New York State Law Digest

REPORTING IMPORTANT OPINIONS OF THE COURT OF APPEALS AND IN SPECIAL SITUATIONS OF OTHER COURTS

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SPOLIATION OF ELECTRONIC DATA: FAILURE TO PUT TIMELY "LITIGATION HOLD" ON COMPUTER TO PRESERVE RELEVANT DATA PRODUCES SANCTION OF "ADVERSE INFERENCE" AGAINST VIOLATOR

MAJOR TREATMENT BY APPELLATE DIVISION, ADOPTING FEDERAL *ZUBULAKE* DECISION

The first major case on electronic discovery in New York was Justice Austin's supreme court decision in Nassau County in *Lipco Electrical Corp. v. ASG Consulting Corp.*, 2004 WL 1949062, Aug. 18, 2004. There were a number of New York decisions on the subject after that, addressing the key question of what to do when a party has failed to preserve computerized data (such as emails and the like) that might be relevant in a potential litigation. The data has earned itself a formal name, "electronically stored information", and the honor of an acronym, ESI.

The most extensive treatment yet to appear on this key procedural subject in the New York courts is the recent *Voom HD Holdings LLC v. EchoStar Satellite LLC*, 2012 WL 265833 (Jan. 31, 2012), from the First Department, a unanimous decision with an opinion by Justice Manzanet-Daniels. The court's bottom line is a finding that the defendant Echostar (D), a provider of satellite TV services, was evading its "litigation hold" obligation by failing to suspend its computers' automatic erasure of data, including emails, that might be relevant to its dispute with the plaintiff Voom (P), a television programmer and one of its customers.

The opinion details the dates involved in the dispute and shows clearly – to D's chagrin – that it failed to apply the litigation hold until four months after P had commenced the action, when it had been on notice, from communications long before that, that there was a strong probability that litigation would ensue, imposing on D the obligation to preserve its relevant ESI during the pre-action period. The record is so strong to that effect that the court finds no difficulty in charging D with gross negligence and apparently even bad faith.

The finding supports awarding an "adverse inference" charge in favor of P, the court holds. And had there not been some other evidence available to P on the subject of the dispute, the court suggests that the sanction imposed on D would have been worse than that: the penalty of a default, which is the ultimate sanction for spoliation under CPLR 3126, the statute that supplies, in degrees, the proper punishment for disclosure misconduct.

Adding to the strong factual basis for finding D's conduct this egregious is that D was shown to have been involved in an earlier litigation with a different party in which it was found guilty of the same kind of misconduct.

Judge Scheindlin's influential 2003 *Zubulake* federal decision – *Zubulake v. UBS Warburg*, 220 F.R.D. 212 (S.D.N.Y.) – is relied on by the court, which says at the outset of its opinion that it approves "the standard for preservation set forth in" *Zubulake*. *Zubulake* held that

> [o]nce a party reasonably anticipates litigation, it must suspend its routine document retention/destruction policy and put in place a 'litigation hold' to ensure the preservation of relevant documents.

The court finds this "harmonious with New York precedent in the traditional discovery context" and that it sufficiently advises litigants of their electronic discovery obligations.

D's flagrant conduct here doubtless eased the court's path to its "adverse inference" determination. In the face of D's failings, a presumption of relevance arose here and while D was free to rebut it, D failed to. Hence the spoliation conclusion.

Several cases from the appellate division have now used the "adverse inference" penalty in similar circumstances. In *Ahroner v. Israel Discount Bank of N.Y.*, 79 A.D.3d 481, 913 N.Y.S.2d 181 (1st Dep't 2010), the court listed three showings needed for a spoliation sanction: (1) the party had an obligation to preserve the material; (2) the destruction was with a "culpable state of mind"; and (3) the destroyed evidence was relevant. The court there found all three satisfied and applied the adverse inference penalty, as *Voom* does now.

One may wonder whether such a charge really suffices to deter similar conduct in the future. Computer finaglers whose conduct lends itself to characterizations of "gross negligence" and "bad faith" might be disposed to be more circumspect if they saw a few precedents on the books in which an outright default was the penalty. In *Voom*, for example, a default judgment against D would have established the merits of P's claim of breach of contract and left only damages to be tried. Millions of dollars were at stake in *Voom*, adding to the potency of the lesson that a default could have taught.

D also argued that there were settlement talks going on with P, and that this made a "litigation hold" unnecessary, an argument the court rejects out of hand. It "would encourage parties who actually anticipate litigation, but do not yet have notice of a 'specific claim', to destroy their documents with impunity".

COURT OF APPEALS

EDUCATING INSTITUTIONALIZED CHILDREN

District of Child's Residence Must Pay Education Costs, Not District of Institution

The Court of Appeals faced in earlier cases similar issues of who pays for the education of certain categories of children, such as in its 2004 *Longwood* (Digest 533) and 1991 *Catlin*

(Digest 381) decisions. It now resolves a more recent case, *Board of Ed. of the Garrison Union Free School District v. Greek Archdiocese Institute of St. Basil*, 18 N.Y.3d 355, ... N.Y.S.2d .... (Jan. 5, 2012), along the same lines.

In *Longwood*, the subject was foster children. The Court held that the district responsible for schooling them is that of the children's last permanent residence, not that of their temporary foster placement. In the yet earlier *Catlin* case, the Court held that handicapped children remain resident in their parents' district even though actually residing with a family elsewhere. Now, in *Garrison*, the Court considers children living in a "child care institution" and decides, consistently, that the school district of the institution is not responsible for furnishing a tuition-free education; it remains the responsibility of each child's residence district, with residence presumed to be the same as the child's parents.

The issue is governed, as in the earlier cases, by § 3202 of the Education Law, whose very caption suggests the answer in all three cases: "Public schools free to resident pupils; tuition from non-resident pupils".

The facts are that the St. Basil's institute, located in the Garrison school district, housed children of Greek families whose parents were unable to care for them. The dispute about who had to pay for their education was a longstanding one, coming to a head – which produced this case – when in 2002 St. Basil tried to register 26 children, tuition-free, in the Garrison district. The district scheduled a residency hearing, in which the hearing officer ruled that none of the 26 were local residents. The state education commissioner upheld that ruling.

St. Basil after that applied for and was granted a formal license to operate a residential child care institution. Apparently not waiting for St. Basil to start further judicial proceedings in the hope that the license would turn things around, the school district itself brought – successfully – the present action for a judgment declaring that the St. Basil's licensure

> did not mean that Garrison was now required to pay for the education costs of the children at St. Basil who were not residents of the school district.

St. Basil argued that the matter was governed by a different provision of the Education Law, § 4002, part of Article 81, which contains the general requirement that children at a child institution are entitled to a free education, but that, holds the Court, "must be read in conjunction with" § 3202, noted above, which addresses who pays for the education and says it's the district of the child's residence. In an opinion by Judge Pigott the Court says that a reading of Article 81

> reveals that the Legislature did not intend to put the financial burden on the local school district for all of the children living in a child care institution

and that the license can't alter things because it does not change the residence of the children.

ENVIRONMENTAL CONSERVATION

DEC Didn't Exceed Its Authority With Regulation Aimed at Cleanup of Inactive Hazardous Waste Sites

In its 1989 *Superfund* case (Digest 368), the Court of Appeals held that the Department of Environmental Conservation can regulate a hazardous waste site only when it poses a "significant" environmental threat; that a mere "potential" threat won't do.

In another such cleanup decision, the Court divides on whether certain DEC regulations meet those 1989 criterion.

In *New York State Superfund Coalition, Inc. v. New York State Dep't of Environmental Conservation*, 18 N.Y.3d 289, 938 N.Y.S.2d 266 (Dec. 15, 2011; 5-2 decision), the majority, in an opinion by Judge Jones, says they do; the dissent, in an opinion by Judge Pigott, says they don't and would set aside the contested regulations. The petitioner, the same in both the 1989 and the present decisions, is described as "a not-for-profit corporation whose members consist of commercial entities that own land ... on a registry of sites subject to ... regulation".

The petitioner brought what the Court describes as a "combined CPLR article 78 proceeding and declaratory judgment action" challenging as ultra vires the remedial programs addressed in the new regulations. The challenge does not succeed.

Section 27-1313(5)(d) of the Environmental Conservation Law allows the DEC through regulations to devise and implement "an inactive hazardous waste disposal site remedial program" with, as the dissent stresses, the goal of making the program, with respect to each site addressed by the DEC

> a complete cleanup of the site through the elimination of the significant threat to the environment posed by the disposal.

The aim, according to the dissent, was the complete "elimination" of a current "significant threat". The DEC, however, in its view of what contaminants at a site constitute a "significant threat", includes not just those that are a present threat but also those that are "reasonably foreseeable" as a future threat. That, to the dissent, goes too far; it's too "expansive" a reading of the statute.

The majority's position is that the aspiration of the statute is to effect a "complete" cleanup and that this allows the DEC to implement "limited actions that reduce rather than completely eliminate dangers". Reduction rather than complete elimination is what the DEC has undertaken here, and quite properly, says the Court.

There are no specific fact patterns addressed in the opinion. The petitioner brought its proceeding as a frontal attack on the whole regulatory program. It wasn't just one or a few owners objecting to the regulations' application to specific parcels.

One of the regulations stated the goal to be to restore each site to "pre-disposal conditions". Another said that the DEC can consider not only "current, intended" land uses, but also "reasonably anticipated future land uses". The petitioner feared that this meant requiring removal of "every last molecule" of contamination and restoration of each site addressed to "pre-

Columbian environmental quality". The DEC, however, "disavows" any such intention, notes the Court, adding that the regulation requires cleanup only to the extent "feasible".

In reconciling the 1989 decision with the present one a quarter century later, an observer might conclude that the judges, like the public at large, have come to a more sensitive appreciation of the accelerating risks of environmental contamination and have consequently become more deferential to the burdens of the agencies trying to counter them.

MARTIN ACT

N.Y.'s Martin Act – Contemplating Enforcement by Attorney General – Doesn't Bar Private Actions for Breach of Fiduciary Duty or Gross Negligence

Those are common law claims that exist independently of and are hence not preempted by the Martin Act, holds the Court of Appeals, and the fiduciary and gross negligence claims pleaded in this case have their bases in the common law itself and can stand as such independently of the act. *Assured Guaranty (UK) Ltd. v. J. P. Morgan Investment Mgmt. Inc.*, 18 N.Y.3d 341, ... N.Y.S.2d .... (Dec. 20, 2011).

The Martin Act (Article 23-A of the General Business Law), first enacted in 1921, is New York's "blue sky" law. As the Court said in its 2009 *Kerusa* decision (Digest 593), it authorizes the attorney general "to investigate and enjoin fraudulent practices in the marketing of stocks, bonds and other securities within or from New York". Before the act, injunctive relief was the AG's primary tool against securities fraud. Amendments of it also allowed the AG to seek money relief on behalf of defrauded investors. Those remain its gifts, but the Court observes that nowhere in the act is there an express mention of common law claims that individuals may have, much less any evidence of an intent to eliminate them.

To hold otherwise, the Court adds in an opinion by Judge Graffeo, would leave the marketplace less protected than it was before the Martin Act, which could not have been the act's goal. The case goes back for further proceedings.

It will be especially interesting to follow those proceedings if they're reported.

In *Assured*, a certain entity (E) had an investment portfolio with defendant J.P. Morgan (D). The Court describes the plaintiff (P), which guaranteed E's investment, "[a]s an express third-party beneficiary of an investment management agreement between [D] and [E]". We are not given details about it. (Today it might come as a surprise that any sane and solvent body would guarantee stock and like investments, unless the risk is truly minimal or the guarantor driven by either blackmail or libido.)

P's claim, even in its special "guarantee" context, is all too typical of the claims of hundreds of thousands (at least) of other investors from the period a few years back, few likely to have had any kind of guarantor in the picture.

Listen to the Court's description of the claim P asserts in the *Assured* case. It's that banker D invested the funds of the insured E

> in high-risk securities, such as subprime mortgage-backed securities, and failed to diversify the portfolio or advise [E] of the true level of risk.

There was more, but on the basis of the quoted allegations alone, many losers in the recent recession will be tuned in sharply to see whether the claims in *Assured* get upheld after remand.

High-risk securities? Subprime mortgage-backed securities? A failure to diversify? If those activities lead to a substantive recovery in a case like *Assured* – with or without the element of an intervening "guarantor" – one would need an adage and perhaps the Bible to describe the future, with "Deluge" a key player.

However the merits may go, P in *Assured* has the Court's leave to proceed. If P can now convince the triers that D's recited conduct amounted to the breach of a fiduciary duty or to gross negligence, and P is awarded full damages for it, P will be the guest of honor at a great many celebrations and its attorneys will enjoy a high standard of living.

LABOR LAW § 240(1)

Falling While Standing Astride Dumpster to Rearrange Debris May Give Worker "Elevation-Related" Injury Under Statute

"Elevation-related" is of course the key element under § 240(1) of the Labor Law. The Digest meets this statute often. It's designed to require safety devices for work at elevations and if such a device is found necessary to the work and isn't provided, the worker injured by its absence gets a free ride on the issue of liability, which becomes absolute in that case.

This plaintiff was doing demolition work during renovation of a Brooklyn apartment building. One of his tasks was to rearrange debris in a six-foot-high dumpster to clear more room in it for more debris. To do this, he stood on the top of the dumpster with one foot on its ledge and the other either on another part of the ledge or on the debris already in the dumpster. He lost his balance, fell, and was injured.

Does this qualify as an elevation-related injury under § 240(1) such as to have mandated the use of some device of the kind enumerated in that statute, such as a scaffold? Maybe, holds the Court of Appeals; resolution of the issue requires further proof on this record, in which both sides moved for summary judgment but neither showed enough to get it. *Ortiz v. Varsity Holdings, LLC*, 18 N.Y.3d 335, 937 N.Y.S.2d 157 (Dec. 20, 2011).

The lower courts thought the defendants – the owner of the building and its manager – had earned it, but the Court of Appeals says no, distinguishing its 2005 *Toefer* decision (Digest 548), in which the plaintiff fell from a flatbed truck about five feet high. The worker in that case might reasonably have been "expected to protect himself by exercising due care in stepping down", the Court now explains in an opinion by Judge Pigott, distinguishing *Ortiz* because the particular task itself – rearranging the debris in the dumpster – required the worker "to stand at the top of the dumpster, six feet above the ground, with at least one foot perched on an eight-inch ledge".

The defendant didn't show that standing in that way was not required for the task, or that a § 240(1)-type device wouldn't have avoided the fall. That's what the defendant had to show to earn summary judgment, and it failed to.

But neither did the plaintiff show entitlement to summary judgment on its cross-motion. He would have had to show – as a matter of law – that he was "required to stand on or near the ledge" of the dumpster to do his job, and his cross-motion papers didn't establish that.

Hence neither side makes out the kind of matter-of-law showing needed to put a summary judgment end to the case.

Citing here its 2001 *Narducci* decision (Digest 499), the Court says that on the *Ortiz* record each of these matters is a triable issue of fact, including a showing by the plaintiff, if he wants to win under § 240(1), that "a safety device of the kind enumerated in § 240(1) that could have prevented his fall" exists but was not furnished by the defendants.

N.Y.C. TAXI RATES

Under "Standard Lease Cap" That Rule Imposes on Cab Owners Leasing to Drivers, Owners Can Add in Sales Taxes

The rule is § 1-78(a)(4) of the New York City Taxi and Limousine Commission. It establishes a "Standard Lease Cap" for what cab owners may charge drivers to whom they lease their cabs, keyed to 12-hour shifts. The rule was adopted in 2009. Before then, owners added sales taxes to the lease caps. The rule purported to bar that. Several owners of taxis and their trade association challenged the change. They failed in the lower courts, but succeed in the Court of Appeals. The practice of the owners adding in the sales tax is upheld, and the rule purporting to bar it is annulled. *Metropolitan Taxicab Board of Trade v. New York City Taxi & Limousine Commission*, 18 N.Y.3d 329, 937 N.Y.S.2d 153 (Dec. 15, 2011).

Section 2304(c) of the City Charter provides that the commission "may consider" all facts bearing on rate fixing, with "due regard" to the expenses involved in the cab operations. The commission, to support the rule change, relied on the "may consider" phrase as making the consideration of financial data discretionary; the owners relied on the "due regard" phrase as making its consideration mandatory.

In an opinion by Judge Smith, the Court labels the issue "abstract" and sees no need to resolve it on this record because, it says, "the conflict between the parties' interpretations may be more apparent than real".

The Court says that a change in the caps "does have to be justified by something", and that that's where the commission rule in this case fails. The Court apparently sees it as the commission's burden to justify a change in the rule, and finds nothing in the commission's submissions supporting the change. The commission argued that the tax-adding practice in the industry was "inconsistent" and "the resulting confusion justified a new, uniform rule". The Court finds no record support for the inconsistency claim.

Hence the bottom line in this case is just what the owners claim it is: an unsustainable "arbitrary and capricious decision to transfer money from taxi owners to taxi drivers".

COMBINING ORDINARY ACTION WITH SPECIAL PROCEEDING?

INCREASING USE OF "COMBINED CPLR ARTICLE 78 PROCEEDING AND DECLARATORY JUDGMENT ACTION"; ANY PROCEDURAL BARRIERS?

The Court of Appeals describes the matter before it in the *Superfund* decision (treated above) as a "combined CPLR article 78 proceeding and declaratory judgment action". It has so described it in similar cases in the past, such as the *United Teachers* case in Digest 614. The Court is obviously unperturbed by any procedural barriers that might be cited to bar such a combination. Are there any procedural objections?

The only serious one would be an attempt by the Article 78 petitioner to try to extend the short statute of limitations applicable to the Article 78 proceeding – four months under CPLR 217(1) – by phrasing it in terms of an action for a declaratory judgment, which, standing alone and with proper use, enjoys the much longer "residual" six-year period of CPLR 213(1).

Any such attempt was soundly rejected by the Court of Appeals in its 1980 *Solnick* decision, on which we did a lead note in Digest 246. (See also the treatment in Siegel, New York Practice 5th Ed. § 438.)

Are there any other procedural objections to the joining of the two devices? A few might be cited – and the lawyer should be alert to them – but they appear to be curable at worst and hence to leave the combination intact, enabling the court to get right on with the merits.

One possible barrier is that the two devices have different commencement features. The action is commenced with papers that advise the defendant of the claim and offer a stated period in which to respond to it. It's open-ended in that the applicable period doesn't start to run until the service is made, or "complete". (See CPLR 308.) The Article 78 proceeding, on the other hand, is not open-ended. Brought on with procedures akin to those of a motion, it requires the setting of a specific return day for the hearing. (CPLR 7804[c].) Suppose the return day turns out to be earlier than the deadline that would have applied had the initial steps been those of an action?

The courts should be able to answer that obstacle with an application of the CPLR's general mistakes-forgiving statute, CPLR 2001, especially in view of its 2007 amendment. Mistakes at commencement time had been deemed jurisdictional and hence beyond the corrective reach of CPLR 2001. The amendment was designed to extend the statute to reach those cases, too. If the objecting party just needs more time, for example, the court under CPLR 2001 should just allow it, with an adjournment if needed.

Another procedural issue is that the Article 78 proceeding lies only against a "body" or "officer" (CPLR 7802), i.e., a governmental or quasi-governmental creature. Suppose the combined device we're discussing has also named a private individual or company? The very fact that the

declaratory judgment action is part of the combination should resolve that. As an "action", it's free of the "body" or "officer" restriction that hems in the Article 78 proceeding.

Other CPLR provisions also offer support for the combination.

If the case can be perceived by the court as posing a mere defect in form, for example, CPLR 103(c) lets the court "make whatever order is required for its proper prosecution". (See Siegel, id., § 4.) If the two devices were brought separately but involved any common question of law or fact, for example, CPLR 602 would permit the court to put them together. (Caselaw today allows the court to consolidate an action with a special proceeding. See id., § 128.) In that light, how can a court reasonably conclude that an action and proceeding can't be brought together when there's authority on the books for the court to put them together when they're brought separately?

With effective cures like these at hand for what might otherwise impede the simple joinder of an action with a special proceeding – and that goes for any special proceeding, not just the Article 78 proceeding – the only insurmountable barrier would remain the attempt to use the declaratory judgment action to circumvent the short statute of limitations applicable to the proceeding.

Which means that when time issues are not part of the case, it should face no procedural impediments at all, or in any event no insurmountable ones. The casual description of "combined CPLR article 78 proceeding and declaratory judgment action" used in the *Superfund* opinion suggests that the Court of Appeals shares that view.