CONSTRUCTION LEGAL EDGE

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"PAY-IF-PAID" CLAUSES IN CONSTRUCTION CONTRACTS

"Pay-If-Paid" clauses are contingent payment clauses that Contractors sometimes insert in construction contracts whose effect is to forfeit or delay payment from the Contractor to the Subcontractor based upon the Contractor's receipt of payment from the Owner. Owners do not pay for work completed for a variety of reasons. One example is when the Owner does not have funds to pay. Another example is when the Owner, through its Architect, is dissatisfied with the quality of the work and refuses to pay until the work complies with the contract documents. The "Pay-If-Paid" clause passes the risk of Owner non-payment to the Subcontractor.

Many states prohibit enforcement of "Pay-If-Paid" clauses either by case law or statute on the basis that such clauses violate public policy. One of the reasons given to void such clauses is that the risk of non-payment should not be placed on a Subcontractor who has no relationship with the Owner and, unlike the Contractor, is not in a good position to determine the credit worthiness of the Owner.

In this current economic downturn General Contractors defend and justify such clauses arguing that General Contractors should not bear the entire risk of non-payment and be held liable to all Subcontractors on the job in circumstances when Owners lose their financing or otherwise have cash flow problems. The General Contractor argues that it is not the financier of the project. The General Contractor also argues that it should be able to distribute the risk especially in light of the right of the Subcontractor to file a mechanics lien against the property.

Interestingly, most states permit the enforcement of "Pay-If-Paid" clauses based on the public policy preference for "freedom to contract".

States that do enforce "Pay-If-Paid" clauses require such contingent payment clauses to be unequivocally clear. If the risk of the Owner's non-payment is to be shifted from the Contractor to the Subcontractor, then this shift must be clearly articulated in the Agreement. Lack of precision will risk non-enforcement of "Pay-If-Paid" clauses by the courts. The subcontract should at a minimum specifically state that the Contractor is only required to pay the Subcontractor if the Owner pays Contractor. If the "Pay-If-Paid" clause is later challenged in court by the Subcontractor as being imprecise and therefore unenforceable, from the Contractor's perspective it would be helpful if the contract drafter also stated in the subcontract that the Subcontractor expressly assumes the risk of non-payment due to the Owner's failure to pay the Contractor. It is important to be aware that the courts construe terms of a contract against the party who drafted or supplied the agreement. The courts often take into account the uneven bargaining positions of the parties when construing a contract. Courts are also prone to interpret contract language as ambiguous in order to construe the contract in favor of the Subcontractor.

A Subcontractor should consider requesting the Contractor to either eliminate the "Pay-If-Paid" clause or substitute a "Pay-When-Paid" clause during contract negotiation. A "Pay-When-Paid" clause relates to the timing of payment owed to Subcontractor; not whether the Subcontractor is ultimately paid. A "Pay-When-Paid" clause will delay payment to Subcontractor until Contractor receives payment from the Owner; however, unlike "Pay-If-Paid" clauses, the Subcontractor is entitled to payment from the Contractor within a reasonable time, even if the Owner fails to pay the Contractor. An example of such a clause is found in AGC Document No. 650, Standard Form of Agreement Between Contractor and Subcontractor, which provides that the Contractor assumes the risk of Owner non-payment. It states in relevant part, as follows:

> "Progress payments to the Subcontractor for satisfactory performance of the Subcontractor Work shall be made no later than seven (7) days after receipt by the Contractor of payment from the Owner for the Subcontract Work. If payment from the Owner for such Subcontract Work is not received by the Contractor, through no fault of the Subcontractor, the Contractor will make payment to the Subcontractor within a reasonable time for the Subcontract Work satisfactorily performed."

If a Subcontractor cannot negotiate with the Contractor to remove or modify a "Pay-If-Paid" clause, what strategies should the Subcontractor pursue? Please keep in mind when answering this question that the Payment Bond of the General Contractor will generally not protect the Subcontractor in this factual situation because the Contractor's obligation to pay the Subcontractor does not arise if there is a "Pay-If-Paid" clause in the contract until the Contractor actually gets paid by the Owner. And so, during the contracting process, the Subcontractor should consider asking the Contractor for information about the Owner's ability to pay for the cost of the construction project. Whenever possible, the Subcontractor should get in writing that Owner Financing is in place prior to entering into a Subcontract. This writing should come from the Owner and/or the financing institution. Unfortunately, a credit insurance policy is not an option for a Subcontractor because one of the prohibited classes under a credit insurance policy is the field of construction.

In conclusion, in today's economic environment a "Pay-If-Paid" clause is often preferred by Construction Contractors to be part of their subcontracts with Subcontractors. The "Pay-If-Paid" clause is not, however, a desirable clause from the perspective of Subcontractors because the risk of non-payment by Owners of Construction Projects is shifted to Subcontractors.

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SUFFERING FOR THE SINS OF ANOTHER: WHAT CONTRACTORS NEED TO KNOW ABOUT HONEST SERVICES FRAUD

You are a contractor working for the local municipality. You have a close personal and/or business relationship with the administrator responsible for awarding public contracts. Your relationship with the administrator results in you providing to him or her gifts (in a personal context) or compensation (in a business context), though not with any improper intent to bribe or influence the administrator. Nevertheless, if the administrator fails to disclose these gifts or compensation to the public, you could be found criminally liable for aiding and abetting the administrator's failure to disclose a conflict of interest under the theory of "honest services fraud." 18 U.S.C. § 1346.

<u>Honest Services Fraud</u>

The honest services fraud doctrine criminalizes, among other things, attempts to defraud the public of the honest services of their public officials. Honest services fraud is a subtype of mail fraud and wire fraud. Accordingly, the government must prove the same core elements, including participation in a fraudulent scheme and the use of the mail or interstate "wires," including telephone and e-mail, in furtherance of the scheme. While such prosecutions often target bribery, the government also uses the honest services fraud theory to prosecute public officials who fail to disclose conflicts of interest. Most often, such prosecutions are limited to situations in which disclosure of the conflict was required by state ethics laws.

State ethics laws generally create a duty for public officials to disclose conflicts of interest to the public. For example, in Pennsylvania, the law requires reporting from virtually anyone with decision-making power over: (1) contracting or procurement; (2) grants or subsidies; (3) planning or zoning; and (4) inspecting, licensing, regulating or auditing. These individuals must report a range of information related to their financial interests, including: loans over $6,500; sources of income of $1,300 or more; the source of any gifts whose total value is $250 or more; and the source of transportation, lodging, or hospitality whose total value is $650 or more.

At first glance, it would seem that a contractor who does not engage in outright bribery has little to fear from honest services fraud prosecutions. This is untrue, as demonstrated by the recent case of U.S. v. Carbo, 572 F.3d 112 (3d Cir. 2009). In Carbo, the Third Circuit found that a contractor can be held criminally liable under an honest services fraud theory for a public official's failure to disclose a conflict of interest.

U.S. v. Carbo

Thomas Carbo was a snow plowing and paving contractor in Norristown, Pennsylvania. He occasionally rented a truck from a Norristown borough administrator, Anthony Biondi, to perform paving and snow plowing services. Mr. Carbo also occasionally employed Mr. Biondi as a truck driver. As borough administrator, Mr. Biondi was responsible for awarding contracts for paving and plowing services in the borough, and often awarded contracts to Mr. Carbo.

When Mr. Biondi drove his truck for Mr. Carbo, Mr. Carbo paid him between $300 and $400 per day. Mr. Carbo paid Mr. Biondi close to $10,000 during 2003. Between January 2002 and April 2004, Norristown paid Mr. Carbo’s company more than $33,000 for paving and plowing contracts. Mr. Carbo made his payments to Mr. Biondi exclusively in cash, at Mr. Biondi’s request. Mr. Biondi did not report this income on his statements of financial interest.

At trial, rather than arguing that Mr. Carbo bribed Mr. Biondi to receive paving and plowing contracts, the government argued that Mr. Carbo aided and abetted Mr. Biondi's failure to disclose his income by helping him conceal various aspects of their relationship. In support of its position, the government offered evidence to support its position that Mr. Carbo knew his relationship with Mr. Biondi was improper.

Specifically, the government offered evidence that Mr. Biondi co-owned, at different times, two trucks with Lawrence Mazzerle, another paving and snow plowing contractor, but titled the trucks in the names of Mr. Mazzerle and Mr. Mazzerle’s partner, William Moran. Mr. Carbo purchased the first, a 1988 Mack truck, from Biondi and Mazzerle for

$20,000. Mr. Carbo paid $10,000 of that with a bank check; on the same day, he made a cash withdrawal from his company's bank account for $10,000, which his records described as being for "job materials." Mr. Carbo was aware that the second truck, a 1995 Peterbilt, was not properly titled. The government claimed that the cash payment, misleading records, and Mr. Carbo's knowledge of the improperly titled vehicle demonstrated his intent to help Mr. Biondi conceal their relationship.

Additionally, the government offered taped conversations between Mr. Carbo and a cooperating witness. In one such conversation, Mr. Carbo said that Messrs. Mazzerle and Moran billed Norristown for work that they did not perform, but expressed disbelief that Mr. Biondi was involved in anything improper, saying "if I do a job he won't even let me buy him dinner," and "all I know is he never took anything from me and always insisted he didn't want anything." Mr. Carbo said that there was a "paper trail to hell" for Mr. Mazzerle's improper behavior.

Finally, it was not unusual for Mr. Carbo to pay his workers or vendors in cash; however, his records were disorganized. His office manager had devised a receipt system to keep track of cash payments, but the receipts for any given cash payment generally did not match withdrawals from the company bank account. The name "Biondi" did not appear on any of the time cards that the office used to track driving hours, but the name "Anthony" appeared on nine time cards. The government argued that this evidence demonstrated that Mr. Carbo intended to conceal what he knew was an improper relationship with Mr. Biondi.

Based upon this evidence, Mr. Carbo was convicted of aiding and abetting the administrator's failure to disclose a conflict of interest. The district court reversed the conviction; finding that there was insufficient evidence that Mr. Carbo knew that the law required the administrator to disclose his conflict of interest.

On appeal, the Third Circuit reversed. The Court of Appeals held that knowledge of the law is required to sustain a conviction for aiding and abetting honest services fraud under a failure to disclose theory. Nonetheless, it found that the government proved that Mr. Carbo paid the administrator in cash, disguised these payments in his records by referring to the administrator using a "code name," and expressed concern that the administrator and another contractor were creating a "paper trail to hell" regarding a similar conflict of interest. The Court found that a conviction for aiding and abetting honest services fraud was appropriate, so long as: (1) there was evidence that the defendant assisted the public official in concealing the conflict of interest; and (2) there was evidence the defendant knew that such an undisclosed conflict was illegal. It also found that a conviction for honest services fraud does not require that the contractor know the details of the public official's reporting requirements.

Practical Implications of *Carbo*

The Third Circuit's decision in Carbo, while limiting the scope of honest services fraud in this context to those with knowledge of a public official's disclosure requirements, affords the government substantial latitude as to what constitutes sufficient evidence of "knowledge" to sustain a conviction. As a result, contractors with any financial relationship (personal or professional) with a public official should take steps to mitigate their exposure to possible criminal liability.

Any contractor who has any sort of financial relationship or interaction with a public official must be cautious about any payments made to that official. If the official is the ultimate beneficiary of a financial transaction, payments should be made directly to the official whenever possible. Where it is not possible to pay the public official directly, but where the public official will directly benefit (due to the nature or structure of the transaction), records of the transaction should reflect the official's involvement. Indirect payments or benefits may be used to demonstrate intent to conceal, and serve as circumstantial evidence of knowledge of reporting requirements.

Awareness of the wrongdoing of business associates is another factor that may result in culpability for a public official's failure to disclose. In Carbo, the government relied heavily on Mr. Carbo's awareness that the administrator and the other contractor had improperly titled the rented trucks in the name of the other contractor, when in fact they were owned by the administrator. Upon learning of potential malfeasance by a public official, a contractor should consult with experienced counsel to determine the appropriate course of action.

Poor financial records may also demonstrate intent to conceal and knowledge of reporting requirements. Mr. Carbo often paid contractors in cash, and relied on his payees to provide receipts in order to keep accurate records. Where the payee failed to do so, or provided inaccurate receipts, Mr. Carbo's records were also inaccurate. The government used Mr. Carbo's failure to adequately document his payments to the borough administrator as proof of his intent to conceal the administrator's conflict of interest. Mr. Carbo's example demonstrates the necessity of maintaining complete and accurate business records. To avoid the appearance of impropriety or concealment, all payments to public officials, cash or otherwise, must be accounted for accurately. Additionally, where appropriate, a contractor should submit a 1099 form for any such payment. To the extent that the government can provide evidence that an individual made a payment but did not document it, the government may be able to prove concealment and constructive knowledge of reporting requirements.

Conclusion

Mr. Carbo's example demonstrates the need for contractors to be vigilant in their dealings with public officials. Though the U.S. Supreme Court is currently considering three separate honest services fraud cases, the Court's decisions are unlikely to impact this issue unless the Supreme Court Justices declare honest services fraud unconstitutional altogether. Accordingly, prudence suggests that contractors should tread lightly in their financial relationships with public officials, lest they suffer the consequences for the criminal acts of others.

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INDEMNIFICATION CLAUSES IN CONSTRUCTION CONTRACTS

Most construction contracts contain some form of an indemnification provision, typically including owners, contractors, and subcontractors. In the usual situation, owners are looking to be indemnified by contractors or subcontractors and contractors are looking to be indemnified by subcontractors for claims made against them for personal injury or property damage. Although many indemnification provisions appear to be fairly straight forward at first reading, a second, third, or fourth reading, particularly in the context of litigation, often demonstrates that this is not so. Thus an owner or a general contractor may believe that the indemnification provision requires its subcontractor to fully indemnify, making the subcontractor responsible for all damages – except perhaps those resulting from the general contractor's or the owner's "sole negligence" – but a court may find that the inartfully drafted indemnification provision makes the subcontractor responsible for indemnifying the general contractor (or the owner) only for something that was the subcontractor's fault. In other words, the general contractor (or the owner) gets less protection than it thought it was getting and must provide its own cover for its own negligence.

An example of such a "misreading" of an indemnification provision by an owner and general contractor can be found in <u>Greer v. City of Philadelphia</u>, a 2002 Pennsylvania Supreme Court case. In that case, the owner of the particular project at issue was PennDOT, the general contractor was Green Electric, and the subcontractor was CTS. CTS was engaged to manage traffic while Green Electric was removing large overhead signs on I-95 in Philadelphia. Greer was rear-ended when his car was stopped during a traffic stoppage for sign removal. A jury found that the plaintiff, Greer, was 12% negligent and that PennDOT, Green Electric, CTS, and the driver of the car which rear-ended Greer were each 22% negligent. Green Electric and PennDOT claimed that as among CTS and the two of them, CTS had to completely indemnify them for their share of the damages because the jury said that CTS was negligent and neither Green Electric, nor PennDOT, was solely negligent.

The Supreme Court said "No" to that argument and ruled that the phrase "only to the extent caused by" CTS' negligence contained in the indemnification provision did not mean that CTS had to completely indemnify Green Electric and PennDOT if they were found to be at fault and CTS was also found to be at fault. Nor did it mean that CTS had to indemnify Green Electric and PennDOT by an amount equal to the amount CTS paid. Rather, the phrase meant that CTS only had to indemnify Green Electric or PennDOT if one or the other of them ended up paying any part of CTS' proportionate share, as calculated by the jury, of Greer's damages. PennDOT, Green Electric, and CTS were each responsible for covering first base and were each individually responsible for their own negligence.

The court in Greer, and courts in similar cases, have been emphatic in stressing that a party who wants to be paid for damages for which it may be at least partially at fault for causing must take care to ensure that the indemnification provision in its contract with the party(ies) it wants to hold liable says what it wants that provision to say — plainly and unambiguously. Particularly if large sums are at stake, it is important to consult with an attorney for advice on drafting, including how courts have interpreted language in the provision under consideration. The same caution holds true for subcontractors, and others, whose intent is to not end up paying for damages that were caused by another party to the contract, or by the owner.

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NEW EPA LEAD PAINTING REGULATIONS ANGER PENNSYLVANIA CONTRACTORS

On April 22, 2010, the controversial EPA Lead Based Paint Regulations finally came into effect after several negotiated delays. These latest Regulations come almost one year after Pennsylvania's home improvement contractors were required to register with the Attorney General and revise their contracts and advertising materials under the Home Improvement Consumer Protection Act. This latest EPA regulation is seen as another expensive and crippling blow to small construction and home improvement businesses struggling to survive.

The new EPA Lead Based Paint Regulations require all contractors who receive compensation for their work to be EPA-certified to perform lead paint removal and renovation activities. The Regulations apply to "target housing" which is defined as any housing built prior to 1978. Exceptions to the Regulations are minimal. To be exempt, a certified inspector must have determined that the project is free from lead paint beyond permitted levels. Alternatively, if the work is of a minor nature - that is defined as work that is disturbing less than six square feet for an interior or less than 20 square feet for an exterior, the Regulations would not apply.

Contractors now have extensive obligations that require them to give disclosure in writing to the building occupants regarding the hazards of lead and the correct methods of renovating. More importantly, the Regulations mandate general, yet somewhat vague requirements for contractors in how they are to go about performing their lead paint removal activities. For example, when working with possible lead issues, workers will need to place heavy plastic sheets on the ground, seal the room, seal off vents to the area where the project is taking place, remove or cover furniture in the area, cover the ground and plants outside of the work area, close all windows, and mark off the work area to keep non-workers away. Contractors will be required to post warning signs, restrict occupants from work areas, prevent dust and debris from spreading, conduct a thorough cleanup, and verify that the cleanup was effective.

The EPA stands behind its new Regulations and points to the fact that more than one million people are poisoned annually by lead paint. Lead-based paint was used in more than 38 million homes until it was banned for residential use in 1978. Ingesting lead can lead to behavioral and learning disorders, according to EPA spokesman Roy Seneca. While most people believe that lead poisoning in children is caused by young children eating or chewing on paint, the facts reveal that approximately 60% of today's lead poisoning cases are caused by lead dust stirred up in building renovations.

Although contractors may not dispute the good intentions behind the Regulations, the general consensus is that the new Regulations will cause the cost of a painting or renovation project to double or even triple. Pennsylvania home improvement contractors are cautioned to obtain the appropriate training in lead based paint removal prior to engaging in this type of work to avoid incurring costly fines and penalties. Sanctions for performing renovation work on homes built prior to 1978 without the proper certification can result in fines that are equal to $37,500 per day.

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SEVERE PENALTIES AVAILABLE FOR NOT PRESERVING ELECTRONIC DATA

Companies and private individuals facing litigation are required to retain all relevant documents which presently exist and any created thereafter. These requirements have been extended to electronic data such as e-mails and must be produced during litigation. Very often, courts permit litigants to choose how they accomplish their duty to preserve relevant evidence. In recent years, many courts have developed stringent requirements mandating compliance with court-ordered discovery. These mandates are applied to suits involving both large international corporations and private individuals.

A. Obligation to Preserve Evidence

The inclusion of electronic data in the scope of discovery is merely an extension of the existing obligation created by courts' procedural rules. In Zubulake v. UBS Warburg, LLC, 220 F.R.D. 212, 218 (S.D.N.Y. 2003), Federal District Court Judge Shira A. Scheindlin of the Southern District of New York stated that a party must make available "information that is relevant to the claims or defenses of *any* party or which is 'relevant to the subject matter involved in the action.'" Id. at 218 (emphasis in original) (citing F.R.C.P. 26(b)(1)). The Court found that the duty to preserve evidence extends to electronic documents – even those documents prepared for individuals who might possess discoverable information, "to the extent those documents can be readily identified (e.g., from the 'to' fields in e-mails)." Id. On the other hand, the Court did set reasonable limits on the duty to preserve electronic data:

> Must a corporation, upon recognizing the threat of litigation, preserve every shred of paper, every e-mail or electronic document, and every backup tape? The question is clearly, "no". Such a rule would cripple large corporations…that are almost always involved in litigation.

Id. at 217.

The Court endeavored to create a rule based in common sense whereby a party to a lawsuit, or anyone who anticipates becoming a party to a lawsuit, must not destroy relevant evidence that might be useful to an adversary. Id. With this scope in place, a party's duty to preserve evidence begins once a party "reasonably anticipates litigation" and, after that point, the party "must suspend its routine document retention/destruction policy and put in place a 'litigation hold' to ensure the preservation of relevant documents." Id. at 218. This is an important point as many potential litigants would not expect any discovery obligations to begin until after the suit is filed.

In early 2010, Judge Scheindlin, the author of the Zubulake decisions, again addressed the retention of electronic discovery in an opinion entitled "Zubulake Revisited: Six Years Later." Pension Committee of the Univ. of Montreal Pension Plan v. Banc of America Securities, LLC, 2010 WL 184312, at *1 (S.D.N.Y. Jan. 15, 2010). Judge Scheindlin again stated that courts expect that parties and their counsel must "take the necessary steps to ensure that relevant records are preserved ... and that such records are collected, reviewed, and produced to the opposing party." Id. at *1. When these steps are not taken, the integrity of the judicial process is affected and courts are required to determine an appropriate remedy. Id.

Echoing Zubulake, the Court held that the duty to preserve evidence arises when a party reasonably anticipates litigation – not when the writ or complaint officially beginning the suit is filed. Id. at *4. Using familiar language, the Court repeated its statement in Zubulake that "once a party reasonably anticipates litigation, it must suspend its routine document/destruction policy and put in place a 'litigation hold' to ensure the preservation of relevant documents." Id. (citing Treppel v. Biovail, 249 F.R.D. 111, 118 (S.D.N.Y. 2008)).

Where a party has breached its duty to preserve relevant electronic data, the exact remedy to be imposed by a court depends on the nature of the evidence not retained or the inaction by the party which led up to the failure to retain the appropriate evidence. Courts will look to the level of culpability (i.e., was the conduct acceptable or was it negligence, gross negligence, or willful) to determine whether and how severe sanctions are appropriate. Id. at *2. Judge Scheindlin defined negligence as unreasonable conduct that "creates a risk of harm to others" while willfulness, on the other hand, involves "intentional or reckless conduct that is so unreasonable that harm is highly likely to occur." Id.

B. Significant Failures to Preserve Evidence

Judge Scheindlin was particularly troubled by specific failures by the parties in Pension Committee. The Court flatly concluded that it was gross negligence for a party to not write and issue a "litigation hold" letter – a document instructing employees to actively retain information, including electronic data, and suspend deletion of e-mails and other records falling within the scope of the litigation. Id. at *3. Failing to issue such a letter is problematic in the Court's view "because that failure is likely to result in the destruction of relevant information." Id.

Also at the severe end of the spectrum of discovery failures, the Court found that the following inactions supported a finding of "gross negligence" where parties had a duty to preserve evidence:

- Failure to identify all "key players" and to ensure that their electronic and paper records are preserved;
- Failure to stop the deletion of e-mails and preserve records of former employees in a party's possession or control; and
- Failure to preserve backup tapes when such tapes are the sole source of relevant information or contain relevant information that is not otherwise readily accessible.

Id. at *7.

C. Sanctions for Failure to Preserve Evidence

Courts have remedies of varied severity at their disposal which may be imposed for the negligence or gross negligence of parties to litigation. Such sanctions serve to (1) deter parties from destroying evidence, even inadvertently, (2) impose the risk of an improper result of litigation on the party who created the risk, and (3) restore the prejudiced party to the position it would have been absent the wrongful destruction of evidence by the opposing party. Id. at *6.

In determining whether sanctions are appropriate, courts will first determine whether a particular party had a duty to preserve evidence. Failing to preserve evidence which results in the loss or destruction of relevant information may be negligence, gross negligence, or willful, depending on the circumstances. Id. at *3. Similarly, the failure to collect electronic or paper records may be either gross negligence or willful negligence after the duty to preserve such evidence has begun. Id.

From the least to most severe, courts can order additional discovery, cost-shifting, fines, special jury instructions, preclusion of offering certain evidence or testimony, and the entry of default judgment. Id. The availability of fines and other monetary sanctions exist to punish the party responsible for the destruction or loss of the evidence in order to deter further conduct and send the message that egregious conduct will not be tolerated. Id. at *7 (citing Green (Fine Paintings) v. McClendon, 2009 WL 2496275, at *6 (S.D.N.Y. Aug. 13, 2009)). In particular, monetary sanctions serve "the remedial purpose of compensating [the innocent party] for the reasonable costs it incurred." Id. at *7.

D. The Adverse Inference Instruction May be Fatal at Trial

If a particular party violates its duty and destroys relevant evidence – termed "spoliation", a court can also provide an instruction to the jury at trial permitting an "adverse inference." This instruction would permit the jury to infer from the destruction of evidence that the destroyed evidence would have been harmful to the party which destroyed it. Often juries surmise that the data was deliberately deleted, despite facts to the contrary, by a culpable party to boost its own position.

Courts have explained that this adverse inference instruction is often too difficult a hurdle to overcome and "the party suffering this instruction will be hard pressed to prevail on the merits." Zubulake, 220 F.R.D. at 219-20. An adverse inference instruction is an extreme sanction and is given when three elements mandate such an extreme sanction: (1) the party having control over the evidence had an obligation to preserve it at the time it was destroyed; (2) the records were destroyed with a "culpable state of mind"; and (3) the destroyed evidence was "relevant" to the other party's claim or defense such that a reasonable trier of fact could find that it would support that claim or defense. Id. at 220. Nevertheless, where appropriate, courts give this instruction to juries which can be fatal to a party's case.

In closing, those facing litigation - as well as those who presently find themselves in litigation – will be well-served by issuing a "litigation hold" letter and supervising its implementation. Courts are progressively less sympathetic to parties who fail to stop the routine deletion of relevant e-mails, especially when tied to key witnesses. Such preventative measures to preserve relevant data are a "lesser evil" when compared to the prospect of losing the case or being forced to absorb the other side's discovery costs or attorneys' fees.

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