YOUNG CONAWAY

CLIENT ALERT

# *Goldstein v. Denner, et al.*

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On January 26, 2024, the Delaware Court of Chancery issued an opinion in *Goldstein v. Denner, et al.,* C.A. No. 2020-1061-JTL ("*Goldstein*") granting plaintiff's request for sanctions against defendants for failing to preserve text messages (the "Opinion").[1] Therein, the Court imposed two adverse evidentiary inferences and increased the burden of proof for defendants at the upcoming trial. In connection with issuing these sanctions, the Court addressed when preservation obligations arise and outlined its expectations for when and how text messages should be preserved.

With trial scheduled to begin in April 2024, defendants filed an application asking the Court to certify an interlocutory appeal of the Opinion to the Delaware Supreme Court (the "Supreme Court"). On February 26, 2024, the Court denied that application.[2] Defendants continued to pursue an interlocutory appeal with the Supreme Court, which was denied on March 14, 2024.[3]

## I. Summary of the Decisions

Facts

Alexander Denner ("Denner") is the founder and controlling principal of Sarissa Capital ("Sarissa"), an activist hedge fund. In 2017, Denner was also a director of Bioverativ, Inc. ("Bioverativ").

Sanofi SA ("Sanofi") approached Denner and another Bioverativ director expressing an interest in acquiring Bioverativ. Denner and the other director allegedly told Sanofi that the time was not right for an acquisition. Days after Sanofi's overture, Sarissa began purchasing Bioverativ stock. Based on these acquisitions, Sarissa allegedly stood to make significant profits if a transaction

[1] *Goldstein v. Denner, et al.*, C.A. No. 2020-1061-JTL, 2024 WL 303638 (Del. Ch. Jan. 26, 2024).
[2] *Goldstein v. Denner, et al.*, C.A. No. 2020-1061-JTL, 2024 WL 776033 (Del. Ch. Feb. 26, 2024).
[3] *Denner, et al. v. Goldstein*, C.A. No. 80, 2024, 2024 WL 1103110 (Del. Mar. 14, 2024).

with Sanofi happened at least six months after the purchases. As such, plaintiff alleges that Denner delayed a transaction with Sanofi so that Sarissa could reap these profits. A Bioverativ-Sanofi transaction was announced on January 21, 2018.

In connection with the transaction, on February 21, 2018, Bioverativ circulated a litigation hold. Sanofi issued a litigation hold on March 15, 2018. Denner received both.

Thereafter, on September 4, 2019, the Securities and Exchange Commission ("SEC") subpoenaed Denner and Sarissa seeking documents about trading in Bioverativ securities. The next day, on September 5, 2019, Sarissa's general counsel circulated a litigation hold to "All staff" – which included Denner.

After circulating the hold, Sarissa's general counsel spoke with outside counsel about implementation of the hold, and they discussed text messaging. Sarissa's general counsel represented that he did not text for business purposes and that he did not believe that Denner did either, but that he would confirm. He later represented to outside counsel that he reviewed Denner's text messages and confirmed that there were no relevant texts. Based on those representations, the general counsel and outside counsel agreed to hold off on collecting text messages but asked that text messages be preserved.

On December 15, 2020, plaintiff filed suit alleging that that Denner and Sarissa engaged in insider trading in connection with the Sanofi-Bioverativ transaction. In response to the lawsuit, Denner and Sarissa moved to dismiss the claims. After completing briefing, plaintiff served document requests in September 2021. Denner and Sarissa sought to stay discovery, and that request was denied.

In November 2021, after the request to stay discovery was denied – and almost a year after the litigation was initiated – Denner and Sarissa started to collect documents. Neither Denner nor any other Sarissa custodians had any texts despite the fact that other defendants produced text messages from Denner. Denner apparently lost all of his texts when he upgraded his phone, another custodian's phone allegedly fell in a swimming pool, and a third custodian had his phone set to delete texts after thirty days. And, the text messages from the three phones were not backed up to the cloud or to other devices.

## Relevant Rulings

The Court held that Denner and Sarissa should have taken steps to preserve data sooner – and, if they had, text data would not have been lost. As to timing, the Court held that "[t]he plaintiff filed the case in December 2020. Defense counsel should have started taking steps to identify and preserve information *by at least then*"[4] – and "undoubtedly [the duty to preserve] arose much earlier"[5] – even before the first litigation hold was issued in February 2018 – because "litigation involving M&A transactions is sufficiently common that Denner and Sarissa should have reasonably anticipated litigation challenging the Bioverativ-Sanofi transaction."[6]

[4] *Goldstein*, 2024 WL 303638, at *7 (emphasis added).
[5] *Id.* at *16.
[6] *Id.*

The Court explained that part of preserving data includes identifying the reasonably likely sources of information and taking "reasonable" – not necessarily perfect – "steps to collect and preserve it."[7] As to specifically how Denner and Sarissa should have preserved text messages, the Court held that steps could have included "imaging phones or backing up [phone] data."[8] None of this was done, and Denner and Sarissa were unable to "com[e] forward with other locations where the texts might be found"[9] – such as from Denner's phone carrier or third-parties.

The Court found that Denner and Sarissa's failure to preserve the text messages was, at a minimum, reckless. To remedy the prejudice to plaintiff, the Court issued sanctions holding that the Court "will presume at trial that the hedge fund traded on the basis of a non-public approach"[10] from Sanofi, and that Sarissa's "trading caused the sale process to fall outside a range of reasonableness."[11] The Court also held that it would "require the defendants to meet a burden of proof that is increased by one level" such that, "[r]ather than rebutting the presumptions or proving issues by a preponderance of the evidence, the defendants will have to adduce clear and convincing evidence."[12] The Court also awarded plaintiff fees and expenses in pursuing the motion.

In response to the Opinion, defendants filed an application with the Court to certify an interlocutory appeal, and one of their arguments was that in the Opinion the Court adopted "new, difficult-to-impossible discovery standards, and penalized Defendants for not satisfying them" and that the "Opinion requires every potential litigant in Delaware to undergo the costly and invasive process of creating full forensic images of every potential custodian's phones every time they anticipate litigation."[13]

The Court rejected defendants' argument, stating:

> Contrary to the defendants' alarmist framing, the Opinion did not hold that everyone who might be a custodian in a Delaware action must image their phones immediately after receiving a litigation hold. Yes, the Opinion states that the defendants, 'should have taken steps to preserve ESI, including by imaging phones or backing up their data. . . . In a world where people primarily communicate using personal devices, it will almost always be necessary to image or backup data from phones.' But the defendants seem not to understand the disjunctive conjunction 'or.' The sentence that the defendants pick out spoke of *either* making an image *or* backing up data.

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[7] *Id.* at *19.
[8] *Id.* at *21. *See also id.* at *2 ("The hedge fund and its principal failed to take reasonable steps to preserve texts, most notably by not imaging any personal devices."); *id.* at *23 ("A reasonable preservation effort would have resulted in counsel imaging or backing up both phones.").
[9] *Id.* at *17.
[10] *Id.* at *2.
[11] *Id.*
[12] *Id.*
[13] *Goldstein*, 2024 WL 776033, at *24 (quoting defendants' application for interlocutory appeal).

> The Opinion did not establish a rigid checklist or bright line rule. It reiterated that parties must take reasonable steps to preserve evidence in a world where texts are often a source of evidence. A party can image or back-up a device to ensure there is no data loss. Or a party could turn off auto-delete features and let the texts accumulate. Or a party could just collect the text messages.[14]

After the Court denied defendants' interlocutory appeal application, defendants continued to pursue an appeal with the Supreme Court. On March 14, 2024, the Supreme Court held that "interlocutory review is not warranted" because "the Court of Chancery's decision in a discovery matter does not meet the strict standards for certification."[15] The Supreme Court concluded by noting that "[t]rial is scheduled for next month, and the defendants may raise their claims of error on appeal following the entry [of] a final judgment if they are unsuccessful."[16]

## II. Key Takeaways

***When does the duty to preserve arise?*** As outlined by the Court in *Goldstein*, the duty to preserve often arises well before litigation is initiated – when litigation is reasonably anticipated. Often, this duty coincides with the issuance of a litigation hold, but the duty can arise well before then. Indeed, in *Goldstein*, the Court noted that that the duty to preserve "undoubtedly arose much earlier" than the issuance of the first litigation hold "because litigation involving M&A transactions is sufficiently common such that Denner and Sarissa should have reasonably anticipated litigation challenging the Bioverativ-Sanofi transaction well before that."[17] The Court did not, however, specify precisely when that might have been – such as when Sanofi first reached out to Denner, or later as negotiations developed, or when the board approved the merger. *Goldstein* suggests that when negotiating an M&A transaction, a party to negotiations should carefully consider whether, under the circumstances, there is a duty to preserve.

***For purposes of preservation, is circulating a litigation hold enough?*** While circulating a litigation hold is important, and often a first step, the Court may not view it as enough for purposes of preservation. In *Goldstein,* the Court held that the "organization must take steps to ensure that the recipients of the hold understand what it means and abide by it."[18] This is particularly true for data that a company does not control – such as personal email and text messages – the latter of which was the Court's focus in *Goldstein*.

***How should data be preserved?*** When a duty to preserve arises, "a party must act reasonably to preserve the information that it knows, or reasonably should know, could be relevant to the litigation, including what an opposing party is likely to request."[19] The standard, however, is not perfection – it is reasonableness – which requires "first taking reasonable steps to identify the information that should be collected and preserved."

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[14] *Id.* at *25-26.
[15] *Denner*, 2024 WL 1103110, at *1.
[16] *Id.*
[17] *Goldstein*, 2024 WL 303638, at *16.
[18] *Id.* at *19.
[19] *Id.* at *18.

Importantly, there is not a "rigid checklist or bright line rule"[20] for preservation. For phone data, which was the Court's focus in *Goldstein*, there are a variety of ways to ensure the data is preserved: "A party can image or back-up a device to ensure there is no data loss. Or a party could turn off auto-delete features and let the texts accumulate. Or a party could just collect the text messages."[21] The specific approach taken will likely depend on the circumstance of the given case. In any case, it will likely be important to speak with custodians of potentially relevant data at the outset of litigation, if not sooner, to determine potential sources of data and methods of ensuring the data is preserved.

[20] *Id.* at *19.
[21] *Goldstein*, 2024 WL 776033, at *26.