

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

FINAL 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

Following an evidentiary hearing on March 21, 2014 on a motion for sanctions that had been filed by Defendants Thomas Hennings ("Hennings") and Foray Technologies, LLC ("Foray, and collectively, "Defendants"), on May 2, 2014 the Court issued its order to show

1 cause why Plaintiffs John Kwan (“Kwan”) and Kwan Software Engineering, Inc. (known as
2 “VeriPic,” and collectively “Plaintiffs”) and their former counsel Grellas Shah have not violated
3 Code of Civil Procedure section 128.7, and the Court’s order to show cause why Plaintiffs and
4 their former counsel should not be subject to monetary, issue, evidentiary and terminating
5 sanctions for their conduct pursuant to the Court’s inherent authority and the Discovery Act
6 (“Court’s OSC”). All parties and Plaintiffs’ former counsel, George Grellas (“Grellas”) and
7 Dhaivat Shah (“Shah”) of Grellas Shah LLP were given multiple opportunities to file pleadings
8 and present evidence, testimony and argument regarding Defendant’s motion for sanctions and
9 the Court’s OSC.

10 The evidentiary hearing on Defendant’s motion for sanctions was held on March 21,
11 2014, and hearings on the Court’s OSC were held on September 19, 2014, December 12, 2014
12 and February 27, 2015 in Department 9 before the Honorable Mary E. Arand.

13 On December 12, 2014, the Court announced its decision and issued its Interim Order
14 (“December Interim Order”), but allowed final briefing on the issue of sanctions. In making
15 these findings and orders, the Court has considered the various pleadings, briefs, memoranda,
16 and declarations filed by the respective parties in connection with this OSC and related motions,
17 the testimony and evidence presented at all related hearings, the arguments made, and the
18 documents contained within the Court’s file.

19 The Court now issues its Final Order and hereby adopts and incorporates all findings and
20 intended findings stated in the December Interim Order, finds that all facts stated in the
21 December Interim Order are true, and orders as follows:

22 **I. Findings and Orders on Court’s OSC**

23 **A. *Grellas Shah***

24 The Court finds that due process prevents the Court from imposing sanctions against
25 Grellas Shah and its attorneys because they cannot provide a complete response to the OSC
26 because of the exercise of the Fifth Amendment privilege by their client, John Kwan, and the
27 duty of loyalty owed to their former clients.

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

6 Based on these findings, and the findings in the December Interim Order incorporated
7 here, IT IS HEREBY ORDERED that sanctions shall not be imposed by the Court against
8 Grellas Shah or its individual attorneys.

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

11 The Court finds that the Kwan emails, quoted in the Court's OSC, demonstrate that
12 Kwan's statements in declarations sworn under penalty of perjury and filed with the Court were
13 false; that Kwan made false statements under oath in declarations submitted to the Court under
14 penalty of perjury; and that Kwan and VeriPic filed multiple verified pleadings that contained
15 false statements of fact. Based on these findings and the findings in the December Interim Order
16 incorporated here, the Court finds that Kwan and VeriPic violated the prohibitions found in Code
17 of Civil Procedure section 128.7 as described in the Court's OSC by the relentless pursuit of the
18 demonstrably false Caveat Emptor claims, first alleged in the Second Amended Complaint and
19 repeated through each successive amended complaint through the Seventh Amended Complaint.

20 The Court also finds that Kwan and VeriPic took steps to spoliage evidence, in that Kwan
21 and VeriPic took affirmative steps to hide, conceal, and suppress relevant evidence related to its
22 own claims and their defense of affirmative claims by the Defendants. (See definition of
23 spoliation found in the following cases: *Williams v. BASF Catalysts LLC* (3d. Cir 2014) 765 F.3d
24 306, 320; see also *R.S. Creative, Inc. v. Creative Cotton, Ltd.* (1999) 75 Cal.App.4th 486, 497;
25 *Willard v. Caterpillar, Inc.* (1995) 40 Cal.App.4th 892, 907, disapproved on other grounds in
26 *Cedars-Sinai Medical Center v. Super. Ct. (Bowyer)* (1998) 18 Cal. 4th 1, 18; *Rosen v. St.*
27 *Joseph Hospital of Orange County* (2011) 193 Cal.App.4th 453, 462; see also *Cedars-Sinai*
28 *Medical Center v. Super. Ct. (Bowyer)* (1998) 18 Cal. 4th 1, 4 see also Evid. Code 413.)

1 The Court finds that Kwan and VeriPic withheld, and attempted to conceal or alter
2 evidence that would have shown that Kwan's sworn statements filed with the Court, deposition
3 testimony, and the pleadings and claims made in this case were false, and that VeriPic, through
4 Kwan, presented claims that they knew were without evidentiary basis.

5 Although the Court finds that multiple pleadings filed with the Court and signed by Kwan
6 on behalf of VeriPic violated Code of Civil Procedure section 128.7(b), sanctions based on Code
7 of Civil Procedure section 128.7 are DENIED, based on the other orders the Court is not issuing.

8 **C. The Court's inherent authority to dismiss**

9 Kwan first invoked his right not to incriminate himself at a deposition taken after he had
10 dismissed his individual claims against Foray (without prejudice). However, Kwan appeared at
11 that deposition as the designated PMK for Plaintiff VeriPic. VeriPic was still a plaintiff, but
12 through Kwan, attempted to exercise a fifth amendment right.

13 "Corporations have no privilege against self-incrimination." *Navel Orange*
14 *Administrative Committee v. Exeter Orange Co.* (9th Cir. 1983) 722 F.2d 449, 454. "[T]he
15 constitutional privilege against self-incrimination is 'essentially a personal one, applying only to
16 natural individuals.' It 'cannot be utilized by or on behalf of any organization, such as a
17 corporation.'" *George Campbell Painting Corp. v. Reid* (1968) 392 U.S. 286, 288-289.

18 VeriPic's refusal to testify, and failure to produce any evidence to controvert the factual
19 statements in the OSC, is sufficient among other affirmative evidence presented to support the
20 Court's findings that the facts stated in the OSC are true.

21 VeriPic's claim that Defendants are not prejudiced fails to account for over five years of
22 litigation costs and court costs involved in defending frivolous and meritless litigation or the
23 Court's own costs involved in handling the litigation. The Court finds that Defendants will be
24 prejudiced if VeriPic is allowed to continue to pursue its peripheral claims that may also lack
25 merit, and for which VeriPic has failed to offer evidentiary support. Further, prejudice to an
26 opposing party as a result of the misconduct is not one of the inquiries "to be made by trial courts
27 when determining whether a plaintiff's actions warrant a dismissal with prejudice," as stated by
28 *Stephen Slesinger, Inc. v. Walt Disney Co.* (2007) 155 Cal.App.4th 736, 740 ; rather, the holding

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

5 Here, after careful consideration of the nature, deliberateness and egregiousness of the
6 misconduct, the Court’s strong preference for adjudicating claims on the merits, the integrity of
7 the Court as an institution of justice, the effect of the misconduct on a fair resolution of the case,
8 and the availability of other sanctions to cure the harm, based on the findings made here and in
9 the December Interim Order incorporated here, the Court finds all of these factors to weigh in
10 favor of dismissal of VeriPic’s complaint and terminating sanctions. The Court has already
11 discussed the nature, deliberateness and egregiousness of VeriPic’s bad faith misconduct, but the
12 Court also finds that VeriPic intended to commit such bad faith misconduct as detailed in the
13 OSC, including: the manufacture and spoliation of evidence to needlessly increase the cost of
14 litigation, harass Defendants and cause unnecessary delay; filed false declarations under penalty
15 of perjury to needlessly increase the cost of litigation, harass Defendants, and cause unnecessary
16 delay; despite knowledge of the falsity of its allegations and assertions and statements under
17 penalty of perjury, and manufactured nature of its evidence, VeriPic sought and received
18 attorney’s fees and costs based at least in part on those false allegations, assertions and
19 statements and manufactured evidence; despite knowledge of the falsity of its allegations and
20 assertions and statements under penalty of perjury, and manufactured nature of its evidence,
21 VeriPic sought and received orders favorable to it, based at least in part on those false
22 allegations, assertions and statements and manufactured evidence; provided and received false
23 deposition testimony under penalty of perjury to needlessly increase the cost of litigation, harass
24 Defendants and cause unnecessary delay; continued to file papers and pleadings that contained
25 allegations and assertions that were knowingly untrue to needlessly increase the cost of litigation,

26
27 ¹ The *Slesinger* court stated that “[t]he decision whether to exercise the inherent power to dismiss requires
28 consideration of all relevant circumstances, including the nature of the misconduct (which must be deliberate and
egregious, but may or may not violate a prior court order), the strong preference for adjudicating claims on the
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.)

1 harass Defendants and cause unnecessary delay; continued to file papers and pleadings that
2 contained allegations and assertions that were knowingly supported by manufactured evidence to
3 needlessly increase the cost of litigation, harass Defendants and cause unnecessary delay; and,
4 despite knowledge of the frivolity of its claims, VeriPic pursued litigation lasting five years and
5 throughout the case has expanded its allegations to needlessly increase the cost of litigation,
6 harass Defendants and cause unnecessary delay. Even considering the Court's strong preference
7 for adjudicating claims on the merits, substantial evidence demonstrates that VeriPic's
8 misconduct was so severe and deliberate that sanctions other than dismissal would not be
9 sufficient to protect the fairness of the trial on VeriPic's own claims, and, violated the integrity
10 of the Court as an institution of justice.

11 IT IS HEREBY ORDERED that VeriPic's claims are dismissed with prejudice pursuant
12 to the Court's inherent authority, and based on Kwan and VeriPic's egregious and deliberate
13 misconduct during the course of the litigation such that any remedy short of dismissal would be
14 inadequate to preserve the fairness of the trial. (See *Slesinger, supra*, 155 Cal.App.4th at p.761-
15 765.)

16 Based on this order, and the finding that issue and evidentiary sanctions would not be
17 sufficient to protect the fairness of the trial on VeriPic's own claims, the Court will not otherwise
18 address the subjects of issue and evidentiary sanctions. This order is not intended to preclude
19 VeriPic from presenting a defense to Foray's claims; however, the Court leaves it to the trial
20 court to determine what, if any, impact the exercise of the Fifth Amendment privilege by Kwan
21 on his own behalf and as the PMK of VeriPic, has on VeriPic's or Kwan's presentation of
22 evidence.

23 **D. Sanctions for VeriPic's misuse of the discovery process pursuant to the**
24 **Discovery Act**

25 In light of the Court's ruling above ordering dismissal of VeriPic's claims, the Court
26 declines to award sanctions pursuant to the Discovery Act and Code of Civil Procedure section
27 2023.030. Also, the Court has considered whether issue and evidentiary sanctions are
28 appropriate with regards to VeriPic's defenses in the cross-action and finds that the terminating
sanctions of VeriPic's own claims is appropriately calibrated to sanction the wrong.

1 **E. The disgorgement of attorneys' fees in connection with the special motion to**
2 **strike the second amended complaint by VeriPic and Kwan**

3 As previously stated in the Court's OSC and the December Interim Order, VeriPic was
4 awarded substantial attorney fees in connection with the special motion to strike the second
5 amended complaint.

6 The Court finds that, as detailed in the Court's OSC and the December Interim Order,
7 VeriPic filed a number of declarations by Kwan under penalty of perjury that contained
8 knowingly false statements, referred to manufactured evidence, and contained arguments and
9 reference to allegations that knowingly lacked factual and evidentiary support to support
10 VeriPic's opposition to defendants Witzke, Temple and McFall's special motion to strike, and
11 VeriPic's motion to take discovery pursuant to Code of Civil Procedure section 425.16,
12 subdivision (g), that led to orders favorable to VeriPic. Specifically, the Court denied
13 Defendants' special motion to strike, and awarded Kwan \$60,462.50 in attorney's fees plus costs
14 of \$22,721.83, for a total award of \$83,184.33. Kwan originally sought more than \$400,000.

15 Based on these findings and on the findings in the December Interim Order incorporated
16 here, the Court finds that fairness and equity require an order that VeriPic and Kwan shall
17 disgorge fees and costs that they received because of misrepresentations, false allegations,
18 manufactured evidence and unsupported arguments. It would be inequitable and unjust to allow
19 Kwan and VeriPic to retain funds they received because of their wrongful conduct, and only fair
20 to require the return of wrongfully obtained funds to place Defendants in a position where they
21 should have been.

22 IT IS HEREBY ORDERED that VeriPic and Kwan shall disgorge to Defendants the
23 \$83,184.33 in attorney fees and costs paid to them by defendants Witzke, Temple and McFall,
24 not to punish VeriPic and Kwan for their misconduct, but as restitution and the return of those
25 fees according to the Court's equitable powers, within twenty days of issuance of this order.

26 **F. Sanctions for VeriPic's and Kwan's "fraud on the court"**

27 Based on the findings here and in the December Interim Order incorporated here, the
28 Court finds that the undisputed evidence clearly and convincingly demonstrates that VeriPic and
 Kwan have committed "fraud on the court" through their: fabrication of and spoliation of

1 evidence; presentation of evidence to the Court, made under penalty of perjury despite
2 knowledge of its untruthfulness; reference to that evidence in papers, arguments and allegations
3 despite knowledge of its untruthfulness; seeking and receiving attorney fees and orders favorable
4 to them, based at least in part on those false allegations, assertions and statements and fabricated
5 evidence; the filing of knowingly false deposition testimony under penalty of perjury; and the
6 continued pursuit of frivolous claims for more than five years and expansion of their claims
7 despite knowledge of the falsity of the essence of its allegations, with intent to needlessly
8 increase the cost of litigation, harass Defendants and cause unnecessary delay. The performance
9 of these acts were a part of VeriPic's and Kwan's unconscionable, egregious, deliberate, willful
10 and knowing scheme calculated to interfere with the judicial system's ability impartially to
11 adjudicate a matter by improperly influencing the Court and unfairly hampering the presentation
12 of the opposing party's claims and defenses.

13 The Court's order of sanctions payable to the Court is intended solely as restitution of a
14 modest portion of the cost incurred by the Court associated with the frivolous litigation, willful
15 misconduct, and fraud on the court perpetuated for four years by VeriPic and Kwan, and is not
16 intended to punish Kwan and VeriPic's misconduct.

17 The Court finds that this case has been an enormous burden not only on the parties but
18 also on the Court's resources. (See *Finnie v. Town of Tiburon* (1988) 199 Cal.App.3d 1, 17
19 (noting that, in addition to the parties to the instant case, "other... parties, many of whom wait
20 years for a resolution of bona fide disputes, are prejudiced by the useless diversion of this court's
21 attention" in a frivolous appeal, and that "[i]n the same vein, the appellate system and the
22 taxpayers of this state are damaged by what amounts to a waste of this court's time and
23 resources"); see also *Pierotti v. Torian* (2000) 81 Cal.App.4th 17, 35 (stating that "[b]ecause a
24 frivolous appeal, or one taken for improper reasons, harms the court, not just the respondent, a
25 growing number of courts are ordering appellants to pay sanctions directly to the court clerk to
26 compensate the state for the cost of processing such appeals"); see also *Singh v. Lipworth* (2014)
27 227 Cal.App.4th 813, 830 (stating that "[c]ourts, with increasing frequency, have imposed
28 additional sanctions, payable to the clerk of the court, to compensate the state for the cost to the

1 taxpayers of processing a frivolous appeal”; also noting that the average costs associated with
2 processing an appeal is \$8,000.)

3 Based on the evidence found in the Alicia Vojnik declaration that reflects only a portion
4 of the costs that the Court can presently measure over the past four years, that does not include
5 much more costly expense to the Court such as research staff and judges, the Court has expended
6 at least \$22,212.80 on meritless claims. As this only reflects the clerical costs to take in the
7 pleadings and prepare those documents for hearing, the actual costs to the Court greatly exceed
8 this amount.

9 IT IS HEREBY ORDERED pursuant to the Court’s inherent authority, that Kwan and
10 VeriPic shall pay the sum of \$22,000 to the Clerk of the Court within twenty days of issuance of
11 this order.

12 **II. Orders on related motions:**

13 **A. VeriPic’s motion for leave to amend**

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

16 **B. Foray’s motions**

17 For the reasons stated in the Court’s December Interim Order, the motion by Defendant
18 Foray for terminating and monetary sanctions against Kwan, VeriPic and Grellas Shah pursuant
19 to section 128.7, and as a misuse of the discovery process, is DENIED.

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

22 Foray’s motion for summary adjudication of VeriPic’s Lanham Act claims was ordered
23 off calendar as moot.

24
25 July 9, 2015

Mary E. Arand

26
27 _____
Mary E. Arand
Judge of the Superior Court