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Litigation Alert

The Impact of Disregarding Document Preservation Obligations

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Parties are repeatedly being sanctioned for e-discovery violations. Yet, many organizations fail to proactively address preservation and discovery obligations when an organization is selling off assets, reorganizing, merging, divesting or acquiring interests. This alert describes recent rulings involving document preservation and control and offers best practices for organizations engaged in transactions that involve document preservation.

An organization has a duty to preserve and produce not only those documents that are within its possession, but also those documents within its custody or control.[1] That duty to preserve documents does not disappear when there is a subsequent sale of the company, reorganization or sale of relevant assets. In *Centimark Corp. v. Pegnato & Pegnato Roof Management, Inc.*,[2] the defendant sold assets after litigation had commenced. As part of the asset sale, the defendant turned over relevant documents to the third-party purchaser, which, in turn, lost or destroyed the information. The court found that because the documents were within the possession, custody or control of the defendant, the defendant was responsible for the spoliation of the documents. The court believed that the defendant should have retained a copy of the relevant documents, given the plaintiff access to the documents before the sale or ensured that the plaintiff would have access to the documents after completion of the sale. Similarly, in *In re NTL, Inc. Securities Litigation*,[3] the defendant filed for bankruptcy and emerged from bankruptcy as two different companies. As part of the bankruptcy plan, one company became the successor-in-interest for purposes of the lawsuit, while the other company obtained relevant documents and assets of the original bankruptcy debtor. The nonparty company destroyed relevant information and documents. The court sanctioned the defendant for spoliation of documents that had been in the possession of the nonparty company. As in *Centimark*, the court in *In re NTL* found that the defendant should have itself preserved a copy of the information or ensured that the third party would preserve the information before turning it over to the third party.

In the same way, if an organization acquires a business, acquires assets, acquires an interest in a claim or receives an assignment of a patent, courts will likely presume that the organization has possession, custody or control over relevant documents.[4] Therefore, the failure of a target or seller to preserve information could have drastic consequences for the purchaser.

To confront potential preservation issues before they arise, an organization that is reorganizing its operations, selling off assets or a line of business or assigning a patent or other asset that is the subject of ongoing litigation should retain a copy of any information relevant to the ongoing litigation and provide the litigation opponent with access to the relevant information prior to the conclusion of the reorganization, sale or assignment.

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[1] *See* Fed. R. Civ. P. 34(a)(1).
[2] 2008 WL 1995305 (W.D. Pa. May 6, 2008).
[3] 244 F.R.D. 179 (S.D.N.Y. 2007).
[4] *See Dean v. New Werner Holding Co.*, 2008 WL 2560707, at *7 (D. Kan. Jun. 26, 2008) (noting that "defendant, by its purchase of certain assets of Werner Company, has some degree of control over documents in the possession of Werner Company"); *American Rock Salt Co. LLC v. Norfolk Southern Corp.*, 228 F.R.D. 426 (W.D.N.Y. 2004) (when there is a merger and acquisition, "the acquiring company retain[s] control, if not actual physical custody and possession, Fed. R. Civ. P. 34(a), over the requested [target] documents").

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In the same way, if the organization acquires a business, acquires assets, acquires an interest in a claim or receives an assignment of a patent, the organization should seek a copy of relevant information when acquiring the interest. Moreover, an organization acquiring assets should—

- conduct due diligence on the target's preservation and disposition policies
- review written litigation holds that have been put in place by the target
- ascertain whether subsequent reminders of the litigation hold have been distributed
- evaluate whether the target is actually monitoring compliance with the litigation hold and, if so, how
- assess whether there is actual compliance with the litigation hold.

If, during the course of due diligence, the organization determines that the target has failed to implement or comply with a written litigation hold, the organization should require the target to undertake immediate preservation efforts and notify the court or opposing parties of such failure.

Finally, whether a seller or a purchaser, an organization should contractually obligate the third-party purchaser or seller to preserve relevant information it possesses; provide access to the information; delineate the client's rights in the event of a litigation, subpoena, or government investigation; and grant the right to request preservation of records in the event of subsequent litigation. Any information provision should also provide for an indemnification if the third party fails to retain or turn over relevant information.

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