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A legal update from Dechert's Antitrust/Competition and Mass Torts and Product Liability Groups

Courts Impose Severe Sanctions for Electronic Discovery Abuses

Key Points

- Effective management of electronic discovery can mean the difference between winning and losing.
- Courts appear increasingly willing to enter terminating sanctions against litigants, including individuals as well as corporate parties, for ESI abuses.
- Litigants—including third parties—must thoroughly investigate potentially producible ESI early on in order to set and meet reasonable production deadlines.

It should by now be clearly understood by practitioners that the stakes are extraordinarily high for litigants in managing electronic discovery.[1] Three recent decisions reinforce the serious consequences that can result from a failure to follow proper procedures regarding the preservation and production of electronically stored information ("ESI"). As these decisions demonstrate, courts are increasingly willing to enter the most severe sanctions, including the dismissal of claims and defenses, for discovery violations involving ESI. Even third parties are at risk for harsh sanctions when responding to a subpoena.

In *Kvitka v. Puffin Co., L.L.C.*,[2] a district court in the Middle District of Pennsylvania dismissed the plaintiff's claims after she failed to preserve—and apparently destroyed—key evidence. In *Gutman v. Klein*,[3] a district court in the Eastern District of New York entered a default judgment against a defendant who had deliberately destroyed ESI just prior to a court-ordered inspection of a computer. This appears to be the first case in which a district court in the Second Circuit entered default judgment against a party solely for ESI discovery abuses.

In *In re Fannie Mae Securities Litigation*,[4] the U.S. Court of Appeals for the District of Columbia Circuit upheld a district court decision forcing a third-party government agency to turn over documents it sought to withhold as privileged for failing to comply with ESI production deadlines. These sanctions were imposed despite the fact that the agency submitted evidence that it had spent over ***nine percent*** of its annual budget responding to the third-party subpoena.

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1 *See*, e.g., Benjamin R. Barnett & Philip N. Yannella, *Decisions Up Stakes in Managing E-Discovery Cases*, Legal Intelligencer, July 30, 2008, *available at* www.law.com/jsp/article.jsp?id=1202423378845.

2 No. 1:06-cv-0858, 2009 U.S. Dist. LEXIS 11214 (M.D. Pa. Feb. 13, 2009).

3 No. 03-cv-1570, 2008 U.S. Dist. LEXIS 97707 (E.D.N.Y. Dec. 1, 2008) ("*Gutman II*") (adopting the Report and Recommendation of the magistrate judge and entering default judgment).

4 552 F.3d 814 (D.C. Cir. 2009).

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Kvitka v. Puffin Co., L.L.C.

In *Kvitka*, a district court in the Middle District of Pennsylvania took the severe step of dismissing with prejudice the claims of a plaintiff who had thrown away her laptop with the intent to destroy relevant e-mails after the duty to preserve her e-mails had arisen.[5] Plaintiff Kvitka was a purchaser and seller of antique dolls. Defendant Puffin was a publisher of specialty doll collecting magazines. Puffin terminated Kvitka's right to advertise in its magazines after complaints arose regarding Kvitka's business practices. Letters threatening legal action were exchanged, and the defendants wrote to plaintiff's counsel asking it to preserve all relevant e-mails in anticipation of litigation. Kvitka herself appeared to acknowledge the centrality of her e-mails to the dispute, writing at that time that "[a]pparently, this entire thing has a lot to do with some e-mails."[6]

Kvitka initiated an action in the Pennsylvania Court of Common Pleas on January 6, 2006. About two months later, she discarded the laptop computer that contained her e-mails. When the judge in the state court case asked Kvitka about the status of the original e-mails, she discontinued the state court litigation, and filed suit in federal court in April 2006. Over a year and a half later, in October 2007, she finally revealed for the first time in a discovery response in her federal suit that she had discarded her laptop. Over the next several months, Kvitka continued to insist that no files or e-mails had been recovered from her old laptop and transferred to her new laptop. When the defendants tested that assertion by moving to inspect the new laptop, Kvitka informed the defendants that she did in fact have "some" of her old e-mails on her new laptop.[7] The defendants then moved for sanctions.

The court found that there was "no question" that Kvitka had destroyed evidence in bad faith. Moreover, the court found that Kvitka had been "manipulative and evasive" in an effort to cover up her actions.[8] As for prejudice, the court found that by throwing out her laptop, Kvitka had effectively thrown away the defendants' key evidence. The court determined that no sanction less than dismissal would be sufficient, reasoning that an adverse inference instruction would neither aid the defendants in defending against Kvitka's claims nor deter similar conduct in the future.

Gutman v. Klein

In *Gutman*, the court imposed the most severe possible sanction—default judgment—against a defendant for intentionally deleting relevant information from his computer hard drive just prior to the inspection of that hard drive by the plaintiffs' experts.[9] *Gutman* involved a commercial dispute between business partners. The magistrate judge ordered defendant Klein to make his computers available to the plaintiffs so that their retained expert could copy the hard drives. When plaintiffs' counsel and expert arrived at Klein's residence to copy the hard drives, Klein allowed them access to his desktop but refused to produce his laptop for nearly two hours.

A forensic expert appointed by the court later found evidence that someone had selectively deleted files and reinstalled the operating system in the two days prior to the inspection. The expert also found evidence that someone had changed the settings on the laptop's system clock the morning of the inspection to make it appear as though the reinstallation had occurred several years earlier, when these events had in fact occurred just days before. The expert concluded that the sum of the evidence was "indicative of the behavior of a user who was attempting to permanently delete selected files from the machine and then cover up the chronology of system changes occurring in the hours and days just prior to a forensic preservation."[10] Klein and his computer technician's explanations under oath "left little doubt that they were not telling the truth."[11]

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5 2009 U.S. Dist. LEXIS 11214, at *15-16.

6 *Id.* at *3 (emphasis omitted).

7 *Id.* at *6 (internal quotation marks omitted).

8 *Id.* at *9-15.

9 *Gutman v. Klein*, No. 03-CV-1570, 2008 U.S. Dist. LEXIS 92398 (E.D.N.Y. Oct. 15, 2008) ("*Gutman I*"), adopted by, judgment entered by, *Gutman II*, 2008 U.S. Dist. LEXIS 97707, at *4.

10 *Gutman I*, 2008 U.S. Dist. LEXIS 92398, at *16-17 (internal quotation marks omitted).

11 *Id.* at *28-29. Klein's credibility was further damaged when he contended that a thief had stolen a different laptop containing evidence relevant to the case. *Id.* at *34. There were no witnesses or physical evidence to corroborate this claim. *Id.* at *35. According to the court, either Klein was lying about the missing laptop, which would "abundantly merit sanctions," or even if there really was a missing laptop, sanctions would still be appropriate because Klein

The magistrate found that Klein had spoliated evidence in bad faith, and that the only appropriate sanction was default judgment in the plaintiffs' favor. The magistrate found that an adverse inference instruction was insufficient as a sanction because it would not restore the parties to their original positions.[12] The district court adopted the magistrate's Recommendation in full.[13]

In re Fannie Mae Securities Litigation

Fannie Mae involved a discovery dispute between the Office of Federal Housing Enterprise Oversight ("OFHEO") and several senior executives at Fannie Mae. These executives were among a group of individual defendants in private civil litigation that arose out of an investigation by OFHEO, which regulates Fannie Mae and Freddie Mac. OFHEO was not a party to the litigation, but the individual defendants subpoenaed over thirty categories of documents from OFHEO. OFHEO moved to quash the subpoenas, but the district court denied the motion, giving the agency four months to comply.

About three months later, OFHEO asked for and later received a one-month extension of the deadline. OFHEO subsequently reported to the court that it had completed the production. It later came to light, however, that OFHEO had failed to search all of its off-site disaster-recovery backup tapes, and the defendants moved to hold OFHEO in contempt. The motion was held in abeyance following a stipulation by the parties requiring OFHEO to conduct searches of its backup tapes and provide all responsive documents and privilege logs by January 4, 2008.

As that deadline approached, OFHEO informed the district court that it could produce all non-privileged documents by the January 4, 2008 deadline, but that it would be unable to produce the required privilege logs until February 29, 2008. The district court held OFHEO in contempt. The court recognized that OFHEO had undertaken "extensive efforts to comply with the stipulated order" by hiring 50 contract attorneys and spending over $6 million, more than nine percent of its entire annual budget. The court found, however, that these efforts were "'too little too late.'" It stated that OFHEO had treated its deadlines as "'movable goal posts,'" repeatedly miscalculating "'the efforts required for compliance.'"[14] As a sanction, the court ordered production of all documents that had been withheld on the sole basis of the qualified deliberative process privilege[15] and that had not been logged by the January 4, 2008 deadline. The court stopped short of permitting waiver of the privilege, ordering instead that the documents be provided only to the individual defendants' counsel and that OFHEO could recover documents found to be privileged.[16]

The D.C. Circuit affirmed the decision of the district court. The circuit court acknowledged OFHEO's "extensive efforts" to comply with the stipulated order and noted that it might not have held OFHEO in contempt if it were deciding the matter in the first instance, but declined to find an abuse of discretion. The court explained:

> Given the district court's intimate familiarity with the details of the discovery dispute, the scale of the production requested, and the progress of the multidistrict litigation as a whole, we are ill-positioned to second-guess that assessment. Were we on this record to overturn the district court's fact-bound conclusion that OFHEO dragged its feet until the eleventh hour, we would risk undermining the authority of district courts to enforce the deadlines they impose.[17]

Implications

Although *Kvitka* and *Gutman* may not break new ground by reinforcing the obvious lesson that destroying evidence and lying about it are sanctionable, they demonstrate that courts will not hesitate to enter

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had failed to disclose that the laptop requested was missing, and thus was not the laptop he produced for imaging. *Id.* at *36.

12 *Id.* at *42-43.

13 *Gutman II*, 2008 U.S. Dist. LEXIS 97707, at *4.

14 *In re Fannie Mae Secs. Litig.,* 552 F.3d at 817-18 (quoting the district court).

15 The deliberative process privilege covers "documents reflecting advisory opinions, recommendations and deliberations comprising part of a process by which governmental decisions and policies are formulated." *Dep't of the Interior v. Klamath Water Users Protective Ass'n*, 532 U.S. 1, 8 (2001) (internal quotation marks and citation omitted).

16 *In re Fannie Mae Secs. Litig.*, 552 F.3d at 818, 823-24.

17 *Id.* at 822-23.

terminating sanctions for ESI abuses. They also suggest that some litigants still have not gotten the message about ESI preservation. While it might be quite evident that parties should not destroy data and then misrepresent their behavior to the court, these cases do underscore the need for counsel to advise clients from the outset of litigation of the duty to preserve evidence. It is also worth noting that these cases involved sanctions against individuals, whereas most reported sanctions decisions up to this point have involved large corporate parties.

Fannie Mae demonstrates the importance of conducting a proper investigation of all potentially producible ESI even in a third-party context so that reasonable deadlines are set and met for its production. In retrospect, OFHEO appears to have agreed to deadlines that it had little chance of meeting. Though OFHEO appears to have had a legitimate burden argument arising from the stipulated order, burden was not enough in light of OFHEO's repeated failure to meet deadlines to which it had agreed. Even though the circuit court found that the sanction did not effectively waive the deliberative process privilege, the prospect of allowing opposing counsel to review otherwise privileged internal communications should give any litigant pause.

In order to make sure that any deadlines proposed are realistic, litigants responding to discovery should conduct a thorough investigation of their potentially producible ESI ***well before*** responding in any way to the opposing party or to the court—so that well-informed decisions can be made regarding a reasonable timeline for production. While this may be common sense for litigants, after *Fannie Mae,* it needs to be part of the ESI calculus for third parties.

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