
IN THE UNITED STATES DISTRICT COURT FOR THE DISTRICT OF UTAH
CENTRAL DIVISION

PHILIPS ELECTRONICS NORTH AMERICA CORPORATION, a Delaware corporation; KONINKLIJKE PHILIPS ELECTRONICS NV, a foreign corporation; and PHILIPS MEDICAL SYSTEMS (CLEVELAND), INC., a California corporation,

Plaintiffs and Counter Defendants,

v.

BC TECHNICAL,

Defendants and Counter Claimants.

REPORT AND RECOMMENDATION

Case No. 2:08-CV-639-CW-SA

District Judge Clark Waddoups

Magistrate Judge Samuel Alba

This case involves large amounts of electronic information. Under the federal rules, in addition to this court's discovery orders, the litigants and counsel were expected to take the necessary steps to ensure that relevant records were preserved when litigation was reasonably anticipated or began, and that those records were collected, reviewed, and produced to the opposing party during the discovery process. Unfortunately, as discussed herein, the court has concluded that Defendant and Counter Claimant BC Technical (hereafter "BCT") did not fulfill its discovery obligations or comply with this court's orders with respect to five of its laptop computers. BCT's behavior has resulted in great expense from the efforts made to uncover and retrieve the information that was deleted or destroyed. Further, the court must now determine

how to address a situation where - in violation of this court's direct orders and the Federal Rules of Civil Procedure - thousands of computer files were deliberately deleted and destroyed.

Before the court are the following motions: (1) Plaintiffs' Motion for Spoliation Sanctions (Doc. 135); (2) Plaintiffs' Motion for Order Holding Defendant In Contempt of Court Pursuant to Fed. R. Civ. P. 37(b) (Doc. 136); and (3) Plaintiffs' Second Motion for Spoliation Sanctions and for Order Holding Defendant in Contempt of Court (Doc. 174). Having reviewed these motions as well as all the pleadings in this matter, having conducted an evidentiary hearing, and having heard oral arguments, the court submits this Report and Recommendation.

BACKGROUND

In January 2005, Philips sent BCT's then-President, Mr. Chuck Hale, a letter, dated January 20, 2005, alleging that BCT was improperly and illegally distributing software, was providing misleading information at a trade show booth, was publishing misleading literature, was making libelous and disparaging remarks on its website regarding Philips, and was systematically and deliberately attempting to damage Philips by targeting key Philips employees for employment with BCT. BCT's counsel sent Philips a responsive letter. In a third letter, dated February 16, 2005, Philips' counsel responded to BCT's letter.

Approximately three years later, on January 16, 2008, Plaintiffs and Counter Defendants Philips Electronics North America Corporation, Koninklijke Philips Electronics NV, and Philips Medical Systems (Cleveland), Inc. (hereafter collectively referred to as "Philips") filed this action in the United States District Court, Western District of Washington at Seattle. (Doc. 2-4.) Philips alleged claims of copyright infringement, federal trademark infringement,

misappropriation of trade secrets, tortious interference with business relations, and violation of the Washington Consumer Protection Act. (Doc. 2-4.) Philips sought injunctive relief and damages and requested attorneys' fees and costs. (Doc. 2-4.)

On May 22, 2008, BCT filed a motion to transfer the case to this court (Doc. 2-9), which motion was opposed by Philips (Doc. 2-12). On August 1, 2008, the court granted BCT's motion to transfer, and the case was transferred to this court. (Doc. 3-17.) On August 26, 2008, this court received the documents in this case transmitted from the Western District of Washington, Seattle, and the case was eventually assigned to United States District Judge Clark Waddoups. (Docs. 1-3, 18.) BCT filed its Answer on October 17, 2008. (Doc. 15.) Based on the parties' stipulation, Philips filed an Amended Complaint on March 2, 2009. (Doc. 25.) On May 15, 2009, BCT filed an Amended Answer. (Doc. 55.) On April 9, 2009, Judge Waddoups referred the case to United States Magistrate Judge Samuel Alba pursuant to 28 U.S.C. § 636(b)(1)(A).

On March 20, 2009, Philips filed a motion to compel. (Doc. 32.) The court granted that motion to compel on May 22, 2009. (Doc. 59.) On June 19, 2009, BCT filed a motion to compel. (Doc. 65.) The court granted that motion on July 20, 2009.¹ (Doc. 80.)

On June 23, 2009, hours after being deposed in this case, BCT's Chief Operating Officer, William Biddle, sent an email to all BCT employees stating the following:

¹In July 2009, MSouth Equity Partners acquired BCT. MSouth Equity Partners formed BCT Holdings, Inc. for the purpose of purchasing BCT. (Doc. 262.) Because the distinction between BCT and MSouth does not matter to the court's analysis, and for convenience, the court refers to both BCT and MSouth as "BCT" throughout this Report and Recommendation.

Folks—

This is a reminder that you are to save any electronic records that could possibly be associated in any way to the Philips' litigation. If there is any question in your mine [sic] then make sure to retain the information.

Feel free to give your respected manager a call if you would like to discuss.

(Doc. 194, Ex. 1.)

On July 10, 2009, Philips filed a second motion to compel responses to Philips' first requests for production. (Doc. 72.) On July 15, 2009, Philips filed a motion to compel BCT to preserve relevant information. (Doc. 75.) In its motion to compel BCT to preserve relevant information, Philips expressed concerns that even though this case had been pending for about eighteen months, BCT had (1) failed to issue a litigation hold memo to its employees to preserve information, (2) failed to modify or suspend document destruction practices in light of the litigation, (3) failed to image the hard drives of its key custodians, and (4) continued its practice of routinely overwriting back-up tapes until Philips brought those problems to this court's attention by motion on July 15, 2009. (Docs. 75-76, 79.) Philips expressed its concern that BCT was destroying key evidence.

On August 18, 2009, the court held a hearing on Philips' two motions. (Doc. 98.) The court granted in part Philips' second motion to compel responses (Doc. 98, 105), and granted Philips' motion to compel BCT to preserve relevant information (Doc. 105).

The court's written order granting Philips' motion to compel BCT to preserve relevant information ordered that within five days of the August 18, 2010 order, BCT shall:

- (1) Issue and circulate a thorough litigation hold memo to employees likely to have relevant information. The litigation hold memo should identify categories of relevant information and the subjects of plaintiffs' discovery requests. Further, defendant shall provide a copy of the litigation hold memo to plaintiffs, and identify the persons to whom the litigation hold memo is provided;
- (2) Provide all its existing backup tapes to its attorneys and suspend the practice of overwriting any information on those backup tapes until further order of this Court, or the termination of this litigation;
- (3) Cease "wiping" or "re-imaging" the hard drives of employees likely to have relevant information until further order of the Court, or the termination of this litigation.

(Doc. 99, at 2.) The order further provided that "this Order is without prejudice to plaintiffs' right to pursue additional relief to ensure that defendant complies with its preservation obligations moving forward, and/or to seek sanctions or spoliation instructions should it be discovered that relevant information has been destroyed." (Doc. 99, at 2-3.) At the August 18, 2009 hearing, BCT's attorney assured the court that he understood the requirements of the order and BCT would "follow it." (Doc. 139, Kindley Dec., Ex. 0 at 37:2-4.)

On August 25, 2009, Biddle circulated another email to all BCT employees. The email's importance was rated "high" and, as instructed by the court's order following the August 18, 2009 hearing, attached a Litigation Hold Memo. The Litigation Hold Memo directed all employees to preserve the following documents on their computers: (1) personnel records for any person who, at any time, was a Philips' employee; (2) correspondence between BCT and Philips; (3) correspondence or written communication between Philips and any third party; (4) brochures, flyers, circulars, website materials, e-mails or other documents relating in any way to

BCT's efforts at marketing goods or services in any way involving Philips' products, such as ADAC, AutoSPECT, AutoQUANT, or Pegasys; (5) price quotes, bids or other written offers to perform services or sell goods, generated either by BCT or Philips; (6) all business records (including, but not limited to, invoices, work orders, bids, quotes, field service notes, billing statements, or correspondence (relating in any way to BCT's servicing, repairing or maintaining any Philips-manufactured device or system)); (7) all business records relating to the purchase of any parts or materials from any Philips entity by BCT or by any third party; (8) all service records relating to the installation of software onto repaired or refurbished nuclear medical devices or systems manufactured by Philips; (9) lists or databases of actual or prospective customers of Philips or BCT, concerning the furnishing of repair, maintenance or service on Philips-manufactured devices or systems. (Doc. 194, Ex. 2). The Litigation Hold Memo explained that the foregoing list "does not attempt to itemize all of the types of documents and materials that must be retained, but rather it is intended to provide you with examples of the types of documents that must be retained. If you have any questions regarding whether particular documents must be retained, please contact William Biddle at (801) 280-2900." (Doc. 194, Ex. 2.) The memo also instructed BCT employees in detail concerning how documents were to be preserved. The memo told employees that if they had not already done so, to conduct a diligent search of their on-site files to identify any relevant documents, including the identification of all computer-stored information as well as all paper copies of email, notes, drafts and tapes of telephone conversations, folios, reports, statements, personnel records, payroll records, etc. The memo instructed employees to then contact Biddle to arrange for the documents to be reviewed

by a member of the legal team. The memo instructed employees not to destroy any potentially relevant documents, even if they otherwise routinely would be discarded or destroyed in the ordinary course of business, including preventing any periodic purging or deletion of documents or information (including emails) off computer systems that otherwise might occur. The memo told employees that if they needed technical assistance to insure the preservation of documents to contact Biddle. In addition, the memo instructed employees not to re-use data backup tapes; instead, all backup tapes were to be preserved and provided to BCT's legal counsel.

The memo instructed employees to cease "wiping" or "re-imaging" their hard drives until the lawsuit with Philips was over. Employees were instructed, for all paper documents that were maintained in filing cabinets or other containers that would be needed to conduct ongoing business, to affix to the cabinet or container a note which stated: "The contents of this cabinet/container must be retained pursuant to a directive from BCT management. Make and use copies only. Do not remove originals except to make copies, and then return originals to the exact location from which they were removed." Further, employees were told that, to the extent they or their staff may have sent potentially relevant documents off-site to archives or storage, to identify those documents and contact Biddle to obtain further instructions. In addition, employees were told not to create any new documents describing or commenting on anything contained in this memorandum unless they were directed to do so by BCT or by an outside counsel representing BCT. (Doc. 194, Ex. 2.)

On July 31, 2009, Philips filed a third motion to compel responses from BCT (Doc. 85), and on August 18, 2009, BCT filed a cross motion for a protective order (Doc. 91). On

September 22, 2009, the court held a hearing on these two motions. The court verbally granted Philips' third motion to compel. (Docs. 108, 111, 114.) Philips' attorney made an oral motion for attorneys fees, which the court granted. (Docs. 108, 111, 114.) The court ordered that all of BCT's computers and servers be turned over for collection since BCT had not complied with discovery requests due in July. The court ordered the attorneys for Philips and BCT to finalize a stipulation regarding the collection of BCT's electronically stored information (hereafter "ESI"), which was incorporated into this court's written Order Granting Plaintiffs' Third Motion to Compel and Awarding Sanctions to Plaintiffs. (Docs. 110-11.) The court's written order required BCT to provide Lighthouse Document Technologies (hereafter "Lighthouse") with "immediate access to all of BCT's laptops, desk computers and all servers" and to "fully cooperate" in the process of collecting, retrieving and processing the ESI. (Doc. 111.) The court found moot BCT's cross motion for a protective order. (Docs. 108, 114.)

As just mentioned, among other things, the written order following the hearing incorporated into it the parties' stipulation regarding BCT's ESI. (Docs. 110, 111.) In that stipulation, signed on September 24, 2009, by attorneys representing both Philips and BCT, the parties agreed to the following:

1. [BCT] shall provide Lighthouse Document Technologies ("Lighthouse") with immediate access to all of BCT's laptops, desk computers and all servers. [BCT] shall provide a list of all business computers located at West Jordan, Utah (or for laptops of employees that work from West Jordan) by name of employee, job title and length of employment and computer model and serial number to counsel for Philips. BCT shall use its best efforts to provide this list by the end of the day September 24, 2009. At the present time, Philips has designated 10 laptops from field service

engineers that are not located in West Jordan, Utah: these are for Ava Bixler, Mike Landis, Jerry Williams, Ed Sokolowski, Marcus Carter, Scott Dorchin, Paul Schenker, Dan Gasparovich, Steven Cook and Tony Butler. These laptops will be sent to BCT offices in West Jordan and be available by Friday morning at 8:30 am, September 25, 2009, or as soon thereafter as Federal Express deliveries arrive on Friday morning. Philips reserves the rights to designate further laptops at a later time should it be necessary to do so, but this will be coordinated in advance between counsel.

2. Philips shall pay for the cost of collecting this information, but if BCT wants any of the information or data from Lighthouse, BCT shall pay half the cost of processing the data after it has been collected.

3. BCT shall make all computers and servers available at West Jordan for Lighthouse. BCT shall turn over all of its backup tapes to Lighthouse for Lighthouse to reproduce in Seattle and Lighthouse will return the original backup tapes to BCT.

4. Lighthouse will process the electronically stored information that is collected. In the course of processing any email, email that has been sent to or from a domain name of "joneswaldo.com" will be sent to counsel for defendant, Vince Rampton, for review of privilege. That data will be reviewed and any data that should be produced will be produced within 20 days from its receipt to counsel for plaintiffs.

5. [BCT] will fully cooperate with Lighthouse in the process of collecting, retrieving and processing the electronically stored information. Currently, all parties and Lighthouse anticipate the collection of the data at [BCT's] office can be done on Friday and Saturday, September 25 and 26, 2009.

6. All data collected by Lighthouse shall be treated as "Confidential" pursuant to the terms of the Protective Order in this case.

7. Lighthouse will use its own equipment to search BCT's computers and hard drives, and will not download or install any software, applications or programs on any BCT computer.

(Doc. 110.)

As discussed in more detail below, within hours of this court's order, BCT executives and employees began deleting a massive number of files from their computers just ahead of the

court-ordered collection by Lighthouse of BCT's ESI. (Doc. 140, Norberg Dec. ¶¶ 4-16, Exs. 1-13.)

On the evening of Tuesday, September 22, 2009, BCT's IT Director, Derek Tolboe, sent an email to several BCT employees, including Jerry Williams, Ed Sokolowski, Marcus Carter, and Dan Gasparovich, instructing them to turn in their laptop computers by that Friday. (Exhibit 2 of Plaintiff's Exhibits from the Hearing (hereafter "Ex. __").) In response to that email, Ed Sokolowski sent a reply email requesting a telephone conference, stating: "As Philips continues to 'fish' for information, I (as I am sure others as well) would feel more at ease if the two of you could specifically tell all of us - that we are protected from any personal wrong-doing during the course of our employment with BCT." (*Id.*) As discussed more below, that telephone conference occurred later that week. (Ex. 3.)

Lighthouse began its data collection at BCT's West Jordan, Utah facility on Friday, September 25, 2009. During that process, Lighthouse captured forensic images of the hard drives of eight BCT executives and employees: Chuck Hale, Scott Dorchin, William Biddle, Marcus Carter, Paul Schenker, Ed Sokolowski, Jerry Williams, and Dan Gasparovich. Although BCT had been ordered to do so, BCT failed to provide Lighthouse with access to the laptops of Rex Lindsey, Luciano Albuquerque, or to Chuck Hale's second laptop during Lighthouse's initial collection effort in West Jordan between September 25 and 27, 2009. Philips complained about this noncompliance with the court's order and the parties' stipulation. (Doc. 139, Kindley Dec., Ex. B.) Lighthouse finally was given those last three laptops on October 9, 2009. Once Lighthouse received the three additional laptops, it also took forensic images of their

