

***Foster v. Dingwall*, 126 Nev. Adv. Op. 6 (Feb. 25, 2009)¹**

CIVIL PROCEDURE – SANCTIONS

Summary

This case pertained to a contracts action. Appellants appealed the district court’s decision to strike the appellants’ pleadings and enter a default judgment against them as a discovery sanction, as well as the district court’s decision to award compensatory damages and attorney and special master fees to the appellees.

Disposition/Outcome

Affirmed in part and reversed in part. The Nevada Supreme Court, sitting en banc, held that the district court did not abuse its discretion when it struck the pleadings and entered a default judgment because it acted pursuant to NRCP 37(b) (2) (C),² and (d).³ Furthermore, the Court upheld Dingwall’s compensatory damages award because he established a prima facie case for such damages during the NRCP 55 (b) “prove up hearing.”⁴ However, the Court held the district court did abuse its discretion when awarding Yang and Chai compensatory damages because the award was duplicative, or in the alternative, because appellees Yang and Chai did not establish a prima facie case against the appellants. Finally, the court held the district court did not abuse its discretion when it awarded all appellees attorney and special-master fees.

Facts and Procedural Background

The underlying dispute in this case arose in August 2005 when Innovative Energy Solutions, Inc. (“IESI”), a full-service energy corporation, filed suit against Dingwall, a director at IESI.⁵ On behalf of IESI, Dingwall filed an amended answer and third-party complaint, where he asserted claims against appellants Dornan, Foster, Cochrane, directors of IESI, in their individual capacities. Shareholders Yang and Chai filed a motion to intervene on behalf of Dingwall, which the district court granted, and Yang and Chai subsequently asserted derivative claims against Dornan, Foster and Cochrane. Yang and Chai also alleged that IESI was mismanaging corporate assets.⁶ In response to these allegations, the district court appointed a special master to examine the records at IESI.⁷

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² NEV. R. CIV. P. 37(d) permits a court to enter sanctions against a party who fails to attend his or her depositions. Sanctions include striking a party’s pleadings and entering a default judgment. *Id.* at 37 (b) (2) (C).

³ *Id.* at 37(d).

⁴ A prove-up hearing is when the trial court “determine[s] the amount of damages” to award a prevailing party after the court entered a default judgment against the defaulting party. *Id.* at 55(b)(2).

⁵ IESI alleged that Dingwall breached his corporate fiduciary duties, usurped corporate opportunities, and engaged in civil conspiracy and conversion.

⁶ Specifically, Yang and Chai sought to recover individually for either intentional or negligent misrepresentation, alleging that they were wrongfully induced by Dornan, Foster, and Cochrane into selling or transferring their stock.

⁷ The district court held a hearing concerning appointment of a special master. During the hearing, the parties and the court discussed how the special-master fees would be allocated. Foster and Cochrane agreed to split the fees

During discovery, Dingwall arranged to depose Dornan, Foster, and Cochrane. However, counsel for Dornan, Foster, and Cochrane later informed Dingwall that he could not proceed because he had motioned the district court to withdraw because his clients did not pay their legal fees.⁸ Foster also stated that he would not attend his deposition because he was in poor health and unable to pay for legal counsel to represent him. As a result, neither Dornan, Foster, nor Cochrane attended the arranged deposition.

Dornan, Foster, and Cochrane continued to ignore the district court's discovery orders. The three failed to appear to another deposition and also provided deficient responses to interrogatories and requests for production of documents. Dingwall thereafter filed his first motion for the court to strike the pleadings and enter default under NRCP 37(b) (2) (C). Yang and Chai joined this motion. Neither Dornan, Foster, nor Cochrane opposed Dingwall's motion for sanctions. Thus, pursuant to Eighth Judicial Court Rule (EDCR) 2.20(c), the court deemed all allegations in Dingwall's motion admitted.

The district court did not immediately grant Dingwall's motion, but ordered Dornan, Foster, and Cochrane to attend their depositions within thirty days and to supplement their deficient responses to interrogatories and requests for production of documents within ten days of that date (January 12, 2007). Dornan, Foster and Cochrane failed to comply with the district court's order.⁹ Thereafter, Dingwall filed a second motion seeking to strike the pleadings against him and requesting that the court enter a default judgment against Dornan, Foster and Cochrane. Following an evidentiary hearing, the district court granted Dingwall's motion and announced it would hold a prove-up hearing to determine the amount of damages.

At the prove-up hearing, Dingwall testified that he had worked with a certified public accountant to calculate an estimate of damages. He also presented demonstrative evidence to show how his causes of action related to the damages sought. Second, the district court heard from Yang, who testified that his derivative claims were based on the testimony and evidence presented by Dingwall.

The district court subsequently entered a judgment detailing its findings of fact, conclusions of law, and award of damages. The district court ultimately awarded Dingwall, derivatively on behalf of IESI, compensatory damages totaling approximately 2,890,000 dollars, and punitive damages for approximately 8,673,000 dollars. In response to Yang and Chai's request to reinstate their IESI stock, the district court declared that Yang and Chai were entitled to their vested shares. The district court also awarded Yang and Chai compensatory damages totaling 15,000,000 dollars and punitive damages totaling 45,000,000 dollars.¹⁰ The district court further awarded Dingwall, Yang and Chai attorney fees and special-master fees. Dornan, Foster and Cochrane appealed.

equally. However, the court informed the parties that, after the disposition of the case, the losing party must pay the prevailing party the fees that the latter paid to the special master.

⁸ The district court ultimately granted counsel's motion to withdraw.

⁹ Foster actually did attend his deposition, but the district court determined that he failed to answer many relevant questions.

¹⁰ Although the district court awarded punitive damages to Dingwall, Yang, and Chai, all three parties withdrew their claims for punitive damages during oral argument. Therefore, the Court did not address the propriety of the punitive damages award in its opinion.

Discussion

District Court's Decision to Strike the Pleadings and Enter Default Judgment

The Court first addressed the issue of whether the district court abused its discretion when it struck the pleadings and entered a default judgment against appellants. Ordinarily, the Court reviews imposition of discovery sanctions under the abuse of discretion standard.¹¹ However, the Court uses a heightened standard of review where the district court's sanction strikes the pleadings, resulting in dismissal with prejudice. Under this somewhat heightened standard, the district court abuses its discretion if its sanctions are not just and do not relate to the claims at issue in the discovery order that the defaulting party violated.

The Court held, primarily, that the provisions of the NRCP granted the district court the power to impose discovery sanctions. NRCP 37 (b) (2) (C) and (d) specifically provide that the court may strike a party's pleadings if that party fails to attend his or her own deposition. Moreover, the Court stated that it had upheld entries of default in the past where litigants were unresponsive, like appellants, and similarly engaged in abusive litigation practices that cause interminable delays.¹² The Court also urged that discovery sanctions were appropriate in this case to deter future litigants from disobeying court orders. Finally, the Court noted that the district court had drafted a lengthy strike order, which set forth detailed findings of fact, conclusions of law, and the factors found in *Young v. Johnny Ribeiro Building*¹³ that a court should consider when imposing such a discovery sanction. Accordingly, the Court held the district court did not abuse its discretion when it decided to strike appellants' pleadings and enter a default judgment against them.

Compensatory Damages Awarded to Dingwall

The Court next addressed the issue of whether the district court abused its discretion when it awarded compensatory damages to Dingwall. The Court first noted that the district court had the authority to conduct a prove-up hearing under NRCP 55 to determine the amount of damages against the defaulting party. The Court added that, in the hearing, the non-offending party need only establish a prima facie case in order to obtain the default judgment.¹⁴

The Court proceeded to clarify what exactly constitutes a prima facie case and how the courts and the parties interact in a NRCP 55(b) prove-up hearing. Reasoning from precedent, the Court concluded that the non-offending party establishes a prima facie case when it sufficiently demonstrates, by substantial evidence, that it is entitled to the damages or relief sought.¹⁵

¹¹ *Young v. Johnny Ribeiro Building*, 106 Nev. 88, 92, 787 P.2d 777, 779 (1990).

¹² *See, e.g., id.* 106 Nev. at 94, 787 P.2d at 780; *Temora Trading Co. v. Perry*, 98 Nev. 229, 230-31, 645 P.2d 436, 437 (1982). *See also* *Hamlet v. Reynolds*, 114 Nev. 863, 865, 963 P.2d 457, 458 (Nev. 1998) (upholding the district court's strike order where the defaulting party's "constant failure to follow [the court's orders] was unexplained and unwarranted.").

¹³ *See Young*, 106 Nev. at 93, 787 P.2d at 780.

¹⁴ *See id.* at 95, 787 P.2d at 781.

¹⁵ The Court drew from *Young* to establish this burden. In that case, the party seeking damages substantiated their damages assessment by including fifteen pages worth of accounting partnership disbursements, receipts, liabilities,

Furthermore, the Court held that while the district court has broad discretion to administer the prove-up hearing as it deems appropriate under NRCP 55(b)(2), it must be wary of any “fundamental defect[s]”¹⁶ in the non-offending party’s case.¹⁷ The Court added that the defaulting party may present evidence indicating a fundamental defect with a non-offending party’s case during a prove-up hearing. The Court warned that disregarding such defects could constitute an abuse of discretion.

After a careful review of the record, the Court held that Dingwall presented sufficient evidence to support a prima facie case for each derivative cause of action for three reasons. First, the factual allegations contained in Dingwall’s amended complaint sufficiently demonstrated that he was entitled to the relief he sought as it related to each cause of action. Second, Dingwall presented substantial evidence at the prove-up hearing to support his claim for damages.¹⁸ Third, the district court did not unnecessarily prevent appellants from participating in the prove-up hearing. Appellants cross-examined Dingwall, and although the court allowed them the opportunity, they declined to cross-examine Dingwall’s certified public accountant. In light of these reasons, the Court concluded that the district court did not abuse its discretion when it awarded compensatory damages to Dingwall.

Compensatory Damages Awarded to Yang and Chai

The Court next addressed the issue of whether the district court abused its discretion when it awarded Yang and Chai compensatory damages. The Court first observed that Yang and Chai principally sought declaratory judgments—the reinstatement of their stock ownership at IESI and the cancellation of appellants’ stock—which the district court granted. However, the district court *also* awarded monetary relief (15,000,000 dollars). The Court considered the latter award duplicative recovery for a single cause of action.

Even if the award was not duplicative, the Court concluded that Yang and Chai did not present sufficient evidence to establish a prima facie case for intentional or negligent misrepresentation. Because both intentional and negligent misrepresentation require a showing that the claimed damages were caused by the alleged misrepresentations, it was insufficient for Yang and Chai to merely assert the fact that they were damaged without showing substantial evidence of the harm caused by the misrepresentation. Thus, because the award was duplicative and Yang and Chai did not present substantial evidence to show the award was related to the harm caused, the Court held the district court abused its discretion and reversed its judgment awarding Yang and Chai compensatory damages.

and assets. *Id.* The court suggested that this was an example of substantial evidence proving that the party seeking damages is entitled to relief.

¹⁶ *See id.*

¹⁷ Examples of fundamental defects the court cites are when the non-offending party seeks monetary damages without demonstrating entitlement to the relief sought or when the damage award is unreasonable or violates due process.

¹⁸ For instance, Dingwall testified that he arrived at his damages estimate by working with a certified public accountant to review roughly 50,000 pages of documents gathered over the past two years. Furthermore, Dingwall presented evidence to show that, as directors of IESI, Foster used corporate funds to advance a competing entity (IESI Canada); that Dornan, Foster, and Cochran used IESI corporate funds for their personal benefits; and that advances were made toward a company that had no business relationship with IESI. Dingwall then demonstrated how he estimated and calculated the damages as a result of these indiscretions.

Attorney and Masters Fees

The next issue the Court addressed was whether the district court abused its discretion when it awarded the appellees attorney fees after it entered default judgment against appellants. The Court noted that NRCPC 37(b) (2) permits the district court to require the offending party to pay reasonable attorney fees as sanctions for discovery abuses. The Court upheld the attorney fee sanctions based on the appellants' repetitive, abusive, and recalcitrant actions. Furthermore, the Court cited the fact that appellants' claims and defenses were not based in law or fact and, as such, were frivolous and brought in bad faith.¹⁹ In light of such considerations, the Court held the district court did not abuse its discretion when it awarded the appellees attorney fees.

The final issue the Court addressed was whether the district court abused its discretion when it awarded the appellees special master-fees. The Court held that because the district court clearly communicated in a previous hearing that the special-master fees were recoverable by the prevailing party, the district court did not abuse its discretion when it awarded special masters fees to appellees.

Concurrence in Part and Dissent in Part

Justice Cherry, joined by Justices Pickering and Saitta, concurred in part and dissented in part. The Justices agreed that the award of damages to Yang and Chai was duplicative and not supported by substantial evidence. However, these Justices thought that the appellant did not display the requisite degree of willfulness necessary to support the striking of pleadings and ordering of sanctions and that the sanctions were too severe in light of the totality of the circumstances.²⁰

Conclusion

The Nevada Supreme Court concluded that the district court did not abuse its discretion when it struck appellants pleadings and entered a default judgment against them. Furthermore, appellee Dingwall was entitled to compensatory damages because he established substantial evidence of such damages at the prove-up hearing. However, the district court abused its discretion when it awarded Yang and Chai compensatory damages because such damages were duplicative and Yang and Chai did not establish substantial evidence of such damages. Finally, the Court held the district court did not abuse its discretion when it awarded all appellees attorney and special-master fees.

¹⁹ NEV. REV. STAT. § 18.010(2) (b) (2007) permits a district court to award attorney fees when a party's claims are brought without a reasonable ground or to harass a prevailing party.

²⁰ Among other factors, the Justices noted that Dornan suffered from health problems and was unable to comply with discovery requests and that the district court failed to properly consider the appellants reasons for noncompliance.