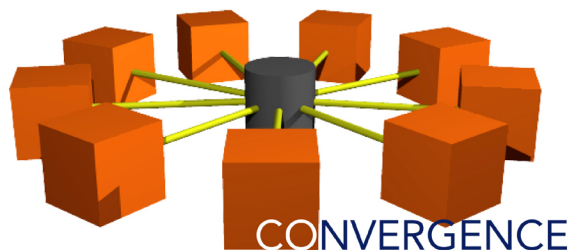


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## DISCOVERY SANCTIONS

With the rapid expansion of technology and the constant stream of information now available to individuals and corporations alike has created a new set of challenges to attorneys engaging in discovery, as well as the judges who oversee that process. These challenges have included not only the technical — how to collect, store, and obtain this information — and the strategic — what information should be produced or requested and in what format — but also concerns with enforcement. Many companies are understandably wary of allowing even limited access to their electronic data and still others are simply unwilling to retain the information, for logistical or strategic reasons. Courts, however, are increasingly responding to the enforcement challenge and indicating their willingness to impose sanctions against those litigants who fail to comply with electronic discovery. Willful intent to destroy or conceal evidence is no longer a universal prerequisite for the imposition of sanctions — courts have imposed harsh sanctions even against litigants who have simply failed to halt automatic deletion programs already in place.

When faced with discovery abuse or failure to comply with electronic discovery, district courts and magistrate judges can be quite creative and sanctions can take many forms. *See, e.g., In re Old Banc One Shareholder Sec. Litig.*, 2005 WL 3372783 (N.D. Ill. Dec. 8, 2005) (defendant prevented from cross-examining plaintiff's expert); *Tilberg v. Next Management Co.*, 2005 WL 2759860 (S.D.N.Y. Oct. 24, 2005) (extending discovery period and expanding scope of permitted electronic discovery when defendant prevented plaintiff's expert from accessing certain email servers).

Certain types of sanctions have become more common than others. These include monetary sanctions, limitations on evidence and testimony, adverse inference instructions, and default judgments. These sanctions, along with representative cases in which they have been awarded, are described below.

### Monetary Sanctions

Courts often consider monetary sanctions a lesser punishment for discovery abuses, awarding such sanctions in lieu of adverse inference instructions, default judgments, and other seemingly harsher punishments. Nevertheless, monetary sanctions can themselves be stiff, ranging from tens of thousands to hundreds of thousands of dollars and sometimes including an award of the opposing party's attorney fees.

- In *Channel Components, Inc. v. Am. II Electronics, Inc.*, 915 So.2d 1278 (Fla. Dist. Ct. App. 2005), the appellate court affirmed the trial court's award of \$75,000 in sanctions, based on a fine of \$2,500 a day for a maximum of thirty days. The plaintiffs in this case had repeatedly sought court intervention to obtain the defendants' compliance with discovery requests. Despite the admission by the defendants in depositions that they frequently used email to communicate and defendants' references to computer software used to track correspondence with customers, defendants indicated to the court that no documents embodying such communications existed. Following a change in counsel and threats from the judge of sanctions in the amount of \$2,500 a day, the defendants later produced the communications in question. Despite arguments from defendants' counsel that a fine of \$75,000 would bankrupt the defendants, the appellate court agreed with the trial court that such a sanction was warranted and implied that the defendants were fortunate to avoid a default judgment against them. The court noted that defendants had improperly prolonged the discovery process by more than two years and had failed to produce the documents despite multiple opportunities — and court orders — to do so.
- In *E&J Gallo Winery v. Encana Energy Servs., Inc.*, 2005 WL 3709885 (E.D. Cal. July 5, 2005), the court ordered sanctions against the defendants' law firm in the amount of \$102,079. Plaintiff had sought even greater sanctions as punishment for actions by defendants and their counsel that resulted in the cancellation of a third-party deposition scheduled by plaintiff. In awarding the sanctions, the Magistrate Judge focused in large part on past discovery disputes and abuses. Particularly egregious was a meritless motion to compel brought by defendants in retaliation for a successful motion by plaintiff to compel certain electronic discovery, including email communications and searches of computer hard drives. The court noted: "Defendants' papers reveal this motion retaliates for Gallo's successful motion to search the traders' computers. This motion mimics Gallo's motion, except that it lacks support or merit. The gist of defendants' position is that since the traders computers will be searched, Gallo should endure searches." This abuse of electronic discovery, in combination with the abuses of which plaintiff complained, merited monetary sanctions against defendants' counsel.
- In *Kamatani v. Benq Corp.*, 2005 WL 2455825 (E.D. Tex. Oct. 4, 2005), the court fined the defendant \$500,000 for willful disregard of discovery orders. Certain affirmative defenses were also struck and defendant was ordered to pay plaintiff's attorney fees associated with the show cause hearing. Defendant had refused to produce source code and other documents from a third-party, claiming that it lacked access to the third-party's technology. However, there was extensive evidence, including network access agreements and statements from defendant's deposition, indicating that defendant did in fact have access to the requested information. When pressed, defendant served the third party with a subpoena, despite the third-party's

expressed willingness to provide the information upon request. When informed by defendant that it had served the subpoena only when forced by plaintiff's counsel, the third-party declined to accept service and indicated that the request would have to go through the Hague Convention. The judge awarded the sanction as a response to this "blatant and extensive" discovery abuse, which it noted was "far in excess of anything this Court has ever encountered."

### **Evidentiary and Testimonial Limitations**

As a separate sanction, or in addition to other sanctions, courts respond to discovery abuses by limiting the evidence or testimony that may be introduced by the sanctioned party or limiting that party's ability to object to the opposing party's evidence. Courts often focus on evidence that was not timely or properly produced, but may also limit expert testimony on the subject.

- In *Serra Chevrolet, Inc. v. General Motors Corp.*, No. CV-01-VEH-2682-S (N.D. Ala. May 20, 2005), the court struck three of defendant's affirmative defenses and levied a \$700,000 fine. In addition, the court prohibited defendant from challenging plaintiff's expert with regards to the expert's lack of information or knowledge regarding the information defendant failed to timely produce. The sanctions were based on defendant's repeated delays in responding to discovery requests, which it did not do until ordered to respond by the court, and defendant's disregard for the deadlines set by the court for compliance with discovery orders. In particular, upon learning only six days before the deadline to purge itself of contempt that its computer search was incomplete, the defendant waited more than a month before undertaking a manual search and testimony indicated that this search was still incomplete.
- In *In re Old Banc One Shareholder Sec. Litig.*, 2005 WL 3372783 (N.D. Ill. Dec. 8, 2005), the defendant was sanctioned for failing to institute and implement a litigation hold over documents and underlying data. Finding that the loss of the documents, while "poor judgment" was negligent and not the result of willful destruction of documents, the court declined to enter a default judgment or an adverse inference instruction and instead imposed a lesser sanction: Defendant was not permitted to cross-examine the plaintiffs' expert and the jury was instructed as to this limitation and the reason for it.

### **Adverse Inference Instruction**

One common response to discovery abuses, and in particular to the destruction of electronic data and other evidence, is an instruction to the jury which details the discovery misconduct and informs the jury that they are to draw an adverse inference from this misconduct — i.e., the jury is to assume that the missing evidence would have

been damaging to the party responsible for its unavailability. Where key documents or large amounts of information are missing, the adverse inference instruction can be almost as serious as the entry of a default judgment.

- In *DaimlerChrysler Motors v. Bill Davis Racing, Inc.*, 2005 WL 3502172 (E.D. Mich. Dec. 22, 2005), the defendant was sanctioned for failing to take affirmative steps to preserve relevant emails that were otherwise subject to routine deletion. The Magistrate Judge noted that the defendant was on notice that the emails were or might be relevant to the litigation and thus had a duty to suspend its normal procedures for the deletion of documents. The failure to take such steps could be evidence of bad faith. Although he determined that the failure to preserve the electronic data was not in bad faith, the magistrate found that an appropriate sanction would be 1) an order allowing plaintiff to present evidence regarding the defendant's failure to preserve electronic data, 2) an instruction to the jury that it could presume, based on the destruction of the evidence, that the destroyed evidence would have been favorable to the plaintiff, and 3) permitting plaintiff's counsel to argue in favor of the negative inference.
- In *Lyondell-Citgo Refining, LP v. Petroleos de Venezuela, S.A.*, 2005 WL 1026461 (S.D.N.Y. May 2, 2005), the court ordered an adverse inference instruction following defendant's refusal to make electronic databases available for the plaintiff's inspection. The court gave little or no weight to the defendant's arguments that Venezuelan law prohibited it from granting access to the information. The court found that the defendant's repeated arguments that the information was relevant, event after the court had ruled on the relevancy issue, and defendant's refusal to allow access were sufficient evidence of bad faith. The court also found no proof that the Venezuelan Ministry was adequately informed of the court's orders on the subject. The magistrate's order was affirmed by the district judge.
- In *Mosaid Technologies, Inc. v. Samsung Electronics Co.*, 348 F. Supp. 2d 332 (D. N.J. 2004), the granted the plaintiff's request for an adverse inference instruction and attorney fees after the defendant had failed to institute a litigation hold preventing the automatic deletion of email. As a result of defendant's failure, defendant was unable to produce a single technical email in response to discovery in this very technical patent litigation. The court found that, although defendant's destruction of the evidence had been merely negligent and not willful or intentional, "negligent destruction of relevant evidence can be sufficient to give rise to the spoliation inference."

## Default Judgment

A default judgment is the most serious litigation sanction the court can award. However, in a few cases, the courts have determined that a party's discovery abuses are

so pervasive and egregious that terminating sanctions are warranted. These sanctions sometimes come in the form of an order to strike the defendant's answer or the entry of a default judgment against the party found to be abusing the discovery process or egregiously failing to comply with its discovery duties.

- In the well-publicized case of *Coleman (Parent) Holdings, Inc. v. Morgan Stanley & Co., Inc.*, 2005 WL 679071 (Fla. Cir. Ct. Mar. 1, 2005), the court had initially crafted an adverse inference instruction to be read to the jury, including a detailed account of Morgan Stanley's failures to comply with the plaintiff's discovery requests and to institute and enforce a litigation hold on the deletion of relevant documents. However, following the adverse inference order, the court learned that Morgan Stanley had intentionally hidden information from plaintiff and the court about its discovery violations. This included coaching witnesses to avoid mention of problems with obtaining deleted documents from back-up tapes. Morgan Stanley also revealed that it would not be able to complete its review of the files from the back-up tapes in time for trial. The court entered a default judgment against Morgan Stanley and deemed the majority of the plaintiff's complaint established. The complaint was read to the jury, which subsequently returned a verdict against Morgan Stanley for \$604 million in compensatory and \$850 million in punitive damages.
- In *Electronic Funds Solutions v. Murphy*, 36 Cal. Rptr. 3d 663 (Cal. App. 2005), the court vacated a \$24 million dollar damage award as far in excess of the amount requested in the complaint but upheld the terminating sanctions striking the defendant's answer for discovery abuse. Defendants' discovery abuses were numerous, and included the failure to produce electronic documents and data as well as the intentional destruction of data through the use of "Data Eraser" software. The defendants also made false representations to the court regarding their compliance with discovery requests and orders. The court struck the defendants' answer and ordered the entry of a default judgment against defendants.

The cases described above are only a sampling of the decisions addressing electronic discovery. And while it is true that sanctions are not awarded in every case, these cases and others like them appropriately create a strong incentive for companies and attorneys alike to carefully review their approach to electronic discovery and document retention. With new federal rules going into effect at the end of the year and courts becoming increasingly knowledgeable about the ways that data may be maintained and accessed, there is reason to believe that enforcement will only become more stringent. A considered and comprehensive approach to the retention and production of electronic data, before litigation as well as during discovery, is rapidly becoming an essential element of litigation success.

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