

Cases Underscore Need For E-Discovery Expertise

Law360, New York (January 22, 2010) -- Years ago, at one of the first meetings of the Sedona Conference Working Group on Electronic Document Retention and Production,[1] a judicial roundtable participant noted that in the mid-2000s judges were likely to be forgiving when it came to electronic discovery in light of the relative novelty of emerging technologies, standards and rules. At the same time, more than one of the panelists that day noted that a time would come when judicial patience would wear thin.

A trio of decisions issued near the end of 2009 indicates that judicial patience is indeed wearing thin. A brief review of these cases shows that the premium on getting discovery (especially e-discovery) right is rising quickly.

These signs provide a clear warning to corporate parties large and small — you need to know what you are doing with respect to the preservation and production of electronic discovery or else face significant consequences for discovery failures.

Gambling in Discovery Is a Bad Idea

In *Maggette v. BL Devel. Corp.*,[2] the United States District Court for the Northern District of Mississippi was faced with a motion for sanctions for the alleged failure of the defendants (who operate gaming facilities across the country) to properly preserve, disclose, and produce relevant documents.

In analyzing the motion, the court noted significant concerns regarding the defendants' efforts to comply with the discovery requests for electronically stored information (ESI):

- Despite the court's direct order that "all defendants ... search any available databases for responsive information and produce it to the plaintiffs ...," the defendants are unable to describe the databases searched, the search terms, methods, or parameters used to search the databases or provide any expert information confirming that there are no documents, electronically stored information, or other information responsive to plaintiffs' discovery requests."
- The defendants were unable to provide "any concrete reason or rationale for the numerous discrepancies within their discovery responses and the deposition testimony of their own employees."
- The defendants were unable to articulate "a satisfactory response to the court's doubts expressed at the hearing that corporations as large and sophisticated as the defendants, which operate numerous gaming facilities across the country with various operations centers, do not have either paper files, electronic files, or information or — even in light of Hurricane Katrina — backup measures and files for at least some of the information requested by plaintiffs."

After examining applicable and instructive case law, including Judge Scheindlin's series of Zubulake decisions, the court noted that, although it did not appear that defendants had complied with their duties, the court could not conclusively reach a decision without further review by a third party.

Accordingly, the court ordered that the parties agree upon the identification of a neutral who would be expert at e-discovery as well as the gaming industry "to determine whether the defendants have met the standards for preservation of electronic evidence and disclosed all relevant evidence."

Further, in light of the defendants' failure "to satisfy the court's inquiries calculated to determine the legitimacy of their searches to date or whether they have in good faith attempted to use preservation techniques reasonably available to them," the court ordered that the entire cost of the expert would be the responsibility of the defendants.

Discovery Problems Trump the Merits

In *TR Investors LLC v. Genger*,^[3] the Delaware Chancery Court was faced with a motion for sanctions up to and including default judgment. The underlying case involved a dispute between a former executive (Arie Genger) with a company known as TRI and one of its largest investors, the Trump Group.

As the dispute emerged into a court battle, the parties entered into a temporary standstill agreement to see if a settlement could be reached. Part of that agreement included a standard provision requiring the preservation of evidence.

During the weekend of Sept. 5-7, 2008, lawyers, technical consultants, Genger, and TRI took steps to identify and copy documents and ESI that were subject to preservation. Of great concern to Genger was the segregation (and encryption) of non-relevant materials related to his outside activities concerning Israel as well as his personal divorce proceedings. TRI and its attorneys and consultants did not create forensic or mirror images of the servers or laptop hard drives. Instead, outside counsel for Genger opened and reviewed files to determine which items should be copied for preservation.

The court noted that this process: (a) failed to preserve the unallocated disk space that could have contained copies of temporary documents opened and saved during the normal course of operations and (b) failed to preserve the temporary files in the unallocated disk space created by the attorneys during their weekend review.

This became critical in the court's analysis because Genger, upon learning from his personal technology consultant that the review process created temporary files that were not encrypted, agreed that wiping software should be run to erase the unencrypted files. Of course, the software also eliminated every other file that would have been present in the unallocated space. Genger and his personal consultant did not consult with the attorneys or other consultants engaged by the lawyers before undertaking the actions, nor did they inform them immediately afterward.

After reviewing Genger's defense to the motion, the court concluded that the destruction of evidence was knowing and culpable. In particular, the court rejected the contention that the deletions were only intended to delete non-relevant information and, in light of the secrecy and competence of the personal technology consultant, the court concluded that the deletions were purposely done to restrict the amount of information available to the litigation adversary, the Trump Group.

The court found that the record showed that e-mails and other documents located in other sources were missing from the active TRI files, which in the courts view likely would have existed on the unallocated space that was wiped clean.

The court thereafter found Genger to be in contempt of court for violating the standstill order and to have intentionally despoiled evidence.

In fashioning a remedy, the court noted that: (a) part of Genger's motivation — segregating and protecting clearly non-relevant information — was legitimate, (b) Genger had preserved all active files that contained a significant amount of relevant information, and (c) the Trump Group had failed to take appropriate steps to protect Genger's personal information as it had agreed and been ordered to do. In light of these factors, the court declined to enter a default judgment.

Nonetheless, the remedies ordered were severe. First, Genger was ordered to produce specific privileged documents. Second, the court "elevate[d] by one level the burden of persuasion upon Genger to prevail on any affirmative defense or counterclaim that he has raised" in the lawsuit. An example of the impact of this remedy is the fact that if Genger would have had to prevail only by a preponderance of the evidence, he would now have to prevail at trial by producing clear and convincing evidence.

Additionally, the court noted that Genger would be unable to prevail on any material factual issue if the only evidence in support of his position is his own testimony.

Further, the court awarded the Trump Group their reasonable attorneys' fees and expenses related to the motions for contempt and spoliation — which the court estimated to be \$750,000.

Yes, You Can Lose It All in Discovery

In *Magana v. Hyundai Motor Am.*,^[4] the Supreme Court of Washington reviewed the legitimacy of a district court's imposition of a default judgment of \$8,000,000 against Hyundai because of numerous discovery failures.

Notably, the district court found that: (1) there was no agreement between the parties to limit discovery, (2) Hyundai falsely responded to Magana's request for production and interrogatories, (3) Magana was substantially prejudiced in preparing for trial, and (4) evidence was spoiled and forever lost. The trial court considered lesser sanctions but found that the only suitable remedy under the circumstances was a default judgment.

Hyundai then appealed, which led to an intermediate appellate court ruling overturning the district court's imposition of the default judgment. The Washington Supreme Court granted further review.

The Washington Supreme Court reversed the intermediate court and reinstated the default judgment. The court specifically found that the district court did not abuse its discretion in finding that Hyundai had willfully violated the discovery rules. Notably, in its discussion, the court stated:

"A corporation must search all of its departments, not just its legal department, when a party requests information about other claims during discovery. Here Hyundai searched only its legal department. Hyundai's counsel told the trial court that in response to request for production 20, Hyundai's search 'was limited to the records of the Hyundai legal department' and that 'no effort was made to search beyond the legal department, as this would have taken an extensive computer search.' As the trial court correctly found, '[t]here is no legal basis for limiting a search for documents in response to a discovery request to those documents available in the corporate legal department. This would be the equivalent of limiting the responses in *Smith* to a search for chemical tests which were on record in the corporate legal office, without disclosing that the search was so limited.' The trial court went on to say, 'the legal department at Hyundai worked closely with the Consumer Affairs Department with respect to customer complaints and claims, including product liability claims. The vehicle owners' manual directed customers to call the Consumer Affairs number.' Hyundai had the obligation to diligently respond to Magana's discovery requests about other similar incidents. It failed to do so by using its legal department as a shield. The trial court

also found 'Hyundai had the obligation not only to diligently and in good faith respond to discovery efforts, but to maintain a document retrieval system that would enable the corporation to respond to plaintiff's requests. Hyundai is a sophisticated multinational corporation, experienced in litigation.' Id. Hyundai willfully and deliberately failed to comply with Magana's discovery requests since Magana's initial requests in 2000 and continued to do so."

The Washington Supreme Court thereafter found that the district court did not err in concluding that the discovery failures prejudiced Magana's ability to prepare for trial and that no lesser sanction would suffice.

Accordingly, the court ordered the reinstatement of the default judgment against Hyundai, as well as the award of attorneys' fees at the district court and appellate court levels.

What It All Means

These cases are a wake-up call to corporations across the country that have either scoffed at or ignored the need to take action to be adequately prepared for discovery in the modern era (including e-discovery).

These cases also provide substantial support for those who have built or are seeking to build internal momentum for creating and running a repeatable, defensible discovery program (including both in-house and outside resources) that reduces risks as well as costs.[5]

The Maggette decision highlights the critical need to have counsel that can articulately and credibly address the inquiries of the court to avoid the intimation of impropriety that can lead to significant expenses incurred by the appointment of third parties to investigate alleged wrongdoing. It also focuses attention on the need to have a good, repeatable process to execute and document the preservation, collection, and production efforts.

The Genger case makes clear the problems that can arise when parties and counsel are not fully coordinated in all aspects of discovery compliance and management. If counsel fully understood the client's concerns about confidentiality, perhaps a different litigation and review strategy could have been implemented to avoid the spoliation accusations and ultimate sanctions imposed.

Also, if counsel and its consultants would have taken different steps to secure the evidence, then there would have been less of an opportunity for their client to have — innocently or not — tampered with the evidence in a way that could and did lead to severe consequences.

The Magana case highlights the consequences of failing to: (a) undertake appropriate searches for information, (b) make adequate disclosures regarding discovery conduct, and (c) take appropriate steps to secure judicial involvement as necessary to impose limits on discovery (as opposed to undisclosed, self-help remedies).

Beneath the level of the obvious point of not making misrepresentations in discovery, the discussion by the Washington Supreme Court highlights the expectations by the judiciary that counsel understands the proper scope of discovery and has the competence to ensure that clients follow appropriate procedures to preserve and produce relevant information in a timely manner.

Importantly, it was the inadequate discovery responses of counsel, the failure of outside and in-house counsel to ensure that the search of discovery was appropriate, and the failure of the client and counsel to move for a protective order regarding scope limitations that resulted in the substantial discovery violations that the court used to justify the imposition of a default judgment remedy.

The 2009 Kroll On-Track Year in Review Report (released on Dec. 1, 2009)[6] appears to support the notion that judicial impatience with discovery problems (especially e-discovery failures) is growing. Notably, the number of reported e-discovery cases where sanctions were an issue increased by 14 percent (up to 39 percent in 2009 vs. 25 percent in 2008).

While these numbers may not have scientific precision, they certainly give credence to the proposition that the Maggette, Genger, and Magana cases are not aberrations but rather prologue for those who do not understand that a different world of discovery has emerged that requires a new level of competence, diligence, disclosure, and cooperation from outside counsel and clients alike.

The costs of “getting it right” with respect to discovery today are not insignificant. Developing defensible programs and hiring experienced discovery counsel cost money. But the costs of “getting it wrong” are far higher, and can have collateral consequences that far outlive the momentary failure in any one case. 2010 may well be that time when judicial patience with e-discovery incompetence and failures comes to a natural end.

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[1] www.thesedonaconference.org

[2] *Maggette v. BL Devel. Corp*, 2009 U.S. Dist. LEXIS 116789 (N.D. Miss. Nov. 24, 2009).

[3] *TR Investors LLC v. Genger*, 2009 WL 4696062 (Del. Ch. Dec. 9, 2009).

[4] *Magana v. Hyundai Motor Am.*, 2009 WL 4070952 (Wash. Nov. 25, 2009).

[5] See Corporate Board Member/FTI Consulting 2009 Legal Study (available at www.boardmember.com/Article_Details.aspx?id=3820)(e-discovery compliance rated as the second highest area of concern for general counsel behind only managing outside legal fees).

[6] Available at: www.krollontrack.com/news-releases/?getPressRelease=61396.