial phase during which each party can request and in many cases compel the production of documents and other forms of evidence from other parties. It is based on the premise that parties should not be subject to surprises at trial, but in modern legal practice discovery also allows both parties to judge the relative strength of each side's case; this function tends to

produce settlements, thereby eliminating the expense and risk of trial.

The stated purpose for recent revisions is to make it easier for courts and litigating parties to manage the usage of electronic records during discovery, which in recent years has become pervasive – and expensive. According to Gartner, the average cost for a corporation to defend itself in a lawsuit is now close to \$1.5 million.

The underlying premise for these changes is that electronically-based documents are cheaper to manage and can be preserved, retrieved, produced and reviewed far more efficiently than paper media. On the surface, this is true. A simple 650MB CD-R can hold the equivalent of nine 5-drawer lateral file cabinets, or about 75 document storage boxes. Reproducing electronic files on a plastic disc is cheap and easy; but as technology has become more complex everything that happens before and after reproduction is not. The proliferation of electronic information, massive increases in forms of data and media, and the litigious nature of our society have combined to create a

'perfect storm' within the legal community centered on electronic discovery, or more commonly, e-discovery. The FRCP had to change to keep pace with this growth and to clarify what is, and is not acceptable with regard to the use of electronic information in e-discovery.

Although the legal community has been aware of the pending rule changes for quite some time, the reality of their impact on IT and the potential for added cost has yet to be fully appreciated. Many lawyers are not tech-savvy enough to understand the implications of the rule changes for IT and most IT people don't diligently follow federal rule changes. Depending on an IT department's current level of sophistication, these changes could require a major transformation in the way electronic content, including e-mail, is managed.

#### So What's Different?

The changes to FRCP rules are complex, technical (from a legal perspective), and primarily aimed at encouraging the use of e-discovery

*(Continued on page 2)*

## Inside this issue:

<b>Featured Article</b>	1
FRCP Changes: <i>What They Are and Why CIOs Should Care</i>	
<b>Leaders' Notes</b>	1
Thanks! <i>A year-end message from our MDs</i>	
<b>Arc Announcements</b>	2
Fred Post Earns Prestigious CFA <i>Our own globally recognized expert!</i>	
<b>Arc Events</b>	3
O'Sullivan Family Survives Boat Fire At Sea <i>"Just like the Titanic!" ...priceless</i>	

## Leaders' Notes

### Thanks!

On behalf of the Arc team, Brendan, John, and I extend best wishes to our clients, colleagues, and friends and hope you enjoyed a happy, healthy and safe holiday season.

We also want to thank our many loyal clients for showing their confidence in us by using our services in 2006. We continued many of our longstanding relationships with organizations such as Credit Suisse, HSBC, American Express, Citigroup, Calyon and LandAmerica Financial Group.

We also began new relationships with organizations including Barclays Global Investors, Washington Mutual Bank, McGraw Hill, GSO Capital Partners, and in a new twist on a familiar type of work, we were engaged this year for the first time by an institute of higher learning, Hofstra University.

Arc Partners celebrated its 10th anniversary in 2006. Since we began, Arc has performed more than 400 projects for over 50 different clients. About 90% of our projects are repeat business with companies

or executives we've worked with in the past. We are looking forward to another 10 challenging, interesting, and rewarding years of service to our clients, and we hope to continue to extend our client community through new projects and relationships.

We wish you a prosperous and rewarding 2007 from all of us at Arc!

– Don Harder is a Managing Director at Arc Partners.

*“For IT this may mean that classes of data and information you hadn’t considered ‘critical’ must now be considered when creating strategies for back-up and disaster recovery.”*

## FRCP Changes: (continued)

(Continued from page 1)

by promoting early agreement as to the form and substance of information being sought. Attorneys have been requesting and using electronic information in lawsuits for years; the difference now is they must ensure all required forms of electronic information are made available and, to be blunt, carelessness in handling electronic records is no longer tolerated by courts.

In this article we focus exclusively on rule changes that carry implications for IT. [Rules are referenced so that you may discuss these issues with your attorney—Ed.]

### EXPLICIT CREATION OF A NEW CATEGORY OF INFORMATION:

The amendments to the FRCP formalize, for the first time, a category of discoverable information known as **‘electronically stored information.’** The intent is to place discovery of electronic information on an even legal footing with discovery of paper-based information. The new

definition explicitly broadens the scope of discoverable material to include **“writings, [including e-mail, IM, Blackberry, chat—Ed.] drawings, graphs, charts, photographs, sound recordings, images, and other data stored in any electronic storage medium from which information can be obtained [and] translated, if necessary, into reasonably usable form...”** [Rule 34]

*For IT this may mean that classes of data and information you hadn’t considered ‘critical’ must now be considered when creating strategies for back-up and disaster recovery. It may also mean you need a defined Discovery Strategy.*

*A few key questions: Are you capturing the text of all e-mail and IM traffic? Are Blackberry communications captured? Do you commonly back-up PST files on laptops or data from laptops? If your employees use Webmail for business purposes are you able to capture and store those messages? Are drawings, images, or recordings a*

*regular part of your day-to-day business operations? How would you retrieve these types of information about only one person?*

**AN ACTIVE DUTY TO IDENTIFY, PRESERVE, AND PRODUCE RELEVANT ELECTRONIC DOCUMENTS:** With few exceptions, and without being asked for it, your attorney **must** either share all available electronic information, provide a list of such information, or provide a list and explain why she will not share the information. [Rule 26(f)]

A newly required discovery planning conference is mandated where the parties agree on what electronic information will be produced and in what format. [Rule 16(a)]

As an adjunct to FRCP changes, recent court decisions require preservation and retention policies that enable a company to place a ‘litigation hold’ on required documents. When a company has sufficient reason to believe that there is credible threat of a federal lawsuit, an active duty is

(Continued on page 3)

## Arc Announcements

### Fred Post Earns Prestigious Chartered Financial Analyst Designation

Fred Post, a Director at Arc Partners in New York City has earned the prestigious Chartered Financial Analyst® (CFA®) designation.

The CFA charter is a globally recognized credential for investment analysis and management. The CFA program sets a globally recognized standard for measuring the competence and integrity of financial analysts, portfolio managers and investment advisers. Currently, more than 74,000 investment professionals in 123 nations and territories hold the CFA charter.

Recipients of the CFA charter have successfully completed a graduate-level, self-study curriculum and series of three intensive examinations taken sequentially over at least two years. It is recommended that candidates prepare a minimum of 250 hours per exam, with substantially more recommended for individual circumstances.

Since the inception of the CFA program 44 years ago, pass rates at each of the three exam levels have averaged about 52 percent. Because of the rigor of the program, only about one in five candidates who enter the program pass all three exams and successfully complete all the requirements to earn the charter.

Administered exclusively in Eng-

lish, the international language of business, the three, six-hour exams cover ethical and professional standards, securities analysis and valuation, financial statement analysis, quantitative methods, economics, corporate finance, portfolio management, and performance measurement.

Fred has worked in the financial services industry for 23 years. A graduate of Columbia University’s School of Engineering in New York City, he holds an MBA from New York University. Post began his financial career at Swiss Bank Corporation (SBC) as an Operations Analyst in New York in 1983. At SBC and later its successor UBS, he held positions in New York, Basel, Zurich and London in operations, strategic planning, risk management and technology. He then joined Arc Partners, Inc. in 2000 and was promoted to Director in 2002.

“I am delighted to have received my charter. The CFA program has provided rigorous training in a broad range of subject areas that are of immediate use” said Post.

The CFA program is administered worldwide by CFA Institute, a not-for-profit professional association with offices in Virginia, New York, London, and Hong Kong.

Robert R. Johnson, PhD, CFA, managing director of the CFA and CGIPS Programs Division, explained what motivates candidates to make such a significant investment of their time and energy to seek to earn the CFA designation.

“For more than 40 years, candidates have sought to earn the CFA charter for two chief reasons,” Johnson said, “one, to expand and test their knowledge of current practice across a broad range of investment topics, and two, to demonstrate to clients, employers and peers their mastery of a demanding body of knowledge.”

#### About CFA Institute

CFA Institute is the global, not-for-profit professional association that administers the CFA curriculum and examination program worldwide and sets voluntary, ethics-based professional and performance-reporting standards for the investment industry. CFA Institute has more than 86,000 members in 129 countries. Its membership includes the world’s 74,000 CFA charterholders, as well as 134 affiliated professional societies in 55 countries. CFA Institute is headquartered in Charlottesville, Va., with additional offices in London and Hong Kong. More information may be found at [www.cfainstitute.org](http://www.cfainstitute.org).

## Arc Events

### O'Sullivan Family Survives Boat Fire at Sea

For three days all went exactly as planned – but when disaster struck it took quick action, calm heads, teamwork, and a bit of luck to bring everyone through alive.

Arc Partners Managing Director, Brendan O'Sullivan, his wife Jane, and their four children, Matthew, 16, Peter, 14, Connor, 13, and Mary, 9, had planned what seemed the perfect vacation. On June 18, they flew to Tortola in the British Virgin Islands and the next day boarded a 46-foot cruiser catamaran, *Twin Power*, for a five day cruise around the islands, enjoying the sea, a few favorite water sports, and the joy of being together as a family.

Brendan, an avid boat captain with many years experience, was at the helm when the first signs of trouble occurred. "We were motor-ing toward Great Camanoe, past the Dog Islands, at about 10 knots in 70 ft of water" he began. "At about 12:30 p.m. the starboard engine lost power. I put both engines in neutral, then in drive again, but still nothing. Seconds later, Jane shouted from the salon that she smelled burning rubber." Quickly, Jane moved to check the control panel. "There was nothing amiss—no flashing lights, seemingly no cause for alarm. The generator was off, and yet the smell got stronger," she said. But when light gray smoke

began coming from the starboard engine cover she yelled, "Brendan, Matt, we're on fire!"

Brendan raced down the stairs, turned off the electrical panel switches and opened the starboard engine compartment. "Smoke and then flames shot out and the smoke thickened and became black. We grabbed the nearby



fire extinguishers but none of them worked," said Brendan.

Matt, now a senior at Regis High School in New York City, swung into action, handing Mary and Jane the two nearby lifejackets, then dashing up the stairs to retrieve more. He returned and made sure his siblings lifejackets were secure, then led them through the large salon window in the bow and watched as they jumped in the water to safety.

Meanwhile, Brendan rushed back to the helm to signal for help. "SOS Mayday, SOS Mayday," he radioed while scanning the horizon for any potential source of assistance, but

*(Continued on page 4)*

### FRCP Changes: (continued)

*(Continued from page 2)*

immediately placed on the company to identify, preserve and produce all electronic records related to the dispute that will be used to support the company's case. This does not mean "protect records when suit is filed," it means you must take active steps as soon as a credible threat of suit exists. (see 'Zubulake' and 'Coleman (Parent) Holdings' decisions)

*For IT this may mean that you must have records management knowledge and capability that you do not currently possess. If you do have a records management strategy in place does it include electronic records?*

*Identification, preservation and production of information relevant to a case requires all companies to know the source, location, format, medium and 'ownership' of all relevant electronic data and information. (This level of detail is required in the list the attorney must share with opposing counsel.)*

*Key questions: Do you have the ability to place an immediate 'litigation hold' on electronic records slated for destruction if they are subject to pending legal action?*

*Assuming you are not currently capturing all 'electronically stored information,' if you had to preserve it on an emergency basis how would you go about it?*

*It is unlikely your attorney will be aware of the different types of information available to support his case: active data, metadata, replicated data, archives in various forms... IT must provide this information. The only question remaining is, do you prepare in advance or do it 'on the fly'?*

#### DOCUMENT RETENTION POLICY:

[Rule 37(f), Rule 45(d)(1)(D)]. These two rules do not establish an active duty to create a document retention policy, rather, they provide "safe harbor" protections for your company if, ***in good faith and under circumstances beyond your control***, you cannot comply with a record production requirement because you or your systems destroyed a required record or if the information sought is not reasonably accessible due to (provable) undue burden or cost.

The best way to establish the requisite 'good faith' is to have in place a solid document management, retention and destruction policy that contains an effective 'litigation hold' provision. Then, if you can show that your Electronic Records Management operatives religiously hold to your policy, your case has a much better chance of survival in situations where you fail to disclose required information.

#### Why not just keep everything?

You can. But your attorney will tell you that this exposes the company to unnecessary risk from documentation that could and should have been legally destroyed. If you've kept it, it's discoverable.

#### How does this affect Broker/Dealers?

Broker-dealers are already required to meet strict rules for the management of electronic records, e-mail, instant messages, and other electronic communication related to their business, so the requirement to preserve electronic information may sound like old news, but it's not that simple. To some degree companies complying

with SEC and NASD rules are ahead of the game. But even they are not out of the woods because the FRCP rules can require the retention of documentary evidence that is outside of normal SEC/NASD rules.

The SEC and NASD have an interest in records, transactions and communications related to the "business as such," particularly of a financial or fiduciary nature. But the FRCP rules apply to lawsuits, and companies can be sued by anyone over almost anything. This greatly expands the scope of discoverability to include records that have nothing to do with operations as broker/dealers, as in the *Zubulake* case where a firm was required to save all e-mail correspondence related to alleged age discrimination practices.

So broker/dealers must evaluate their records retention and discovery practices, if for nothing more than to determine how retention and preservation will be accomplished on an emergency basis for records not currently being captured.

#### Doesn't Sarbanes-Oxley Require the Same Thing?

Yes and No. Sarbanes-Oxley Section 802 requires regulated firms to retain all records for 7 years when the records are related to pending legal and/or compliance actions against a company. However, the FRCP rules are both broader (applies to all companies dealing with federal courts, even if they are not subject to SOX) and more specific (specifies preservation of electronic records).

SOX only says "all records" and since SOX is primarily concerned with corporate fiduciary responsibility this has left the door open for the

question, 'what constitutes a record?' ... that door is now closed.

#### Why Is This Important To My Company (or Me)?

First, lawsuits are largely won or lost in pre-trial discovery. Litigation strategy is based upon the information gathered and it is common for settlement to be reached after discovery. Additionally, dollar figures in recent lawsuits decided on e-discovery issues have run to billions of dollars, so it doesn't require a giant leap of faith to surmise that doing e-discovery right can be important.

Second, the FRCP changes make lawyers directly responsible for knowing more about their client's information systems and technical capabilities than ever before. The rules place the crosshairs directly on the attorney, but the source of this required knowledge and the mechanisms for making information available lie with IT management.

Failure to follow procedural rules can result in sanctions: fines, enforcement orders, evidence precluded from use at trial, claims partially or wholly dismissed, and even summary judgment. We leave it to you to judge how many times an IT department can be the source of such sanctions and continue to operate with impunity. *Translation: The crosshairs may be on the attorney, but you are still in the line of fire.*

Third, many of our clients deal with issues where federal courts will have jurisdiction. However,

*(Continued on page 4)*



# Arc Events: Surviving a Boat Fire at Sea (continued)

(Continued from page 3)

he didn't see anyone near, nor did he have time to wait for a reply. The boat was rapidly being overtaken by flames and thick, black smoke.

Jane had tried but failed to release the inflatable boat from outside the salon when she heard Brendan repeatedly shouting "Get off the boat!" and Matt yelling for her. "I heard the voices and knew everyone was safe, but had no



voice to answer. It was totally terrifying," Jane recalled. The cabin was so full of black smoke that she couldn't see to escape the way the children had gone. Grabbing the pocketbook that had been sitting beside her (which contained all six passports) she jumped off the port side to safety and swam toward the voices of Peter, Connor, and Mary.

When they were sure the rest of the family was in the water, Brendan and Matt jumped in and began assessing their situation. Matt formed the family into a swimming circle while Brendan steered the family away from the potentially explosive boat and toward the barren islands on the horizon.

It had been only two minutes from the time the engine lost power to the time the last two had jumped from the flaming deck. Now, as they bobbed around alone on the ocean they watched as what had been their home for the last three days become engulfed in orange and yellow flames, and then melt down to the hull.

The family was in the water for about 10 minutes when the first rescuers arrived on the scene, attracted by the smoke that could be seen for miles. Two non-English speaking men in an inflatable were the first to pick them up.

The Water Police brought fire equipment to try to douse the flames, but by then the *Twin Power* had already burned to the water line and soon sank to the bow tip. "Just like *The Titanic!*" exclaimed Mary.



The family transferred to a small tourist vessel before a charter company boat arrived to take them back to the marina in Road Town.

"In retrospect, it's a miracle we all survived," said Jane. "Luckily, all the children are excellent swimmers and have spent time on boats.

We're all grateful for Matt's calm, quick thinking and courage."

The Arc Partners family is also grateful, and thankful that the O'Sullivan's came through their ordeal.

## FRCP Changes: (cont'd)

(Continued from page 3)

most of the work of corporate attorneys is brought through state courts. Although the current changes only apply to federal courts, most state court systems promulgate procedural rules based on the FRCP. Given the predominance of electronic information in commerce it is likely that these rules will eventually be almost universally applied across the U.S., meaning, you're probably going to have to deal with it sooner or later.

Although the FRCP amendments are complex, what you can do to minimize the risks of violating them is clear. You must:

- 1) Be able to identify sources of electronic evidence
- 2) Know where it resides, in what format, and who 'owns' it
- 3) Pre-determine how you will produce it for counsel if necessary.

To meet the requirements of the rule changes, many companies will likely need to add additional IT infrastructure and capabilities. However, by implementing a set of best-practices for electronic discovery, companies can minimize additional

infrastructure expenditures, control the cost of legal proceedings, and maximize the effectiveness of litigation in the federal court system.

While a discussion of e-discovery best practices is beyond the scope of this article, it may be the subject of a future newsletter if interest warrants the effort. ☞

*While Arc Partners cannot keep your company entirely free of extraneous legal entanglements, we can help you survive the experience.*

*Our expertise in Compliance Assessment & Strategy and Compliance Solution Implementation can help you determine what to do and how to do it. We work closely with your Legal, Compliance, IT, and Business divisions to ensure that all compliance requirements are successfully met.*

For more information, contact:

John Marinelli  
(212) 370-9460 x204  
(john.marinelli@arcpartners.com)  
or  
John Harris  
(212) 370-9460 x316  
(john.harris@arcpartners.com)



**"Transforming your vision into profitable reality"**

Arc Partners, Inc.  
Three Park Avenue, 27th Floor  
New York, NY 10016

Phone: (212) 370-9460  
Fax: (212) 370-4121  
Email: editor@arcpartners.com

VISIT US ON THE WEB:  
WWW.ARCPARTNERS.COM

Arc Partners was founded during a time of unprecedented business and technology change in the financial services industry. Our goal is to assist financial services companies in improving business performance through better management and application of technology.

We are a high performance management consulting firm that works with clients to ensure key business process and technology initiatives succeed. We don't do projects to our clients. Our combination of industry expertise and consultative skills allows us to creatively analyze fast-changing environments and recommend best-fit solutions.

Arc Partners has earned a reputation for high quality, value-added service. We perform multiple engagements for over 90% of our clients, reflecting their satisfaction with their service. We continue to expand, but pace our growth to ensure continued excellence in the quality of our work.

Arc Horizon is published quarterly by Arc Partners, Inc.. Special editions may be published intermittently as circumstances require.

Copyright © 2007 Arc Partners, Inc.

This publication may not be reproduced in any form or by any electronic or mechanical means, including information storage and retrieval systems, without prior written permission. All Rights Reserved.