The New ESI Sanctions Framework under the Proposed Rule 37(e) Amendments

By Philip Favro

The debate over the necessity, substance, and form of the proposed eDiscovery amendments to the Federal Rules of Civil Procedure (Rules) has been ongoing now for over four years. Since the Duke Conference convened in May 2010, the Judicial Conference Advisory Committee on the Civil Rules (Committee) has been working to address many of the perceived shortcomings in the current Rules regime.[1] Their efforts have not been conducted in a vacuum. Interest groups representing parties on either side of the "v" in litigation, the U.S. Department of Justice, and even individual federal judges have lobbied the Committee in an effort to shape the final form of the proposed amendments.[2] This process, while both lengthy and necessary, may finally be reaching its closing stages. With the Standing Committee on Rules of Practice and Procedure having approved the Rules amendment package this past month, the proposed changes appear to be on track for implementation by December 1, 2015.

Viewed holistically, the proposed changes are designed to usher in a new era of proportional discovery, increased cooperation, reduced gamesmanship, and more active judicial case management.[3] For many litigants, however, the amendments of greatest significance are those affecting Rule 37(e). If enacted, the changes to Rule 37(e) would provide a uniform national standard regarding the issuance of severe sanctions to address spoliation of electronically stored information (ESI). They would also introduce a new framework for determining whether sanctions of any nature should be imposed for ESI preservation shortcomings. Simply put, the draft changes to Rule 37(e) are significant. Counsel, clients, and the courts should all be aware of the impact that these changes could have in litigation and on client information governance programs.

This article will analyze these issues. After covering the deficiencies with the current version of Rule 37(e), the article will consider the new sanctions framework under the proposed amendments. This includes an analysis of the factors that parties would be required to satisfy in order to justify the imposition of sanctions. It also describes the severe measures calculated to remediate the most harmful ESI preservation failures, along with lesser sanctions designed to cure prejudice stemming from less egregious forms of spoliation. The article concludes by focusing on some key questions about the Rule 37(e) revisions that remain unanswered and that will likely be resolved only by motion practice.

THE NEED FOR REVISIONS TO RULE 37(e)

The Committee has spent countless hours considering the over-preservation of ESI and the appropriate standard of culpability required to impose sanctions for its spoliation. Even though the current iteration

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[1] *See* JUDICIAL CONFERENCE OF THE UNITED STATES, REPORT OF ADVISORY COMMITTEE ON CIVIL RULES 306-07 (May 2, 2014) (REPORT).

[2] *See generally id*. at 95-305, 331-411 (summarizing the nature of the comments the Committee received on the published versions of the proposed Rules amendments).

[3] *See* Philip J. Favro, *A Comprehensive Look at the Newly Proposed Amendments to the Federal Rules of Civil Procedure*, 26-Oct Utah B. J. 38.

of Rule 37(e) is supposed to provide guidance on these issues, amendments were deemed necessary to address these issues given the inherent limitations with the rule.[4]

As it now stands, Rule 37(e) is designed to protect litigants from court sanctions when the good faith, programmed operation of their computer systems automatically destroys ESI.[5] Nevertheless, the rule has largely proved ineffective as a national standard. While there are many reasons that could explain its futility, three problems predominate with the present version of the rule.

First, Rule 37(e) did not expressly abrogate the negligence standard that the U.S. Court of Appeals for the Second Circuit implemented for severe sanctions involving preservation failures under *Residential Funding Corp. v. DeGeorge Financial Corp*.[6] By allowing the *Residential Funding* case to remain in effect, courts in the Second Circuit and beyond were free to impose adverse inference instructions or order other doomsday sanctions for negligent spoliation of ESI.[7] With the Second Circuit – one of the epicenters of U.S. litigation – following a sanctions touchstone that generally varies from the rest of the country, the rule has failed to become a uniform national standard for ESI sanctions.[8] Moreover, the Second Circuit's negligence standard is increasingly viewed as an anachronistic rule given the current challenges associated with ESI production.[9]

The second reason that Rule 37(e) has failed as a so-called "safe harbor" from sanctions is the emphasis the 2006 Committee note placed on requiring litigants to stop the routine destruction of ESI once a preservation duty attached.[10] While litigants may be required to suspend particular aspects of their electronic information systems once a preservation duty is triggered, this is certainly not the exclusive or the determinative factor in every sanctions analysis. As U.S. District Judge Paul Grimm emphasized in *Victor Stanley, Inc. v. Creative Pipe, Inc.*, a court should also consider as part of that analysis the "reasonableness and proportionality" of a party's efforts to preserve relevant ESI.[11] Nevertheless, most courts applying Rule 37(e) have instead generally focused on whether and when a party suspended

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[4] REPORT, *supra* Note 1, at 318.
[5] Philip J. Favro, *Getting Serious: Why Companies Must Adopt Information Governance Measures to Prepare for the Upcoming Changes to the Federal Rules of Civil Procedure*, 20 RICH. J.L. & TECH. 5, 27 (2014).
[6] Residential Funding Corp. v. DeGeorge Financial Corp., 306 F.3d 99 (2nd Cir. 2002). *See* REPORT, *supra* Note 1, at 314, 321-22.
[7] *See*, *e.g.*, Sekisui Am. Corp. v. Hart, 945 F. Supp. 2d 494 (S.D.N.Y. 2013) (relying on *Residential Funding* to impose an adverse inference instruction as a sanction for the plaintiffs' grossly negligent spoliation of ESI).
[8] *See* Philip J. Favro, *Sea Change or Status Quo: Has the Rule 37(e) Safe Harbor Advanced Best Practices for Information Management?*, 11 MINN. J.L. SCI. & TECH. 317, 328-29, 332 (2010) (discussing the Committee's intent to establish the present version of Rule 37(e) as a national standard when it was implemented in 2006).
[9] REPORT, *supra* Note 1, at 314 (observing, among other things, that because "ESI is more easily lost than tangible evidence…the sanction of an adverse inference instruction imposes a heavy penalty for losses that are likely to become increasingly frequent as ESI multiplies exponentially and moves to the 'cloud.'").
[10] *See* Favro, *supra* Note 8, at 327-28.
[11] *Victor Stanley, Inc. v. Creative Pipe, Inc.* (*Victor Stanley II*), 269 F.R.D. 497, 523 (D. Md. 2010) (observing that an "assessment of reasonableness and proportionality should be at the forefront of all inquiries into whether a party has fulfilled its duty to preserve relevant evidence.").

particular aspects of its computer systems after a preservation duty attached.[12] This has led to sanctions rulings that are out of step with mainline ESI preservation jurisprudence.[13]

A final factor contributing to the futility of Rule 37(e) is that courts have frequently used their inherent authority to bypass the rule's protections.[14] This is because Rule 37(e) only applies to conduct that occurred during the litigation. It does not govern pre-litigation activities such as the destruction of ESI that occurred *before* the commencement of litigation.[15] As a result, courts have often wielded their inherent powers to fashion remedies for ESI destruction free from the rule's present constraints.[16]

With varying preservation standards, the inordinate focus on one factor in the preservation analysis, and the ease in which the rule's protections can be bypassed, there can be little doubt as to why a revised version of Rule 37(e) is needed.

THE PROPOSED RULE 37(e) AMENDMENTS

The proposed amendments to Rule 37(e) are designed to address these issues by providing a straightforward framework for the issuance of any sanctions stemming from failures to preserve relevant ESI. They also encourage courts to draw on a wide range of factors to fashion sanctions awards that cure prejudice caused by less harmful forms of ESI spoliation. In addition, the proposed changes establish "a uniform standard in federal court" for the imposition of severe remedial measures resulting from ESI preservation failures.

The New Sanctions Framework

The Committee has established a set of requirements in the proposed rule that must be satisfied before a court could impose sanctions on a litigant for failing to preserve ESI. The reason for doing so is to ensure that sanctions for preservation failures are based on the designated criteria and not the potentially arbitrary use of a court's inherent powers:

> New Rule 37(e)…authorizes and specifies measures a court may employ if information that should have been preserved is lost, and specifies the findings necessary to justify these measures. *It therefore forecloses reliance on inherent authority* or state law to determine whether measures should be used.[17]

The prerequisites that a party must satisfy when moving for sanctions under the amended Rule 37(e) proposal are as follows:

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[12] *See* Favro, *supra* Note 8, at 327-28.
[13] *See*, *e.g.*, Phillip M. Adams & Assoc., L.L.C. v. Dell, Inc., 621 F. Supp. 2d 1173 (D. Utah 2009).
[14] Thomas Y. Allman, *Dealing with Spoliation in the Federal Rules (Again): The Proposed Amendment to Rule 37(e)*, IAALS/NJC E-Discovery Summit 2013, *available at* http://iaals.du.edu/images/wygwam/documents/publications/E-Discovery_Panel_2_Preservation.pdf.
[15] *Id*. at 5.
[16] *See*, *e.g.*, Escobar v. City of Houston, No. 04-1945, 2007 WL 2900581, at *17 n.5 (S.D. Tex. Sept. 29, 2007) (describing the circumstances under which courts may exercise their inherent authority).
[17] REPORT, *supra* Note 1, at 318-19 (emphasis added).

1. Relevant ESI "should have been preserved in the anticipation or conduct of litigation,"
2. Relevant ESI was "lost,"
3. The party charged with safeguarding the lost ESI "failed to take reasonable steps to preserve the information," and
4. The lost ESI "cannot be restored or replaced through additional discovery."[18]

While the first two steps essentially reflect existing common law requirements,[19] the third step includes a key notion memorialized in *Victor Stanley II*: that preservation efforts must be analyzed through the lens of reasonableness.[20] This is a significant step since it would oblige courts to examine preservation issues with a broader perspective and not focus exclusively on whether and when the party modified aspects of its electronic information systems.[21] Moreover, it would direct preservation questions away from a mythical standard of perfection that has unwittingly crept into eDiscovery jurisprudence over the past several years.[22] Instead of punishing parties that somehow failed to preserve every last email that could conceivably be relevant, the rule would essentially require a common sense determination of the issues based on a benchmark – reasonableness – with which courts and counsel are familiar.

The fourth and final provision is significant since it would prevent the imposition of sanctions where there is essentially no harm to the moving party given the availability of replacement evidence.[23]

Severe Sanctions vs. Curative Measures

To obtain the most severe measures under Rule 37(e)(2), the moving party must additionally demonstrate that the alleged spoliator "acted with the intent to deprive another party of the information's use in the litigation."[24] This specific intent requirement is designed to create a uniform national standard by ensuring that severe sanctions are imposed only for the most flagrant violations of ESI preservation duties.[25] These violations appear to include bad faith destructions of ESI that occur in connection with the instant lawsuit.[26] They do not, however, include negligent or grossly negligent conduct. The draft Committee note makes clear that the Rule 37(e) amendments "reject[] cases such as *Residential Funding Corp. v. DeGeorge Financial Corp.*, 306 F.3d 99 (2nd Cir. 2002), that authorize the giving of adverse-inference instructions on a finding of negligence or gross negligence."[27]

The severe sanctions that a court could issue under Rule 37(e)(2) are limited to dismissing the case, entering default judgment, or "instruct[ing] the jury that it may or must presume the information was unfavorable to the party."[28] Alternatively, a court could presume that the lost ESI was unfavorable to the

[18] *Id*. at 318.
[19] *Id*. at 319.
[20] *Id*. at 319-20.
[21] *Id*.
[22] *Id*. at 320 ("This rule recognizes that 'reasonable steps' to preserve suffice; it does not call for perfection.").
[23] *Id*. ("If the information is restored or replaced, no further measures should be taken.").
[24] *Id*. at 318.
[25] *Id*. at 306, 308.
[26] *Id*. at 313 ("This intent requirement is akin to bad faith.").
[27] *Id*. at 321-22.
[28] *Id*. at 318.

alleged spoliator.[29] Nevertheless, a court is under no obligation to order any of these measures even if the specific intent requirement is satisfied. As the Committee cautions in the draft note, "[t]he remedy should fit the wrong, and the severe measures authorized…should not be used when the information lost was relatively unimportant or lesser measures…would be sufficient to redress the loss."[30]

If the moving party cannot satisfy the specific "intent to deprive" requirement, the court could then resort to curative measures under Rule 37(e)(1) to address prejudice resulting from the loss of the ESI.[31] The sanctions that a court could order pursuant to that provision would be "no greater than necessary to cure the prejudice" to the aggrieved party.[32] That wording was drafted broadly to ensure that jurists would have sufficient discretion to craft remedies that could ameliorate the prejudice.[33] While the precise range of these remedies is not delineated in the rule, the draft Committee note suggests the remedies could include the following:

- "[P]reclude a party from presenting evidence,"[34]
- "[D]eem some facts as having been established," [35]
- "[P]ermit[] the parties to present evidence and argument to the jury regarding the loss of information,"[36] or
- "[Give] the jury instructions to assist in its evaluation of such evidence or argument, other than instructions to which subdivision (e)(2) applies."[37]

Thus, a moving party could very well obtain weighty penalties against an alleged spoliator even if it is unable to establish the specific "intent to deprive." Nevertheless, the draft Committee note makes clear that any such sanctions must be tailored so they do not equal or exceed the severe measures of Rule 37(e)(2).[38]

KEY ISSUES FOR MOTION PRACTICE UNDER THE NEW RULE 37(e)

While the new Rule 37(e) proposal addresses the main problems associated with the current rule, there are several questions about the revised rule that remain unanswered and that will likely be the subject of vigorous motion practice. I will consider two of those questions in this section.

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[29] *Id*.
[30] *Id*. at 322-23.
[31] *Id*. at 318.
[32] *Id*.
[33] *Id*. at 321 ("The range of such measures is quite broad . . . [m]uch is entrusted to the court's discretion.").
[34] *Id*. at 312.
[35] *Id*.
[36] *Id*. at 321.
[37] *Id*.
[38] *Id*. ("Care must be taken, however, to ensure that curative measures under subdivision (e)(1) do not have the effect of measures that are permitted under subdivision (e)(2) only on a finding of intent to deprive another party of the lost information's use in the litigation.").

What are "Reasonable Steps to Preserve" ESI?

One of the principal battlegrounds under the revised version of Rule 37(e) will certainly involve deciphering the meaning of "reasonable steps to preserve" ESI. This is because the "reasonable steps" provision is an express – though undefined – prerequisite for obtaining sanctions. This is confirmed by the wording of the draft Committee note: "Because the rule calls only for reasonable steps to preserve, it is inapplicable when the loss of information occurs despite the party's reasonable steps to preserve."[39] Thus, a party who employs "reasonable steps" to keep relevant ESI cannot be sanctioned for its loss.[40]

However, as to the precise meaning of "reasonable steps," the Committee provides only general guidance. For example, the draft note suggests that sanctions may not be appropriate if the destroyed ESI is either outside of a preserving party's control or has been wiped out by circumstances (*e.g.*, flood, fire, hackers, viruses, etc.) beyond the party's control.[41] Nevertheless, the note does not suggest that these *force majeure* circumstances are an absolute defense to a sanctions request. Instead, it advises courts to view the context of the destruction and what steps the preserving party could reasonably have taken to prepare for the problem before it occurred.[42] Engaging in this type of hindsight analysis has its limitations, though, which the Committee acknowledges in the draft note.[43]

The note also suggests that the range of a party's preservation efforts should be tempered by proportionality standards.[44] However, as U.S. Magistrate Judge James Francis observed in *Orbit One Communications, Inc. v. Numerex Corp.*, proportionality is an "amorphous" and "highly elastic concept" that may not "create a safe harbor for a party that is obligated to preserve evidence."[45] Therefore, while notions of proportionality may factor into the preservation analysis, it is unlikely that they alone will determine the issue of "reasonable steps to preserve."

In the absence of meaningful direction on this issue, courts will likely turn to existing case law to help guide their decision on whether a party has or has not taken "reasonable steps" to retain ESI. To be sure, the jurisprudence on this issue is far from uniform. Nevertheless, there are many cases that delineate the acceptable boundaries of preservation conduct.[46] How those cases are applied under the

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[39] *Id*. at 320.
[40] *Id*. ("Because the rule calls only for reasonable steps to preserve, it is inapplicable when the loss of information occurs despite the party's reasonable steps to preserve.").
[41] *Id*.
[42] *Id*. ("Courts may, however, need to assess the extent to which a party knew of and protected against such risks.").
[43] *Id*. at 319 (cautioning generally about the limited perspective that hindsight provides into the nature of a party's conduct).
[44] *Id*. *See* Philip J. Favro and Derek P. Pullan, *New Utah Rule 26: A Blueprint for Proportionality under the Federal Rules of Civil Procedure*, 2012 MICH. ST. L. REV. 933, 952 (2012) (citing authorities holding that preservation efforts "must be viewed through the lens of proportionality" and not just the "kaleidoscope of relevance").
[45] Orbit One Communications, Inc. v. Numerex Corp., 271 F.R.D. 429, 436, n.10 (S.D.N.Y. 2010).
[46] *See*, *e.g.*, Micron Tech., Inc. v. Rambus Inc., 645 F.3d 1311, 1322 (Fed. Cir. 2011) (approving information retention policies that eliminate documents for "good housekeeping" purposes); Brigham Young Univ. v. Pfizer, Inc., 282 F.R.D. 566, 572 (D. Utah 2012) (denying plaintiffs' motion for sanctions since the evidence at issue was destroyed pursuant to defendants' "good faith business procedures").

revised Rule 37(e) will turn – as they always have – on the facts of the case, the quality of counsel's advocacy, and the court's perception of the issues.

What does "Intent to Deprive" mean?

Another likely area of dispute between litigants will be on the meaning of the "intent to deprive" requirement of revised Rule 37(e)(2). While the draft Committee note makes clear that this specific intent requirement does not include negligent or grossly negligent conduct, the question confronting clients, counsel, and the courts is what conduct does it refer to?

The Committee report issued in connection with the Rule 37(e) proposed amendments explains that the "intent requirement is akin to bad faith." [47] Despite this straightforward explanation, the draft Committee note does not take such a restrictive view. Instead, the note indicates that sanctions under Rule 37(e)(2) are limited "to instances of intentional loss or destruction."[48] Conduct that is "intentional" that results in the spoliation of ESI is not necessarily tantamount to bad faith.[49] Indeed, that intentional conduct is a lesser standard than bad faith was confirmed by the United States Court of Appeals for the Seventh Circuit many years ago. In addressing a document spoliation question, the Seventh Circuit noted the distinction between bad faith and intentional conduct: "That the documents were destroyed intentionally no one can doubt, but 'bad faith' means destruction for the purpose of hiding adverse information."[50]

If the "intent to deprive" requirement does encompass lesser forms of ESI spoliation than bad faith, the question then becomes what is the level of conduct punishable under Rule 37(e)(2)? The answer is that "intentional" spoliations may very well include instances where parties have been reckless or willful in their destructions of ESI.[51] Whether that conduct is sufficient to justify the severe measures that a revised Rule 37(e) authorizes will once again turn on the nature and circumstances surrounding the spoliation. In other words, the courts will again be left to sort out the meaning of a key provision from the rule.

CONCLUSION

While not every issue associated with ESI preservation failures has been addressed by the Rule 37(e) proposal, it is unrealistic to expect that any rule could do so. Moreover, the revised rule appears to have resolved many of the shortcomings with the current version. By creating a basic analytical framework, widening the analysis to ensure that a broad set of factors are analyzed in connection with preservation conduct, and establishing a uniform standard for severe sanctions, lawyers may finally have a workable paradigm to provide straightforward advice to clients on ESI preservation questions.

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[47] REPORT, *supra* Note 1, at 313 ("This intent requirement is akin to bad faith.").
[48] *Id*. at 322.
[49] *See Micron Tech.*, 645 F.3d at 1327 ("In determining that a spoliator acted in bad faith, a district court must do more than state the conclusion of spoliation and note that the document destruction was intentional.").
[50] Mathis v. John Morden Buick, Inc., 136 F.3d 1153, 1155 (7th Cir. 1998).
[51] *See generally* Pension Comm. of the Univ. of Montreal Pension Plan v. Banc of America Sec., LLC, 685 F.Supp.2d 456, 464-65 (S.D.N.Y. 2010) ("*willfulness* involves intentional or reckless conduct that is so unreasonable that harm is highly likely to occur").

About the Author

Philip Favro brings fourteen years of expertise to his position as an independent discovery counsel. Phil is an industry thought leader, a global enterprise consultant, and a legal scholar on issues such as eDiscovery, data protection, and information governance. Phil's expertise has been enhanced by his practice experience as a business litigation attorney in which he advised a variety of clients regarding complex discovery issues. Phil is a member of the Utah and California bars. He is an active member of the American Bar Association and also contributes to Working Groups 1 and 6 of The Sedona Conference. Phil also is the editor-in-chief for *The Core Perspective*, a leading eDiscovery blog.