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Bad Behavior in eDiscovery is Still Very Costly!

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WHAT WERE THEY THINKING? AMENDED RULE 37(E) IS WORKING BUT PRESERVATION BAD BEHAVIOR IS STILL VERY COSTLY

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For those of us who practice regularly in the ediscovery realm, the December 1, 2015 amendment to Rule 37(e) was a much needed game-changer. In simple terms, amended Rule 37(e) eliminated the risk of the severest sanctions for ESI preservation failures unless a court first determined that the failing party acted "with the intent to deprive" the other party of the ESI requested during discovery. Thus, under the amended rule, the severest sanctions were deemed available only when, for example, a party deliberately set out to delete emails, wipe servers or destroy equipment so that ESI either no longer existed or could not be collected. And, indeed, such case most certainly do exist. See, e.g., Omnigen Research v. YongQuiang Wang, 321 F.R.D. 367 (D. Or. 2017) (intentional destruction of numerous computer files; default judgment granted); TLS Mgmt. & Mktg. Servs. v. Mardis Fin. Servs., 2018 U.S. Dist. LEXIS 13784 (S.D. Miss. Jan. 29, 2018) (intentional deletion of computer files, user profiles and metadata; use of computer "wiping" tool; default judgment entered).

But, with the amendment's adoption, gone were the days – and scary they were – when "gross negligence" in preserving ESI could lead to striking of pleadings or, for example, an adverse inference jury instructions mandating that the jury view the missing documents as detrimental to the party that failed to preserve properly. See Fed. R. Civ. P. 37(e) advisory committee note to 2015 amendment (describing amendment's intention to override Residential Funding Corp. v. DeGeorge Financial Corp., 306 F.3d 99 (2d Cir. 2002) which permitted severe sanctions for grossly negligent preservation failures).

That is the good news. The "bad" news is that bad preservation behavior continues. Indeed, really bad behavior (or perhaps better said, "amazingly grossly negligent" behavior) continues – and although the severest sanctions may no longer be available, parties and their lawyers need to recognize that the price can still be very high, both from an evidentiary perspective, as well from potential fees awarded arising from that bad conduct.

Before examining some recent examples of "bad behavior," we should pause for a moment to ask why is it that really bad preservation conduct, albeit conduct shy of intentional efforts to deprive, continues. It has been twelve years now since the federal rules were first amended and explicitly came to recognize "ESI" – that is emails, electronic documents, excel spreadsheets, PowerPoints, and a myriad of other electronic materials – as "documents" within the meaning of the discovery rules. In the interim, the business world is now more and more paperless or trying to be – even ATMs now have the common sense to ask us whether we want a paper receipt of a transaction. Meanwhile, the average lay person has moved into a personal electronic universe that is getting "smarter" every day. Since 2006, we have said good-bye to our flip phones and hello to our smartphones. We regularly download apps to ensure our connectedness to just about anything, on any subject, at any time. We now speak aloud to Alexa and her competing counterparts and expect instant answers. We can ask our refrigerators what groceries we need to buy and we can check our phone screens to see who is walking up the stairs to our front doors, even when we are miles away. In short, we have entered into a brave new world of constant communications – some of us enthusiastically and others kicking and screaming – but it would be impossible to deny that for a huge portion of the American population, our lives, both personal and business, have altered and will continue to do so for the foreseeable future.

Now, while we have seemingly adopted and adapted, it is safe to assume that the vast majority of us do not have a clue how or why any of our daily electronic systems or gadgets work. And, we really don't care. We just want them to work (and maintain our privacy too!). In fact, we get quite angry when they don't work and shake our fists at the wifi gods and other cyber spirits floating somewhere in "the cloud" when we can't communicate exactly when and how we want to.

All of that said, there are some basic things that people at least in the business community should have come to understand over the last 12 years. Among them are if litigation is occurring or is about to occur, a company is obligated to take reasonable steps to ensure that its relevant (or potentially relevant) ESI is preserved. That means getting out the word quickly – whether by way of a formal written litigation hold or otherwise – that employees and electronic systems managers/overseers need to take steps to stop either conscious or system-wide deletions or purges of potentially relevant ESI. By now, business owners, their IT employees, and their in-house and outside counsel really should have no doubt about this obligation and how to accomplish it. Granted, meeting this obligation can get dicey and difficult when it comes to things such as employee text messages, social media postings, telephone messages, and structured data. However, in terms of emails and basic electronic documents – the mainstays of business life – there should be no question or hesitation about what needs to be done.

And yet . . . and yet, very recent decisions demonstrate that executives, managers and yes, even lawyers, either remain willfully ignorant of how these business systems work or are determined to pass the buck, having assumed that some mysterious "someone else" in the company was handling things. Well, while courts no longer can impose the most draconian of sanctions, no one should kid him or herself – judges continue to have very potent sanctions options available and are very willing to use them when confronted with preservation misconduct borne of ignorance, indifference or good old-fashioned boneheadness. The following are a few telling examples – and were issued in just the last few weeks – and each leaves us with the question – what were they thinking??

Lokai Holdings LLC v. Twin Tiger USA LLC, 2018 WL 1512055 (S.D.N.Y. Mar. 12, 2018).

This case involves claims of trade-dress infringement, unfair competition and false advertising relating to the design of a bracelet. Plaintiff's counsel sent a cease and desist letter to defendants (two individuals, along with their company) in May 2015 and then filed suit in November 2015. Once sued, defendants retained litigation counsel who provided the broad-brush advice that defendants should search for emails relating to plaintiff and not delete anything having to do with the case. What counsel apparently did not understand, however, was that defendants conducted business through a web-based email service provider that only provided up to 10,000 megabytes of storage space to the company. In order to avoid bumping up against that limitation, defendants during the pendency of the case simply continued to delete emails in order to free up storage space for new emails. About a year into the litigation once discovery was in full throttle, plaintiff's counsel began claiming spoliation. At that point – for the first time – defendants contacted the service provider to discuss setting up an archiving system. Over the course of the next few months, through a series of continual misunderstandings (or ineptitude), the archiving system was delayed and delayed, and was not actually instituted until almost a year later. Moreover, defense counsel had no direct involvement with efforts to set up the archiving system for many months. The bottom line is that emails and other business documents that should have been preserved were not.

Plaintiffs filed various spoliations motions and sought the most severe sanctions. Magistrate Judge Debra Freeman ultimately found that there was not clear and convincing evidence (the standard that she found applicable) that defendants had deliberately deleted emails and other ESI in order to deprive plaintiffs of documents relevant to the litigation. She did, however, find that there had been spoliation and prejudice to plaintiffs and imposed sanctions in the form of: a) plaintiff's attorneys' fees for work arising from the spoliation and its sanctions motions; b) precluding defendants at trial from offering testimony about the contents of any unpreserved emails or suggesting that they would have supported defendants' case; and c) allowing plaintiffs to seek pre-trial a favorable jury instruction concerning extrapolations from the limited evidence available.

Most notably, Judge Freeman, was relatively forgiving of defendants themselves, while taking litigation counsel to task for their failures in overseeing the discovery process. Specifically and quite generously, she stated – without citation – that defendants "run very small companies with very few employees and should not be held to the same standard as a large corporation with greater resources." Id. at *11. As to counsel, however, she chastised that they "fell far short of meeting their responsibilities," which included overseeing compliance with litigation holds, monitoring defendants efforts to retain and produce relevant documents and becoming familiar with their client's data systems. Id. (citing Zubulake v. UBS Warburg LLC ("Zubulake V"), 229 F.R.D. 422, 431-32 (S.D.N.Y 2004). She pointed in particular at defense counsel's failure to provide any explanation as to why they failed to supervise their clients' document preservation efforts more closely and found that their "periodic and perfunctory reminders to [defendants] of their obligations to preserve relevant documents were inadequate to ensure that Defendants' preservation obligations were met." Id. at *10 and 11.

Ouch! For anyone who thought that the Zubulake line of cases had lost some of their punch over the last decade or so due to changing norms in the body of ediscovery case law and thinking . . . well, think again. According to Magistrate Judge Freeman, a lawyer's obligations under Zubulake remain very much intact and failure to adhere to those standards can lead to serious and very expensive repercussions.

EPAC Technologies, Inc. v. HarperCollins Christian Publishing, Inc., 2018 WL 1542040 (M.D. Tenn. Mar. 29, 2018)

This matter concerns a contract dispute between plaintiff EPAC, a book printing company, and defendant, a publisher of religious-themed books. Suit was first filed in 2012, but as the magistrate judge explained, the last three years have focused on heated discovery disputes that have turned the case "into a quagmire of adversarialism" and one that has "passed through the dockets of six district judges and two magistrate judges." Id. at *1. This most recent decision includes an in-depth review of recommendations from the ediscovery Special Master who had been brought on in an effort to address the on-going discovery disputes. And, by the way, that Special Master was well-known ediscovery expert and commentator Craig Ball.

The spoliation in this matter was quite significant. Over 750,000 emails and attachments from the key time period were not preserved; none of the tens of thousands of allegedly flawed hard-copy books were maintained; the regular purge of the warehouse supply chain management system was not overridden; and "sacred" monthly sales data saved on tapes essentially became inaccessible after defendant was purchased by HarperCollins and the data was migrated to different systems.

The loss of information, here, occurred despite what appear at the onset to be acceptable initial steps to preserve. Within a few days of receiving plaintiff's initial preservation demand as part of a letter suggesting that future litigation may be in the offing, defendant's in-house counsel sent an informal litigation hold email to the company's top management. Interestingly, Special Master Ball wrote in his report that the issuance of a litigation hold within six days after being put on notice of possible litigation was valid because "there must nonetheless be a reasonable time to get the notice, read it, access its impact and initiate a hold." Id. at *16. The Magistrate Judge, however, stated that he "finds this grace period [to be] generous." Id. Certainly, while the general rule is that a party is obligated to take "immediate" steps to preserve potentially relevant material once put on notice of possible litigation, anyone who has ever sought to implement a litigation hold involving an on-going business operation understands that short of curtailing, on a company-wide basis, all destruction/deletion of any documents and ESI, it indeed does take time to develop an appropriately targeted and reasonably tailored litigation hold protocol, identify a universe of potential custodians, draft a notice that is sufficiently understandable to non-lawyers such that their compliance is easily achievable; and distribute that notice to the proper custodians. Apparently, however, Magistrate Judge Newbern feels differently.

In any case, what ensued over the following several years in terms of ESI preservation, at times reads like farce – except it isn't funny. In-house counsel sent out a January 2012 document hold notice to various employees but the Special Master characterized it as "boiler-plate" and deployed with no guidance or follow-up – and that "it was ignored by all recipients." Id. at *7. So much for relying on employee compliance! Meanwhile, no one thought to contact the manager of the warehouse records management system to inform him about a litigation hold until three (yes, three) years after the obligation to preserve had been triggered and, thus, routine purging of data continued unabated. Id. When the January 2012 litigation notice was first sent out, in-house counsel did not consult beforehand with the company's IT staff, provide any guidance or direction about implementing the hold, and did not ensure that proper steps were taken to preserve. Id. As it so happened, when the IT department first received the hold notice, a network administrator checked the system and determined that litigation holds were already in place. Id. at *8. However, sixteen months later, when he went to retrieve emails for discovery purposes, he saw for the first time that the automatic purge had not been reset to a 10 year interval as he had presumed, but instead had remained on a one-year cycle, meaning that millions of emails had been purged that should have been retained. Id.

The Special Master and the Magistrate Judge came to the same conclusion – that while the preservation efforts were woefully inadequate, there was no indication that the failures arose from an intentional desire to deprive plaintiff of relevant information. But, both the Special Master and the Judge had some choice words about defendant and in particular in-house counsel, including that the problems arose due to "arrogance by management, lack of initiative by IT and a pitiable lack of legal leadership, the last at the very heart of the failure." Id. at *9 (quoting Special Master). Likewise, the company "fail[ed] to meet minimum standards of diligence and competence"; was "casual and careless" and "homebrew, sluggish and sloppy," and showed "paralysis or even purposeful sluggishness" with its "commitment to defensible collection and search [being] at best perfunctory." Id. at *18 (quoting Special Master). Moreover, the Magistrate noted that defendant's "perfunctory" efforts stood in sharp contrast to how the company proceeded during a concurrent DOJ investigation (evidently on unrelated issues) for which the company hired ediscovery counsel and an ediscovery vendor and which resulted in "meticulous" preservation efforts. Id. at *22. Defendant argued that the amounts in

controversy in the two separate matters meant that the preservation standards expected should be "drastically different." Id. at *n.14. That is certainly an interesting variation on a proportionality argument – i.e., when it is the government calling and perhaps the company is looking at a substantial financial loss, the cost of hiring ediscovery expertise is justified, but when it is a commercial contract dispute, "casual, careless, sluggish and sloppy" are sufficient. Well, Judge Newbern did not bite at this argument.

As to sanctions, Plaintiff argued that defendant's conduct was so sub-par that it should be viewed as "willful blindness" and treated as equivalent to "intent to deprive" within the meaning of Rule 37(e). Id. at *18. The Magistrate, however, refused to go that far, noting that amended Rule 37(e) specifically and explicitly drew a stark line between gross negligence and intent. Id. The Magistrate, nonetheless, did impose substantial sanctions, although not as harsh as those recommended by the Special Master or sought by plaintiff. Specifically, the Judge stated that the jury would be instructed about the data loss and that the lost data affirmatively would have provided information relevant to the claims and defenses; defendant would be precluded from offering certain evidence in support of its defense; plaintiff would be able to re-depose, at defendant's cost, defendant's key witnesses about belatedly produced "substitute" data; and defendant would be responsible for 75% of the Special Master's fees and costs and 50% of plaintiff's attorneys' fees incurred during the Special Master proceedings. While a final amount has not yet been decided, post-order filings by the parties indicate that the financial penalties will reach into the seven figures. Certainly, defendant's "sloppiness" is going to prove to be very expensive.

Bankdirect Capital Finance, LLC v. Capital Premium Financing, Inc., 2018 WL 1616725 (N.D. Ill. Apr. 4, 2018)

This case involves breach of contract claims relating to a marketing collaboration agreement between the parties. Suit was filed in November 2015, and plaintiff understood at that time that all documents "good or bad" needed to be preserved. Id. at *2.

The period 2010 through late 2011 was a key time period for discovery purposes but no documents were produced for those dates. Plaintiff's explanations for the dearth of historic emails evolved overtime. First, plaintiff took the position that it was unlikely that any emails were retained longer than a year and were discarded in the normal course of business. Id. at *5. Then plaintiff explained that the company had changed emails servers in 2011-2012 and no emails prior to that time were retained. Id. at *3. That explanation was plausible given that the change in email servers occurred years before litigation was being explored and during that time there would have been no preservation reason to archive historic emails. Except that this explanation proved to be utterly false – a fact that was learned when defendant deposed a plaintiff's representative about the email servers and document preservation.

During the deposition, defendant learned that, actually, at the time the new servers were implemented, all emails dating back five years were retained and then were automatically purged on a going forward basis as the emails aged past the five year mark. One can only wonder if plaintiff's counsel knew this before putting up the deponent or whether they too were surprised to learn this fact while sitting at the deposition. In any case, this testimony established that as of November 2015, when suit was filed, emails dating back to November 2010 did exist on the company's new servers and could have been preserved – but they weren't. Id. at *4.

At a subsequent deposition, plaintiff's president and CEO acknowledged that he was personally responsible for putting in place a litigation hold, but he did not learn until a year after litigation was filed that the email system had a five-year purge policy. Id. at *4. Meanwhile, he further testified that the loss of the historic emails did not matter because during the 2010-2011 period, there would have been no "bad" emails given that the parties were operating quite well with each other. Id. at *5. He further testified that he did not believe that "good" emails would be relevant to the litigation or the opposing party's defenses. Id.

The Magistrate Judge described the CEO's testimony as "simply not credible" and stated that no reasonably successful businessman would take the position that the historic emails were not potentially relevant, in particular given that emails "are an integral part of the day-to-day operations of any modern business, to say nothing of the absolutely critical role that they often play in modern litigation. Id. at *5 and *6. He further found that accepting plaintiff's ultimate explanation of "oops" and that the loss of the emails occurred because of an inadvertent mistake (i.e., failing to instruct the IT personnel to suspend the five year purge protocol) would require the court to abandon common sense – something the court was not willing to do. Id. at *6. The court found that the company's lapse, which it finally admitted after changing explanations several times, was intentional – i.e., that the company intentionally chose not to take reasonable (and quite easy) steps to preserve [the historic emails]." Id. at *9 (italics in original).

Having so found, the Magistrate, however, declined to make the ultimate decision under Rule 37(e) – whether plaintiff acted with the intent to deprive defendant of deleted information. Instead, he took the position that the

question should best be left for the jury to decide and so recommended that the trial court follow that course, or in the alternative, the trial court could issue a permissive spoliation instruction explaining that the jury could, but was not required to, consider the loss of the emails in considering the parties claims and defenses. Id. at *12. Thus, despite finding plaintiff's story not credible and taking the position that it acted intentionally in failing to issue an instruction to suspend the five-year email purge protocol, the Magistrate elected not to make a final determination as to intent. That decision, of course, leaves the whole issue of intent hanging over the heads of the parties as the case proceeds forward, assuming the trial court accepts the Magistrate's recommendation.

A final note of interest – and one that is a bit curious. The Magistrate pointed out in his opinion that it was a "reasonable assumption" that in working with plaintiff before suit was filed, and consistent with counsel's Rule 11 obligations, the attorneys would have been actively involved in reviewing what evidence existed to support the "complicated, 149-paragraph, 38-page Complaint" that was filed in this action. Id. at *2. The Magistrate further posited that "plaintiff's highly experienced, talented lawyers" likely would have instructed plaintiff to put a litigation hold on documents even before the filing of the complaint. Id. Indeed, in reviewing the Magistrate's decision, one cannot help thinking "did plaintiff's counsel know what had happened with the email preservation (or lack thereof) and, if so, when did they know it and what did they do about it?" Yet, instead of pursuing those Zubulake-type questions, the Magistrate went out of his way to state that plaintiff's counsel is a firm "made up of experienced and accomplished counsel, with an important, nationwide clientele." Id. He then later added after describing plaintiff's ever changing story as suspicious and not credible, that "we should not be understood as impugning in the slighted the integrity and good faith of the lawyers in this case and nothing that we have said should be taken as some sort of negative observation about them. Id. at *7.

Thus, unlike the magistrate judges in the prior two cases discussed above, who both pointed at counsels' significant preservation failures, in this case, a Magistrate seemed determined to exonerate outside counsel based, evidently, on their reputations, years of experience and their "important nationwide clientele." The Magistrate did not explain in what way the "importance" of a firm's nationwide clientele militates against questioning counsel's oversight of a client's document preservation activities. Likewise, it would seem that a court would demand more from highly experienced and talented counsel given that one can assume these exceptional lawyers would have had more than a passing familiarity with contemporary expectations about ESI document preservation and the important role that lawyers play in ensuring compliance. Nonetheless, in this particular matter, the Magistrate was content to place the blame at the client's feet alone. Other judges have not been so forgiving and attorneys should remain both vigilant and wary.