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FEDERAL E-DISCOVERY

Expert Analysis

Spoliation Leads to Severe Sanctions in Recent Cases

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The significant growth in the volume and complexity of e-discovery has brought about an inevitable increase in scrutiny over the obligation to preserve and produce relevant electronically stored information (ESI). Given the sheer number of cases that now involve large amounts of ESI, the escalating trend of asserting and defending claims of spoliation should come as no surprise.

The attendant threat of sanctions—ranging from awards of attorney's fees and costs to default judgment—provides yet another compelling reason for counsel and clients alike to work toward good-faith compliance with e-discovery obligations.

It is now clearer than ever that parties who shirk their obligations to preserve and produce ESI do so at great peril. A recent opinion from the Southern District of New York sounds a clear warning that courts, in their wide discretion to impose spoliation sanctions,[1] may regard the destruction of relevant evidence to be serious enough to warrant sanctions that effectively may be dispositive of a claim or defense.

In *Arista Records LLC v. Usenet. com Inc.*, 2009 WL 1873589 (S.D.N.Y. June 30, 2009), Judge Harold Baer held that the appropriate sanction, in light of a record replete with "strong evidence of extreme wrongdoing" by defendants throughout the course of discovery, was to preclude the wrongdoers from asserting their affirmative defense during the remainder of the case. Because that defense constituted the very grounds on which defendants premised their motion for summary judgment, Judge Baer dismissed defendants' motion as moot and went on to grant summary judgment for plaintiffs on all claims.

The Arista plaintiffs, a group of record companies who owned various sound recording copyrights, alleged that defendants Usenet. com Inc., its affiliate and its director, operated an online information sharing network that promoted and permitted the illegal exchange of vast amounts of digital music files owned by the plaintiffs.

To establish their claims of copyright infringement, the plaintiffs sought several categories of ESI, including (i) "Usage Data," or records from Usenet's computer servers reflecting requests from its subscribers to download and upload digital music files using Usenet's service; (ii) "Digital Music Files," or the actual copies of the copyrighted sound recordings at issue; (iii) promotional materials from Usenet's Web site advertising the free exchange of digital music files; and (iv) internal e-mail communications, documents and reports.

> 'Arista' and 'KCH' confirm that courts are fully prepared to impose serious sanctions, even those that are potentially case-determinative, when electronic discovery misconduct is sufficiently egregious.

In two separate motions for spoliation sanctions, the Arista plaintiffs contended that Usenet deliberately destroyed or withheld most of these materials even though they were subject to discovery requests and relevant to substantiating their claims.

On Jan. 26, 2009, Magistrate Judge Theodore H. Katz decided the first of the motions, in which the Arista plaintiffs alleged, among other things, that Usenet acted deliberately to spoliate large portions of the Usage Data and Digital Music Files.[2]

In support of this motion, the plaintiffs presented evidence that, on the same day that defense counsel agreed to produce the requested data, Usenet disabled user access to its services without preserving the Usage Data, and also reconfigured its server to delete and overwrite the existing Digital Music Files, thereby rendering this data irretrievable.

Magistrate Judge Katz rejected Usenet's arguments that it had neither the duty nor the ability to preserve the data at issue, finding clear evidence that Usenet had actual notice of Arista's request for the data and that Usenet subsequently produced "great volumes" of the same data it claimed could not reasonably be preserved.

Upon a further finding that Usenet destroyed evidence that was "highly relevant" and did so in bad faith, Magistrate Judge Katz determined that such conduct justified the imposition of sanctions.

He rejected most of Arista's requested sanctions, which would have established a series of dispositive factual and legal admissions, on the grounds that such a result would have "go[ne] far beyond simply restoring plaintiffs to the same position they would have been in had there been no spoliation of evidence."

Instead, taking into consideration the nature of the spoliated evidence and its relevance to the claims of the plaintiffs, in

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conjunction with "the prophylactic, punitive and remedial rationales underlying the spoliation doctrine,"[3] Magistrate Judge Katz granted an adverse inference that copies of the plaintiffs' copyrighted sound recordings had been transmitted from Usenet's computer servers to the personal computers of its subscribers.

He further recommended that Usenet be precluded from challenging the statistical evidence of the Arista plaintiffs that infringement had been committed via Usenet's services.

Additional Violations

Despite this clear lesson from the court of the serious consequences of failure to preserve evidence, Usenet failed to change course, committing a series of further discovery violations that became the subject of the plaintiffs' second motion for spoliation sanctions.

At the close of discovery, Arista alleged that Usenet "wiped clean" seven of its former employees' hard drives without backing up or preserving the data in any manner and engaged in other forms of litigation misconduct, such as providing false and misleading responses to discovery requests and interrogatories, causing their employees to evade depositions by sending them on expense-paid vacations, and violating two court orders compelling defendants to remedy their deficient production.

Arista argued that the extent of Usenet's misconduct warranted striking defendants' answer and entering a default judgment.

Judge Baer acknowledged that plaintiffs produced credible evidence of "a pattern of destruction of critical evidence, a failure to preserve other relevant documents and communications, and at best dilatory (and at worst, bad-faith) tactics with respect to defendants' conduct during discovery."

Although he refrained from imposing "the ultimate sanction," noting that such case-dispositive sanctions should be imposed only in "extreme circumstances, usually after consideration of alternative, less drastic sanctions,"[4] Judge Baer ultimately issued a sanction that, in all likelihood, was less drastic in form only.

He held that the appropriate sanction was to preclude Usenet from asserting an affirmative defense under the safe harbor provision of the Digital Millennium Copyright Act (DMCA),[5] an argument on which they substantially relied in defending against the claims of Arista.

Pursuant to the act's safe harbor provision, Usenet could have avoided liability if it had been able to demonstrate that it implemented a good-faith and reasonable noninfringement policy for its users. Judge Baer noted that the provision required Usenet to establish that it was unaware of any "red flags" indicating infringement on the part of their subscribers, an issue as to which the spoliated evidence would have been directly relevant.

He further explained that the sanction properly took into account the fact that the spoliated evidence prevented Arista from ascertaining the extent to which they had been prejudiced with respect to their own claims or their arguments in opposition to Usenet's affirmative defense.

Although Usenet managed to avoid the harsher sanction of default judgment, the sanctions imposed against them essentially resulted in an adverse judgment.

Usenet's decision to avoid production of what was likely incriminating evidence thus came at a heavy cost, effectively depriving it of its principal defense to Arista's infringement claims or preventing it from rebutting the adverse inference that Magistrate Judge Katz had imposed previously. This sanction thus virtually ensured that Arista would prevail on its motion for summary judgment.

Adverse Inference Instruction

A slightly less draconian sanction was imposed in a recent spoliation case from the Western District of Kentucky, *KCH Services Inc. v. Vanaire Inc.*, 2009 WL 2216601 (July 22, 2009).

In that case, Judge Jennifer B. Coffman sought to impose a sanction for discovery misconduct that would both penalize the defendant for its discovery misconduct and ameliorate the prejudice to the plaintiff from the loss of relevant evidence.

Approximately one month before commencing litigation, the president of plaintiff KCH Services Inc. telephoned his counterpart at defendant Vanaire Inc., and accused Vanaire of improperly using KCH's software.

Immediately after the call, at the direction of its president, Vanaire began deleting any software that the company did not purchase or own. Even after KCH filed its complaint and issued an evidencepreservation letter, Vanaire failed to institute a meaningful litigation hold and continued to delete and overwrite its e-mails and other ESI that were plainly relevant to KCH's claims.

Upon learning of Vanaire's spoliation, KCH sought entry of default judgment, sanctions, or an adverse-inference instruction to the jury at trial.

Judge Coffman held that Vanaire's conduct fell outside the scope of "routine, good faith operation of an electronic information system"— which Rule 37(e) provides will generally not warrant imposition of sanctions—and that Vanaire's intentional conduct deprived KCH of "the very subject of the litigation."

Judge Coffman further acknowledged that Vanaire's spoliation of the ESI was prejudicial to plaintiff and could not be "fully cured." Although she believed that default judgment was not warranted, the judge concluded it would "fairly compensate" plaintiff to grant an adverse-inference instruction to the jury concerning the spoliated evidence.

The practical import of the adverse-inference instructionin *KCH* remains to be seen, but such instructions often deal a serious blow to the prospects of the litigants against whom they are issued.

Conclusion

These recent decisions make clear that "in this day of burgeoning, costly and protracted litigation courts [may] not shrink from imposing harsh sanctions where… they are clearly warranted."[6]

Arista and *KCH* confirm that courts are fully prepared to impose serious sanctions, even those that are potentially case-determinative, when discovery misconduct is sufficiently egregious. The practical reminder here is of the vigilance and good faith that is expected from parties and their counsel in the preservation and production of ESI, and the serious consequences for those who fall shy of the standard.

These cases also highlight, once again, that a proactive and collaborative approach to discovery of ESI—rather than a strategy of obfuscation and stonewalling—is doubtless the best safeguard against finding one's self on the wrong side of a sanctions motion.

1. The authority to impose spoliation sanctions rests with the federal district courts pursuant to their inherent power to manage their own affairs and under Rule 37 of the Federal Rules of Civil Procedure. See, e.g., *Gutman v. Klein*, 2009 WL 4682208, at *11 (E.D.N.Y. Oct. 15, 2008).

2. *Arista Records LLC v. Usenet.com Inc.*, 608 F. Supp. 2d 409, 416-419 (S.D.N.Y. Jan. 26, 2009).

3. *West v. Goodyear Tire & Rubber Co.*, 167 F.3d 776, 779 (2d Cir. 1999).

4. Id.

5. 17 U.S.C. §512(c)(1)(A)(ii).

6. *Cine Forty-Second Street Theatre Corp. v. Allied Artists Pictures Corp.*, 602 F.2d 1062, 1068 (2d Cir. 1979).