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FEDERAL E-DISCOVERY

Court Rejects 37(e), Invokes Inherent Authority to Sanction



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Federal Rule of Civil Procedure 37(e) was intended to be the new national standard setting forth the available sanctions for failure to preserve electronically stored information (ESI). When creating the new rule, the drafters hoped to resolve the circuit court split on this issue. In particular, the drafters rejected the Second Circuit standard in favor of one that is more forgiving, especially in situations where the ESI could be restored or replaced or where there is no prejudice to the aggrieved party. Importantly, the rule also purported to restrict the inherent authority of judges to impose sanctions for the failure to preserve ESI, which has previously resulted in a number of unexpectedly punitive sanctions decisions, particularly in the Second Circuit.

Since the enactment of Rule 37(e), a number of courts have challenged the notion that a rule can limit a judge's



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inherent power to issue spoliation sanctions, especially when a party acted in bad faith. A recent decision from the Southern District of New York went even further. In *Hsueh v. N.Y. State Dep't of Fin. Servs.*, 2017 WL 1194706 (S.D.N.Y. March 31, 2017), Senior District Judge Paul Crotty, in a notable interpretation of the rule, determined that Rule 37(e) was inapplicable when a party intentionally destroys relevant ESI with the intent to deprive another party of its use, even though the rule expressly addresses such conduct. Judge Crotty instead invoked his inherent authority to impose the sanction of an adverse inference jury instruction, a severe sanction that nonetheless would have been available to him under Rule 37(e).

Under Rule 37(e), “[i]f electronically stored information that should have been preserved in the anticipation or conduct of litigation is lost because a party failed to take reasonable steps to preserve it, and it cannot be restored or replaced through additional discovery,” then a court may consider available curative measures or sanctions under the rule. Subsection (e)(2) provides that the court may impose severe sanctions such as an adverse inference jury instruction “only upon finding that the party acted with the intent to deprive another party of the information’s use in the litigation[.]”

In *Hsueh*, the plaintiff, an EEOC complainant, had recorded a conversation with her former employer’s human resources representative, but subsequently deleted it, claiming that “the voice recording itself ... was not very clear, so [she] did not feel it was worth keeping.” A defendant filed a motion for spoliation sanctions in connection with this deletion and asked that the court dismiss the plaintiff’s action or issue an adverse inference jury instruction. On the day plaintiff’s response to the motion

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was due, her attorney advised the court that the plaintiff and her husband had been able to recover the audio recording from a hard drive used to back up their computers. After reopening discovery so that both defendants could depose the plaintiff and her husband about the recording, the court considered the defendant's spoliation motion.

The plaintiff argued that Rule 37(e) was the appropriate legal standard for considering spoliation sanctions. The defendant disagreed, contending, *inter alia*, that Rule 37(e) was inapplicable because it "applies only to situations where 'a party failed to take reasonable steps to preserve' ESI; not to situations where, as here, a party intentionally deleted the recording." Judge Crotty agreed, stating "[t]his makes sense." He cited to the Advisory Committee Notes to the 2015 Amendment to Rule 37 and to another SDNY decision for the notion that the intended goal of Rule 37(e) was to curtail the excessive burden and costs associated with over-preservation of potentially relevant ESI due to fear of spoliation sanctions. Judge Crotty concluded that "[t]hese considerations are not applicable here. It was not because [the plaintiff] had improper systems in place to prevent the loss of the recording that the recording no longer existed on her computer; it was because she took specific action to delete it." Judge Crotty held that "[b]ecause Rule 37(e) does not apply, the Court may rely on its inherent power to control litigation in imposing spoliation sanctions."

Looking to Second Circuit precedent for guidance, Judge Crotty outlined a three-factor test for whether the

sanction of an adverse inference jury instruction was appropriate in this situation. Under this test, a party seeking an adverse inference instruction "must establish (1) that the party having control over the evidence had an obligation to preserve it at the time it was destroyed; (2) that the records were

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destroyed with a culpable state of mind; and (3) that the destroyed evidence was relevant to the party's claim or defense such that a reasonable trier of fact could find that it would support that claim or defense."

During his analysis, Judge Crotty explored the plaintiff's argument that sanctions were not warranted because she was able to restore the recording. He found this argument unpersuasive, determining that "there is good reason to conclude that the produced recording is incomplete." Ultimately, Judge Crotty found that all three factors of the Second Circuit test had been satisfied and that "[u]nder either Rule 37(e) and the Court's inherent authority, an adverse inference is the appropriate remedy in light of the Court's findings." He also granted the defendants their attorney's fees and costs for the spoliation motion and for reopening discovery.

While Judge Crotty seems to have hedged his bets in writing that he would have reached the same decision under Rule 37(e) as he did under his inherent authority, clarification of the basis for

his decision may be in order. Rule 37(e) provides courts options for imposing sanctions and curative measures when a party fails to take reasonable steps to preserve ESI and that ESI cannot be restored or replaced. It further specifies a court's options for imposing sanctions when it finds that a party acted intentionally to deprive an adversary of the use of that ESI. Judge Crotty, in *Hsueh*, seems to be threading a needle in arguing that intentional deletion is not addressed by the rule. Moreover, his endorsement of the continued ability of courts to invoke their inherent powers to sanction for failure to preserve ESI is part of a broader trend, although one that rests uneasily with the statement in the Advisory Committee Notes that Rule 37(e) "forecloses reliance on inherent authority or state law" in determining when sanctions are appropriate.

Judge Crotty's decision adds to a growing body of law supporting such an application of a court's inherent power. Additionally, in endorsing a circuit-specific test for the applicability of an adverse inference sanction for failure to preserve ESI, the decision may contribute to uncertainty around sanctions that Rule 37(e) was intended to remove and may reopen the circuit court split that the rule was designed to resolve.