

(ENDORSED)
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DAVID H. YAMASAKI
Chief Executive Officer/Clerk
Superior Court of CA County of Santa Clara
BY Henry Keniston DEPUTY

SUPERIOR COURT OF CALIFORNIA
COUNTY OF SANTA CLARA

KWAN SOFTWARE ENGINEERING, INC.,
dba VERIPIC, INC.,

Plaintiff,

vs.

FORAY TECHNOLOGIES, LLC, ET AL.
Defendants,

AND RELATED CROSS-ACTION.

Case No. 1-09-CV-149780

INTERIM ORDER RE:

(1) COURT'S ORDER TO SHOW
CAUSE WHY PLAINTIFFS AND
THEIR COUNSEL HAVE NOT
VIOLATED CODE OF CIVIL
PROCEDURE SECTION 128.7(B);
ORDER TO SHOW CAUSE WHY
PLAINTIFFS AND THEIR FORMER
COUNSEL SHOULD NOT BE
SUBJECT TO MONETARY, ISSUE,
EVIDENTIARY AND TERMINATING
SANCTIONS FOR THEIR CONDUCT
PURSUANT TO THE COURT'S
INHERENT AUTHORITY AND THE
DISCOVERY ACT; and,

(2) DEFENDANT FORAY'S
MOTIONS FOR MONETARY AND
TERMINATING SANCTIONS

On September 19, 2014, at 9:30 a.m., in Department 9, defendants Thomas Hennings ("Hennings") and Foray Technologies, LLC's ("Foray") (collectively, "Defendants") and plaintiffs John Kwan ("Kwan"), Kwan Software Engineering, Inc. dba VeriPic, Inc.'s ("VeriPic"

1 or “corporate plaintiff”) (collectively, “Plaintiffs”) and Plaintiffs’ former counsel, George Grellas
2 (“Grellas”) and Dhaivat Shah (“Shah”) of Grellas Shah LLP were given the opportunity to
3 present further evidence, testimony and argument regarding the Court’s order to show cause why
4 Plaintiffs and their former counsel have not violated Code of Civil Procedure section 128.7, and
5 the Court’s order to show cause why Plaintiffs and their former counsel should not be subject to
6 monetary, issue, evidentiary and terminating sanctions for their conduct pursuant to the Court’s
7 inherent authority and the Discovery Act (“Court’s OSC”). In making these findings and orders,
8 the Court has considered the various pleadings, briefs, memoranda, and declarations filed by the
9 respective parties in connection with this OSC and related motions, the testimony and evidence
10 presented, the arguments made, and the documents contained within the Court’s file.

11 **I. Procedural History**

12 On March 21, 2014, the Court first heard argument and received testimony and evidence
13 on Defendants’ motion for terminating and monetary sanctions pursuant to the Civil Discovery
14 Act and Code of Civil Procedure section 128.7 (“Defendants’ Motion for Sanctions”).
15 Following that hearing, on May 2, 2014 the Court issued its OSC, and with the agreement of the
16 parties, ultimately set the Court’s OSC for hearing on September 19, 2014.

17 After full consideration of the evidence submitted, the arguments made at the hearing,
18 and the authorities submitted by each party, the court makes the following rulings and findings as
19 to the Court’s OSC and Defendants’ Motion for Sanctions:

20 On March 21, 2014, Kwan and VeriPic appeared at an evidentiary hearing ordered by the
21 Court on the Defendants’ Motion for Sanctions. Although Kwan and VeriPic were still
22 represented at that time by Grellas Shah, attorney Mark Fredkin appeared on a limited scope
23 basis for VeriPic, and attorney Gregory Hull appeared on a limited scope basis for Kwan,
24 because of the Court’s expressed concerns about a conflict of interest. Grellas Shah also
25 appeared at that hearing.

26 At the March 21, 2014 hearing, when called to testify Kwan asserted his Fifth
27 Amendment right not to incriminate himself as to all questions directed to him regarding any
28 issues involving this case. VeriPic produced no other corporate representative to testify in

1 response to the Defendants' Motion for Sanctions. Earlier, at the deposition of VeriPic's person
2 most knowledgeable ("PMK") on all matters related to the pending motion for sanctions, the
3 corporate plaintiff VeriPic designated Kwan to testify as its PMK. Kwan claimed a Fifth
4 Amendment right against self-incrimination as to all questions at the VeriPic deposition, and, in
5 light of Kwan's refusal to so testify, Defendants' counsel terminated the deposition. At the
6 hearing on March 21, 2014, attorneys George Grellas and Dhaivat Shah (who were subpoenaed
7 as witnesses), also declined to answer most questions on the instruction of their client, on the
8 basis that any such answers would have the potential to incriminate their client.

9 Based on the evidence and testimony presented at the March 21, 2014 hearing on Moving
10 Defendants' Motion for Sanctions, and based on the Court's own review of the documents filed
11 in this case, the Court expressed in its OSC that it appeared that Plaintiffs: presented papers to
12 the Court primarily for an improper purpose, such as to harass or to cause unnecessary delay or
13 needless increase in the cost of litigation; presented and relied upon allegations and other factual
14 contentions that lacked evidentiary support or, were unable to demonstrate evidentiary support
15 after a reasonable opportunity for further investigation or discovery; and, denied factual
16 contentions that were not warranted on the evidence, in violation of Code of Civil Procedure
17 section 128.7, subdivisions (b)(1)-(4). Moreover, the Court found that it appeared that the
18 misconduct of Plaintiffs and Plaintiffs' counsel's in the course of litigation and pervasive
19 litigation abuse was so egregious and deliberate such that no sanction other than dismissal is
20 adequate to ensure a fair trial. Plaintiffs correctly state that the wording of the OSC was intended
21 to provide Plaintiffs and their counsel, Grellas Shah, an opportunity to establish that the
22 impressions stated in the OSC were not correct, and that sanctions were not appropriate.

23 Accordingly, Plaintiffs Kwan and VeriPic, and Plaintiffs' counsel, Grellas, Shah, and
24 David I. Siegel ("Siegel") were ordered to show cause as to why monetary, issue, evidentiary and
25 terminating sanctions should not be issued against them pursuant to Code of Civil Procedure
26 section 128.7, subdivisions (b)(1)-(3), the Discovery Act, Business & Professions Code sections
27 6068 subdivisions (c) & (d), and the Court's inherent authority to properly administer justice and
28

1 to preserve the Court’s integrity.¹ Kwan, VeriPic, and Grellas Shah appeared at the September
2 19, 2014 hearing on the Court’s OSC. Although declarations were filed by Grellas Shah and
3 Mark Fredkin in response to the Court’s OSC, no further declaration or testimony from Kwan or
4 any other VeriPic representative was presented before or at the time of the hearing.

5 In general, the Court incorporates the factual statements in the Court’s OSC, and in
6 general finds those factual statements to be true, except as otherwise provided below.

7 **II. Analysis of and Findings on Court’s OSC**

8 **A. *Grellas Shah***

9 In the Court’s order to show cause, with respect to Grellas Shah and attorneys Grellas,
10 Shah and Siegel, the Court stated:

11 Despite conceding that “the Court eviscerated the legal grounds to
12 continue pursuing claims based on the Caveat Emptor and related
13 communications,” Plaintiffs and their attorneys —the law firm of
14 Grellas Shah LLP, and attorneys Grellas, Shah and Siegel—
15 continued to pursue claims based on “Caveat Emptor”, including
16 the fifth cause of action for false advertising, the eleventh cause of
17 action for false advertising, and twelfth cause of action for unfair
18 competition, both of which continue to incorporate allegations
19 regarding “Caveat Emptor” even after Plaintiffs’ dismissal of
20 certain causes of action without prejudice. Additionally, despite
21 Kwan’s invocation of the Fifth Amendment, Plaintiffs and their
22 counsel continue to rely, in part, on earlier Kwan declarations and
23 deposition testimony in papers and pleadings filed with and
24 presented to the Court.

25 Moreover, even after the February 24, 2012 David Lai deposition
26 Plaintiffs’ counsel continued to pursue claims based on “Caveat
27 Emptor”, apparently neglecting—or intentionally failing—to
28 conduct a reasonable inquiry as to the merit of those claims.

29 Additionally, it appears that Plaintiffs’ counsel instructed its
30 clients to manufacture evidence to support its motions, and take
31 actions to spoliage evidence, and thereafter, Plaintiffs did
32 manufacture evidence and take actions to spoliage evidence, and
33 then filed papers, including the second amended and subsequent

¹ When the Court issued its OSC, the Court also ordered Grellas Shah in a separate OSC to show cause why it should not be disqualified from further representation of Kwan and VeriPic based on the Court’s view that a conflict of interest had arisen between Grellas Shah and its clients. The disqualification issue became moot when Grellas Shah withdrew as counsel, and Mark Fredkin and Gregory Hull became counsel of record for VeriPic and Kwan.

1 complaints, with knowledge that their claims lacked evidentiary
2 support, and were being presented for an improper purpose.

3 It also appears that Plaintiffs' counsel, Mr. Shah, as counsel for
4 David Lai at his deposition, instructed his client David Lai to make
5 certain statements against his client's interests and in favor of his
6 other clients, Plaintiffs, requiring Plaintiffs' counsel to eventually
7 suspend the February 24, 2012 deposition, and David Lai to obtain
8 separate counsel, file an errata sheet to change his deposition
9 answers, and testify again at the April 5, 2012 deposition.
10 Plaintiffs' counsel have been awarded their attorneys' fees and
11 costs as monetary sanctions in discovery proceedings and in
12 connection with the aforementioned anti-SLAPP motion,
13 apparently when they knew or should have known that the basis
14 for the claims were without merit.

15 (Order to show cause, p.52:1-26.)

16 "An attorney has a duty 'to employ, for the purpose of maintaining the causes confided to
17 him or her such means only as are consistent with truth, and never to seek to mislead the judge or
18 any judicial officer by any artifice or false statement of fact or law.'" (*Williams v. Super. Ct.*
19 (*People*) (1996) 46 Cal.App.4th 320, 330, citing Bus. & Prof. Code § 6068, subd. (d).) "Further,
20 a member of the State Bar 'shall not seek to mislead the judge, judicial officer, or jury by an
21 artifice or false statement of fact or law.'" (*Id.*, citing Rules Prof. Conduct, rule 5-200(B).)

22 As the Grellas Shah response states, "[t]he record shows... that plaintiffs did not produce
23 certain emails later produced by Henry Lai." (Grellas Shah's response to order to show cause
24 why Pls. and their counsel have not violated CCP section 128.7(b) and order to show cause why
25 counsel should not be subject to sanctions pursuant to the court's inherent authority and the
26 discovery act ("Grellas Shah's response"), p.16:20-21.) Grellas Shah's response argues that:

27 "There is no basis for the Court's conclusion that any Grellas Shah
28 attorney directed Mr. Kwan to manufacture or spoliage evidence,
let alone the evidence required to support a finding of discovery
misconduct against any of the Grellas Shah attorneys... [because:]
there is absolutely no evidence in the record to identify who the
unnamed 'lawyers' were whose statements Mr. Kwan purportedly
referenced... [;] there is nothing to corroborate the assertions in the
emails that in fact anyone (let alone at Grellas Shah) ever gave
such instructions to Mr. Kwan... [; and,] there would have been no
reason for any of the Grellas Shah attorneys to have requested that

1 Mr. Kwan undertake such efforts with Mr. Lai... [because t]he
2 actions purportedly sought—‘getting rid’ of certain domains,
3 removing VeriPic as to another... were not relevant to any issue in
4 the case, and would not have affected the outcome even if
5 performed (which they apparently were not).”

6 (Grellas Shah’s response at p.18:5-19.)

7 As to the first assertion, Mr. Grellas provides a declaration in which he states that he and
8 Janet Kleinberg, formerly of Grellas Shah, represented Kwan and VeriPic from June or July
9 2009 until August 2010 when Shah began working with Grellas Shah and on the instant case.
10 (See Grellas decl. in support of response to OSC re: sanctions, ¶¶ 7-9.) The claim that issues
11 regarding the disposal of evidence tying the domains to Kwan or VeriPic were not relevant to
12 any issue in the case is simply without merit. Whether the statements in the Caveat Emptor were
13 false was the crux of many of VeriPic’s and Kwan’s claims, first alleged as early as the second
14 amended complaint filed on July 20, 2010. The truth, or falsity, of Kwan’s instructions to
15 BigBiz and attempts to hide VeriPic’s connections with the foray.ca domains was also a material
16 issue of Foray’s cross-complaint, filed on August 20, 2010—long before the February 24, 2012
17 deposition of David Lai.

18 However, Grellas Shah persuasively argues that due process prevents the Court from
19 imposing sanctions against Grellas Shah and its attorneys because they cannot provide a
20 complete response to the OSC. (See Grellas Shah’s response, pp.24:1-28, 25:1-28, 26:1-28,
21 27:1-28, 28:1-13.) Although Evidence Code section 956—the crime fraud exception to the
22 attorney-client privilege—would potentially render the substance of any communications
23 unprotected, the crime fraud exception does not apply to the Fifth Amendment.

24 At the March 21, 2014 hearing, the Court sustained a number of objections to Grellas and
25 Shah’s testimony on the basis of Kwan’s and VeriPic’s invocation of Fifth Amendment rights
26 (but overruled other objections). The Court agrees with Grellas Shah that since they cannot
27 testify as to those communications so as to defend themselves, due process mandates that the
28 Court cannot impose sanctions against Grellas Shah or its individual attorneys.

1 The Court remains troubled regarding the statements by Grellas Shah that were adverse
2 to its clients' interests in a memorandum of points and authorities and Shah declaration filed on
3 January 29, 2014 in support of the Plaintiffs' motion for protective order, and to quash the
4 appearance and testimony of John Kwan, Dhairat Shah and David Siegel at the evidentiary
5 hearing on Foray's Motion for Sanctions. The Grellas Shah response to the Court's OSC
6 mischaracterizes the reference to Shah's statement; the Grellas Shah response claims that "[i]n
7 the OSC, the Court states that it may 'draw any inference it wishes' from Kwan's silence."
8 (Grellas Shah's response, p.28:25-26, fn. 8, citing to the Court's OSC, p.58.) The order to show
9 cause was merely quoting Shah's own statement that "[t]he Court may draw whatever inference
10 it chooses from Kwan's decision... not to testify on the basis of the Fifth Amendment" in the
11 declaration he filed. (See Court's OSC, pp.48:19-26, 49:8-10, 57:16-17, 58:14-18 ("[i]n
12 determining this amount, the Court has considered... Plaintiffs' concession... that the Court may
13 draw any inference it chooses from Kwan's silence; and, the fact that Plaintiffs' counsel made
14 that concession during the representation of Kwan".))

15 Regardless, the making of statements by counsel adverse to its clients' interests so as to
16 support Shah's and Siegel's argument why it counsel's personal appearance to testify was not
17 necessary, and counsel's apparent failure to recognize a conflict of interest between themselves
18 and their client, was eventually ameliorated by Grellas Shah's belated withdrawal. Any violation
19 of the Rules of Professional Conduct is within the purview of the State Bar, not this Court.

20 Accordingly, sanctions will not be imposed against Grellas Shah or its individual
21 attorneys. The Court's ruling is not intended to reflect any determination as to the legitimacy of
22 any amount of monies charged by or paid to Grellas Shah for attorney fees.

23 **B. Monetary, issue, evidentiary and terminating sanctions under Code of Civil**
24 **Procedure section 128.7**

25 As a preliminary matter, in response to the Court's OSC as to why monetary, issue,
26 evidentiary and terminating sanctions should not be issued against them pursuant to Code of
27 Civil Procedure section 128.7, subdivisions (b)(1)-(3), the Discovery Act, Business &
28 Professions Code sections 6068 subdivisions (c) & (d), and the Court's inherent authority to

1 properly administer justice and to preserve the Court's integrity ("OSC"), defendant VeriPic
2 asserts that "[n]o specific sanctions are mentioned in the OSC for the violation of Code of Civil
3 Procedure section 128.7." (See VeriPic's response to Court's OSC, p.8:2-16.) VeriPic's
4 assertion is clearly incorrect. The OSC explicitly states that "VeriPic... [is] ordered to show
5 cause as to why monetary, issue, evidentiary and terminating sanctions should not be issued
6 against them pursuant to Code of Civil Procedure section 128.7, subdivision (b)(1)-(3)..." All
7 of those sanctions are within the purview of the OSC for any violation of section 128.7.

8 **1. VeriPic's assertion that the Kwan emails are "not central to VeriPic's**
9 **claims as alleged in the complaint, including claims premised on the**
10 **Caveat Emptor Letter"**

11 In the OSC, the Court stated that:

12 It appears that Kwan knew that any claims premised on the Caveat
13 Emptor letter were without any evidentiary basis as the assertions
14 in the letter were not 'patently untrue or outrageously false.' In
15 fact, it appears that the assertions in the letter were true and Kwan
16 went to great lengths to hide such facts.... Rather than concede
17 that its claims were without merit, it appears that VeriPic and its
18 counsel instead have taken an unusually aggressive position to
19 ramp up litigation through filing pleadings including declarations
20 under penalty of perjury, motions that were based on facts that
21 were knowingly false and claims that were without merit, and
22 present denials of factual contentions without any evidentiary basis
23 or reasonable basis for such denials.

24 (OSC, p.25:20-28.)

25 In response, VeriPic states that "VeriPic agrees with the Court that Mr. Kwan's
26 statements in declarations and deposition that he did not request Big Biz to set up the 'foray.ca'
27 and other web pages so that any visitors to those sites would be 'directed' to the VeriPic or
28 Propictus web pages, can be read as inconsistent with the statements in his August 20, 2008 and
December 18, 2008 emails." (VeriPic's response to OSC, p.10:3-6.) "And... it appears that Mr.
Kwan... intended to give the impression that Big Biz automatically set up the accounts this way,
and not as a result of anything deliberately done by VeriPic." (*Id.* at p.10:6-11.)

Nevertheless, VeriPic asserts that the Kwan emails are "not central to VeriPic's claims as
alleged in the complaint, including claims premised on the Caveat Emptor Letter." (VeriPic's

1 response to OSC, p.11:6-7.) Instead, counsel now contends that “Plaintiffs’ primary claims in
2 this action were based on Foray’s disparagement of its products, Foray’s assertions that
3 Plaintiff’s hacked into Foray’s computers, and Foray’s assertions that VeriPic was under
4 investigation by authorities.” (*Id.* at p.12:26-28.)

5 The Court disagrees. The Caveat Emptor letter was quoted in full in the OSC, and it is
6 clear that the primary thrust or gravamen of Caveat Emptor is that VeriPic is unethical and
7 dishonest. Caveat Emptor first states that “some companies bend to unscrupulous business
8 practices because of their fear of competition... [and] the unwary and unsuspecting victim could
9 easily be duped and misle[d] by these deceitful and deceptive business practices.” Caveat
10 Emptor refers to “an illegitimate website using the Foray company name... [and] using the guise
11 of SWGIT.COM and SWGDE.COM to mislead and misdirect logical web address entries from
12 the trusted, legitimate websites—SWGIT.ORG and SWGDE.ORG—in an effort to solicit sales
13 leads.” Caveat Emptor then states that “this type of business practice [is] unethical... [and] has
14 the real potential of bringing about a legal challenge regarding the integrity of any digital
15 evidence managed by a software company that is willing to stoop to this level of
16 misrepresentation.” Caveat Emptor then asks the reader if they are “willing to choose to do
17 business with a company whose ethics could be challenged... [or] a product to manage crucial,
18 critical digital evidence that was developed by a solutions provider that uses unscrupulous
19 business practices?” Caveat Emptor—attached by VeriPic’s counsel, Grellas Shah, in support of
20 its special motion to strike and subsequent motions—contains no reference to hacking or
21 investigation by authorities. Caveat Emptor’s sole mention of VeriPic’s products was that they
22 were the product of a company with questionable character.

23 It is clear to the Court that VeriPic’s claims based on Caveat Emptor arise from
24 VeriPic’s issue with the characterization that it is “unethical” or “unscrupulous.” VeriPic alleged
25 in the second amended complaint that “[t]o be successful and profitable in these fields [of
26 providing asset management services to police and fire agencies], it is critical that any vendor,
27 including VeriPic, have a spotless reputation for honesty and integrity. VeriPic conducts itself
28 and its business with honesty, respectability, creditworthiness, trustworthiness, competence and

1 integrity. However, VeriPic's reputation for these qualities has been damaged by the malicious
2 and defamatory conduct of Defendants, and each of them, as further alleged below," with
3 specific reference to Caveat Emptor. (Second amended complaint, ¶ 11.)

4 On October 4, 2010, VeriPic moved to take discovery regarding Caveat Emptor. In its
5 motion, VeriPic quoted the above portions of Caveat Emptor and stated:

6 These statements are false and misleading. It is true that for a
7 point in time, VeriPic registered the domain name "foray.ca." The
8 Foray defendants omit, however, material truthful information
9 about this act that renders the statement misleading. Then they
10 include innuendo and characterizations about VeriPic's bad motive
11 and conduct without disclosing the true information that would
12 render these characterizations inaccurate.

13 The truth is that VeriPic paid less than \$20 to register "foray.ca"
14 for a one-year period of time and let the domain name lapse
15 automatically. *See* Kwan Decl., ¶ 11. During this period, VeriPic
16 just parked the domain name and did not do anything with it. It
17 did not create a website to associate with it or use the domain name
18 in any commercial manner. *Id.* VeriPic did not ask its internet
19 service provider, Bigbiz Internet Services ("Bigbiz"), to route
20 traffic automatically without instructions from [VeriPic] to do so.
21 [VeriPic] did not ask for traffic to the website www.Foray.ca to be
22 referred to the www.Veripic.com website." *Id.* at ¶ 14 & Ex. D....

23 Therefore, the Foray defendants' statements that VeriPic engaged
24 in unethical and dishonest business practices by diverting
25 customers away from the Foray website are false. Had they
26 disclosed the truth about VeriPic's registration of "foray.ca," no
27 customer would draw such negative conclusions. Instead,
28 customers were given conjecture and innuendo without the benefit
of the truth....

29 The Foray defendants used similar tactics in connection with the
30 "swgit.com" and "swgde.com" domain names. For instance, to
31 one customer they wrote that VeriPic "is using the guise of
32 SWGIT.COM and SWGDE.COM to solicit sales leads." Shah
33 Decl., Ex. G. They warned that "[n]ot only is this type of business
34 behavior unethical, it has the potential of leading to a legal
35 challenge regarding the integrity of any digital evidence managed
36 by a software company that is willing to stoop to that level of
37 misrepresentation." *Id.* Then they warned the customer that it
38 should be worried about what VeriPic would do in the future: "If
they are using this type of scam to obtain sales leads, what other

1 deceptions and misleading statements might they make to potential
2 customers, and what type of misrepresentations might they make in
3 the courtroom?" *Id.*

4 To another customer, they wrote that in the context of comparing
5 VeriPic and Foray's products, the customer should be aware of
6 problems with VeriPic's "ethics." The email states that VeriPic
7 took "legitimate domain names" and "registered them under other
8 names."...

9 These statements are repeated in the "Caveat Emptor" letter. In
10 addition to accusing VeriPic of using these two domain names to
11 solicit sales leads, it states that VeriPic posted marketing materials
12 on these sites masquerading as legitimate educational content.... It
13 also repeats the innuendo and conjecture quoted in connection with
14 the "foray.ca" statements, i.e., 1) that the behavior is unethical; 2)
15 that a police department purchasing VeriPic's product risks that
16 any evidence handled by VeriPic will be challenged in court; 3)
17 that there is reason to believe VeriPic is making other
18 misrepresentations to its customers; and 4) there is reason to
19 believe that VeriPic will lie about its technology in the courtroom.
20 *Id.*

21 These statements about "swgit.com" and "swgde.com" are false.
22 The site attached to these domain names was in operation for only
23 a few weeks and was never operated for any commercial purpose.
24 It did not contain an[y] marketing material and never generated
25 any sales leads for VeriPic. Instead, the site contained valuable
26 content that reflected VeriPic's views on its industry and the
27 technology used in its industry because VeriPic believed that it
28 would serve the public interest. *See* Kwan Decl. ¶¶ 16-18.

VeriPic did not put its own logo on the website precisely because it
was not meant to be a site to promote VeriPic. Instead, VeriPic
created Propictus for the purpose of providing educational and
informational materials. It was this non-commercial entity that
was identified with the website. It is not true that VeriPic was
trying to conceal its identity to mislead anyone. Rather,
identifying itself or placing the VeriPic logo on the site would have
served as a form of advertisement, which is what VeriPic was
trying to avoid. *See* Kwan Decl. ¶¶ 17-19, 23.

It is also not true that VeriPic using the Canadian entity TUCOW
or "myprivacy.ca" to conceal its identity. Bigbiz normally uses
TUCOW to register domain names and "myprivacy.ca" is a normal
anti-SPAM feature that is offered by Bigbiz. VeriPic did not ask

1 for these things, it is the normal business practice of the internet
2 service provider. See Kwan Decl. ¶ 24. ...

3 With both “foray.ca,” and “swgit.com” and “swgde.com,” the
4 Foray defendants took innocent actions on the part of VeriPic and
5 mischaracterized them as being unethical and dishonest. Then it
6 used these events as a pretext to launch a defamatory campaign of
7 verbal and written misrepresentations to VeriPic’s clients. As is
8 detailed above, while it is true that VeriPic registered these three
9 domain names, nothing else the Foray defendants said about these
10 acts is true and the Foray defendants used conjecture and innuendo
11 to create a false impression in the minds of VeriPic’s customers.

12 (VeriPic’s memorandum of points and authorities in support of motion for leave to take
13 discovery pursuant to section 425.16, subdivision (g), pp.6:15-28, 7:1-28, 8:1-28, 9:1-28, 10:1-
14 17.)

15 As noted by the Court’s OSC, Kwan, as “President and Chief Executive Officer of Kwan
16 Software Engineering, Inc., dba VeriPic” also submitted a declaration in support of the motion in
17 which he stated that “[p]rior to the Foray defendants’ defamatory campaign against VeriPic,
18 VeriPic had an unblemished reputation for honesty and integrity... [t]his reputation is
19 particularly important in VeriPic’s industry... [as] I believe that customers would make decisions
20 on which product to purchase based, in part, on their perceptions of the trustworthiness of the
21 vendor.” (Kwan decl. in support of motion for leave to take discovery pursuant to section
22 425.16, subdivision (g), ¶ 4.) Kwan also attached Caveat Emptor, in which he stated that the
23 Foray Defendants “accused VeriPic of committing fraud and acting unethically by registering the
24 ‘foray.ca’ domain mane... in a lengthy letter entitled ‘Caveat Emptor’ that the Foray defendants
25 sent to a number of VeriPic customers or potential customers.” (*Id.* at ¶ 10.) As quoted in the
26 Court’s OSC, Kwan’s declaration continued:

27 The characterization that there is anything improper or unethical
28 about VeriPic’s registration of ‘foray.ca’ is false. VeriPic
registered the web domain foray.ca with the internet service
provider Bigbiz Internet Services (‘Bigbiz’) for a one year period
after confirming with Bigbiz that it was available for sale and that
the sale of this domain name to me did not violate the rules of the
Internet Corporation for Assigned Names and Numbers. At the
time that VeriPic acquired foray.ca, it had no clear idea or plan of
what to do with the domain name.... During this period, VeriPic

1 did absolutely nothing with the domain name. It did not create a
2 website of content to attach to the domain name. It did not make
3 attempts to drive traffic to the domain name. We only parked the
4 domain name with BigBiz, and ultimately let the domain name
5 lapse after one year because there was no sense in continuing to
6 pay registration fees for something we did not use.... It is apparent
7 to me that the entire 'issue' of 'foray.ca' was a pretext to disparage
8 VeriPic and gain competitive advantage over it.... VeriPic did not
9 request that Bigbiz automatically forward visitors from 'foray.ca'
10 (of which there was none) to 'veripic.com.' Bigbiz did this as a
11 matter of its normal business practices. At the time, we believed
12 there was nothing unusual about this, and assumed that Bigbiz's
13 normal practices were in line with those of other internet services
14 providers. A March 12, 2010 letter I received from David Lai of
15 Bigbiz corroborates these points. A true and correct copy of this
16 letter is attached as Exhibit D. The letter correctly notes that the
17 registration of 'foray.ca' lasted from September 2008 through
18 September 2009, after which time VeriPic voluntarily allowed it to
19 lapse. The letter states: 'Our standard policy for domain
20 registrations is to automatically refer domain traffic to the default
21 website for our client's account. In the case of [VeriPic] their
22 default website was www.VeriPic.com and the default activity was
23 to refer website traffic for www.Foray.ca to www.VeriPic.com.'
The letter further states: 'We did this activity automatically
without instructions from [VeriPic] to do so. [VeriPic] did not ask
for traffic to the website domain www.Foray.ca to be referred to
the www.VeriPic.com website.'" The letter further states: 'We did
not block the registration of www.Foray.ca by our client even
though a website called www.Foray.com existed because, after a
trademark search, it appeared that www.Foray.com did not possess
a registered trademark on the word Foray. Therefore we
concluded that the registration of www.Foray.ca by [VeriPic] was
proper and unrestricted under the rules of the Internet Corporation
for Assigned Names and Numbers (ICANN) the ultimate authority
for internet domain registrations. We concluded that it was proper
for [VeriPic] to have registered and owned the website domain
www.Foray.ca.'

24 (Kwan decl. in support of VeriPic's motion to take discovery pursuant to section 425.16(g) of the
25 Code of Civil Procedure, ¶¶ 11-14.)

26 The Court finds that the Kwan emails, quoted in the Court's OSC, demonstrate that
27 Kwan's statements in declarations sworn under penalty of perjury and filed with the Court were
28 false.

1 The Kwan declaration also makes false statements with regards to the swgit.com and
2 swgde.com domain names, including statements such as “[t]hese statements... that VeriPic
3 engaged in fraudulent and unethical conduct by registering the ‘swgit.com’ and ‘swgde.com’
4 domain names... are false.” (See Kwan decl. in support of VeriPic’s motion to take discovery
5 pursuant to section 425.16(g) of the Code of Civil Procedure, ¶¶ 15-25 (also concluding that
6 “[i]n short, Propictus was a means through which VeriPic could provide education and
7 information to the community and industry... [t]hrough a series of false statements and
8 innuendo, the Foray defendants created the impression that VeriPic used shadowy Canadian
9 entities and cloaked its own identity to create sales leads... [and t]hese statements are false”).)

10 Subsequently, VeriPic filed its opposition to Defendants’ special motion to strike the
11 second amended complaint, in which the same statements from VeriPic’s prior motion were
12 reiterated in both VeriPic’s opposition to the special motion to strike and Kwan’s declaration in
13 support of the opposition. (See VeriPic’s opposition to Defs.’ special motion to strike, pp.9:1-
14 28, 10:1-28, 11:1-28, 12:1-28, 13:1-3; see also Kwan decl. in support of opposition to special
15 motion to strike, ¶¶ 4, 10-25.)

16 Thereafter, as stated in the OSC, VeriPic filed a third amended complaint, a fourth
17 amended complaint, a fifth amended complaint, a sixth amended complaint, and a seventh
18 amended complaint—each referencing:

- 19 • the critical need to “have a spotless reputation for honesty and integrity”;
- 20 • that “VeriPic conducts itself and its business with honesty, respectability,
21 creditworthiness, trustworthiness, competence and integrity”;
- 22 • the market for the parties’ products is “an ethics based market”;
- 23 • the damage to these qualities caused in part by the accusations that:
 - 24 ○ VeriPic had “behaved unethically and illegally towards Foray as a
25 competitor” with regards to the www.foray.ca website even though “it did
26 nothing with it and simply parked it-as a result, VeriPic’s internet service
27 provider simply pointed the domain to VeriPic.com website as a matter of
28 routine since VeriPic owned this domain”;
 - “VeriPic was ‘unethical,’ ‘devious,’ ‘dishonest,’ resorted to
‘unscrupulous business practices because of its fear of competition’ and
had misused the swgit.com and swgde.com web domains in an ‘effort to
solicit sales’”; and,
 - VeriPic was “‘unethical,’ ‘dishonest,’ ‘disreputable,’ ‘not creditworthy,’
‘not trustworthy’ and a ‘bad influence on the community.’”

1 (See: second amended complaint (“SAC”), ¶¶ 10-12, 20-23, 28-29; third amended complaint
2 (“TAC”), ¶¶ 11-13, 21-24, 29-30; fourth amended complaint (“4AC”), ¶¶ 12-15, 23-26, 33-35;
3 fifth amended complaint (“5AC”), ¶¶ 12-15, 23-26, 33-35; sixth amended complaint (“6AC”), ¶¶
4 12-15, 23-26, 33-35; also seventh amended complaint (“7AC”), ¶¶ 13-16, 24-27, 34-36.)

5 The 4AC, 5AC, 6AC and 7AC also allege that “Kwan is the founder and Chief Executive
6 Officer of VeriPic... [and t]hrough his leadership, VeriPic has obtained a reputation for honesty
7 and integrity that was absolutely unblemished and represented a solid 17-year record of
8 reliability and trustworthiness that is unmatched in the industry.” (See 4AC, ¶ 13; see 5AC, ¶
9 13; see 6AC, ¶ 13; see 7AC, ¶ 14.) As detailed in the OSC, VeriPic consistently and repeatedly
10 stated that Caveat Emptor was at “the heart of” its claims, and indicated that the statements in
11 that letter caused its damages. (See Court’s OSC, pp.26:8-52:18.)

12 VeriPic now contends that Caveat Emptor’s statements regarding VeriPic’s unethical and
13 unscrupulous business practices were “not central to VeriPic’s claims” and that the same
14 damages previously claimed by VeriPic for injury to its reputation for honesty and integrity, are
15 now caused by product disparagement and allegedly false claims of hacking and governmental
16 investigation. VeriPic’s recently developed theories of its case are clearly and directly at odds
17 with VeriPic’s prior sworn statements and arguments made to the Court. VeriPic’s argument
18 that the Kwan emails were not central to its claims is neither well taken nor supported by
19 evidence.

20 VeriPic also argues that portions of its claims are independent of Caveat Emptor. Again,
21 starting in the Second Amended Complaint, and expanded by the time of the seventh amended
22 complaint, VeriPic alleged increasing levels of lost sales from specific clients identified over 10
23 pages of the 7AC in paragraphs 40 through 100, that resulted from the now abandoned claims
24 about Caveat Emptor that were “the heart of” the alleged purported defamatory scheme by
25 Defendants. In VeriPic’s proposed 8th Amended Complaint, VeriPic now alleges that its
26 damages, from what clearly appear to be those same lost sales and accounts, were caused by
27 different allegedly defamatory statements, and not Caveat Emptor.

1 Even if true, that some portion of VeriPic's claims depend on other theories², the Court
2 finds that the relentless pursuit of the demonstrably false Caveat Emptor claims, first alleged in
3 the SAC and repeated through each successive amended complaint through the 7AC, establish
4 the basis for a finding that Kwan and VeriPic violated the prohibitions found in Code of Civil
5 Procedure section 128.7 as described in the order to show cause.

6 **2. VeriPic's explanation of the emails about "getting rid of domains"**

7 VeriPic asserts that the Court "conclu[des] that [the] actions [VeriPic/Kwan took related
8 to the domains] are tantamount to the destruction of evidence... [when] Kwan's email clearly
9 shows that this phrase is used to describe 'unregistering' or 'transferring' the domains."

10 (VeriPic's response to OSC, pp.13:6-28, 14:1-3.)

11 The Kwan emails are quoted in the Court's OSC. Those emails detail VeriPic's intent in
12 its requests to BigBiz to conceal its earlier instructions about the foray.ca domain, including the
13 instruction to send all traffic to foray.ca to a VeriPic website (a fact specifically denied under
14 oath by Kwan), and its subsequent requests to hide VeriPic's connection with the domain. Kwan
15 thereafter removed all trace of his emails to BigBiz from the VeriPic email servers, and/or denied
16 that such emails existed so that orders to compel production would be denied. The Court's OSC
17 does not reference a belief that Plaintiffs had engaged in *destruction* of evidence (although such
18 a finding could be made on this record, from the fact that a third party produced records that
19 should have been found in VeriPic's records). Instead, the OSC discusses VeriPic's apparent
20 steps to spoliage evidence, a term that is not limited to destruction of evidence and includes
21 hiding, concealment, or suppression of evidence. (See *Williams v. BASF Catalysts LLC* (3d. Cir
22 2014) 765 F.3d 306, 320 (stating "[i]n law, spoliation refers to 'the hiding or destroying of
23 litigation evidence, generally by an adverse party'"); see also *R.S. Creative, Inc. v. Creative
24 Cotton, Ltd.* (1999) 75 Cal.App.4th 486, 497 (stating that "[s]poliation is the intentional
25 destruction or suppression of evidence," emphasis added); see also *Willard v. Caterpillar, Inc.*

26
27
28 ²The Court notes that on October 4, 2013, VeriPic dismissed eight of its thirteen causes of action shortly after the Kwan emails were finally produced by a third party witness. After the Court pointed out that the remaining causes of action in VeriPic's seventh amended complaint still contained allegations related to Caveat Emptor, VeriPic's proposed eighth amended complaint only contains three causes of action.

1 (1995) 40 Cal.App.4th 892, 907 (stating that "[s]poliation is the destruction or significant
2 alteration of evidence, or the failure to preserve property for another's use as evidence, in
3 pending or future litigation"), disapproved on other grounds in *Cedars-Sinai Medical Center v.*
4 *Super. Ct. (Bowyer)* (1998) 18 Cal. 4th 1, 18; see also *Rosen v. St. Joseph Hospital of Orange*
5 *County* (2011) 193 Cal.App.4th 453, 462 (noting that complaint alleged spoliation by alleged
6 concealment of evidence critical to case); see also *Cedars-Sinai Medical Center v. Super. Ct.*
7 *(Bowyer)* (1998) 18 Cal. 4th 1, 4 (defining spoliation as "intentional destruction or suppression--
8 of evidence"); see also Evid. Code 413; see also *Deyo v. Kilbourne* (1978) 84 Cal.App.3d 771,
9 793 (stating that "[t]he refusal to reveal material evidence is deemed to be an admission that the
10 claim or defense is without merit".)

11 The Court's OSC explicitly notes that "Kwan went to great lengths to **hide** [his
12 knowledge] that the assertions in the [Caveat Emptor] letter were true... [and] that any claims
13 premised on Caveat Emptor were without evidentiary basis as the assertions in the letter were not
14 'patently untrue or outrageously false.'" (OSC, p.25:20-28.) The Court finds from the facts
15 present here that Kwan and VeriPic withheld, and attempted to conceal or alter evidence that
16 would have shown that Kwan's sworn statements filed with the Court, deposition testimony, and
17 the pleadings and claims made in this case were false.

18 The Court finds that VeriPic, through Kwan, presented claims that they knew were
19 without evidentiary basis.

20 **3. Sanctions pursuant to Code of Civil Procedure section 128.7**

21 In its filed response to the OSC, VeriPic states that "the challenged papers were
22 withdrawn within the safe harbor period." (VeriPic's response to OSC, p.19:5.) VeriPic's
23 counsel has also represented that it does not intend to pursue claims based on "the heart of" the
24 alleged purported defamatory scheme by Defendants. Kwan has dismissed (albeit without
25 prejudice) the claims he originally filed as a plaintiff. Although the Court finds that multiple
26 pleadings filed with the Court and signed by Kwan or Grellas Shah on behalf of VeriPic violated
27 Code of Civil Procedure section 128.7(b), the Court does not intend to issue sanctions based on
28 Code of Civil Procedure section 128.7.

1 **C. The Court’s inherent authority to dismiss**

2 In its filed response to the OSC, VeriPic acknowledges that “a trial court has the inherent
3 power to dismiss the action ‘when the plaintiff has engaged in misconduct during the course of
4 litigation that is deliberate, that is egregious, and that renders any remedy short of dismissal
5 inadequate to preserve the fairness of the trial.’” (VeriPic’s response to OSC, p.21:1-4, citing
6 *Stephen Slesinger, Inc. v. Walt Disney Co.* (2007) 155 Cal.App.4th 736, 740 (hereinafter,
7 “*Slesinger*”).) However, VeriPic argues that:

8 Our case is clearly distinguishable [from *Slesinger*]. There is no
9 evidence that the alleged misconduct cited in the OSC prevents
10 Defendants from having a fair trial on VeriPic’s claims based on
11 product disparagement. To begin, there is no connection between
12 the product disparagement claims and the challenged statements
13 made by Kwan in his declarations. Moreover, even if there were
such a connection, Defendants are in the possession of Kwan’s
August and December 2008 emails and can use them at trial.
There is simply no prejudice established.

14 (VeriPic’s response to OSC, p.21:11-16.)

15 The Court disagrees, and finds that the evidence supports Defendants’ argument that the
16 alleged misconduct prevents Defendants from having a fair trial in this case.

17 VeriPic presented no evidence to dispute any of the Court’s assertions of misconduct by
18 VeriPic, or to deny that VeriPic pursued litigation lasting over five years with dramatically
19 increasing damage claims, while it knew that its claims were meritless and frivolous. The
20 Court’s OSC noted—and Defendants argued—that the second through seventh amended
21 complaints each alleged that VeriPic’s damages were the result of Caveat Emptor. VeriPic now
22 asks the Court to allow it to amend its pleadings to allege that those same damages for lost sales
23 and accounts, damages that VeriPic had alleged in very precise terms, now arose from product
24 disparagement instead of Caveat Emptor.

25 Despite conceding that Kwan—the designated person most knowledgeable for VeriPic—
26 cannot testify as to any matters now that he has invoked the Fifth Amendment right to not
27 incriminate himself, VeriPic does not present any declaration, deposition testimony or other
28

1 evidence by any other person or corporate representative who might be able to testify as to the
2 subjects relevant to Defendants' Motion for Sanctions or the Court's OSC.

3 The Court notes that Kwan, as the person most knowledgeable for VeriPic, has already
4 testified and stated that *he* was the "person most knowledgeable on *all...* topics" [emphasis
5 added]—including damages to VeriPic, "Foray's allegations about website hacking" and the
6 other peripheral claims based on product disparagement (see Kwan deposition transcript,
7 generally). VeriPic does not provide any evidence refuting such statement, and any attempt by
8 VeriPic to contradict his testimony, or to produce another witness, would be viewed with
9 suspicion at best, although the Court provided VeriPic the opportunity to present evidence.

10 Other than VeriPic's bald assertions that its claims could have merit and should be presented to a
11 trier of fact, VeriPic presents no evidence to counter the assertions in the OSC that its claims are
12 meritless and frivolous, even though Kwan refused to testify in response to the Motion for
13 Sanctions or the Court's OSC and no other witness has been produced.

14 VeriPic has argued that the Court cannot take any negative inference from Kwan's
15 invocation of the privilege against self-incrimination, as it assumes the Court has done when
16 quoting from the Grellas Shah declaration. The Court did not do so in its OSC, and does not do
17 so now in making its findings in this Order. The Court is mindful of Evidence Code section 913.

18 However, "[i]n determining what inferences to draw from the evidence or facts in the
19 case against a party, the trier of fact may consider, among other things, the party's failure to
20 explain or to deny by his testimony such evidence or facts in the case against him, or his willful
21 suppression of evidence related thereto, if such be the case." Evidence Code section 413.

22 At the September 19, 2014 hearing, the Court specifically asked why VeriPic did not
23 provide another witness to testify for VeriPic, knowing that Kwan had already refused to testify.
24 VeriPic's counsel responded that that would be an issue for the trier of fact, and "[v]ery frankly,
25 [counsel] never considered providing a declaration relative to the additional evidence that could
26 be provided." (See transcript of September 19, 2014 OSC hearing, pp.17:17-28, 18:1-28, 19:1-
27 28, 20:1-2; see also *id.* at p.31:25-26 (stating that "if I had thought that that was going to make a
28 difference to the Court at this motion we would have provided it").) The point of the Court's

1 OSC was to give VeriPic an opportunity to respond to the issues raised by the Court, both with
2 evidence and argument.

3 In any event, a civil plaintiff acts at its peril by refusing to testify based on a claim the
4 answers may tend to incriminate.

5 "It is well settled the privilege against self-incrimination may be
6 invoked not only by a criminal defendant, but also by parties or
7 witnesses in a civil action. [Citation.] However, while the
8 privilege of a criminal defendant is absolute, in a civil case a
9 witness or party may be required either to waive the privilege or
10 accept the civil consequences of silence if he or she does exercise
11 it. [Citations.] ...While this precise issue has not been reported
12 previously in any California case, sister state authorities addressing
13 the issue teach us that the civil consequences of the invocation of
14 Fifth Amendment rights (including the striking of the pleading and
15 the ensuing dismissal and/or default) may well depend on whether
16 the party asserting the privilege is the plaintiff or the defendant.
17 For, the plaintiff has initiated the action and bears the burden of
18 proving his claim, while the defendant is merely an involuntary
19 participant. Where the plaintiff in a civil action refuses to testify
20 by invoking the privilege against self-incrimination, the action may
21 be dismissed by the court because 'One may not invoke the
22 judicial process seeking affirmative relief and at the same time use
23 the privileges granted by that process to avoid development of
24 proof having a bearing upon his rights to such relief.' [Citation.]

18 *Alvarez v. Sanchez* (1984) 158 Cal. App. 3d 709, 712.

19 Courts do not allow a plaintiff to use the self-incrimination privilege as a "shield and as a
20 sword." Courts are quick to find a waiver of the privilege when a plaintiff seeks damages on the
21 one hand and then attempts to inconvenience or hinder or delay the defense in the prosecution of
22 its case by the imposition of a privilege. *Dwyer v. Crocker Nat'l Bank* (1987) 194 Cal. App. 3d
23 1418, 1432. "If a plaintiff persists in claiming his privilege, he will have to dismiss
24 his lawsuit *with prejudice*. '[Plaintiff] cannot have his cake and eat it too.'" *Hartbrodt v. Burke*
25 (1996) 42 Cal. App. 4th 168, 175, citing *Fremont Indemnity Co. v. Super. Ct. (Sharif)* (1982) 137
26 Cal. App. 3d 554, 560 (emphasis added).

27 Although Kwan first invoked his right not to incriminate himself at a deposition taken
28 after he had dismissed his individual claims against Foray (without prejudice), Kwan appeared at

1 that deposition as the designated PMK for Plaintiff VeriPic. VeriPic is still a plaintiff, but
2 through Kwan, attempted to exercise a fifth amendment right.

3 "Corporations have no privilege against self-incrimination. [Citation.] Here the
4 government is seeking information from a corporation. The fact that the individual officers who
5 have access to that information believe that the information will incriminate them personally
6 does not excuse the corporation from producing that information. Although the individual
7 appellants themselves may not be compelled to produce the information that they allege is
8 incriminating, they may not prevent the corporate appellants from producing that information."
9 *Navel Orange Administrative Committee v. Exeter Orange Co.* (9th Cir. 1983) 722 F.2d 449,
10 454. "[T]he constitutional privilege against self-incrimination is 'essentially a personal one,
11 applying only to natural individuals.' It 'cannot be utilized by or on behalf of any organization,
12 such as a corporation.' [Citations.] If a corporation cannot avail itself of the privilege against
13 self-incrimination, it cannot take advantage of the claimed invalidity of a penalty imposed for
14 refusal of an individual, its president, to waive the privilege." *George Campbell Painting Corp.*
15 *v. Reid* (1968) 392 U.S. 286, 288-289.

16 VeriPic's refusal to testify, and failure to produce any evidence to controvert the factual
17 statements in the OSC, is sufficient to support the Court's findings that the facts stated in the
18 OSC are true.

19 VeriPic's claim that Defendants are not prejudiced fails to account for the over five years
20 of litigation costs and court costs involved in defending the frivolous and meritless litigation or
21 the Court's own costs involved in handling the litigation. The Court finds that Defendants will
22 be prejudiced if VeriPic is allowed to continue to pursue its peripheral claims that may also lack
23 merit, and for which VeriPic has failed to offer evidentiary support. Further, the establishment
24 of prejudice to an opposing party as a result of the misconduct is not one of the inquiries "to be
25 made by trial courts when determining whether a plaintiff's actions warrant a dismissal with
26 prejudice," as stated by *Slesinger, supra*; rather, the holding of *Slesinger* requires the trial court
27
28

1 to measure “the effect of misconduct on a fair resolution of the case”—distinct from prejudice.³
2 The Court finds evidence to support a finding that the alleged misconduct prevents Defendants
3 from having a fair trial on VeriPic’s claims based on product disparagement or its peripheral
4 claims, as stated above.

5 Citing to *People v. Uribe* (2011) 199 Cal.App.4th 836 (hereinafter “*Uribe*”), VeriPic also
6 asserts that “[d]ismissal cannot be based simply on a finding that Kwan was untruthful in his
7 declaration.” (VeriPic’s response to OSC, 21:17-25.) First, the Court’s findings in this case are
8 not based merely on the fact that Kwan was untruthful in his declaration. Rather, the OSC states,
9 and the Court finds to be true, the following:

10 ...plaintiff Kwan, the alleged Chief Executive Officer of plaintiff
11 VeriPic, and designated PMK/PMQ for VeriPic for the majority of
12 issues, filed the initial complaint, FAC, SAC, TAC, 4AC, 5AC,
13 6AC and 7AC, knowing that he had in fact engaged in activity in
14 his capacity as CEO of VeriPic that was “unethical, dishonest,
15 disreputable, not creditworthy, not trustworthy and a bad influence
16 on the community,” despite his allegations to the contrary that any
17 statements to that effect were “patently untrue and outrageously
18 false.” Kwan also filed declarations under penalty of perjury in
19 support of motions to continue the apparently frivolous litigation,
20 including motions for leave to file amended complaints, and
21 motions for summary judgment or adjudication. Kwan has since
22 invoked the Fifth Amendment, and he himself—through his
23 counsel, Mr. Shah—has stated that “the Court may draw any
24 inference it chooses from Kwan’s silence.” In addition, it appears
25 that Kwan, the alleged Chief Executive Officer of plaintiff VeriPic,
26 and designated PMK for VeriPic on the large majority of issues,
27 apparently knowing that his claims and allegations were meritless
28 and frivolous, thereafter pursued litigation lasting five years,
specifically filing a number of complaints—starting with the
second amended complaint—in which the “Caveat Emptor” claims
were “at the heart” of VeriPic’s claims, and exponentially

25 ³ The *Slesinger* court stated that “[t]he decision whether to exercise the inherent power to dismiss requires
26 consideration of all relevant circumstances, including the nature of the misconduct (which must be deliberate and
27 egregious, but may or may not violate a prior court order), the strong preference for adjudicating claims on the
28 merits, the integrity of the court as an institution of justice, the effect of the misconduct on a fair resolution of the
case, and the availability of other sanctions to cure the harm.” (*Slesinger, supra*, 155 Cal.App.4th at p.764.)
VeriPic’s mistaken belief that the *establishment of prejudice* is a factor in determining whether a plaintiff’s actions
warrant a dismissal with prejudice is apparently based on its misreading/misapplication of *Uribe*, discussed below, a
criminal case involving a sanction of dismissal for prosecutorial misconduct—not at issue here.

1 increasing the claimed amount of damages. Thereafter, Kwan
2 added himself as a plaintiff in the 4AC.

3 Despite conceding that “the Court eviscerated the legal
4 grounds to continue pursuing claims based on the Caveat Emptor
5 and related communications,” Plaintiffs and their attorneys —the
6 law firm of Grellas Shah LLP, and attorneys Grellas, Shah and
7 Siegel—continued to pursue claims based on “Caveat Emptor”,
8 including the fifth cause of action for false advertising, the
9 eleventh cause of action for false advertising, and twelfth cause of
10 action for unfair competition, both of which continue to
11 incorporate allegations regarding “Caveat Emptor” even after
12 Plaintiffs’ dismissal of certain causes of action without prejudice.
13 Additionally, despite Kwan’s invocation of the Fifth Amendment,
14 Plaintiffs and their counsel continue to rely, in part, on earlier
15 Kwan declarations and deposition testimony in papers and
16 pleadings filed with and presented to the Court.

17 Moreover, even after the February 24, 2012 David Lai
18 deposition... Plaintiffs did manufacture evidence and take actions
19 to spoliage evidence, and then filed papers, including the second
20 amended and subsequent complaints, with knowledge that their
21 claims lacked evidentiary support, and were being presented for an
22 improper purpose.

23 ...

24 Further, for the reasons specified above, it appears that the
25 misconduct of Plaintiffs... in the course of litigation and pervasive
26 litigation abuse is so egregious and deliberate such that no sanction
27 other than dismissal is adequate to ensure a fair trial. Plaintiffs’ ...
28 apparent pattern of conduct was so severe and deliberate so as to
constitute extreme circumstances and alternatives less severe than
dismissal would not be sufficient to protect the fairness of the trial.
Accordingly, Plaintiffs... are ordered to show cause as to why
terminating sanctions should not be issued pursuant to the Court’s
inherent authority to properly administer justice and to preserve the
Court’s integrity.

Moreover, as previously stated, Plaintiffs’ and their counsel
have been awarded attorney’s fees and costs in connection with
discovery motions and the aforementioned anti-SLAPP motion,
despite apparently having knowledge that the claims of Plaintiffs’
complaint and the defenses to the cross-complaint upon which the
motions were based, were without merit. Plaintiffs... are ordered
to show cause as to why, pursuant to the Court’s inherent authority
of the Court and its power to impose sanctions under the Civil

1 Discovery Act, the attorney's fees and costs in connection with
2 those motions should not be disgorged and returned to Defendants.

3 ...
4 For the reasons specified above, it appears that the
5 Plaintiffs' misconduct in the course of litigation and pervasive
6 litigation abuse is so egregious and deliberate such that it
7 constitutes a fraud on the court...[T]he Court has considered: the
8 apparent bad faith misconduct of Plaintiffs, the apparent level of
9 egregiousness of Plaintiffs, the amounts of attorneys' fees and
10 costs that Plaintiffs and their counsel have apparently wrongfully
11 received through prevailing on motions that were without
12 evidentiary basis, supported by evidence manufactured by
13 Plaintiffs, and/or based on meritless pleadings; the amount of time
14 spent by the Court on this frivolous action, as evidenced by the
15 number of motions involved, and the number of volumes of files of
16 papers filed with the Court (presently consisting of at least 86
17 regular volumes of court files, plus at least an additional 40 inches
18 of pleadings held in sealed envelopes and not contained in the
19 standard court files); the length of time during which Plaintiffs
20 actively pursued litigation in the instant case, despite knowing that
21 their claims were meritless; the amount of escalating damages
22 sought by Plaintiffs through their multiple iterations of their
23 complaints; an appropriate amount significant to deter Plaintiffs
24 from the frauds they continue to visit upon the court system and
25 their adversaries; and, Plaintiffs' concession that the Court may
26 draw any inference it chooses from Kwan's silence. (See Evidence
27 Code section 413.) Plaintiffs are ordered to show cause as to why,
28 pursuant to the Court's inherent authority of the Court and its
power to impose sanctions under the Civil Discovery Act,
monetary sanctions in the amount of \$250,000 should not be
awarded against them.

22 (OSC, pp.51:11-28, 52:1-26, 53:16-28, 54:1-3, 56:21-28, 57:1-12.)

23 The Court also stated that Plaintiffs were ordered to show cause as to why issue and
24 evidentiary sanctions should not be ordered against them. (See OSC, pp.54:3-28, 55:1-28, 56:1-
25 20.)

26 The holding of *Uribe* is inapposite. *Uribe* was a criminal case, involving a criminal
27 defendant's nonstatutory motion to dismiss information based upon the alternative grounds of
28 double jeopardy and outrageous prosecutorial misconduct in violation of his due process rights

1 following reversal for a *Brady* violation. (*People v. Uribe* (2011) 199 Cal.App.4th 836, 840-
2 841.) Ultimately, the appellate court reversed the trial court’s granting of the motion on the
3 ground that the criminal defendant failed to present evidence of, and the trial court did not
4 consider prejudice due to the prosecutorial misconduct. (*Id.* at pp. 870-885.) The *Uribe* court
5 cited to *Slesinger*; however, it specifically stated “*Slesinger* is obviously distinguishable, since it
6 concerned the dismissal of a civil lawsuit due to extreme litigation misconduct... [and] cannot be
7 relied on to support the proposition that a court may, in the exercise of its supervisory powers,
8 dismiss an information as a sanction for nonprejudicial prosecutorial misconduct involving false
9 testimony.” (*Id.* at p.883 (also specifically declining “to find the civil litigation principles
10 of *Slesinger* equally applicable to criminal proceedings”).) Indeed, VeriPic’s response confirms
11 the limited application of *Uribe*, noting that the *Uribe* court held that it was referring to a motion
12 to ““dismiss an information as a **sanction for nonprejudicial prosecutorial misconduct**
13 involving false testimony.”” (VeriPic’s response to OSC, p.21:20-23, quoting *Uribe, supra*, 199
14 Cal.App.4th at p.883 (emphasis added).)

15 Here, after careful consideration of the nature, deliberateness and egregiousness of the
16 misconduct, the Court’s strong preference for adjudicating claims on the merits, the integrity of
17 the Court as an institution of justice, the effect of the misconduct on a fair resolution of the case,
18 and the availability of other sanctions to cure the harm, the Court finds all of these factors to
19 weigh in favor of dismissal of VeriPic’s complaint and terminating sanctions. The Court has
20 already discussed the nature, deliberateness and egregiousness of VeriPic’s bad faith misconduct,
21 but in any event the Court finds that VeriPic intended to commit such bad faith misconduct as
22 detailed in the OSC, including: the manufacture and spoliation of evidence to needlessly increase
23 the cost of litigation, harass Defendants and cause unnecessary delay; filed false declarations
24 under penalty of perjury to needlessly increase the cost of litigation, harass Defendants, and
25 cause unnecessary delay; despite knowledge of the falsity of its allegations and assertions and
26 statements under penalty of perjury, and manufactured nature of its evidence, VeriPic sought and
27 received attorney’s fees and costs based at least in part on those false allegations, assertions and
28 statements and manufactured evidence; despite knowledge of the falsity of its allegations and

1 assertions and statements under penalty of perjury, and manufactured nature of its evidence,
2 VeriPic sought and received orders favorable to it, based at least in part on those false
3 allegations, assertions and statements and manufactured evidence; provided and received false
4 deposition testimony under penalty of perjury to needlessly increase the cost of litigation, harass
5 Defendants and cause unnecessary delay; continued to file papers and pleadings that contained
6 allegations and assertions that were knowingly untrue to needlessly increase the cost of litigation,
7 harass Defendants and cause unnecessary delay; continued to file papers and pleadings that
8 contained allegations and assertions that were knowingly supported by manufactured evidence to
9 needlessly increase the cost of litigation, harass Defendants and cause unnecessary delay; and,
10 despite knowledge of the frivolity of its claims, VeriPic pursued litigation lasting five years and
11 expanded its allegations to needlessly increase the cost of litigation, harass Defendants and cause
12 unnecessary delay. Even considering the Court's strong preference for adjudicating claims on
13 the merits, substantial evidence demonstrates that VeriPic's misconduct was so severe and
14 deliberate that sanctions other than dismissal would not be sufficient to protect the fairness of the
15 trial on VeriPic's own claims, and, violated the integrity of the Court as an institution of justice.

16 Pursuant to its inherent authority, based on VeriPic's egregious and deliberate
17 misconduct during the course of the litigation that any remedy short of dismissal would be
18 inadequate to preserve the fairness of the trial, the Court intends to order the dismissal of
19 VeriPic's claims with prejudice. (See *Slesinger, supra*, 155 Cal.App.4th at p.761-765.) Based
20 on this order, and the finding that issue and evidentiary sanctions would not be sufficient to
21 protect the fairness of the trial on VeriPic's own claims, the Court will not otherwise address the
22 subjects of issue and evidentiary sanctions.

23 This order is not intended to preclude VeriPic from presenting a defense to Foray's
24 claims; however, the Court leaves it to the trial court to determine what, if any, impact the
25 exercise of the Fifth Amendment privilege by Kwan on his own behalf and as the PMK of
26 VeriPic, has on VeriPic's or Kwan's presentation of evidence.

1 **D. Sanctions for VeriPic’s misuse of the discovery process pursuant to the**
2 **Discovery Act**

3 In light of the Court’s ruling above ordering dismissal of VeriPic’s claims, the Court
4 declines to award sanctions pursuant to the Discovery Act and Code of Civil Procedure section
5 2023.030. Also, the Court has considered whether issue and evidentiary sanctions are
6 appropriate with regards to VeriPic’s defenses in the cross-action and finds that the terminating
7 sanctions of VeriPic’s own claims is appropriately calibrated to sanction the wrong.

8 **E. The disgorgement of attorneys’ fees in connection with the special motion to**
9 **strike the second amended complaint by VeriPic and Kwan**

10 As previously stated in the OSC, VeriPic was awarded substantial attorney fees in
11 connection with the special motion to strike the second amended complaint.

12 The Court finds that, as detailed in the OSC, VeriPic filed a number of declarations by
13 Kwan under penalty of perjury that contained knowingly false statements, referred to
14 manufactured evidence, and contained arguments and reference to allegations that knowingly
15 lacked factual and evidentiary support, to support VeriPic’s opposition to defendants Witzke,
16 Temple and McFall’s special motion to strike, and VeriPic’s motion to take discovery pursuant
17 to Code of Civil Procedure section 425.16, subdivision (g). (See OSC, pp.26:8-28, 27:1-28,
18 28:1-17.) On March 24, 2011, the Court [Hon. Pierce] denied the defendants’ special motion to
19 strike, specifically noting that VeriPic “demonstrates a probability of prevailing on its claims,”
20 citing to Kwan’s declaration, the allegations of the SAC, emails relating to Caveat Emptor and
21 also “find[ing] that Defendants’ conduct falls under the commercial speech exemption under
22 section 425.17, subdivision (c).” (March 24, 2011 order re: special motion to strike the second
23 amended complaint, pp.2:18-22 (citing to “emails between defendant Foray Technologies, LLC
24 (‘Foray’) and various potential customers regarding VeriPic and the Caveat Emptor article”);
25 2:23-25, 3:4-8 (stating that “VeriPic demonstrates a probability of prevailing on its claims”),
26 citing to the Kwan declaration, the allegations of the SAC, and the emails regarding Caveat
27 Emptor).)

1 On August 19, 2011, VeriPic filed a motion for attorney fees in connection with the
2 special motion to strike. In support of this motion, VeriPic filed a memorandum that noted that
3 “the section 425.17 (c) exemption mandated that the motion be denied and cited to numerous
4 items of evidence that supported this finding... [and] that VeriPic demonstrated a probability of
5 success on its claims.” (VeriPic’s memorandum of points and authorities in support of motion
6 for attorney’s fees, p.2:7-10 and 14-15.) VeriPic contended that the defendants’ motion was
7 “unethical and improper” and frivolous, and criticized the defendants’ reply by deeming it as
8 “fluff” that avoided addressing the authorities and evidence presented by VeriPic.

9 VeriPic requested a fee award of \$400,615 plus costs in the amount of \$22,721.83.
10 VeriPic’s supporting memorandum on the motion noted that it was seeking attorney fees for
11 depositions in order to make its prima facie showing that the alleged defamatory statements were
12 false. (See VeriPic’s memorandum of points and authorities in support of motion for attorney
13 fees, p.9:13-22.) VeriPic’s supporting memorandum then noted that “VeriPic’s counsel was then
14 forced to prepare an extensive discovery motion, supported by four percipient witness
15 declarations and extensive documentary evidence that established the falsity of defendants’
16 statements.” (*Id.* at p.9:26-28.) Again, that motion was largely supported by a declaration by
17 Kwan and related to Caveat Emptor. (See Shah decl. in support of motion for attorney fees, exh.
18 D, pp.6:4-28, 7:1-28, 8:1-28, 9:1-28, 10:1-28, 11:1-17.) VeriPic specifically sought attorney fees
19 for the work expended in relation to the discovery motion, alone, in the amount of \$43,650. (See
20 VeriPic’s memorandum of points and authorities in support of motion for attorney’s fees,
21 p.10:5-6.)

22 VeriPic’s supporting memorandum on the motion for attorney fees also contended that
23 due to the “evidentiary showing required... [t]he Opposition [to the anti-SLAPP motion] was
24 accompanied by several percipient witness declarations... [and w]hile some of the declarations
25 were similar to those filed in the prior discovery motion, one of them was substantially expanded
26 to include evidence regarding damages.” (*Id.* at p.10:13-19.) The declaration VeriPic described
27 was Kwan’s declaration. VeriPic sought attorney fees for the work expended in relation to the
28 opposition to the anti-SLAPP motion in the amount of \$90,837.50. (*Id.* at p.10:21-22.)

1 VeriPic's supporting memorandum on the motion for attorney fees also sought \$22,950 for the
2 work its counsel expended in the actual motion for attorney fees. (*Id.* at p.10:23-26.) The
3 motion for attorney fees presented the SAC, the prior motions, the Caveat Emptor emails and the
4 Kwan declaration. As stated in the OSC, on September 22, 2011, the Court awarded Kwan
5 \$60,462.50 in attorney's fees plus costs of \$22,721.83, for a total award of \$83,184.33.

6 In its response to the OSC, VeriPic argues that "the record does not support the
7 conclusion that the challenged conduct was the cause of the Court's prior orders awarding fees."
8 (VeriPic's response to OSC, p.22:21-22.) At both the hearing on the OSC and in its filed
9 response to the OSC, VeriPic argues that the anti-SLAPP motion was denied because the
10 defendants failed to meet their initial burden, and "[i]t follows that the subsequent fee award
11 based on the denial of the motion was not tainted by any suspect testimony given by Mr. Kwan."
12 (VeriPic's response to OSC, pp.22:22-28, 23:1-8; see also transcript of September 19, 2014 OSC
13 hearing, pp.34:19-28, 35:1-16.)

14 First, the Court disagrees that the record does not support the conclusion that the
15 challenged conduct was a cause of the Court's prior orders awarding fees. Second, VeriPic is
16 confused on the statutory basis for an award of fees pursuant to section 425.16. A plaintiff
17 opposing a special motion to strike pursuant to 425.16 may only obtain attorney's fees if the
18 special motion to strike was "frivolous or is solely intended to cause unnecessary delay." (See
19 Code Civ. Proc. § 425.16, subd. (c)(1); see also *California Back Specialists Medical Group v.*
20 *Rand* (2008) 160 Cal.App.4th 1032, 1037-1038 (stating that "[b]efore awarding attorney fees to a
21 plaintiff who has successfully opposed an anti-SLAPP motion, the court must find that the
22 motion to strike is 'frivolous or is solely intended to cause unnecessary delay,' and the court
23 must comply with the procedural provisions of section 128.5... [including] a written order
24 reciting in detail the conduct or circumstances justifying the order".))

25 The Court's September 2, 2011 order regarding the motion for attorney's fees specifically
26 notes that it considered the issue regarding section 425.17, subdivision (c)—to which the court
27 cited the Caveat Emptor emails in the March 24, 2011 order denying the special motion to
28 strike—and the discovery and depositions ordered pursuant to Code of Civil Procedure section

1 425.16, subdivision (g), largely based on the Kwan declaration. VeriPic's assertion that "the
2 record does not support the conclusion that the challenged conduct was the cause of the Court's
3 prior orders awarding fees" is without merit.

4 VeriPic also argues that "the Court's proposed disgorgement sanction would appear to
5 violate Section 1008 of the Code of Civil Procedure, which prohibits a court from reconsidering
6 prior orders on motions made more than 10 days after the order in question and based on new
7 facts, law or circumstances." (VeriPic's response to OSC, p.22:13-16.) VeriPic is mistaken.
8 The court in the case of *Le Francois v. Goel* (2005) 35 Cal.4th 1094, a case cited by VeriPic,
9 plainly held that Code of Civil Procedure section "1008 limit[s] the parties' ability to file
10 repetitive motions [e.g. via the 10-day time limitation for such an application] but do[es] not
11 limit the court's ability, on its own motion, to reconsider its prior interim orders so it may correct
12 its own errors." (*Id.* at pp.1098, 1107.)

13 Finally, citing to *Bauguess v. Paine* (1978) 22 Cal.3d 626, and *Vidrio v. Hernandez*
14 (2009) 172 Cal.App.4th 1443, VeriPic argues that the Court lacks inherent authority to disgorge
15 attorney's fees awarded. (See VeriPic's response to OSC, p.22:7-9.) VeriPic is correct that trial
16 courts lack the inherent authority to impose monetary sanctions as a *punishment* for misconduct.
17 (See *Bauguess, supra*, 22 Cal.3d at pp.637-638; see also *Slesinger, supra*, 155 Cal.App.4th at
18 p.764, fn.19 (stating that "a trial court must be mindful that under *Bauguess*, its inherent
19 authority to sanction for egregious misconduct does not include the power to award attorney fees
20 to punish that misconduct"); but see *In re the Marriage of Lyon* (2004) 2004 Cal. App. Unpub.
21 LEXIS 10267 *1, *31-*32 (stating that "as the court had the inherent power to control the
22 proceedings before it, and the evidence showed that Elizabeth was attempting to submit a false
23 claim, the court acted well within its discretion in imposing \$ 2,500 in sanctions against
24 Elizabeth") (nonpub. opn.); see also *Smith v. Ricca* (2014) 2014 Cal. App. Unpub. LEXIS 8475
25 *1, *62 (unpublished case where trial court sanctioned party \$38,000 for "fraud on the court" in
26 underlying action); see also *Rudnick v. Rudnick* (2009)179 Cal.App.4th 1328, 1335 (stating that
27 "the *Bauguess* court affirmed that a court's equitable powers are distinguishable from its
28

1 supervisory powers when the court noted that ‘Courts have used their inherent equitable power in
2 limited situations to award attorney’s fees when it was warranted by the equities of the case’).)

3 The Court finds that an order that requires VeriPic and Kwan to disgorge fees and costs
4 that it received because of its misconduct is not intended to *punish* for that misconduct, but rather
5 to provide for an equitable restitution of amounts that were awarded to VeriPic and Kwan only
6 because of their misrepresentations, false allegations, manufactured evidence and unsupported
7 arguments. The Court finds that fairness and equity require this result. It would be inequitable
8 and unjust to allow Kwan and VeriPic to retain funds they received because of their wrongful
9 conduct, and only fair to require the return of wrongfully obtained funds to place Defendants in a
10 position where they should have been.

11 As *Slesinger* indicates, “[t]he essential requirement... [in a court’s exercise of its inherent
12 power] is to calibrate the sanction to the wrong.” (*Slesinger, supra*, 155 Cal.App.4th at p.763.)
13 The exercise of the court’s inherent authority “derives in part from the court’s historic powers in
14 equity.” (*Id.*) The disgorgement of fees wrongfully awarded against one party so as to restore
15 that party to its former position, is restitutionary in nature. (See *Meister v. Mensinger* (2014) 230
16 Cal.App.4th 381, 398 (noting that “[t]here are two types of disgorgement: restitutionary
17 disgorgement, which focuses on the plaintiff’s loss, and nonrestitutionary disgorgement, which
18 focuses on the defendant’s unjust enrichment”); also stating that “[t]ypically, the defendant’s
19 benefit and the plaintiff’s loss are the same, and restitution requires the defendant to restore the
20 plaintiff to his or her original position”); see also *Feitelberg v. Credit Suisse First Boston, LLC*
21 (2005) 134 Cal.App.4th 997, 1013 (stating that “[w]ith restitutionary disgorgement, the focus is
22 on the plaintiff’s loss... [i]t is typified by the situation where ‘the disgorged money or property
23 came from the prospective plaintiff in the first instance’”).)

24 As the disgorgement of fees in this context is restitutionary in nature, it does not violate
25 *Bauguess*’ prohibition on the awarding of attorney fees to punish misconduct. Moreover, the
26 disgorgement of fees does not violate *Bauguess*’ prohibition on awarding attorney fees to punish
27 misconduct as the Court is not *awarding* fees; rather the Court is ordering the return of fees that
28 were previously wrongfully awarded. (See *People v. Super. Ct. (Jayhill Corp.)* (1973) 9 Cal.3d

1 283, 286 (stating that “a court of equity may exercise the full range of its inherent powers in
2 order to accomplish complete justice between the parties, restoring if necessary the *status quo*
3 *ante* as nearly as may be achieved”); see also *Fletcher v. Sec. Pac. Natl. Bank* (1979) 23 Cal.3d
4 442, 452 (stating that “[e]ven in the absence of the specific authorization contained in section
5 17535 [of the UCL], a trial court has the inherent power to order restitution as a form of ancillary
6 relief”); see also *People v. Pacific Land Research Co.* (1977) 20 Cal.3d 10, 19 (same); see also
7 *Rogers v. Bill & Vince's, Inc.* (1963) 219 Cal. App. 2d 322, 324 (stating that “[i]t is settled law...
8 that the trial court has inherent power to afford [restitution]”); see also *Bank of America Nat'l*
9 *Trust & Sav. Assn. v. McLaughlin* (1940) 37 Cal.App.2d 415, 417 (stating that “the trial court has
10 the power to order such restitution, which power is inherent and exists independently of any
11 statute”); see also *Rutherford v. Owens-Illinois, Inc.* (1997) 16 Cal.4th 953, 967 (stating that
12 “[c]ourts have inherent power... [that] entitles trial courts to exercise reasonable control over all
13 proceedings connected with pending litigation in order to insure the orderly administration of
14 justice”; also stating that “[c]ourts are not powerless to formulate rules of procedure where
15 justice demands it”).) Accordingly, the Court intends to order VeriPic and Kwan to return the
16 \$83,184.33 in attorney fees and costs to defendants Witzke, Temple and McFall.

17 **F. Sanctions for VeriPic’s and Kwan’s “fraud on the court”**

18 The Court also finds that the undisputed evidence clearly and convincingly demonstrates
19 that VeriPic and Kwan have committed “fraud on the court” through their: fabrication of and
20 spoliation of evidence; presentation of evidence to the Court, made under penalty of perjury
21 despite knowledge of its untruthfulness; reference to that evidence in papers, arguments and
22 allegations despite knowledge of its untruthfulness; seeking and receiving attorney fees and
23 orders favorable to them, based at least in part on those false allegations, assertions and
24 statements and fabricated evidence; the filing of knowingly false deposition testimony under
25 penalty of perjury; and the continued pursuit of frivolous claims for more than five years and
26 expansion of their claims despite knowledge of the falsity of the essence of its allegations, with
27 intent to needlessly increase the cost of litigation, harass Defendants and cause unnecessary
28 delay. The performance of these acts were a part of VeriPic’s and Kwan’s unconscionable,

1 egregious, deliberate, willful and knowing scheme calculated to interfere with the judicial
2 system's ability impartially to adjudicate a matter by improperly influencing the Court and
3 unfairly hampering the presentation of the opposing party's claims and defenses. (See *Aoude v.*
4 *Mobil Oil Corp.* (1st Cir. 1989) 892 F.2d 1115, 1118 (stating that "[a] 'fraud on the court' occurs
5 where it can be demonstrated, clearly and convincingly, that a party has sentiently set in motion
6 some unconscionable scheme calculated to interfere with the judicial system's ability impartially
7 to adjudicate a matter by improperly influencing the trier or unfairly hampering the presentation
8 of the opposing party's claim or defense".))

9 At the hearing, VeriPic presented no argument regarding "fraud on the court." However,
10 in its response to the OSC, VeriPic again argues that the Court lacks the authority to use fee
11 awards to punish misconduct pursuant to its inherent authority and the OSC does not indicate
12 that the Court intends to impose sanctions under its contempt power. (See VeriPic's response to
13 OSC, pp.25:18-28, 26:1-2, citing to *Andrews v. Super. Ct. (Thomas)* (2000) 82 Cal.App.4th 779,
14 782 (stating that "a punitive monetary sanction such as the one before us is not authorized under
15 either section 128 or the inherent powers of the courts"), citing *Bauguess, supra*, 22 Cal.3d 626,
16 637-638; also citing *Vidrio, supra*, 172 Cal.App.4th at pp.1454-1455 and *Trans-Action*
17 *Commercial Investors v. Firmaterr* (1997) 60 Cal.App.4th 352, 366, likewise citing to *Bauguess,*
18 *supra*, 22 Cal.3d 626.)

19 As previously stated, the Court does not intend to award attorney fees as punishment for
20 Plaintiffs' misconduct. The sanction the Court contemplates does not involve attorney fees;
21 instead the Court intends to order a modest portion of the cost incurred by the Court associated
22 with the frivolous litigation, willful misconduct, and fraud on the court perpetuated for four years
23 by VeriPic and Kwan. As with the disgorgement of the attorney fee award, the power involved
24 is restitutionary in nature—and within the parameters of the Court's inherent authority.

25 In its response to the OSC, VeriPic also argues that "the record does not demonstrate a
26 'fraud' that would warrant sanctions in the magnitude proposed... [as] the apparent
27 inconsistencies between Kwan's August and December, 2008 emails and his later declarations
28 relating to whether he told BigBiz to direct any traffic internet traffic [sic] to the subject

1 domains to VeriPic is not a substantial part of this case.” (VeriPic’s response to OSC, p.26:3-6.)
2 VeriPic concludes that “[t]he record does not support the conclusion that VeriPic’s or Kwan’s
3 assertion of this defense was pervasive or that it caused the Court or Foray any substantial harm,
4 certainly not in the magnitude of \$250,000.” (*Id.* at p.26:8-10.) Yet, in the next section, VeriPic
5 states that “[t]he Court should not have the impression that the seriousness of the OSC has been
6 lost on VeriPic... [and that] VeriPic does not condone or attempt to minimize problems that have
7 occurred.” (*Id.* at pp.26:28, 27:1-13.)

8 Nevertheless, VeriPic’s continues to minimize the seriousness of its behavior, and the
9 damage caused. As described in detail above, the Court disagrees with VeriPic’s
10 characterization of the pervasiveness of VeriPic’s misconduct. Contrary to VeriPic’s
11 unsupported assertions, the evidence and record clearly and convincingly demonstrates VeriPic’s
12 fraud on the court for the reasons mentioned. As to VeriPic’s argument that four years of
13 frivolous claims failed to cause any substantial harm to the Court or Foray, VeriPic apparently
14 ignores the Court’s comments at the hearing. This case has been an enormous burden not only
15 on the parties but also on the Court’s resources. (See *Finnie v. Town of Tiburon* (1988) 199
16 Cal.App.3d 1, 17 (noting that, in addition to the parties to the instant case, “other... parties, many
17 of whom wait years for a resolution of bona fide disputes, are prejudiced by the useless diversion
18 of this court’s attention” in a frivolous appeal, and that “[i]n the same vein, the appellate system
19 and the taxpayers of this state are damaged by what amounts to a waste of this court’s time and
20 resources”); see also *Pierotti v. Torian* (2000) 81 Cal.App.4th 17, 35 (stating that “[b]ecause a
21 frivolous appeal, or one taken for improper reasons, harms the court, not just the respondent, a
22 growing number of courts are ordering appellants to pay sanctions directly to the court clerk to
23 compensate the state for the cost of processing such appeals”); see also *Singh v. Lipworth* (2014)
24 227 Cal.App.4th 813, 830 (stating that “[c]ourts, with increasing frequency, have imposed
25 additional sanctions, payable to the clerk of the court, to compensate the state for the cost to the
26 taxpayers of processing a frivolous appeal”); also noting that the average costs associated with
27 processing an appeal is \$8,000.)
28

1 Including complex cases filed in this court, the vast majority of civil cases—greater than
2 75%--have the papers contained in a fraction of a single file volume. (See Vojnik decl., ¶ 3.)
3 Including the pleadings filed under seal, the instant action will exceed 100 file volumes; thus, by
4 this one measure alone, the Court has utilized a hundred times more of its scarce resources on
5 this single case than on a typical case. The total number of separate pleadings and papers filed
6 since the second amended complaint are 1,230. (See Vojnik decl., ¶ 4.) For the time spent by
7 court staff just to accept and place these pleadings into the court file, the Court expends
8 approximately \$11.21 per paper filed. (See Vojnik decl., ¶ 4.) At least for now, the Court must
9 store all filed pleadings on site, at a cost the Court cannot measure.

10 Additionally, the Court has held 175 hearings in this case (see Vojnik decl., ¶ 4),
11 including a number of special set hearings due to the complexity of the issues raised. The cost to
12 the Court for its clerical staff to simply process the paperwork, prepare the files, calendar a
13 motion, and organize the documents for a hearing, and prepare the minutes, is approximately
14 \$48.14 per hearing. (See Vojnik decl., ¶ 4.) The costs estimated here do NOT include the cost
15 of the court reporter, the courtroom deputy, research staff, or the judicial officer, and do not
16 include the additional clerical and courtroom clerk time that is expended for a variety of other
17 tasks, including, *inter alia*, searching for misplaced pleadings, phone calls (which consume a
18 surprising amount of the courtroom clerk's time), and moving and organizing a file of this
19 magnitude.

20 For that portion of the costs that the Court can presently measure over the past four years,
21 and not including much more costly expense to the Court such as research staff and judges, the
22 Court has expended at least \$22,212.80 on meritless claims. (See Vojnik decl., ¶ 4.) As this
23 only reflects the clerical costs to take in the pleadings and prepare those documents for hearing,
24 the actual costs to the Court greatly exceed this amount.

25 The Court, thus, under its inherent authority, intends to order payment of \$22,000,
26 payable to the Clerk of the Court by Kwan and VeriPic.

1 **G. VeriPic’s motion for leave to amend**

2 In light of the Court’s ruling regarding terminating sanctions, VeriPic’s motion for leave
3 to amend is MOOT.

4 **H. Foray’s motion for sanctions and for attorney fees**

5 Defendant Foray moved for terminating and monetary sanctions against Kwan, VeriPic
6 and Grellas Shah pursuant to section 128.7. As already addressed above, Kwan dismissed his
7 claims and, as stated in VeriPic’s response to the OSC, “the challenged papers were withdrawn
8 within the safe harbor period.” (VeriPic’s response to OSC, p.19:5.) VeriPic’s counsel has also
9 represented that it does not intend to pursue claims based on “the heart of” the alleged purported
10 defamatory scheme by Defendants. For reasons already articulated, Foray’s motion for sanctions
11 pursuant to Code of Civil Procedure section 128.7 is DENIED.

12 Defendant Foray also moved for terminating and monetary sanctions against Kwan,
13 VeriPic and Grellas Shah pursuant to Code of Civil Procedure section 2023.030, as a misuse of
14 the discovery process. As to the motion’s request for monetary sanctions, the supporting
15 memorandum fails to state any amount sought. More recently, Foray filed a motion for attorney
16 fees with new factual bases for its motion—apparently realizing the original motion’s
17 deficiencies—and now seeks \$4 million. The initial motion did not reference any such amount.
18 The Court finds that it would not be proper for the Court to order attorney fees incurred by Foray
19 for defense of the Plaintiffs’ claims based on the Court’s OSC based on fraud on the Court, as
20 such an award could be considered as punishment for the misconduct the Court has found has
21 occurred. Foray’s motion for monetary sanctions is DENIED.

22 As to Foray’s motion for terminating sanctions, the motion is MOOT in light of the
23 Court’s ruling on the OSC.

24 **I. Additional orders on pending matters**

25 Foray’s motion for summary adjudication of VeriPic’s Lanham Act claims is ordered off
26 calendar as moot.

1 **Further Hearings on the Court's OSC**

2 As the Court indicated when it set this court date with the intention to provide the order
3 to the parties, the Court will allow Kwan and VeriPic to respond to the Court's intended rulings
4 as to specific sanctions. Accordingly, Kwan and VeriPic will be allowed to each file a single
5 brief addressing only the order to disgorge attorney fees and the payment of sanctions to the
6 Court. The parties have had an adequate opportunity to brief the issue of terminating sanctions,
7 and the Court does not intend to allow further argument on the topic of terminating sanctions.

8 The Court will set a briefing schedule and schedule a final hearing after consultation with
9 the parties.

10
11 December 12, 2014

Mary E. Arand

Mary E. Arand
Judge of the Superior Court