

INSIGHTS

The U.S. Supreme Court Limits Sanctions to Compensation, Not Punishment

Publications
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It is not every day the U.S. Supreme Court pays attention to matters that affect the practice of discovery, but that day came with *Goodyear Tire and Rubber Co. v. Haeger*, 581 U.S. ____, 137 S.Ct 1178 (April 18, 2017). Writing for a unanimous Court, Justice Kagan explained that when a court exercises its inherent power to sanction bad-faith conduct by ordering a party to pay the other side's legal fees, the award is limited to the fees that would not have been incurred but for the sanctioned party's conduct.

The Court's decision provides useful guidance, but leaves open interesting questions that litigants and district courts will be wrestling with for years to come.

The Facts

The underlying matter is a products-liability case in which the Haegers sued Goodyear Tire & Rubber Company after their motorhome swerved off the road and flipped after one of its tires blew out. The Haegers alleged that Goodyear's G 159 tire was not designed to withstand conditions experienced when used on a motorhome at highway speed levels. Over the course of several years, the Haegers repeatedly requested internal test results for the G 159 tire and Goodyear repeatedly claimed it had produced "all testing data". The Haegers pursued the issue to the point that the District Court "became exasperated with Plaintiff's apparently unsubstantiated claims that additional information must exist."

Like most cases, the parties settled for an undisclosed amount on the eve of trial. And that is the end of the story. . . . Except it wasn't.

Almost a year later, the Haegers' lawyer was reading a newspaper when he discovered that in another case involving the same tire, Goodyear disclosed a set of test results never produced to the Haegers. The results were incriminating; showing that the G 159 became unusually hot at speeds above 55 miles per hour.

District Court

Though the case had settled, the Haegers moved for sanctions. They claimed that Goodyear committed discovery fraud and that the settlement was smaller than it otherwise would have been if Goodyear had produced the test results as they were required to do.

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In its 66 page sanctions order, the Arizona District Court noted 25 times Goodyear's lawyers or designee made false or misleading statements. See *Haeger v. Goodyear Tire and Rubber Co. et al.*, Order, No. CV-05-02024 (D. Ariz. Nov. 8, 2012). The District Court concluded Goodyear engaged in a course of repeated and deliberate bad-faith conduct over several years, which frustrated resolution of the case on the merits.

The District Court then needed to decide what sanctions were appropriate to address Goodyear's misconduct at this late stage in the proceeding. Its options were limited:

- Rule 11 is designed as a deterrent for improper pleadings, motions, and other documents or other misrepresentations to the court and it is unavailable after a final judgment;
- Rule 26(g) is limited to abuses which stem from initial and pretrial disclosures or formal written discovery;
- Rule 30(d) addresses sanctionable conduct during a deposition;
- Rule 37 permits sanctions for violations that occur during disclosure or for the failure to preserve or cooperate during discovery; and
- 28 U.S.C. § 1927 permits the imposition of sanctions against a lawyer, but not a litigant, who engages in dilatory litigation tactics.

The District Court concluded that because the case had settled, no statute or rule permitted it to impose sanctions. Instead, the District Court determined it could use its "inherent powers" to sanction Goodyear, awarding the Haegers \$2.7 million in legal fees and costs. This amount represented the full value of the attorney's fees incurred in the litigation "since the moment, early in the litigation, when Goodyear made its first dishonest discovery response."

The District Court noted that fees awarded must be causally connected to misconduct, but it found an exception where, as in this case, the misconduct occurred early on and rose to a "truly egregious level." Perhaps expecting its decision may be overturned, the District Court also crafted an alternative sanction applicable if it was reversed, which reduced the award to \$2 million for fees incurred that were causally linked to the misconduct.

The Ninth Circuit

The Ninth Circuit affirmed the District Court's award agreeing that a court's inherent authority permitted it to sanction a litigant for an amount it reasonably believed the Haegers incurred "during the time" Goodyear acted in bad faith.

Judge Watford dissented arguing the sanction was punitive, which required protections available to criminal defendants, rather than compensatory, which requires only adequate notice and an opportunity to be heard. He argued that the sanction was not compensatory because there was not a causal connection between the misconduct and the sanction amount.

Supreme Court

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The U.S. Supreme Court agreed with Judge Watford and reversed the Ninth Circuit. The Supreme Court, held that a sanction “order is limited to the fees the innocent party incurred solely because of the misconduct—or put another way, to the fees that party would not have incurred but for the bad faith.” The Court rejected a temporal test that would allow a Court to reach a sanction amount equal to all fees incurred “during the time when [Goodyear was] acting in bad faith”.

The Court explained that discovery sanction “must be compensatory rather than punitive. . . . The fee award may go no further, than to redress wronged parties for injuries sustained.” This *but for* test is not eliminated even if the misconduct rose to a “truly egregious level”.

But there are instances where the *but for* test would permit a court to shift all of a party’s fees, from either the start or some midpoint of a suit. The Court gave several examples, including where a plaintiff initiates suit in bad faith, where a defendant’s entire course of conduct is unethical and part of a scheme to defeat a valid claim, or where a party fails to disclose evidence fatal to its position – essentially all cases where the litigation should have never started or would have ceased immediately if the sanctionable party behaved appropriately.

The Heagers did not show that they had this type of case. They did not demonstrate that the case would have settled as soon as Goodyear divulged the heat-test results. Instead, the Supreme Court agreed with Judge Watford’s dissent that Goodyear would still have had a colorable defense by arguing that the debris in the road was the cause for the blow out, not a defective tire.

Takeaways

While it is helpful that the Supreme Court addressed an important discovery issue – how can a court sanction recalcitrant defendants that refuse to meet their discovery obligations – it is important to not extend it too far. Some commentators have warned that the failure to punish bad actors will result in egregious discovery abuses. This is unlikely given counsel’s duty to the court, the risks a party runs of an adverse ruling while the case is pending, and the likelihood of expensive follow on litigation.

The better way to view this decision is that it provides some level of certainty for discovery sanctions. No discovery process is perfect. And in cases where those mistakes warrant sanctions, it is instructive to know that those sanctions will be tied to the injury caused to the opposing party as opposed to a punitive figure untethered to the amounts at issue in the case or the damages suffered by the parties.