XIII.
The Law and Tactics of Sanctions

By
C. William Phillips, Esq. [1]

Covington & Burling LLP

New York, New York

The law on sanctions motions continues to evolve. For decades, sanctions motions were rare; amendments to Rule 11 in 1983 ushered in an age of roaring sanctions litigation. In 1993, Rule 11 was amended again to curtail excessive litigation over whether underlying lawsuits so utterly lacked merit that counsel should be penalized, and focused instead on deterring such litigation.

The 1993 amendments diminished counsel's incentives to initiate satellite litigation over questions of frivolousness. The creation of a ''safe harbor'' and the change in available remedies, with less emphasis on fee-shifting and more on deterrence, has reduced the motivation to resort to sanctions litigation. But the pendulum may be about to swing again, if the direction of securities litigation is any harbinger. In that area, the combination of Congressional blessing and tightening pleading standards may spell an increase in litigation involving sanctions.

This article explores the current state of the law and analyzes the considerations and tactics in the use of sanctions as a tool in federal litigation.

A. History of Sanctions

Federal law imposing sanctions dates back as far as 1937, when the first version of Rule 11 was adopted as part of the Federal Rules of Civil Procedure. The original Rule 11 was seldom invoked, however, with only a couple of dozen opinions addressing the rule before its amendment in 1983.[2] The 1983 amendments, specifically intended to ''reduce the reluctance of courts to impose sanctions,'' [3] came under widespread criticism, among other reasons, for stimulating incivility among lawyers, inhibiting zealous advocacy, and spawning significant, and often distracting, satellite litigation.[4] These criticisms led to the 1993 amendments, which significantly overhauled the rule and, according to Justice Scalia, ''would render the rule toothless.'' [5]

Perhaps most importantly, the 1993 amendments added a twenty-one day ''safe harbor'' provision that allows counsel to withdraw or to correct offending papers. The ''safe harbor'' and a return to a discretionary standard for the imposition of penalties has dramatically reduced the incidence of sanctions for technical or inadvertent violations. In addition, the amendments' focus on deterrence rather than compensation as a remedy has decreased the financial incentives to seek sanctions because attorney fees are less frequently awarded. The satellite litigation created by the more guarded Rule 11 has subsided.[6]

The trends may be changing again, however, and Rule 11 may well regain some of its potency, not so much because of changes in the rule itself but because of legislative and judicial changes in other pleading standards, which invite open opportunities for a renewed use of the rule. Some statutes—most notably the Private Securities Litigation Reform Act of 1995 (''PSLRA'') [7]—invite scrutiny under Rule 11, and, as discussed below, the Supreme Court's recent tightening of standards in *Tellabs, Inc. v. Makor Issues & Rights, Ltd.*[8] and *Bell Atlantic v. Twombly* [9] may also stimulate increased sanctions litigation, as parties test the new standards against meritless claims. Moreover, Rule 11 is not the only remedy against frivolous litigation; state analogues and the federal statute against vexatious litigation, 28 U.S.C. § 1927, provide other, albeit less-used, means to address lawsuits that are wholly without merit.

B. Sanctions Standards and Procedures

1. Rule 11 of the Federal Rules of Civil Procedure

Under Rule 11, ''[e]very pleading, motion or other paper'' filed with a federal court must be signed by counsel warranting that, to the best of the signer's ''knowledge, information and belief, formed after an inquiry reasonable under the circumstances,'' the statements made in the paper, if factual, have an evidentiary basis or are reasonably based on a lack of information and, if legal, are warranted under existing law or a nonfrivolous argument for the extension or modification of existing law.[10] The signer also warrants that the paper ''is not being presented for any improper purpose, such as to harass or to cause unnecessary delay or needlessly increase in the cost of litigation.'' [11] The rule does not apply to discovery requests, responses, or motions, that are the subject of Rules 26 through 37.[12]

The test under Rule 11 is whether an attorney's conduct was ''objectively reasonable at the time he or she signed the pleading, motion, or other paper.'' [13] Rule 11 sanctions are only appropriate ''where it is patently clear that a claim has absolutely no chance of success under existing precedents, and where no reasonable argument can be advanced to extend, modify or reverse the law as it stands . . . .'' [14] Sanctions should

---

[1] C. William Phillips is co-chair of the firm's litigation group. Mr. Phillips' practice focuses on complex financial litigation, including M&A, securities, corporate control, commercial contract disputes, trade secrets, and bankruptcy. Robert Hemm, of Yale Law School, contributed substantially to the research and drafting of this chapter.

[2] *See* Byron C. Keeling, *Towards a Balanced Approach to Frivolous Litigation*, 21 PEPP. L. REV. 1067, 1074–75.

[3] FED. R. CIV. P. 11 advisory committee note (1983).

[4] *See* Matthew G. Vansuch, *Icing the Judicial Hellholes: Congress's Attempt to Put Out "Frivolous" Lawsuits Burns a Hole Through the Constitution*, 30 SETON HALL LEGIS. J. 249, 290–92 (2006).

[5] Amendments to the Federal Rules of Civil Procedure and Forms (Apr. 22, 1993), *reprinted in* 146 F.R.D. 401, 507 (1993).

[6] Vansuch, *supra* note 4, at 306.

[7] 15 U.S.C. § 78u-4

[8] 127 S. Ct. 2499 (2007).

[9] 127 S. Ct. 1955 (2007).

[10] FED. R. CIV. P. 11(a)-(b).

[11] FED. R. CIV. P. 11(b)(1).

[12] FED. R. CIV. P. 11(d).

[13] Mopaz Diamonds, Inc. v. Inst. of London Underwriters, 822 F. Supp. 1053, 1057 (S.D.N.Y. 1993).

[14] Eastway Const. Corp. v. City of New York, 762 F.2d 243, 254 (2d

be imposed carefully lest they chill the creativity essential to the evolution of the law.[15]

Counsel has a duty to investigate all factual allegations; assertions made without adequate inquiry prior to filing are often sanctionable even if later proven true in discovery.[16] Factual allegations that are not presently supported by evidence should be so designated.[17] Some courts have imposed sanctions even upon pleadings that are well-grounded in facts and law if the pleadings have been filed for an improper purpose.[18]

> *Note*: Sanctions may also be granted for the filing of a frivolous motion for sanctions.[19]

Sanctions proceedings may be initiated either upon motion by one of the parties, or sua sponte by the court through an order directing counsel to show cause why Rule 11 has not been violated.[20] A motion to impose sanctions must be made separately—it cannot be embedded within another case-dispositive motion such as a motion to dismiss—and it must describe the particular conduct alleged to have violated Rule 11.[21] The party opposing a sanctions motion must be given a reasonable opportunity to respond, and is provided a 21-day ''safe harbor'' period in which to withdraw or to correct the offending document or to respond in opposition.[22]

The Advisory Committee to the 1993 amendments noted that monetary sanctions are discouraged because they create a financial incentive to file Rule 11 motions.[23] Instead, courts are given discretion to tailor sanctions to fit the violation, but may not impose sanctions greater than those necessary to deter repetition of sanctioned conduct.[24] Parties have an obligation to mitigate damages from Rule 11 violations, including the filing of a Rule 11 motion as soon as practicable and raising case-dispositive issues in a prompt and cost-efficient manner.[25]

State law is also a source for sanctions, and most states have adopted rules or statutes that generally resemble Rule 11. Many of these states follow the 1983 version of the rule; fewer have incorporated the 1993 amendments.[26] Georgia is a significant outlier, with a very strict sanctions provisions.[27]

2. 28 U.S.C. § 1927

Section 1927 provides that:

> Any attorney . . . who so multiplies the proceedings in any case unreasonably and vexatiously may be required by the court to satisfy personally the excess costs, expenses, and attorneys' fees reasonably incurred because of such conduct.[28]

Only counsel—not clients—may be sanctioned under § 1927; ''[b]ad faith is the key element . . . .'' [29] Moreover, ''bad faith may be inferred 'only if actions are so completely without merit as to require the conclusion that they must have been undertaken for some improper purpose such as delay.' '' [30] For instance, motions to disqualify opposing counsel that were determined to be frivolous and presented for harassment or delay have resulted in sanctions under § 1927.[31] Courts also have imposed sanctions under § 1927 for pursuit or continuance of actions that were clearly time-barred.[32]

There is no clear procedure set forth in the statute for seeking sanctions under § 1927. Requests for an award under the statute may be brought at any time, by separate action or by motion in an existing action.[33]

3. Rule 37 of the Federal Rules of Civil Procedure

Rule 37 governs motions for sanction for discovery violations. Generally, if a motion to compel discovery is granted, Rule 37 also authorizes the court to require the party or deponent whose conduct was at issue to pay the moving party's reasonable expenses (including attorneys' fees) incurred in

---

Cir. 1985); *see also* Simon DeBartolo Group, L.P. v. Richard E. Jacobs Group, Inc., 186 F.3d 157, 167 (2d Cir. 1999).

[15] Katzman v. Victoria's Secret Catalogue, 167 F.R.D. 649, 659 (S.D.N.Y. 1996) (citing Knipe v. Skinner, 19 F.3d 72, 78 (2d Cir. 1994)).

[16] *See* Garr v. U.S. Healthcare, Inc., 22 F.3d 1274, 1279 (3d Cir. 1994); 2 MOORE'S FEDERAL PRACTICE § 11.11(2)(a) (Matthew Bender 3d ed. 1997).

[17] FED. R. CIV. P. 11(b)(3).

[18] The circuits are largely split on the question of whether sanctions can be imposed for filing a complaint or document for an improper purpose even though that complaint may be well-grounded. The Seventh Circuit has held that such filings may be sanctioned. *See* Szabo Food Serv., Inc. v. Canteen Corp., 823 F.2d 1073, 1083 (7th Cir. 1987). By contrast, the Second, Fifth, and Ninth Circuits have held that filing a well-founded document may not be sanctioned, however improper the purpose. *See* Sussman v. Bank of Israel, 56 F.3d 450, 459 (2d Cir. 1995); National Ass'n of Gov't Employees v. National Fed'n of Fed. Employees, 844 F.2d 216, 223, 128 L.R.R.M. (BNA) 2297 (5th Cir. 1988); Golden Eagle Dist. Corp. v. Burroughs Corp., 801 F.2d 1531, 1538 (9th Cir. 1986).

[19] FED. R. CIV. P. 11 advisory committee notes (1993); *see also* Riccard v. Prudential Ins. Co., 307 F.3d 1277, 1294 (11th Cir. 2002) (affirming sanctions against plaintiffs for filing a frivolous motion for sanctions).

[20] FED. R. CIV. P. 11(c)(1).

[21] FED. R. CIV. P. 11(c)(1)(A); *see also* Nuwesra v. Merrill Lynch, Fenner & Smith, Inc., 174 F.3d 87, 94-95 (2d Cir. 1999).

[22] FED. R. CIV. P. 11(c)(1)(A).

[23] FED. R. CIV. P. 11 advisory committee notes (1993)

[24] FED. R. CIV. P. 11(c)(2); *see also* Jayhawk Investments, L.P. v. Jet USA Airlines, Inc., No. 98-2153-JWL, 1999 U.S. Dist. LEXIS 16413, at *2 (D. Kan. Aug. 25, 1999) (''It is well-settled that the primary purpose of Rule 11 sanctions is to deter future violations, rather than to compensate the moving party.'').

[25] *See* Hamil v. Mobex Managed Servs. Co., 208 F.R.D. 247, 250 (N.D. Ind. 2002).

[26] *See* John B. Oakley, *A Fresh Look at the Federal Rules in State Courts*, 3 NEV. L. J. 354, 385 (2003).

[27] GA. CODE ANN. § 9-15-14 (2007); *see also* Keeling, *supra* note 2, at 1106-10 (1994) (describing Georgia's stringent sanctions regime and its chilling effect on litigators).

[28] 28 U.S.C. § 1927.

[29] Wood v. Brosse U.S.A., Inc., 149 F.R.D. 44, 48 (S.D.N.Y. 1993).

[30] Schlaifer Nance & Co., Inc. v. Estate of Warhol, 194 F.3d 323, 336 (2d Cir. 1999) (quoting Shafii v. British Airways, PLC, 83 F.3d 566, 571 (2d Cir. 1996)).

[31] *See, e.g.*, *In re* Wis. Steel Co., 48 B.R. 753 (N.D. Ill. 1985).

[32] *See, e.g.*, Steinle v. Warren, 765 F.2d 95 (7th Cir. 1985).

[33] *See* Gordon v. Heimann, 715 F.2d 531 (11th Cir. 1983).

making the motion. Sanctions may be imposed only after affording a reasonable opportunity to be heard and are not appropriate if the court finds that the nondisclosure was substantially justified or ''that other circumstances make an award of expenses unjust.'' [34]

Rule 37 also provides for sanctions for failure to obey discovery orders. Possible sanctions include the entry of orders establishing facts for the purposes of the action; prohibiting the disobedient party from opposing certain claims or defenses; and striking pleadings or defenses.[35] In addition, the rule provides that the court *shall* require the disobedient party to pay reasonable expenses and attorneys' fees caused by the failure to obey a discovery order, unless the court finds that the failure was substantially justified or an award of fees and expenses otherwise unjust.

4. PSLRA

The Private Securities Litigation Reform Act of 1995 essentially reinstates the 1983 version of Rule 11 for the purposes of securities litigation that falls within its coverage, and makes the imposition of sanctions upon finding a violation mandatory, removing the court's discretion.[36] Upon a final adjudication, the Act requires courts to make [written] findings whether the parties have complied with Rule 11.[37] The Act focuses specifically upon complaints, and presumptively imposes an award of attorneys' fees and expenses if a complaint is in ''substantial'' violation of Rule 11.[38]

C. Strategic Uses of Sanctions Motions

The common wisdom among litigators is that judges generally hate sanctions motions, and particularly if they are not well-founded. Indeed, much of the criticism of the 1983 Amendments to Rule 11 focuses on the satellite litigation created by those amendments.[39] Judge Schroeder of the Ninth Circuit observed that ''[a]sking judges to grade the accuracy of advocacy in connection with every piece of paper filed in federal court multiplies the decisions which the court must make as well as the cost for litigants.'' [40] Thus, encouragement of sanctions litigation tended to undercut the very goals that the availability of sanctions was intended to achieve: streamlining litigation and court dockets by penalizing frivolous litigation. Instead, valuable court resources were used sorting through satellite sanctions litigation.

As a tactical matter, then, counsel is less likely to press motions for sanctions unless they address serious issues and cannot be easily avoided. Because it provides a pathway to avoid a sanctions motion, the ''safe harbor'' provision of the 1993 amendments, in practice, has the effect of reducing frivolous litigation; the ability to withdraw a paper filed with a mistaken or even frivolous assertion means that litigants are less likely to file sanctions motions to try to gain advantages from inadvertent mistakes. Moreover, the ''safe harbor'' provision makes it easier for complaining counsel to raise the issue of sanctions by invoking Rule 11; the decision about whether to pursue a motion can be made after reviewing the response. And the decision of counsel to stand by a paper challenged as frivolous—rather than withdraw it or change it to address the alleged problem—increases the likelihood that the issue to be presented is serious and material to the litigation.

Congress's decision to make sanctions review mandatory in the securities litigation area paradoxically also tends in practice to reduce the amount of litigation over sanctions, while discouraging frivolous complaints. The requirement of mandatory review after a final adjudication means that, at least with respect to complaints, the issue can be put off until a final adjudication. Since the vast majority of securities lawsuits that survive a motion to dismiss eventually settle, there is never a final adjudication and the mandatory sanctions review usually never happens.

The same may be true of actions to enforce Section 1927. The determination of vexatiousness is difficult to make before the conclusion of litigation, and therefore the statute is most commonly directed to cost recovery at the end of a lawsuit. But most lawsuits settle, thus eliminating the incentives for the parties to continue to fight after coming to agreement to end their differences. And even where the parties continue to fight to the bitter end, most litigators know that the last thing that the court wants to hear, after deciding a case or presiding over the decision by a jury, is a motion attacking the other side for vexatious litigation. By that time the damage is done; the motion cannot be used to dissuade the other side from pursuing litigation.

There are still strategic uses of sanctions motions, however, to achieve litigation ends, including uses in addition to the imposition of sanctions. Of course, most important is the rationale for the sanctions statutes themselves— to dissuade an adversary from pursuing a certain set of wholly meritless and resource-wasting claims or arguments, and the ''safe harbor'' rule largely facilitates this effect. However, sanctions motions can also be used in an attempt to prevent opposing counsel from misusing the limited record available to defeat a Rule 12(b)(6) motion. For example, sanctions motions can be used to bring to the court's attention ''smoking gun'' evidence that completely undercuts a complaint or answer, which might not be easily done on a motion to dismiss because of its exclusive focus on the allegations of the complaint. Furthermore, sanctions motions are sometimes used as distractions by better funded adversaries to create a litigation sideshow—perhaps even with discovery—at least until a court comes to share that view.

The Supreme Court's recent decisions in a pair of cases, *Bell Atlantic Corp v. Twombly* [41] and *Tellabs, Inc. v. Makor Issues & Rights, Ltd.*,[42] may also encourage increased use of sanctions motions against frivolous pleadings. *Twombly* revises longstanding precedent of *Conley v. Gibson* [43] on pleading requirements under Rule 8, holding that thin and speculative

[34] FED. R. CIV. P. 37(a)(4)(A).
[35] FED. R. CIV. P. 37(b)(2).
[36] 15 U.S.C. § 78u-4(c)(2).
[37] 15 U.S.C. § 78u-4(c)(1)
[38] 15 U.S.C. § 78u-4(c)(3)(A)(ii).
[39] *See* Keeling, *supra* note 2, at 1083-86.
[40] Golden Eagle Distrib. Corp. v. Burroughs Corp., 801 F.2d 1531, 1540 (9th Cir. 1986).
[41] 127 S. Ct. 1955 (2007).
[42] 127 S. Ct. 2499 (2007).
[43] 355 U.S. 41 (1957).

facts combined with conclusory allegations are no longer sufficient.[44] *Tellabs* interprets the PSLRA's requirement that securities fraud complaints plead facts giving rise to a ''strong inference,'' construing the statute to require facts supporting an inference of scienter that is ''cogent and at least as compelling'' as any innocent interpretation.[45] As plaintiffs are pushed to make stronger and potentially less supportable factual allegations in their complaints to avoid dismissal under these standards, they may increasingly risk running afoul of Rule 11. Counsel defending such claims may find an increase in opportunities to use the threat of sanctions to dissuade plaintiffs from pursuing litigation.

[44] *See Twombly*, 127 S. Ct. at 1965-66.

[45] *Tellabs*, 127 S. Ct. at 2504-05.

