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***Newby* v. *Enron*:** **The Effect of Settlement on an Appeal from an Order Imposing Compensatory Sanctions**

On May 30, 2008, the Court of Appeals for the Fifth Circuit decided *Newby* v. *Enron*, which involved an appeal "seeking vacatur of the district court's imposition of compensatory attorneys' fees in light of the [parties'] settlement of [their underlying suit]."[1] The court held that the parties have the right "to bargain away sanctions designed to compensate the parties themselves."[2] However, "where a district court has reviewed a case of misconduct and issued a well reasoned sanctions order," the court will not vacate the order in its entirety, as the "court's right to sanction parties for misconduct remains."[3]

I. BACKGROUND

Courts disagree on the issue of the effect of a settlement on an appeal from an order imposing sanctions payable to the opposing party.[4] The dominant view is that, once the parties settle a dispute, "a determination by an appellate court of the legal issues underlying the sanctions order is no longer necessary to compel payment of the fees and cannot prevent it; therefore, the settlement moots the appeal."[5] On the other hand, some courts find "that the parties cannot bargain away the court's discretion

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1 Newby v. Enron, No. 07-20277, 2008 WL 2231661, at *3 (5th Cir. May 30, 2008).

2 *Id.* at *9.

3 *Id.*

4 2A Fed. Proc., L. Ed. § 3:259 (Apr. 2008).

5 *Id.*

relating to the imposition of sanctions so that an appeal of the sanctions order after settlement of the case between the parties is not moot."[6]

II. FACTS AND PROCEDURAL HISTORY

In this case, Fleming & Associates L.L.P. represented several consolidated plaintiffs asserting claims against the former outside directors of Enron in the Southern District of Texas.[7] During the course of discovery, the plaintiffs timely submitted an expert report, but subsequently revised it after the expert discovery deadline without notice to the defendants.[8] The defendants became aware of the revision at the expert's deposition and halted the questioning to file a motion to exclude the expert's testimony.[9] As a result, on September 14, 2006, the court sanctioned the plaintiffs' counsel, ordering that they compensate the defendants for reasonable attorneys' fees incurred in bringing the motion.[10]

The plaintiffs moved for reconsideration of the sanctions order on September 28, 2006.[11] Then, in early December of 2006, the parties settled the underlying dispute, agreeing to pay their own attorneys' fees and costs.[12] However, "[o]n February 8, 2007, the district court denied reconsideration of its sanctions order," and after a hearing, the magistrate judge ordered plaintiffs' counsel to pay the defendants $15,214.45 in attorneys' fees and expenses.[13]

On appeal of the sanctions order, the plaintiffs argued that, "either the settlement stripped the district court of jurisdiction to impose compensatory sanctions, requiring mandatory vacatur, or the Fleming Plaintiffs should be entitled to equitable vacatur of the sanctions because the settlement made

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6 *Id.*

7 *See Newby*, 2008 WL 2231661, at *3.

8 *Id.*

9 *Id.* at *4.

10 *See id.*

11 *Id.*

12 *See id.*

13 *Id.*

any appeal of the sanctions moot," and that the district court abused its discretion in granting the sanctions order.[14]

III. RATIONALE OF THE COURT

Looking primarily to the Seventh and Eleventh Circuits for guidance,[15] the Fifth Circuit vacated the compensatory portion of the sanctions as moot, but declined to vacate the order in its entirety.[16] The court also cited an Eighth Circuit opinion, agreeing "that '[a]ppellants are entitled to bargain with adversaries to drop a motion for sanctions, but they cannot unilaterally bargain away the court's discretion in imposing sanctions and the public's interest in ensuring compliance with the rules of procedure.' "[17] The court reasoned "that a compensatory sanction — primarily intended to compensate a party for a wrong committed against it by the opposing party — is substantially different from a purely punitive sanction, in which a litigant must pay the court or perform some other penance for misbehavior."[18]

The court vacated the monetary portion of the sanctions as, if "the magistrate judge's March 6, 2007 order [was] the only final sanctions order at issue, the issue of monetary sanctions was moot at that time . . . Alternatively, because the settlement moots any appeal of the compensatory portion of the sanctions," if the September 14 order was final, the court should apply equitable vacatur.[19] The court, however, declined to vacate the order in its entirety, as the non-monetary sanctions issue was not moot prior to the settlement, and therefore the district court had jurisdiction when it issued the sanctions order on September 14, making mandatory vacatur inapplicable.[20] The court also noted that, "[e]ven if

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14 *Id.* at *5.

15 *See Clark Equipment Co.* v. *Lift Parts Mfg. Co.*, 972 F.2d 817, 819 (7th Cir. 1992) (holding that when a district court imposes sanctions in the form of a punitive fine made payable to the court or non-monetary sanctions, these sanctions cannot be avoided by settlement, however, when a court imposes sanctions to compensate the other party, the parties may bargain away that interest by settling); *Kleiner* v. *First Nat'l Bank of Atlanta*, 751 F.2d 1193, 1199 (11th Cir. 1985) (holding that while parties may bargain away compensatory sanctions through settlement, the court otherwise retains the right to sanction parties for misconduct).

16 *See Newby*, 2008 WL 2231661, at *7.

17 *Id.* (quoting *Perkins* v. *General Motors Corp.*, 965 F.2d 597, 600 (8th Cir. 1992)).

18 *Id.*

19 *Id.* at *8.

20 *See id.*

the September 14 order was not a final judgment, equitable vacatur [was] not appropriate because the order [was] nevertheless appealable: Any non-monetary portion of the sanctions not rendered moot by settlement is appealable for its residual reputational effects on the attorney."[21]

Ultimately the court vacated the district court's order to the extent that it made a compensatory award of attorneys' fees, as the issue of monetary sanctions was moot, but "decline[d] to vacate the district court's sanctions order in its entirety because the court did not abuse its discretion when it issued its original sanctions order."[22]

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If you have any questions about the issues addressed in this memorandum or if you would like a copy of any of the materials mentioned, please do not hesitate to call or email Charles A. Gilman at (212) 701-3403 or cgilman@cahill.com; Jon Mark at (212) 701-3100 or jmark@cahill.com; John Schuster at (212) 701-3323 or jschuster@cahill.com.

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21 *Id.*

22 *Id.* at *9.