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LEGAL ISSUES AND DEVELOPMENTS
FROM CARLTON FIELDS JORDEN BURT

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VOLUME IV | FALL 2014

SPOT THE REGULATOR

Plaintiffs' Lawyers Following the Lead

EXPECTFOCUS®, Volume IV, Fall 2014

EXPECTFOCUS® is a quarterly review of developments in the insurance and financial services industry, provided on a complimentary basis to clients and friends of Carlton Fields Jorden Burt, P.A.

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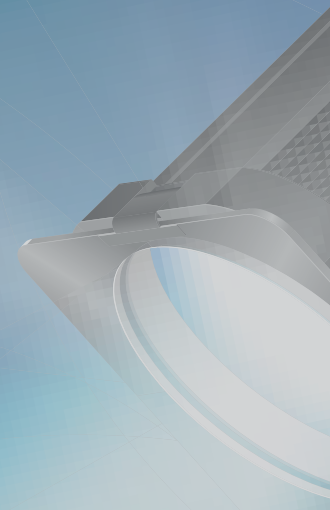
Crisis Management: Five Steps to Take Before Providing That Comment

BY JOHN E. CLABBY & JON M. PHILIPSON

In the digital age, news—good and bad—travels fast. So can its effect on your corporate image and success. From data breaches to innocent and vicious leaks, a corporate crisis can engulf your business in an unforgiving news cycle that crushes consumer confidence, tanks stock values, and spurs feverish litigation.



OUTSIDE COUNSEL CAN BE BETTER ADVOCATES IF APPRISED OF YOUR CRISIS PLAN BEFORE YOUR EMERGENCY PHONE CALL.

By taking these simple steps, corporate counsel and executives can mitigate the inevitable crisis:

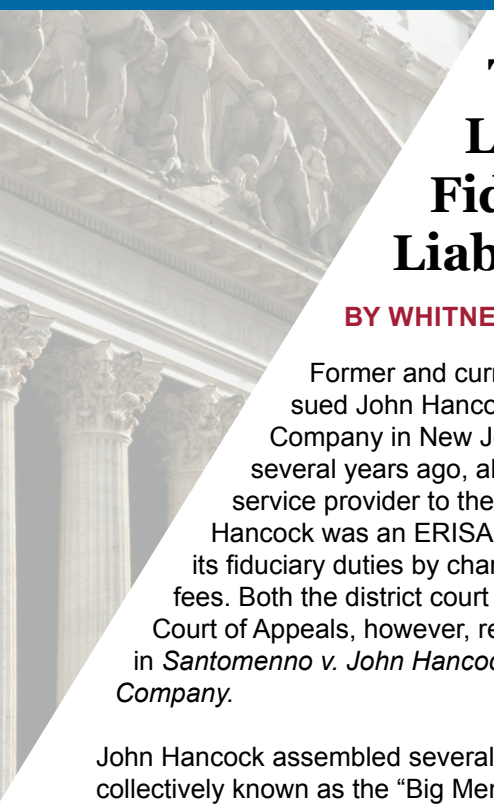
1. **Avoid a Crowded Kitchen** – Designate a "crisis response" team, making one individual the source of all public communication. Clearly designate who has authority to approve final public and internal messages and be consistent. Fewer cooks results in a controlled message.

2. **Develop Press Contacts** – Reporters who call on deadline during a crisis seek sound bites that fit their theme. To help avoid unbalanced coverage, develop genuine relationships with journalists who cover your region and industry. Preexisting relationships help guarantee more comprehensive coverage that puts the crisis in context. Give journalists information and access during calmer times so that, in a crisis, they will be more inclined to trust you.

3. **Say What You Mean to Say** – Avoid defensive responses, which feed conflict-focused news cycles and can cause more damage. Accordingly, instill a "do no harm" ethic within your business units, meaning, no outside communications are allowed until the company has a coordinated message that is communicated only by your designated source.

4. **Shelter Under the Privilege** – Include outside counsel in crisis-response planning. The immediate response to a crisis can have long-term legal and regulatory consequences that extend beyond the newspaper's front page. Through the attorney-client and work product privileges, you may be able to structure your initial investigation for maximum protection from disclosure. Outside counsel can be better advocates if apprised of your crisis plan before your emergency phone call.

5. **Think Long-Term** – In the early moments of a crisis, it's common to attempt to fix today's headline rather than consider tomorrow's. That's a mistake. Remember, the aim is long-term protection. The corporate external and internal message should be structured to shorten the story's life cycle, and then to make your weakness a strength. To do this, your crisis team must have, in advance, a strong understanding of what drives corporate value. That lets them know what their message must protect.



Third Circuit Limits ERISA Fiduciary Liability

BY WHITNEY FORE

Former and current annuity holders sued John Hancock Life Insurance Company in New Jersey federal court several years ago, alleging that, as a service provider to their 401(k) plans, John Hancock was an ERISA fiduciary and breached its fiduciary duties by charging excessive fees. Both the district court and the Third Circuit Court of Appeals, however, rejected these claims in *Santomenno v. John Hancock Life Insurance Company.*

John Hancock assembled several investment options, collectively known as the "Big Menu," for various 401(k) plans and reviewed the investment options on this menu periodically, adding and replacing funds. From the "Big Menu," plan trustees selected which investment options to offer to their plan participants on the "Small Menu."

The plaintiffs, along with the Department of Labor, argued that John Hancock was acting as an ERISA fiduciary due to its discretion regarding the funds on the "Big Menu." The Third Circuit disagreed, aligning itself with other courts of appeal in holding that, because the plan trustee must be given notice and an opportunity to accept or reject any alteration to the "Big Menu" or John Hancock's fees, **"ultimate authority still resided with the trustees." Thus, only the plan trustees were the fiduciaries under ERISA.**

Further, the court held that John Hancock's ability to substitute investment options was irrelevant to the challenged conduct of charging allegedly excessive fees. It explained that "this alleged basis of fiduciary responsibility bears no nexus to the wrongdoing alleged in the complaint: Participants allege the charging of excessive fees, not the rendering of faulty investment advice."

Finally, the court held that John Hancock was not a fiduciary simply because it could change the fees it charged on its own funds. Yet again, it was the trustee who retained the "ultimate authority" required for a fiduciary designation.

Death After Divorce: Who Gets the Proceeds?

BY MICHAEL SAMPSON

Under the common law of some states, if an individual names his or her spouse as the beneficiary on a life insurance policy, gets divorced, and then dies without changing the beneficiary designation, the mere fact of a divorce will not operate to defeat the beneficiary's claim. Some states, however, have enacted statutory provisions to address this situation.

FLORIDA RECENTLY AMENDED ITS STATUTES TO PROVIDE THAT BENEFICIARY DESIGNATIONS SHALL PASS, FOLLOWING A DIVORCE, AS IF THE DECEDENT'S FORMER SPOUSE PREDECEASED THE DECEDENT.

For example, Florida recently amended its statutes to provide that beneficiary designations shall pass, following a divorce, as if the decedent's former spouse predeceased the decedent. Section 732.703 of the Florida Statutes applies not just to life insurance policies, but to annuities, employee benefit plans, individual retirement accounts, and others.

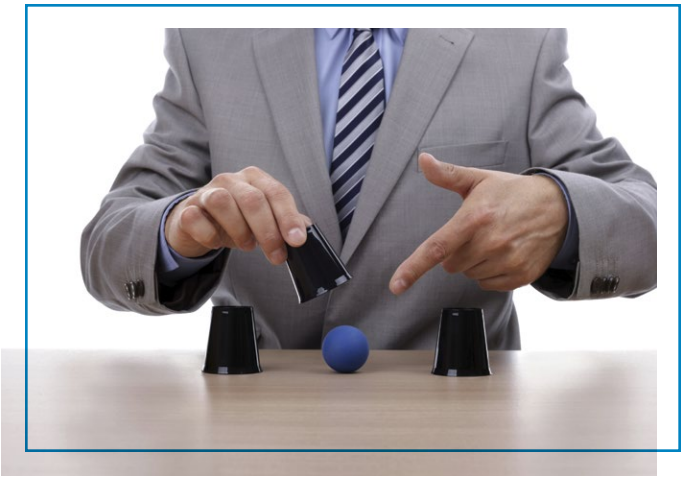
The payor of life insurance proceeds may rely on such statutes to review the deceased insured's marital status on the death certificate and the relationship of the claimant to the deceased, make payment decisions, and avoid the delay and expense of filing an interpleader action. Under the Florida statute, if the death certificate is silent as to marital status at death, the payor is not liable for paying or transferring an interest in the claimed asset to the primary beneficiary if it first obtains, from that beneficiary, a validly executed affidavit in substantially the form set forth in the statute.

There are notable exceptions to the application of these statutes; for example, when a final judgment requires the decedent to maintain the asset for the benefit of the former spouse or children. Insurers or others seeking to rely on the Florida or similar statutes are cautioned to carefully review their provisions prior to relying on them to pay death benefits.

A Life Settlement Investment Shell Game?

BY WHITNEY FORE

American International Group, Inc., through its subsidiary Lavastone Capital, LLC, filed a lawsuit against Coventry First, LLC in New York federal court. Coventry reciprocated by filing a lawsuit against Lavastone in New York state court. **At issue is whether Coventry's failure to negotiate the lowest price when acquiring a large investment portfolio of life settlements resulted in Lavastone's loss of more than $150 million.**



According to Lavastone, since the early 2000s it has paid Coventry more than $1 billion to identify life insurance policies that would make attractive investment vehicles and to acquire them from policyholders at the lowest negotiable price. Lavastone alleges that Coventry did not act in good faith when acquiring policies on its behalf. Specifically, Lavastone claims that Coventry founder Alan Buerger and members of the Buerger family were "scam artists" who bought policies at much lower prices than those disclosed to Lavastone. Coventry allegedly hid the original prices by "systematically concealing and/or failing to disclose material information" from and to Lavastone, and by "falsifying transaction and financial records."

Further, Lavastone alleges that Coventry managed several "shell companies" that were used to purchase the policies at the original price before selling them to Lavastone at "inflated prices." For example, Lavastone claims that a Coventry shell company bought a policy in 2007 for $1.9 million. Three months later, Lavastone allegedly bought the same policy from Coventry for $3.5 million based on Coventry's represented price. According to Lavastone, this constituted a significant overcharge by Coventry on this transaction, which was one of hundreds.

In its state court suit, Coventry contends that Lavastone breached its contract by acquiring life insurance policies in contravention of the exclusivity provision in its origination agreement. Coventry seeks a declaratory judgment as well.

Life Insurer Settles Nationwide "Junk Fax" Class Actions

BY STEPHANIE FICHERA

Recently, there has been a noticeable increase in lawsuits, particularly putative class actions, brought against life insurance companies pursuant to the Telephone Consumer Protection Act of 1991 (TCPA). As amended by the Junk Fax Prevention Act of 2005, the TCPA prohibits the transmission of advertisements via facsimile without the prior express permission of the recipient. It provides for a private right of action and statutory damages of $500 per violation. In August, an Illinois court entered an order preliminarily approving a settlement and certifying a settlement class in two putative TCPA class actions involving MetLife.

The Illinois settlement, which includes a $23 million settlement fund, resolved allegations that an insurance producer, formerly employed by MetLife, sent unsolicited advertisements for life insurance via facsimile to numerous individuals and businesses. The cases, *Fauley v. Metropolitan Life Insurance Co.* (filed in Illinois state court) and *C-Mart Inc. v. Metropolitan Life Insurance Co.* (filed in Florida federal court), arose from faxes that generically advertised "low cost life insurance rates," but did not reference MetLife, the producer, or any other insurance company. The producer had purportedly retained a "fax blasting" service to generate leads.

THE LAWSUITS AROSE FROM FAXES ADVERTISING "LOW COST LIFE INSURANCE RATES" WITHOUT MENTIONING THE INSURER OR PRODUCER.

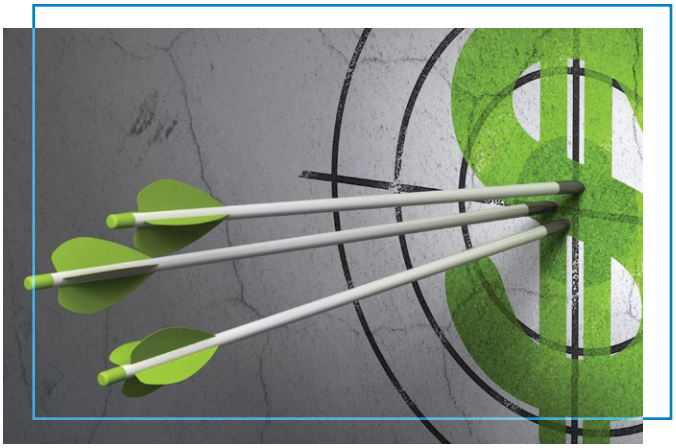
In a memorandum submitted in support of preliminary approval of the settlement, MetLife explained that it "vigorously disputes any liability" for the alleged conduct, but "entered into [the] agreement to settle with the nationwide class based on the risks and uncertainties of litigation …." MetLife contended that the $23 million settlement fund "exceed[ed] the average monetary recoveries that have been approved by other courts across the country in other TCPA class actions."

Proposed Anti-Inversion Regulations Would Affect Foreign Insurers

BY RICHARD D. EULISS

For decades American companies have used so-called "corporate inversions" to lower their tax burdens on foreign-earned income. Typically, the American company is acquired by a foreign company located in a tax-favorable jurisdiction, and then adopts that domicile. Inversions do not alter the taxation of corporate income earned from domestic activities and sources.

Several times the federal government has issued new or revised rules to regulate what it considers abusive inversion transactions. In the recently-released Notice 2014-52, the IRS announced prospective additional regulations intended to stem a surge of inversions under the existing framework. This article only addresses the Notice's treatment of passive assets (the Notice also revises rules for non-ordinary course distributions and post-acquisition stock transfers).



IRS takes aim at inversion transactions.

Under existing rules, the IRS deems a foreign acquiring corporation domestic (thus defeating the tax benefits of the host jurisdiction) if, among other factors, shareholders of the domestic acquired corporation own 80 percent or more of the newly-combined company following the inversion (the "expanded affiliated group"). Other negative tax consequences result if, among other things, those same shareholders own at least 60 percent of the expanded affiliated group. Making these ownership ceilings harder to avoid, **the contemplated regulations take aim at foreign corporations flush with so-called "passive assets" (e.g., assets that generate interest, dividends, and capital gains income)**. Where such a foreign corporation's total assets are more than 50 percent passive, the new rules would disregard for purposes of the ownership calculation that portion of the foreign corporation's stock attributable to those passive assets. The IRS contemplates that such a rule would decrease the amount of inversions, given that foreign corporations with "substantial cash and other liquid assets" are tempting inversion partners.

The Notice carves out of the passive asset rule a "qualifying insurance company," which the Code defines as a foreign insurer that earns more than 50 percent of its premiums from insurance "covering applicable home country risks" (i.e., risks in the foreign insurer's home jurisdiction). Thus, a domestic company can invert into a foreign insurer that is a qualifying insurance company, regardless of that foreign insurer's passive holdings. Insurers in attractive tax jurisdictions, such as Bermuda or the Cayman Islands, however, will almost certainly not insure significant "home country risks." While the IRS likely intended this consequence, it may not have intended to restrict other acquisitions motivated by business purposes other than tax savings. The Notice invites comments to the proposed regulations, meaning that the finalized regulations might provide different treatment for that scenario.

New York Law Governs STOLI Dispute In Texas

BY K. RENEE SCHIMKAT

A Texas appellate court's choice of law determination proved pivotal where a life insurer contested its duty to pay proceeds on the grounds that the policy was fraudulently acquired as part of a stranger-oriented life insurance (STOLI) scheme. In *American National Insurance Co. v. Conestoga Settlement Trust,* Conestoga acquired the rights to the policy's "pay on death benefits" through a series of assignments. ANICO claimed the policy was void because (a) there was no insurable interest; and (b) the application contained fraudulent misrepresentations.

The policy insured the life of a New York resident. ANICO, though a Texas corporation, argued that New Jersey law applied because that was where the contract was negotiated and performed, and because New Jersey's interest in preventing and combating STOLI fraud outweighed any other interested jurisdictions' policy concerns. Conestoga, relying on the Restatement and the most significant relationship test, argued that New York law applied. **Because ANICO challenged the policy's validity after the contestability period had expired, the difference was critical – New York would preclude the challenge (as would Texas); New Jersey would not.**

In holding that New York law applied, the court cited the policyholder's New York domicile at the time she applied for the policy and the lack of any other state with a "more significant relationship" to the issues. It rejected ANICO's arguments that New Jersey had the strongest interest in resolving the policy's validity. Despite ANICO's emphasis on the alleged fraud, or the "evils or legitimacy" of STOLI policies, the court found the "real issue … [was] the ability of an insurance company to challenge the validity of an insurance policy after the expiration of the contestability period." ANICO had agreed to the contestability period when it issued its policy. Any interest New Jersey had in preventing and combating alleged STOLI fraud was "matched by a competing policy interest favoring finality of contracts as expressed in … New York law."

Florida Remains a Non-Member of The Interstate Insurance Product Regulation Commission

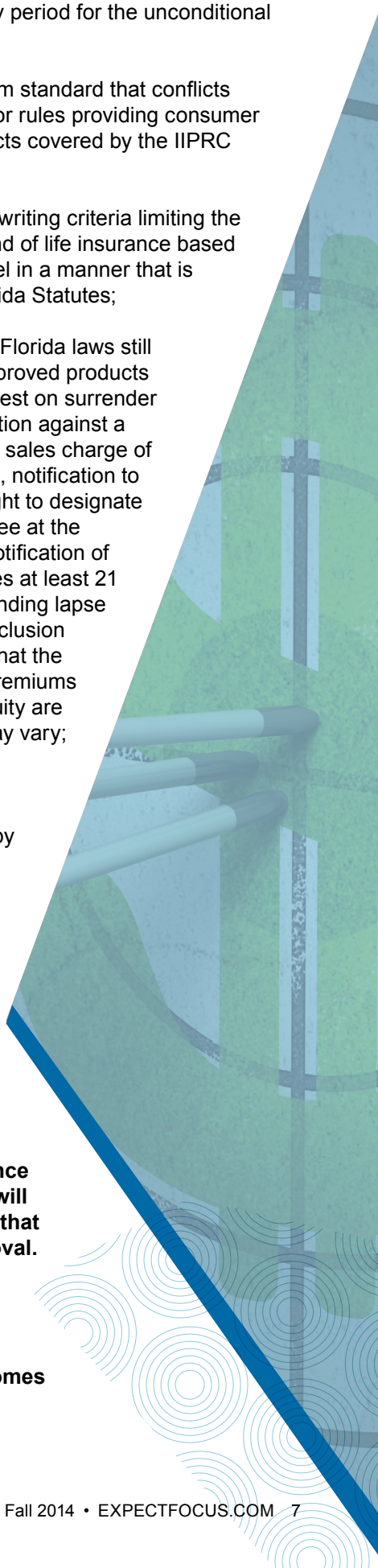
BY KELLY CRUZ-BROWN

During the Summer NAIC meeting, the Interstate Insurance Product Regulation Commission (IIPRC) confirmed it does not recognize Florida as having entered the IIPRC Compact because Florida's Compact Statute contains material variances from the IIPRC Model Compact. According to the IIPRC, this indicates Florida's inability or unwillingness to agree to a "limited delegation to the Commission" as have other compacting states.

The material variances of the Florida Compact Statute include that it:

- specifies that liability for acts, or errors or omissions occurring in Florida of the IIPRC members, officers, executive director, employees, and representatives may not exceed limits of liability under Florida constitution and laws;
- subjects IIPRC's confidential information to Florida's public records laws when in the possession of Florida officials;
- refers requests for trade secrets or matters involving individuals' privacy with respect to IIPRC records requested by a Florida resident to the Florida Commissioner;
- in some circumstances, prospectively opts out of any new uniform standard, or amendments to existing uniform standards, adopted by the IIPRC after March 1, 2013;
- opts out of the 10-day period for the unconditional refund of premiums;
- opts out of any uniform standard that conflicts with Florida statutes or rules providing consumer protections for products covered by the IIPRC Compact;
- opts out of any underwriting criteria limiting the amount, extent, or kind of life insurance based on past or future travel in a manner that is inconsistent with Florida Statutes;
- specifies that certain Florida laws still apply to Compact-approved products in areas such as interest on surrender proceeds, the prohibition against a surrender or deferred sales charge of more than 10 percent, notification to an applicant of the right to designate a secondary addressee at the time of application, notification of secondary addressees at least 21 days before the impending lapse of a policy, and the inclusion of a clear statement that the benefits, values, or premiums under a variable annuity are indeterminate and may vary; and
- specifies that, if the new sections added by the Florida Compact Statutes are invalidated by the courts, such a ruling renders the entire act invalid.

These material variances are significant for insurers that offer products in Florida because t**he Florida Office of Insurance Regulation (the Office) will not recognize products that have only IIPRC's approval. Rather, insurers will be required to have products filed with, and approved by, the Office until Florida becomes an IIPRC member.**



Life Insurers Gain Ground in Legislative Fix

BY KRISTEN REILLY

The U.S. House of Representatives recently voted to pass legislation (H.R. 5461) intended to clarify capital standards for insurance companies under the supervision of the Federal Reserve Board. The bill, sponsored by Republicans, but with broad support on both sides of the aisle, aims to alleviate the unintended "bank-centric" capital standards the Dodd-Frank Act's "Collins Amendment" imposed on life insurance companies. The Act clarifies the Federal Reserve Board's authority to develop insurance-specific standards for life insurers deemed Systematically Important Financial Institutions (SIFIs). The Fed has already declared AIG and Prudential SIFIs, with other life insurers on notice of their likely SIFI designation forthcoming.

Life insurers appreciate the House's efforts.

While the Collins Amendment was intended to provide the Fed discretion in setting appropriate life insurance and bank capital standards from the outset, the Fed interpreted the amendment to require uniform bank-centric standards for all SIFIs, creating unintended, potentially detrimental consequences to SIFI life insurers. Not surprisingly, **life insurance companies, led by the American Council of Life Insurers (ACLI), have made clarifying the Collins Amendment their top regulatory priority.**

The Senate unanimously agreed to this legislative fix earlier this summer. The House, however, bundled this non-controversial issue with three more contentious Dodd-Frank issues, impacting the bill's chances for success in the Senate's upcoming session. The ACLI nonetheless applauds the House's passage of H.R. 5461, and will continue to advocate for the bill's approval.

Like hopeful NCAA college football teams, several matters affecting life and annuity products looked, in 2014, like they would make the playoffs and finally be resolved in early 2015.

- The review of Principle-Based Reserving (PBR) and interim adoption of Actuarial Guideline 48.
- The review of contingent deferred annuities by various NAIC groups to determine if existing laws and regulations provided sufficient solvency and consumer protection, and the CDA (A) Working Group's (CDA WG) development of NAIC guidelines to serve as a reference to states.
- The Separate Account Risk (E) Working Group's (SAR WG's) review of separate accounts usage to fund insurance products guaranteed by the general account.
- Unclaimed life and annuity benefits requirements.
- Actuarial guidelines for index universal life insurance illustrations.

Actuarial Guideline 48, which sets uniform nationwide standards for XXX/AXXX captive reserve transactions, is headed to the playoffs. The PBR Implementation (EX) Task Force

Will Any Matters Addressed at the NAIC's 2014 Fall National Meeting Reach the Playoffs?

BY ANN BLACK & KRISTIN SHEPARD

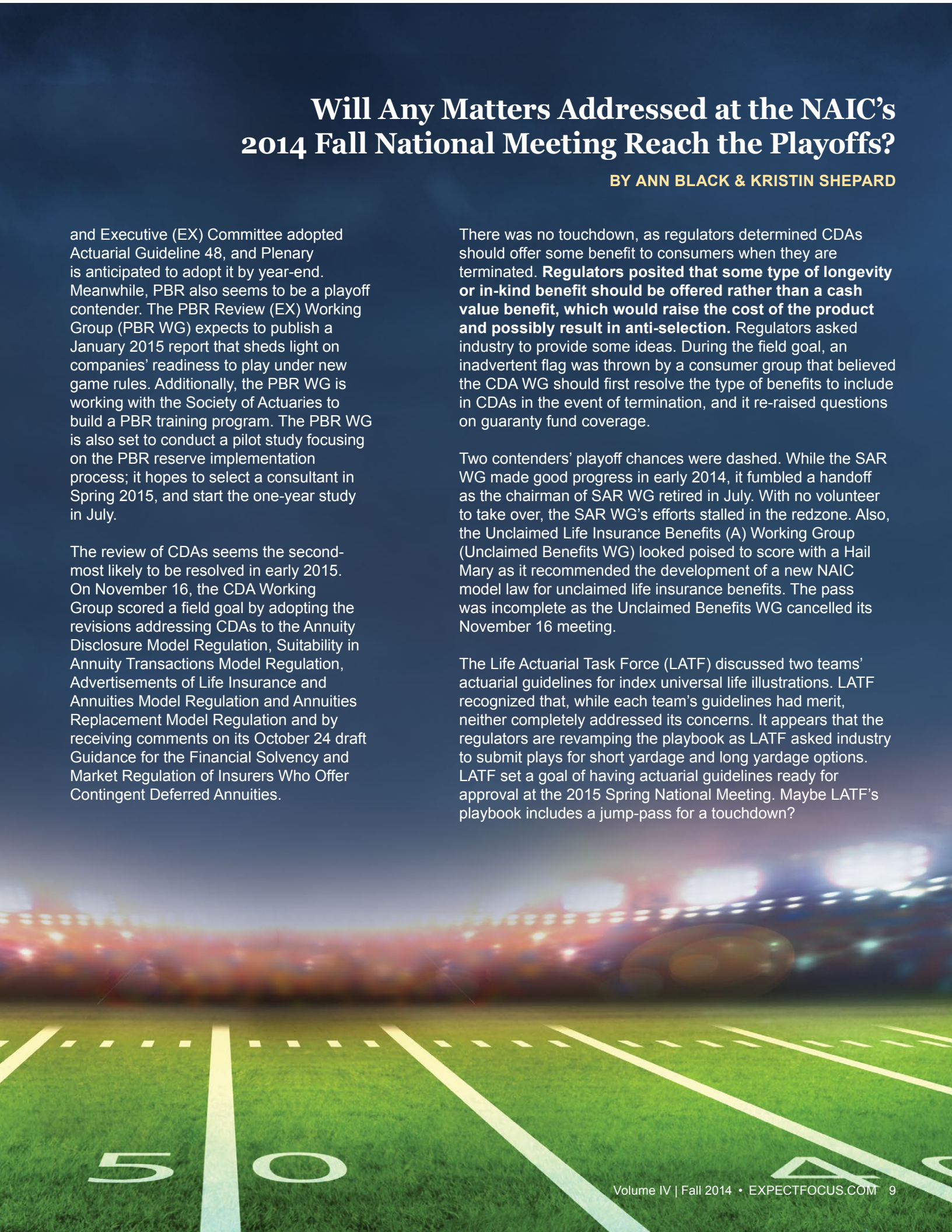
and Executive (EX) Committee adopted Actuarial Guideline 48, and Plenary is anticipated to adopt it by year-end. Meanwhile, PBR also seems to be a playoff contender. The PBR Review (EX) Working Group (PBR WG) expects to publish a January 2015 report that sheds light on companies' readiness to play under new game rules. Additionally, the PBR WG is working with the Society of Actuaries to build a PBR training program. The PBR WG is also set to conduct a pilot study focusing on the PBR reserve implementation process; it hopes to select a consultant in Spring 2015, and start the one-year study in July.

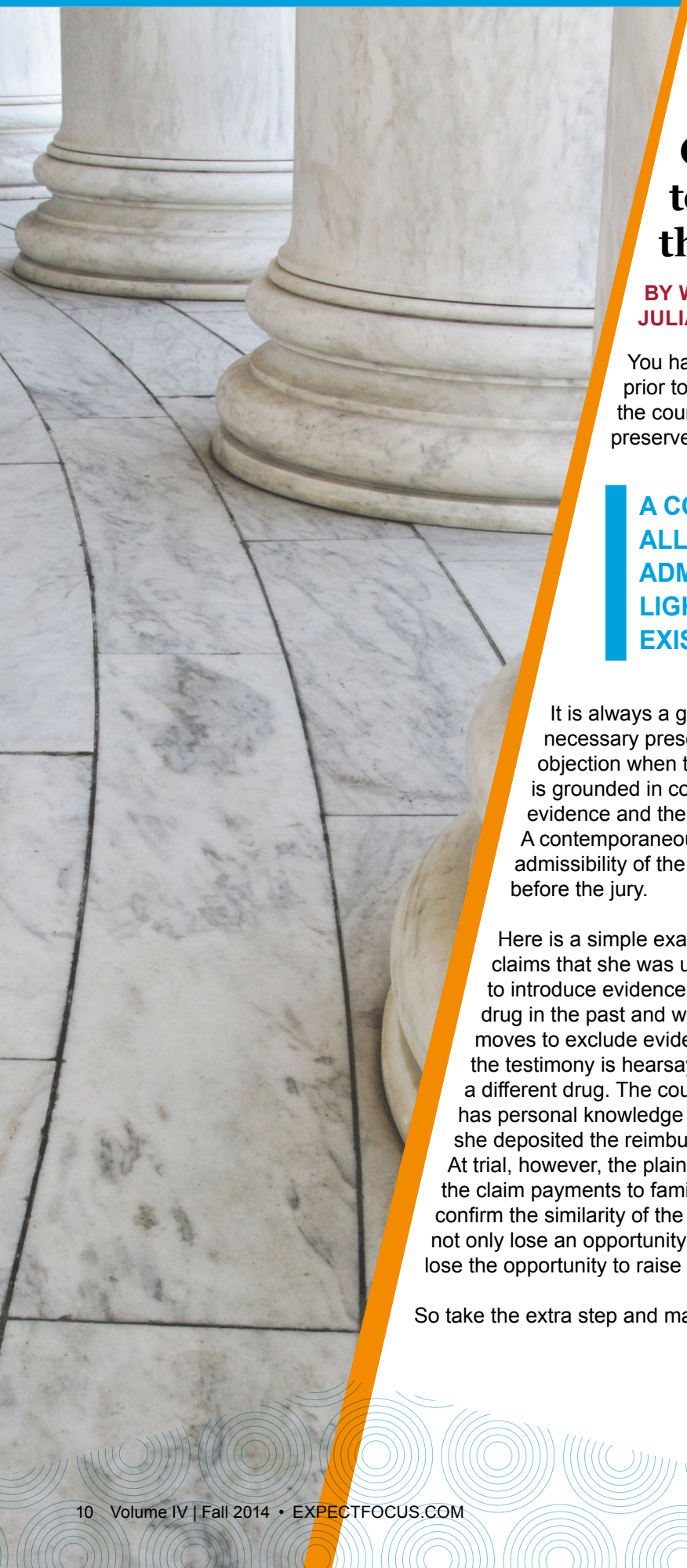
The review of CDAs seems the second-most likely to be resolved in early 2015. On November 16, the CDA Working Group scored a field goal by adopting the revisions addressing CDAs to the Annuity Disclosure Model Regulation, Suitability in Annuity Transactions Model Regulation, Advertisements of Life Insurance and Annuities Model Regulation and Annuities Replacement Model Regulation and by receiving comments on its October 24 draft Guidance for the Financial Solvency and Market Regulation of Insurers Who Offer Contingent Deferred Annuities.

There was no touchdown, as regulators determined CDAs should offer some benefit to consumers when they are terminated. **Regulators posited that some type of longevity or in-kind benefit should be offered rather than a cash value benefit, which would raise the cost of the product and possibly result in anti-selection.** Regulators asked industry to provide some ideas. During the field goal, an inadvertent flag was thrown by a consumer group that believed the CDA WG should first resolve the type of benefits to include in CDAs in the event of termination, and it re-raised questions on guaranty fund coverage.

Two contenders' playoff chances were dashed. While the SAR WG made good progress in early 2014, it fumbled a handoff as the chairman of SAR WG retired in July. With no volunteer to take over, the SAR WG's efforts stalled in the redzone. Also, the Unclaimed Life Insurance Benefits (A) Working Group (Unclaimed Benefits WG) looked poised to score with a Hail Mary as it recommended the development of a new NAIC model law for unclaimed life insurance benefits. The pass was incomplete as the Unclaimed Benefits WG cancelled its November 16 meeting.

The Life Actuarial Task Force (LATF) discussed two teams' actuarial guidelines for index universal life illustrations. LATF recognized that, while each team's guidelines had merit, neither completely addressed its concerns. It appears that the regulators are revamping the playbook as LATF asked industry to submit plays for short yardage and long yardage options. LATF set a goal of having actuarial guidelines ready for approval at the 2015 Spring National Meeting. Maybe LATF's playbook includes a jump-pass for a touchdown?





Motions *In Limine*, Contemporaneous Objections, and the Need to Adequately Preserve the Record

BY WENDY F. LUMISH & JULIANNA THOMAS MCCABE

You have filed your motions *in limine* and obtained rulings prior to trial. You put the motions in a box in the back of the courtroom and figure all of your objections have been preserved. Wrong!

A CONTEMPORANEOUS OBJECTION ALLOWS THE COURT TO CONSIDER THE ADMISSIBILITY OF THE EVIDENCE IN LIGHT OF THE CURRENT RECORD AS IT EXISTS BEFORE THE JURY.

It is always a good practice—and in many jurisdictions a necessary preservation practice—to make a contemporaneous objection when the evidence at issue is offered at trial. The rule is grounded in common sense. The court's understanding of the evidence and the parties' theories may change as the trial develops. A contemporaneous objection allows the court to consider the admissibility of the evidence in light of the current record as it exists before the jury.

Here is a simple example. In a health insurance coverage case, plaintiff claims that she was underpaid for a particular medication. She seeks to introduce evidence that other family members received the same drug in the past and were reimbursed a greater amount. The defendant moves to exclude evidence of the payments to family members arguing the testimony is hearsay, and it is irrelevant because it actually involved a different drug. The court denies the motion, finding that (1) the plaintiff has personal knowledge of the payments made to family members because she deposited the reimbursement checks; and (2) it was for the same drug. At trial, however, the plaintiff testifies that she lacks personal knowledge of the claim payments to family members and she concedes that she cannot confirm the similarity of the claims. Without that renewed argument, you may not only lose an opportunity to convince the court to change its mind, but also lose the opportunity to raise the issue on appeal.

So take the extra step and make a contemporaneous objection at trial.

California's Northern District Bucks Standing Trend in Data Breach Class Action

BY KRISTIN A. SHEPARD & MATTHEW E. KOHEN

A recent California federal district court order may prove a massive boon to data breach class action plaintiffs. The Northern District of California order, issued in *In re Adobe Systems, Inc. Privacy Litigation*, denied Adobe's motion to dismiss. The court found that the plaintiffs have **standing to sue based on their now-increased risk of future harm** due to the alleged compromise of their confidential information by hackers who gained unauthorized access to Adobe's systems.

This ruling breaks with the majority view that increased risk of identity theft following a data breach is insufficient to satisfy the standing requirements of Article III of the United States Constitution, as articulated in the Supreme Court's 2013 precedent in *Clapper v. Amnesty International.* Under *Clapper*, the threat of injury must be "certainly impending" to give rise to standing. Yet after a data breach, victims may not suffer financial harm immediately. Often, they may find that their identity or financial accounts have been compromised months or years after the breach. As a result, most courts have dismissed data breach putative class actions for lack of standing.

> **PLAINTIFFS HAVE STANDING TO SUE BASED ON THEIR NOW-INCREASED RISK OF FUTURE HARM DUE TO THE ALLEGED COMPROMISE OF THEIR CONFIDENTIAL INFORMATION BY HACKERS WHO GAINED UNAUTHORIZED ACCESS TO ADOBE'S SYSTEMS.**

According to the Northern District of California, however, the alleged disclosure of the plaintiffs' nonpublic personal information, including usernames, passwords, and credit card numbers, was sufficient injury to confer standing to sue. The court found that "the threatened harm alleged here is sufficiently concrete and imminent to satisfy *Clapper*."

So far, the decision's effect is unclear. But it certainly provides additional support for plaintiffs seeking to assert claims on behalf of a class injured by a data breach. Nevertheless, the court noted that the most factually analogous case, a data breach class action in the Southern District of Ohio, reached the opposite conclusion. Given the proliferation of data heists targeting large corporations, it is likely that this important question of law will continue to develop rapidly over the coming months.

Where is the "Serve" Button?

BY ZACHARY D. LUDENS

A handful of recent federal and state court decisions have opened the door for plaintiffs to serve defendants digitally via Facebook and LinkedIn messaging. Although this phenomenon was originally restricted to serving foreign individuals under Federal Rule of Civil Procedure 4(f)(3), **it could soon expand to cover U.S. individuals**.

Between March 2013 and February 2014, two federal courts allowed foreign defendants to be served via social media. In both cases, the courts initially determined whether the defendant's resident nation had affirmatively disallowed service via social media in an agreement with the United States. When that question was answered negatively, the courts—the Southern District of New York in *FTC v. PCCare247 Inc.* and the Eastern District of Virginia in *Whoshere, Inc. v. Orun*—examined whether service via social media was "reasonably calculated under the circumstances" to provide notice, in accordance with due process standards. In both cases, the courts allowed service via social media—but required that it be supplemented with service via email.

Then, in September 2014, a family court in Staten Island, New York, allowed a defendant to be served via Facebook when the traditional methods of service proved inadequate. Determining that the defendant had been actively using her Facebook account, the court concluded that Facebook provided **"the best chance of the [defendant] getting actual notice of these proceedings."** Nevertheless, the court also required mailing of service to the defendant's last known address.

These cases appear to demonstrate courts' increased willingness to allow service via social media, at least to the extent that it reflects a broader approach to effectuating service on difficult-to-serve defendants. While these three courts have also required concurrent service via traditional routes, the door has been opened. Nonetheless, perhaps in the near future, service via social media will become as widespread as service via email.

Considering the Impact of Driverless Cars

BY DIANE DUHAIME

Driverless cars, also called autonomous cars, auto-pilot cars, robo-cars, automated cars, connected cars, self-driving cars, or driver-free cars, can navigate and sense the surrounding environment without human input during travel.

According to Wikipedia, as of 2013, laws in California, Florida, Michigan, and Nevada permit driverless cars; cities in Belgium, France, Italy, and the UK have plans to operate driverless car transport systems; and Germany, the Netherlands, and Spain have permitted driverless car testing in traffic. Testing thus far indicates driverless cars have far fewer accidents than their human-driven counterparts because most accidents result from driver error. Testing does not, however, take into consideration such conditions as portable traffic lights, or heavy rain or snow. While many carmakers doubt a fully driverless car will be available anytime in the next 40 years, the auto industry as a whole appears optimistic. **Only last month, the Alliance of Automobile Manufacturers and the Association of Global Automakers published the Privacy Principles for Vehicle Technologies and Services.**

Should the driverless car become integrated into U.S. society, the United States will undergo big changes. The transition would likely occur gradually, and many people would probably never make the switch (just as many still do not use the Internet or mobile phones). Driverless cars could result in societal changes related to:

Freedom

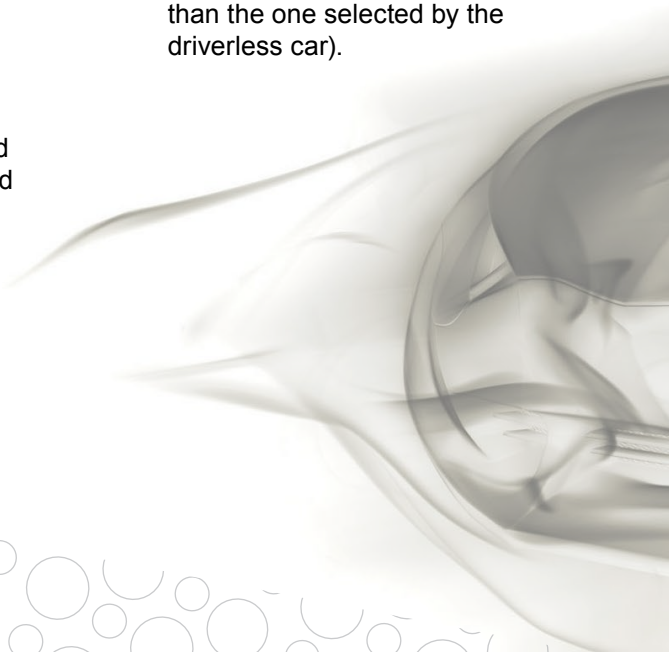
- Mobility for individuals who cannot obtain driver's licenses (e.g., the blind, physically challenged, and elderly).
- Driverless car owners could provide transportation for family members and others (regardless of whether such individuals are licensed).
- Riders could perform tasks that are now illegal while driving (e.g., reading, eating, texting).
- Because some human input is required to operate a driverless car, drinking alcohol and consuming other controlled substances would likely remain illegal.

Licensure

- Skills to obtain a license would be primarily technological, not manual.
- Relaxed age and physical requirements.
- Curfews and other rules applicable to newly-licensed persons would be eliminated or eased.

Liability

- Liability—and auto insurance policy requirements—would shift from driver (human error) to manufacturer (manufacturer error). Auto manufacturers may resist this change by contract, if doing so is not contrary to public policy.
- Driverless cars could be programmed to protect the car in all circumstances, potentially saving one life while harming another. For example, the driverless car could swerve to avoid a pedestrian but crash into another car and kill passengers in both cars.
- Driverless cars could be pre-programmed to match the owner's beliefs regarding, for example, how he or she would react when obstacles suddenly appear in the car's path.
- Override options could permit: (a) manual driving (with a computer, not necessarily a steering wheel); and/or (b) programming changes (e.g., to choose a different detour route than the one selected by the driverless car).



Economy

- Decreased demand for bus drivers, taxi drivers, chauffeurs, and airline and railroad workers, if people choose the privacy of a driverless car over these forms of transportation.

- While riding in their vehicles, postal workers, truck drivers and other delivery workers could perform tasks that would have otherwise been performed by stationary co-workers.

Data Privacy, Criminal Activities, and Cybersecurity Insurance

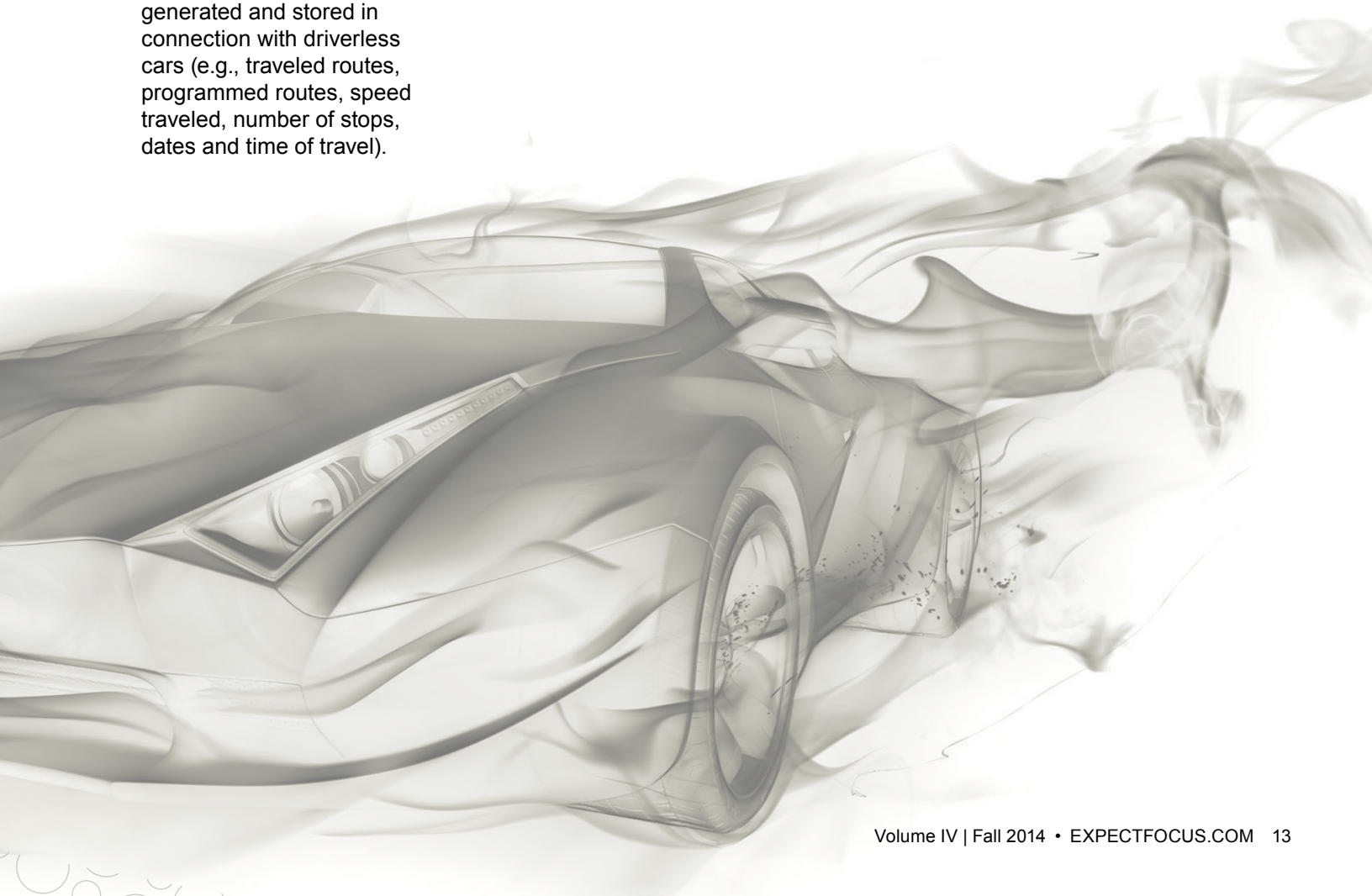
- Issues regarding ownership and licensing of the right to use or access data generated and stored in connection with driverless cars (e.g., traveled routes, programmed routes, speed traveled, number of stops, dates and time of travel).

- Laws to govern protection of driverless car data that is deemed personally identifiable information.

- Hacking into driverless cars to: obtain private data about an individual's transportation history or plans; cause accidents; kidnap passengers; turn driverless cars into lethal weapons. Such hacking activities would present new challenges for law enforcement, and new markets for cybersecurity and other insurance coverages.

- With a search warrant, law enforcement could identify the precise date, time, and location of an individual's vehicle.

While control freaks will likely keep a tight grip on their steering wheels for as long as possible, early adopters will no doubt flock to the driverless car once it becomes commercially available. Expressions like "keep your eyes on the road" and "keep both hands on the steering wheel" may one day become as archaic as "roll down the window," "dial the telephone," and "she sounds like a broken record."

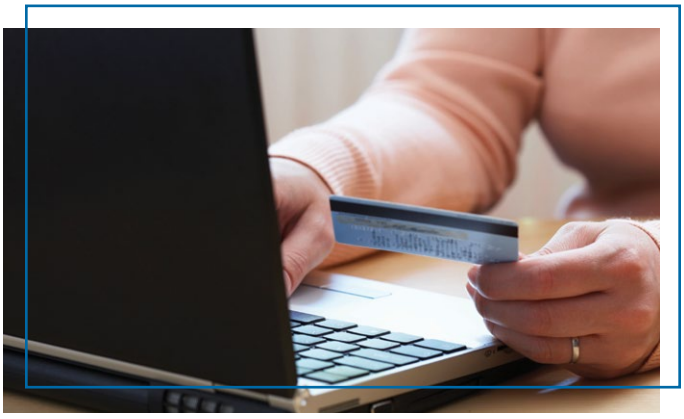


Online Merchants Beware: There's a New FTC Rule on Internet Purchases

BY GAIL PODOLSKY & KATE CELENDER

The Federal Trade Commission (FTC) released a new rule, 16 C.F.R. § 435, covering Internet purchases. It became effective December 8—just in time for holiday shopping. The new rule expanded the FTC's previously issued rule regarding phone and mail orders to include all Internet orders, even those made through a mobile device.

In particular, the new rule "prohibits sellers from soliciting mail, Internet, or telephone order sales unless they have a reasonable basis to expect that they can ship the ordered merchandise within the time stated on the solicitation or, if no time is stated, within 30 days." Further, the rule requires buyer consent for delayed shipments and, if the buyer does not consent, the seller must promptly issue a refund. Specifically, sellers now have seven working days after a buyer's right to a refund vests to process refunds for payments made through third party credit cards. The period for refunding purchases made by first party cards (e.g. where a seller itself issues the credit card) remains one billing cycle.



Online merchants must follow this new rule or risk severe penalties. Indeed, **the rule gives the FTC the power to sue a seller for injunctive relief and civil penalties of up to $16,000 per violation.** Additionally, the seller may be required to redress consumers. Sellers have the burden of proving compliance, and failure to provide the FTC with records or documentary proof establishing the use of procedures assuring shipment of merchandise within the applicable time creates a rebuttable presumption that the seller lacked a reasonable basis for expecting it would be able to timely ship orders. Thus, sellers should verify that they are retaining documentary proof of the procedures used to assure that merchandise was shipped within the timeframe the rule requires to help refute any claim of noncompliance by the FTC or buyers.

Newly-Adopted Privacy Standards for Cloud Service Providers

BY OLEG RIVKIN

The International Standards Organization's new cloud standard, ISO 27018, strives to ensure that public cloud service providers (such as Amazon, Google, and Rackspace) "offer suitable information security controls to protect the privacy of their customers' clients" by securing the personally identifiable information (PII) entrusted to them. The new standard, adopted by ISO and the International Electrotechnical Commission in August, is voluntary. It is expected to be followed by ISO 27017, which will cover non-privacy information security aspects of cloud computing.

According to the ISO, the new standard is intended as "a reference for selecting PII protection controls within the process of implementing a cloud computing information security management system …." Broadly, ISO 27018 addresses the questions of confidentiality and security of the customer's personal information and the prevention of its unauthorized use.

To be certified under ISO 27018, **a cloud service provider must pass an initial audit by an accredited certification entity (and be subject to periodic reviews).** Certification's aim is to achieve full transparency between the cloud service provider and its customer, and to enable the customer to select a provider that has satisfied its legal and regulatory obligations and demonstrated this to the certification body.

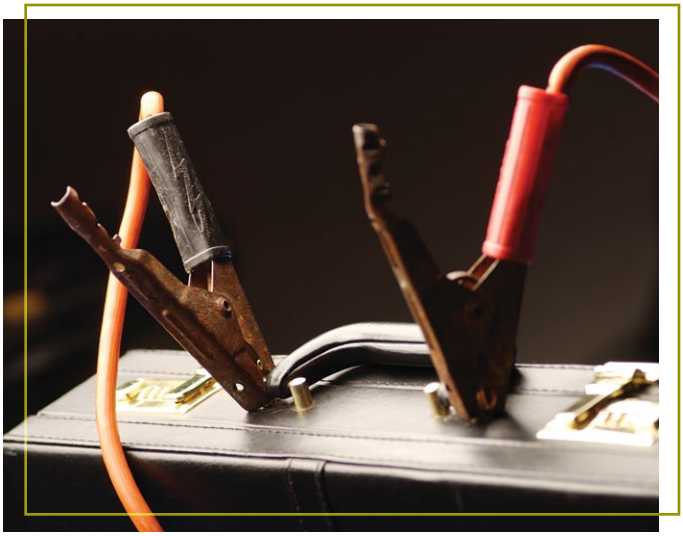
Among the new ISO 27018 standards is the requirement that all personal information be processed pursuant to the customer's instructions; the prohibition against demanding consent to use customer's information for marketing and advertising purposes as a condition of providing cloud service; restrictions on the disclosure of information to third parties; implementation of policies for the return or disposal of personal data; and disclosure of any sub-processors and possible locations where personal information may be stored or processed before entering into a service contract.

In this age of data privacy concerns, ISO 27018 certification may be an important criteria for many customers who are selecting a public cloud service provider for the first time, or determining whether to switch providers.

CFTC Follows SEC's Lead on "General Solicitation"

BY ED ZAHAREWICZ

Seeking to harmonize governing rules, the staff of the Commodity Futures Trading Commission (CFTC), by letter dated September 9, granted exemptive relief that enables commodity pool operators (CPOs) to rely on CFTC Regulations 4.7(b) and 4.13(a)(3) even if they also rely on recent Securities and Exchange Commission (SEC) rule amendments that permit advertising or other "general solicitation" as to certain offerings or resales of interests in private funds.



CFTC responds to help jumpstart U.S. businesses.

In July 2013, the SEC, in response to the Jumpstart Our Business Startups (JOBS) Act, amended its Regulation D to permit, for the first time, the use of general solicitation in private offerings exempt from registration under SEC Rule 506, provided certain conditions are met. The SEC likewise amended its Rule 144A to allow resales of securities to qualified institutional buyers to be made by means of general solicitation.

CFTC Regulation 4.7(b) provides qualifying registered CPOs relief from certain CFTC disclosure, periodic and annual reporting, and recordkeeping requirements, while Regulation 4.13(a)(3) provides an exemption from CPO registration as to funds that trade commodity interests in limited amounts. Both of these CFTC regulations apply only to funds whose offerings qualify for certain exemptions from registration under the Securities Act of 1933. As such, **these regulations are frequently relied upon within the private fund industry to mitigate or avoid the burdens of compliance with CFTC regulatory requirements.**

Because these CFTC regulations are also predicated on interests in the applicable fund being offered or sold "without marketing to the public" or "solely to qualified eligible persons," absent relief, CPOs relying on either regulation cannot also take advantage of the recent liberalization of the SEC's limitations on general solicitations. The relief granted, however, is available only to CPOs that file a notice with the CFTC to claim the exemption, and is subject to certain conditions, as described in CFTC Letter No. 14-116.

FINRA Examines Execution

BY ANN FURMAN

For the past year, FINRA has emphasized that it is stepping up consideration of whether broker-dealers are obtaining best execution of transactions in equities, options, and fixed income securities. It also has pointedly reminded firms of their duty to conduct "a regular and rigorous review of execution quality to assure that order flow is directed to markets providing the most beneficial terms to customers."

FINRA's enhanced efforts include new surveillance patterns to monitor best execution in both equity and fixed income securities. As to equity securities, FINRA's market regulation department is reviewing the processes and procedures of a targeted group of broker-dealers regarding order routing and execution quality of customer orders in exchange-listed stocks. As part of that review, in July these firms received a targeted examination letter requesting a substantial amount of information on their procedures for exchange order routing and limit orders. At a conference in September, FINRA chair and CEO Rick Ketchum warned that "priced order routing deserves more attention [and] is going to be 'a huge priority' for us in the next six months."

As to its fixed income securities surveillance efforts, FINRA is assessing the execution price a customer receives from a broker-dealer relative to that broker-dealer's other recently-executed customer transactions on the same side of the market. As to options, FINRA is reviewing situations where a broker-dealer potentially ignores a favorable price on one options market and executes a trade on another market to its customers' detriment.

FINRA's increased focus on best execution is **a reminder for all broker-dealers to review their policies and procedures for exercising reasonable diligence to determine the best market on behalf of customers.** The July targeted examination letter provides a strong indication regarding at least some of FINRA's concerns.

Money Market Fund Reform Complicates Insurance Product Fund Offerings

BY CHIP LUNDE

In July 2014, the SEC adopted amendments to Rule 2a-7 under the Investment Company Act of 1940 that impose new requirements on money market funds (MMFs). The amendments may have unexpected consequences and impose unique costs for issuers of variable insurance products and for underlying insurance product funds that provide investment options under those products.

New Rule Requirements

The amendments divide MMFs into three general categories: institutional funds, retail funds, and government funds. The amendments require that:

- institutional prime MMFs use a floating net asset value (NAV);
- retail MMFs be limited to beneficial owners who are natural persons; and
- government MMFs invest at least 99.5 percent of their assets in cash, U.S. government securities, and/or fully collateralized repurchase agreements.

The amendments also:

- provide for MMFs to impose liquidity fees or redemption gates (as discussed further below) if the amount of "weekly liquid assets" that they hold falls below certain levels;
- require MMFs to include certain legends in advertisements and prospectuses;
- require MMFs to disclose certain price and liquidity information daily on their websites;
- require MMFs to report certain price and liquidity events on new SEC forms; and
- require MMFs to conduct periodic stress tests.

Considerations for Choosing a Fund Type

The amendments create several problems that are making it difficult for some insurance product funds to decide whether to offer an institutional MMF, a retail MMF, a government MMF, or some combination of the three.

Insurance product funds considering offering an ***institutional MMF*** must consider factors including:

- whether a floating NAV is compatible with the actuarial assumptions of issuers of insurance products for which the MMF serves as an investment option;
- any impact of a floating NAV on insurance product issuers' reserving requirements or ability to hedge;
- the extent to which regulatory positions permitting use of a MMF for purposes such as "free-look" period investments and investment of proceeds from unaffiliated fund liquidations also apply to a floating-NAV MMF. (Note: Historically, some insurance product MMFs have operated on a floating, rather than a stable-NAV basis, and we are not aware that such funds have been considered precluded from the uses we refer to.);
- transition issues related to the conversion or reorganization of an existing stable-NAV MMF; and
- possible complications related to the administration of any fees and gates (see below).

Insurance product funds considering offering a re***tail MMF*** must consider factors including:

- the need to offer an alternative MMF for institutional investors due to the unavailability of retail MMFs to institutional investors (such as owners of bank-owned and other corporate-owned life insurance products);

- transition issues related to reorganization of an existing stable-NAV MMF to remove institutional investors; and
- possible complications related to the administration of any fees and gates (see below).

Insurance product funds considering offering a ***government MMF*** must consider factors including:

- whether investors will expect/demand higher yields than a government MMF is likely able to produce;
- whether insurance product issuers will expect/demand a higher yielding MMF (based on actuarial assumptions or otherwise); and
- potential complications for meeting applicable federal tax law diversification requirements.

Some insurance product funds have considered offering an ultra-short bond fund as a MMF alternative. However, using an ultra-short bond fund may also involve unique considerations, including:

- investors' and insurance product issuers' perception of risk;
- possible unavailability of the fund for free-look period investments and investment of proceeds from unaffiliated fund liquidations;
- tax issues (e.g., the absence of any exemption from the "wash" sale rule); and
- transition issues (including possible loss of prior performance history).

Considerations Relating to Fees and Gates

The amendments require non-government MMFs to impose a default 1 percent redemption (liquidity) fee if the fund's weekly liquid assets fall below 10 percent of its total assets (unless the fund board determines it is not in the fund's best interests).

The amendments also give all MMFs the flexibility to institute liquidity fees (up to 2 percent) and/or redemption restrictions (gates) for up to 10 business days if the fund's weekly liquid assets fall below 30 percent of its total assets and the fund board determines that doing so would be in the fund's best interests.

The considerations relevant to insurance product funds and issuers in deciding whether to offer a MMF that may impose liquidity fees include:

- the insurance product issuers' authority under the applicable variable annuity or life insurance contract to pass on liquidity fees to customers;
- the insurance product issuers' administrative capacity to implement liquidity fees (of up to 2 percent); and
- possible questions regarding how liquidity fees will be treated under variable contracts (e.g., in calculating excess withdrawals and required minimum distributions).

The considerations in deciding whether to offer a MMF that may impose redemption gates include:

- any impact on the variable contract owner's redemption rights under the contract; and
- any other impact on contract or rider functioning (e.g., how to assess contract or rider fees, or implement required asset rebalancing when redemption gates are imposed).

Given the issues and complications the amendments raise, the compliance deadlines of April 2016 (for diversification, stress testing, disclosure, and certain form filings) and October 2016 (for floating NAV and liquidity fees and gates) do not seem overly accommodating.

Broker-Dealer Fee Disclosure Under Microscope

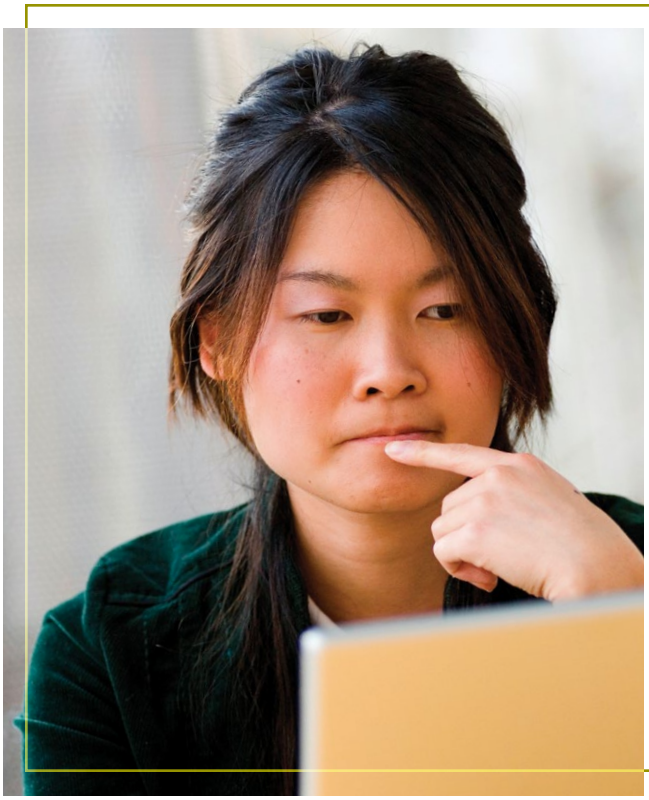
BY TOM LAUERMAN

In September, state securities regulators formed a working group aiming to make broker-dealers' disclosures about their fees more clear, accessible, and useful to investors in comparing different firms' charges. The group plans to finish its work by next fall, and will consider, for example, developing

- a model fee disclosure form;
- guidelines on accessibility, transparency, and uniform use of terminology; and
- recommendations on how to notify customers of fee changes.

In addition to representatives of the North American Securities Administrators Association (NASAA), the working group includes representatives of FINRA, the Securities Industry and Financial Markets Association, the Financial Services Institute, and several broker-dealer firms. NASAA President Andrea Seidt said **"the working group will take into consideration … wirehouse firms, independent broker-dealers, clearing firms, and introducing firms, among others.**"

Earlier this year, a NASAA report on its survey of 34 broker-dealer firms recommended the working group's formation. The survey found a wide disparity of broker-dealer fee disclosure practices. However, that survey, and certain enforcement actions that preceded and partially motivated it, focused particularly on certain problematic fee disclosure practices. For example, some firms allegedly hid the true amount of their compensation for securities transactions by charging unreasonable markups for what they disclosed as "handling," "postage," "delivery of securities in certificated form," or "miscellaneous." The survey also focused particularly on fees firms charge for closing accounts or transferring account securities to another firm.



Looking to make fees more understandable.

Against this background, the working group may focus primarily on disclosure issues regarding a limited number of specific fee types. Alternatively, the working group may seek a more comprehensive approach.

In any case, some of the practices addressed by NASAA's survey and the working group may involve legal violations. Broker-dealers would be well advised to review their own practices with that in mind.

Private Equity Fund Adviser Settles with SEC

BY MARC DRUCKMAN & BILL CHENG

Earlier this year, the Securities and Exchange Commission (SEC) announced plans to expand its task force examining private equity investment advisers. As discussed in the Spring 2014 issue of Expect Focus ("Private Equity: The Next Wave of SEC Enforcement Actions?"), the SEC identified what it believed were violations of law or material weaknesses in compliance controls regarding the collection and allocation of fees and expenses imposed by fund advisers in more than

half of the investment fund manager examinations completed. On September 22, 2014, as a result of the first enforcement action under this heightened scrutiny, one fund adviser, Lincolnshire Management, Inc., agreed to pay approximately $2.3 million (including $450,000 in penalties) to settle a case arising from alleged simple carelessness in the allocation of fees and expenses to portfolio companies.

Lincolnshire acquired two portfolio companies in 1997 and 2001, each for a different Lincolnshire-advised fund. Lincolnshire planned to integrate the two portfolio companies over time for an eventual combined sale. Beginning in 2009, the companies shared a joint management team and operated, in many respects, as one company – even while remaining distinct legal entities and maintaining separate financial statements. The SEC alleged that (1) certain expenses benefiting the portfolio companies were disproportionately allocated by Lincolnshire and (2) no written expense allocation policy existed, resulting in violations of the Investment Advisers Act based on Lincolnshire's purported negligent breach of its fiduciary duty, and its failure to maintain an adequate compliance program. The alleged violations reached as far back as 2005, and many occurred before Lincolnshire became a registered investment adviser in March 2012.

The Lincolnshire case is the first example of a likely trend toward growing SEC assertiveness in enforcement within the private equity industry. Previously, enforcement actions were generally reserved for more egregious legal violations, but **the SEC now appears willing to seek penalties in cases arising largely from apparent "bookkeeping" errors** that involve arguably small amounts of money that do not materially impact the performance of investments. Private equity industry compliance professionals are now officially on notice.

Investment Advisers Craft Fee Rebate Programs

BY KYLE WHITEHEAD

Recently-publicized fee rebate programs may signal a coming trend, as investment advisers seek to market strong cultures of client service and responsiveness.

For example, in August, the Securities and Exchange Commission (SEC) staff issued a no-action letter for a program under which a TD Ameritrade-affiliated adviser automatically rebates advisory fees to clients that invest pursuant to model portfolios that experience two consecutive calendar quarters of negative performance. This follows Charles Schwab's announcement last December of a program that permits clients who are for any reason "not happy" with the advisory services provided to request refunds of the most recent quarter's advisory fees.

Because advisory fee rebates can make the adviser's compensation to some extent contingent upon an account obtaining a certain performance level, TD Ameritrade sought SEC guidance because its program might be construed to violate the Investment Advisers Act's general prohibition on adviser compensation that is based on capital gains or capital appreciation in a client's account. This prohibition reflects Congress' concern that such compensation schemes could encourage advisers to take undue risks and speculate with client assets on a "heads I win/tails you lose" basis.

Congress sought to avoid a "heads I win/tails you lose" approach.

However, this type of conflict is largely absent under the circumstances of both the TD Ameritrade and Schwab programs. For instance, the TD Ameritrade adviser will hire an independent adviser to make the investment decisions for the model portfolios, from which the TD Ameritrade adviser will have only limited discretion to deviate (such as for tax-related considerations and client restrictions). Under the Schwab program, dissatisfied clients may obtain fee rebates regardless of account performance. Therefore, any relationship between the adviser's compensation and any capital gains or capital appreciation is attenuated, at best.

Cybersecurity: Dig That Crazy Important Beat

BY BEN SEESSEL

The SEC and FINRA are maintaining a steady drumbeat to motivate regulated firms to adequately protect themselves from cyber-attack.

The SEC's Office of Compliance Inspections and Examinations (OCIE) began 2014 by prominently emphasizing information security technology in its published examination priorities for the year. These included a specific reference to the cybersecurity issues around broker-dealer trading activities. Then, in March, the Commission held a Cybersecurity Roundtable at which SEC Chairman Mary Jo White and Commissioner Luis Aguilar both emphasized this topic's importance for regulated firms.

In April, OCIE again weighed in, issuing a risk alert that announced an initiative to conduct targeted cybersecurity exams of more than 50 broker-dealers and investment advisers. OCIE included a sample information request as an appendix to the risk alert, "to empower compliance professionals … with questions and tools they can use to assess their firms' level of preparedness" regardless of whether they are subject to an exam.

FINRA also included cybersecurity prominently among its published regulatory and examination priorities for 2014, announcing that it was sending targeted examination letters to broker-dealer firms to assess their approaches to cybersecurity threat management. The concerns itemized in this announcement are similar to those reflected in more detail in OCIE's risk alert and its accompanying appendix. FINRA panelists discussed the findings of FINRA's targeted examination sweep at its South Regional Compliance Seminar in November.

> **FINRA ANNOUNCED THAT IT WAS SENDING TARGETED EXAMINATION LETTERS TO BROKER-DEALER FIRMS TO ASSESS THEIR APPROACHES TO CYBERSECURITY THREAT MANAGEMENT.**

Under the circumstances, **firms that have not already done so should strongly consider assembling a team across business areas to address cybersecurity, in consultation with compliance and legal personnel**. The OCIE Risk Alert Appendix can serve as a very useful guide and checklist for that effort.

Protections Governing Theft and Publication of Medical Records

BY GAVRILA A. BROTZ

As instances of medical data breaches increase, U.S. courts are interpreting the scope of liability stemming from them. In California, the court in *Sutter Health et al. v. The Superior Court of Sacramento County (Atkins)* held that patients can only recover damages if they can prove that their protected medical information was actually viewed by an unauthorized person. Meanwhile, in *Travelers Indem. Co. of Am. v. Portal Healthcare Solutions LLC*, a Virginia federal court found that insurers must defend class actions alleging that their insureds posted confidential records online if their policies cover publication of the information, regardless of whether the records were actually viewed.

California: Were stolen medical records viewed by unauthorized persons?

The California Confidentiality of Medical Information Act (CMIA) provides for nominal damages of $1,000 per patient against health care providers who negligently allow the unauthorized disclosure of their patients' medical information. In October 2011, a thief broke into a Sutter Health office and stole a desktop computer containing more than four million patients' password-protected, but unencrypted, medical records. Sutter Health announced the breach in November 2011. Certain patients' individual lawsuits for nominal damages under the CMIA soon followed, and were ultimately coordinated in a class action, exposing Sutter Health to a potential $4 billion liability. Though the trial court denied Sutter Health's demurrer, the appellate court found that, while the CMIA prohibits unauthorized disclosure of medical information, the records at issue were not "disclosed" to the thief as it was not done voluntarily. However, the CMIA imposes "broader duties" by requiring that such information be kept confidential. Specifically, health care providers must preserve the confidentiality of such records, but no breach of that confidentiality occurs, according to the *Sutter Health* Court, unless "an unauthorized person views the medical information." Therefore, the fact that a thief possessed protected medical information, absent the allegation that the information was indeed viewed, does not give rise to a cause of action for nominal damages under the CMIA. The court emphasized that the CMIA is not named the "Possession of Medical Information Act."

Virginia: "The act or process of making known something that was previously unknown."

Conversely, under Virginia law, confidential medical information is published and disclosed when it is posted online, even unintentionally, and even when there is no evidence a third-party viewed that information. Indeed, even in suits where the only evidence was that patients viewed their own information online by searching for their names and finding their medical records, "publication" and "disclosure" had occurred, obligating an insurer's defense of the underlying action. The definition of publication does not hinge on third-party access.

Travelers insured Portal Healthcare Solutions, a business specializing in the electronic safekeeping of medical records, from claims arising from the records' publication. After the medical records of Glen Falls Hospital patients were mistakenly posted online, a class action was filed against Portal for failing to safeguard them. Travelers then sought a declaratory judgment that it had no duty to defend Portal, its insured, against such claims, arguing that Portal's actions did not constitute "publication" or "disclosure" of confidential information, both coverage prerequisites. The Eastern District of Virginia relied on Black's Law Dictionary's definition of "disclosure" as "[t]he act or process of making known something that was previously unknown; a revelation of facts." Unlike the *Sutter Health* court's interpretation, the *Travelers* court found that this definition allows for involuntary disclosure, and moreover, found disclosure occurred even if the information was not made "known" to any third-party. Because the underlying class action therefore contained enough allegations to constitute publication and disclosure of protected confidential information within the meaning of the subject policies, Travelers was directed to defend Portal.

HIPAA: Deadlines Pass and Definitions Change

BY RADHA BACHMAN & PATRICIA "TRISH" CALHOUN

For all covered entities and business associates, September 22 was the last day for business associate agreements (BAAs) to comply with the Omnibus HIPAA Rule (the Rule) released in January 2013. Before the Rule's release, business associate agreements had to contain a description of permissible uses or disclosures of protected health information, requirements to help the covered entity respond to individual rights, and certain termination provisions.

The Rule generally required covered entities and business associates to update their BAAs by September 23, 2013. But "grandfathered BAAs" – those in place on January 25, 2013 – were given an extra year to comply with additional obligations for BAAs under the Rule. These obligations require references to the business associate's compliance with the HIPAA Security Rule, language regarding subcontractor relationships, and breach reporting requirements. Failure to meet the deadline coupled with an investigation or audit, could subject the covered entity and the business associate to fines and penalties.

UNDER HIPAA, LEGALLY MARRIED PERSONS ARE EACH OTHER'S "SPOUSE," AND SAME-SEX SPOUSES AND THEIR DEPENDANTS MUST NOW BE CONSIDERED "FAMILY MEMBERS."

In other HIPAA news, same-sex marriages must now be recognized.

Following the decision of the Supreme Court in *United States v. Windsor*, which held the Defense of Marriage Act unconstitutional, the U.S. Department of Health and Human Services Office of Civil Rights issued guidance clarifying that legally performed same-sex marriages must be recognized under HIPAA.

Under HIPAA, legally married persons are each other's "spouse," and same-sex spouses and their dependants must now be considered "family members."

This interpretation ensures that same-sex couples and their legal dependants have the right to receive notice of their family member's location, condition, or death pursuant to 42 CFR §164.510(b). In addition, this position extends the protections against genetic discrimination to certain information about the same-sex family members under §164.502(a)(5)(i). Importantly, these definitions apply regardless of whether the married same-sex couple lives in a state that recognizes the marriage.

Aggressive Regulators and the Plaintiffs' Lawyers Who Follow Them

BY MARTY SOLOMON

As soon as a putative class action complaint hits the clerk's office alleging a new theory of liability, plaintiffs' lawyers rush to sign up potential class representatives and file copycat suits in as many jurisdictions as they can cover. This saves would-be class counsel the trouble of trying to come up with their own new liability theories and, under the principle of "where there's smoke, there must be fire," each new filing can create, in the minds of some courts, the impression of more substantive merit than many of these claims actually have. This has been common practice for years.

Never placing a terribly high premium on originality, plaintiffs' lawyers are just as happy to follow on the heels of regulators. Unfortunately, some regulators appear all too ready to cooperate with those efforts. The Consumer Financial Protection Bureau (CFPB), for example, has taken increasingly aggressive positions on murky questions of law under complex and rapidly changing regulations. Moreover it has built into many of its enforcement orders provisions that seem to affirmatively invite the plaintiffs' bar to target entities that cooperate and settle with the CFPB. These provisions increasingly seem to be triggering "regulator chaser" class actions, which lay in wait like landmines for title insurers, other settlement service providers, and financial institutions.

For example, in July 2013, the CFPB sued Cast & Cooke Mortgage LLC in federal court in Utah, alleging that the lender's bonus program violated the Federal Reserve Board's Loan Originator Compensation rule by tying loan officer bonuses to the interest rates of the loans they made. Six months later, Cast & Cooke settled for $9.2 million in restitution and a $4 million civil penalty. **Yet the CFPB insisted on a consent order providing that "Redress provided by the Company shall not limit consumers' rights in any way."** Predictably, consumers soon filed an action seeking certification of a putative nationwide class under TILA and RESPA. The lead plaintiff had received $795.02 from the $9.2 million restitution fund, and alleged that the one year statute of limitations on his RESPA claim had been tolled until he got the CFPB-mandated check from the lender, since he had been "unaware that [the lender] had implemented a secret, illegal bonus program."

The CFPB may be creating similar risks for title insurers, their agents, and other settlement service providers with newly aggressive RESPA enforcement actions. In May, the CFPB levied a $500,000 fine against one of Alabama's largest settlement service provider families, Realty South and its affiliate TitleSouth, LLC, alleging that their Affiliated Business Arrangement disclosures failed to satisfy RESPA's safe harbor provisions. Even though the providers revised their disclosures right away, and voluntarily entered the consent decree, the decree seemed to invite a follow-on civil action, providing that "**In the event that there are…any private damages actions…in order to preserve the deterrent effect of the civil money penalty, Respondents shall not argue that they are entitled to, nor shall Respondents benefit by, any offset or reduction of any monetary remedies…"**

The private plaintiffs' bar will certainly attempt to use the CFPB's authority to lend credence to theories of liability that are so aggressive they might not even have been advanced without the CFPB's lead. The CFPB's June 2014 entry of a consent order with New Jersey's Stonebridge Title Services, Inc., imposing a $30,000 civil penalty for allegedly illegal referral fees, provides chilling regulatory precedent. In this action, CFPB simply disregarded the fact that the fees had been paid to employees who had received W-2s from Stonebridge and alleged that the salespeople were, in fact, independent contractors, and therefore not within the RESPA safe harbor that Stonebridge had probably thought protected it.

Similarly, in September 2014, the CFPB entered a $200,000 consent order with Lighthouse Title, Inc., alleging that the title agent's Marketing Service Agreements (MSAs) with advertisers violated RESPA's anti-kickback provisions. But the CFPB's basis for that conclusion, as recited in the consent order, was so vague and overbroad that an enterprising plaintiffs' lawyer may have little difficulty arguing that it encompasses virtually any MSA.

It is troubling, and more than a little ironic, to consider **that the CFPB's regulatory enthusiasm and apparent willingness to spur on new consumer class actions could ultimately lead to increased costs for consumers** as it drives up the cost of doing business for the settlement service providers and financial institutions that serve those consumers.

New York's Late Notice Statute Leaves No-Prejudice Rule Intact for Out-of-State Policies

BY JOHN PITBLADO

A New York statute provides that liability insurers may not deny claims on grounds of late notice, *unless* they can show they were prejudiced by the delay. The statute applies to policies "issued or delivered" in New York. In October 2014, *in Indian Harbor Ins. Co. v. City of San Diego*, the U.S. Court of Appeals for the Second Circuit ruled that the statute did not abrogate New York's older, common-law rule, which imposed no prejudice requirement, and which still applies to policies issued elsewhere. As a result, the City of San Diego could not avoid the consequences of providing late notice for a pollution claim.

THE SECOND CIRCUIT HELD THAT THE POLICY WAS NOT ISSUED OR DELIVERED IN NEW YORK, BECAUSE IT WAS NEITHER "PREPARED" NOR "SIGNED" WITHIN THE STATE.

Shortly after the statute took effect, San Diego purchased a pollution and remediation legal liability policy from Indian Harbor Insurance Company. The policy, which was governed by New York law, required the city to notify its insurer "as soon as practicable" of any claim regarding "pollution conditions." Trouble arose when the city was notified of three claims against it, including one, by Centex Homes, for "hydrochloric gas emissions." Because the city took 58 days to notify Indian Harbor, the insurer denied the claim and brought a declaratory judgment action.

Historically, under New York common law, courts strictly enforced notice provisions in liability policies, without requiring insurers to demonstrate prejudice. San Diego argued, however, that its policy was subject to the new statute, because it had been "issued or delivered" in New York. It also argued that the statute manifested a public policy against strict enforcement of notice provisions, which would abrogate the common law rule for all insurance policies. Finally, the city denied that its notice was untimely.

The district court rejected these claims and granted summary judgment to the insurer. On appeal, the Second Circuit held that the policy was not issued or delivered in New York, because it was neither "prepared" nor "signed" within the state. The policy did bear the signature of Indian Harbor's president, and his office was in New York, but it was undisputed that the "signature" was actually an electronic stamp that was created in, and mailed from, Pennsylvania. The court also rejected the City's argument that the newly-enacted statute abrogated the common law rule, as the scope of the statute was expressly limited to policies issued within the state.

The Second Circuit also found that notice had, in fact, been "unreasonably" delayed. The city argued that Centex's legal claim had not accrued before the city provided notice of it, but the court found that fact irrelevant. The purpose of the notice provision, the court held, was to "permit the insurance company to investigate promptly." Because the city failed to notify Indian Harbor "as soon as practicable" after learning about "hydrochloric gas emissions," summary judgment was affirmed.

Florida Courts Offer Different Opinions On "Policy Conditions"

BY JEFFREY MICHAEL COHEN

Several recent Florida decisions have addressed the distinction between "conditions precedent" and "conditions subsequent" in insurance policies and the impact of that distinction on issues of prejudice and burden of proof at trial. It is difficult to reconcile the opinions.

In *State Farm Mut. Ins. Co. v. Curran*, the Florida Supreme Court noted that a condition precedent is a condition that must be performed before the insurance contract becomes effective. A condition subsequent presupposes the insurer's obligation under the policy, but provides that the obligation will be negated if the condition is not performed or does not occur. In a suit alleging a policy breach, the policyholder has the burden to plead and prove satisfaction of a condition precedent. However, an insurer has the burden to plead and prove the failure of a condition subsequent, and also to demonstrate prejudice as a result of the failure.

In *Curran*, the policyholder was injured by an underinsured motorist. The policyholder settled with the tortfeasor and then demanded that State Farm pay its limits of uninsured motorist coverage. State Farm attempted to schedule a compulsory medical exam (CME) pursuant to the policy terms, but the policyholder refused to attend. State Farm notified the policyholder that her failure to assist and cooperate might result in a denial of coverage. The policyholder sued and was awarded a summary judgment. The Florida Fifth District Court of Appeal affirmed, holding

that the policy's CME clause was a condition subsequent, thereby requiring State Farm to plead and prove prejudice to defeat coverage.

The decision was certified to the Florida Supreme Court as a matter of great public importance and affirmed by a divided court. The majority opinion relied on precedent holding that a CME provision is a condition subsequent, the non-occurrence of which is an affirmative defense. A concurring Justice approved that result, on the rationale that uninsured motorist coverage is statutorily required, and so that insurers are precluded from imposing conditions that are not authorized by Statute and "directly contrary to the statutory purpose of Uninsured Motorist benefits." Two Justices dissented, because they believed the policy "unambiguously" required a CME as a *condition precedent* that the policyholder had failed to satisfy. The dissent opined that the majority erred by defining a condition precedent as a condition that must be performed before a policy becomes effective, instead of following cases which establish that they are prerequisites only to the right to sue to recover contract benefits. According to the dissent, the policy's CME obligation was an unambiguous condition precedent to the policyholder's right to sue for benefits. Therefore, an insurer need not show that the failure of the condition caused it to suffer prejudice.

A CONDITION SUBSEQUENT PRESUPPOSES THE INSURER'S OBLIGATION UNDER THE POLICY AND PROVIDES THAT THE OBLIGATION WILL BE NEGATED IF THE CONDITION HAS NOT BEEN PERFORMED OR OCCURRED.

Several months after *Curran*, the Florida Fourth District Court of Appeal reached a different result, when a policyholder sued State Farm for failing to pay her property damage claim and suffered an adverse summary judgment. In *Rodrigo v. State Farm Inc. Co.*, the policyholder failed to submit a sworn proof of loss, which the policy required as a condition precedent to relief. The Fourth District Court affirmed the summary judgment in favor of State Farm and distinguished *Curran*, on the ground that the *Curran* rationale was limited to "the unique subject of uninsured motorist coverage and compulsory medical exams." The court noted that the policy specifically provided that the insured had an affirmative duty to provide a sworn proof of loss, "unlike a CME, which is requested by the insurer to substantiate a claim already made by the insured."

In *Solano v. State Farm Florida Ins. Co.*, decided several months after *Rodrigo*, the Fourth District again appears to have departed from *Curran*, although the facts are almost identical. The Solanos sued State Farm for failing to pay their claim for property damage caused by Hurricane Wilma. Following the storm, the Solanos submitted several sworn proofs of loss, each increasing the claim for damage. State Farm requested that they submit to Examinations Under Oath (EUO), as required by the policy as a condition precedent to recovery. Dr. Solano appeared for the EUO and answered questions, but he deferred to his adjuster and his wife regarding the type, extent and cost of the damages. Dr. Solano refused to have his wife submit to the EUO, and the adjuster also refused. State Farm then rescheduled Mrs. Solano's EUO, but the Solanos sued before it occurred. The trial court granted summary judgment for State Farm, because Dr. Solano's failure to provide a meaningful EUO was a failure of a condition precedent to recovery.

On appeal, the Fourth District reversed. Although a refusal to provide an EUO was a breach of a condition precedent, precluding recovery under the policy, the court found that there was a factual dispute regarding over whether the Solanos had totally failed to comply. Thus, there was a question of fact as to whether there was *sufficient compliance* with the policy's condition precedent. The court declined to address *Curran*, because, "While the issue addressed in *Curran* is similar to the issue addressed here, the Court's analysis hinges on matters which are not present in this case."

As a result of these decisions, it is difficult to determine whether a policyholder's failure to comply with a policy condition is a failure of a condition precedent, which defeats coverage, or a failure of a condition subsequent, which shifts the burden to the insurer to prove that the policyholder breached the policy and caused prejudice to the insurer. The Florida Supreme Court will have to clarify whether *Curran* is limited to uninsured motorist claims or applies to all policy conditions.

Suing for Bad Faith Gets a Little Easier in Florida

BY BERT HELFAND

In a ruling that claims merely to clarify a 14-year-old case from the Florida Supreme Court, an appellate court recently held that an insurer may be liable to a statutory claim for bad faith failure to settle, based only on an unfavorable resolution of a property policy's appraisal process. The decision will likely make bad faith claims more common and negotiations with Florida insureds more contentious.

The plaintiffs in *Cammarata v. State Farm Florida Ins. Co.* waited two years to file a claim after their home suffered damage from Hurricane Wilma in 2005. Their insurer estimated the amount of the damage to be below their deductible, but it agreed to submit to the policy's appraisal process. At the end of that process, a neutral umpire reached an estimate that fell between those of the two parties, but which was higher than the policy deductible. The insurer promptly paid the claim. Although there was no allegation that State Farm had obstructed the appraisal, the insureds filed a new action for statutory bad faith.

The circuit court awarded summary judgment to the insurer, holding that the claim was not ripe, because there had not yet been any finding that State Farm was liable for breach of contract. Reversing that decision, the Fourth District Court of Appeal held that a bad faith suit may rest on determinations of nothing more than (i) the amount of damages and (ii) the fact that the insurer is liable to provide coverage. As one of the judges acknowledged in a concurrence, those conditions are satisfied "any time the insurer dares to dispute a claim, but then pays the insured just a penny more than the insurer's initial offer to settle." Thus, State Farm could be required to defend a bad faith suit on the merits, although "the record here provides no basis indicating that the insurer breached the contract, much less failed to act in good faith."

The decision rests primarily on the Florida Supreme Court's somewhat paradoxical 2000 opinion in *Vest v. Travelers Ins. Co.* In *Vest*, the insured brought a bad faith claim, and the insurer responded by paying policy limits. The Supreme Court stated that the bad faith suit had been premature when filed, but that it "ripened" upon the insurer's "settlement." That is, the insurer's voluntary payment was enough of a "determination" of its liability to pay the claim to support an action for bad faith.

THE SUPREME COURT STATED THAT THE BAD FAITH SUIT HAD BEEN PREMATURE WHEN FILED, BUT THAT IT "RIPENED" UPON THE INSURER'S "SETTLEMENT."

What *Vest* did not consider, however, was the practical effect of a rule under which any insurer that submits to an appraisal and ends up paying more than it first offered must then defend a bad faith action on the merits. The concurrence in *Cammarata* did address that problem, urging the Legislature to amend the relevant statute by imposing further requirements on bad faith claims.

New CFPB Regulations Subject Mortgage Servicers to Private Lawsuits

BY ROBERT SCHMIDLIN

The Consumer Financial Protection Bureau (CFPB) amendments to Regulation X, which implements the Real Estate Settlement Procedures Act (RESPA), place new and onerous requirements on mortgage servicers to correct errors and provide information that borrowers request. Under the new rules, borrowers, or their authorized representatives, who notify mortgage servicers of a claimed loan servicing error (Notice of Error) trigger new servicer obligations to respond under tight deadlines. These obligations carry potential litigation risks.

The amendments require servicers to provide written acknowledgement of the Notice of Error within five days. If the claimed error relates to failure to provide an accurate payoff balance, servicers have only seven days from receipt of the Notice of Error to investigate and provide a response that either confirms the error and states it has been corrected, or states that the servicer has determined no error occurred, the basis for that determination, and that the borrower is entitled to request supporting documents. If the Notice of Error claims improper pursuit of foreclosure, servicers must respond within 30 days, or before the foreclosure sale, whichever is earlier. Servicers must respond to all other types of asserted errors within 30 days, although an additional 15-day extension may be obtained to respond to such assertions.

However, the regulations do not require that a Notice of Error be submitted in any particular format. **Servicers could find it challenging to ensure these notices are recognized and properly handled within the response deadlines.**

In its introduction to the new regulations, the CFPB stated that regulations established pursuant toSection 6 of RESPA are subject to Section 6(f) of RESPA, which gives borrowers a private right of action to enforce such regulations. Consequently, plaintiffs' attorneys, who have already filed several actions against servicers alleging failures to respond to qualified written requests that dispute mortgage loan servicing errors, can add a new weapon to their arsenal: claims for failure to respond to Notices of Error within the time or in the manner required by the new regulation.

Financial Institutions Voice Concerns about CFPB Proposal to Publish Narrative Consumer Complaint Data

BY ELIZABETH M. BOHN

In our last issue, we discussed the Consumer Financial Protection Bureau (CFPB) proposal to publicly disclose consumer complaint details filed via its web-based public consumer complaint database by including an unstructured consumer narrative of the events leading to the complaint. The proposal's comment period expired on September 22.

The CFPB received several comments in favor of the concept from consumers and consumer groups. On the final day of the comment period, however, counsel for several large financial institutions submitted a lengthy comment describing industry concerns about, and objections to, the CFPB's policy statement (Statement) in support of the proposal. **They asserted that the proposal would have "serious negative consequences for financial institutions with little or no corresponding benefit to consumers."** The specific concerns mentioned included that the CFPB had not shown that the publication of narratives would improve consumer choice or purchasing decisions, and that the Statement did not resolve privacy concerns regarding the narratives' publication. For example, the comment notes that the proposal to "scrub" personally identifiable information from the narratives to protect consumers' privacy would remove references to dates, locations, and other descriptive information needed for the industry to respond to the complaints.

Additionally, and consistent with the reputational risk we mentioned in our last issue of Expect Focus, the comment also asserts that publication of narratives would create financial and reputational risks for financial institutions, stating that even permitting institutions to respond would not prevent the circulation of potentially erroneous information through publication of narratives. For example, consumers who review the CFPB website might get "the impression that any published narrative represents a legitimate dispute … regardless of the complaint's merit", amounting to "regulation by anonymous online reviews," given that the information would be published on the CFPB's "official" website.

Revised CFPB Ability to Repay Rule Allows Excess Points and Fees Refunds for Qualified Mortgages

BY ELIZABETH M. BOHN

The Dodd-Frank Act amended the Truth in Lending Act (TILA) to require a creditor making a residential mortgage loan to make a reasonable and good faith determination (based on verified and documented information) that, at the time the loan is consummated, the consumer has a reasonable ability to repay it. It further provides that the ability-to-repay requirements are presumed met if the loan is a "qualified mortgage." Qualified mortgages are subject to certain requirements, for example, points and fees charged to the consumer on a qualified mortgage generally cannot exceed 3 percent of the loan principal at the time the loan is made.

IF, AFTER THE LOAN HAS CLOSED, A LENDER OR ASSIGNEE DISCOVERS THAT IT HAS EXCEEDED THE 3 PERCENT CAP, THE LENDERS CAN REFUND THE EXCESS AMOUNT WITH INTEREST TO THE CONSUMER, SO THE LOAN STILL MEETS THE LEGAL REQUIREMENTS OF A QUALIFIED MORTGAGE.

On October 17, the Consumer Financial Protection Bureau (CFPB) made minor changes to the mortgage rules to provide limited circumstances where lenders that exceed the points and fees cap under the Ability to Repay Rule may refund the excess amount, plus interest, to consumers, while allowing the loan to still be considered a "qualified mortgage."

Under the finalized amendments if, after the loan has closed, a lender or assignee discovers that it has exceeded the 3 percent cap, the lenders can refund the excess amount with interest to the consumer, so the loan still meets the legal requirements of a qualified mortgage, under limited conditions. The creditor must have originated the loan in good faith as a qualified mortgage, the refund on the overage must be given within 120 days of consummation, and the creditor or assignee must maintain and follow policies and procedures for post-consummation review of loans and refunding such points and fees overages to consumers.

Eleventh Circuit Reverses *Mais*

BY AARON S. WEISS

In what promises to have significant implications for litigation under the Telephone Consumer Protection Act (TCPA), the Eleventh Circuit Court of Appeals reversed the decision issued by Judge Robert Scola of the Southern District of Florida in *Mais v. Gulf Coast Collection.*

The Eleventh Circuit ruled that Judge Scola exceeded his jurisdiction—as a district court judge—to "enjoin, set aside, annul, or suspend" an FCC Order, based on the Hobbs Act, which provides that any "proceeding to enjoin, set aside, annul, or suspend any order of the Commission" must be brought under the Hobbs Act's procedures.

Judge Scola acknowledged that his "Black's Law Dictionary" reading of the term "express consent" was explicitly contrary to the FCC's definition of the term, but found that, as a district court judge, he was not bound to follow the Hobbs Act. He also ruled that a patient who provides his cell phone number in connection with medical treatment is not consenting to be called at that number for TCPA purposes.

The Eleventh Circuit's decision clarifies the meaning of express consent: **releasing a number to a creditor in connection with a transaction that results in a debt, even if the number is provided in connection with medical treatment, constitutes consent for the debtor to call about the debt**.

The decision will have far-reaching consequences, as other FCC orders are often at issue in TCPA cases. Additional significant aspects of the opinion include:

- The prior express consent language in the 2008 FCC Ruling indicates that it applies to "a wide range of creditors and collectors, including those pursuing medical debts." *Mais* involved a phone number provided on a hospital admission form, and in the context of medical debt collection, the term "health information" included use of plaintiff's cell phone number for billing purposes.

- The court also held that an intermediary may provide consent to call a cell phone. So, it was acceptable for the hospital that was given the number to provide it to a debt collection company.

An Unlikely Condition Precedent to Foreclosure in Florida

BY CHRISTOPHER SMART & APRIL Y. WALKER

Mortgage servicers beware. Mortgagors in Florida are defending residential mortgage foreclosures based on the allegation that the servicer failed to give them notice of assignment of the right to bill and collect on the debt underlying the mortgage before commencing the foreclosure action.

The argument is based on Florida Statute Section 559.715, the Florida Consumer Collection Practices Act (FCCPA), and seizes on an October 1, 2010 amendment that requires the notice be given "as soon as practical after the assignment is made, but at least 30 days before any action to collect the debt."

The argument is misguided, however, as Florida law holds that an *in rem* mortgage foreclosure is an action to enforce a security instrument and not to collect a debt. Numerous cases from the Eleventh Circuit, including *Trent v. Mortgage Electronic Registration Systems, Inc.* and *Warren v. Countrywide Home Loans, Inc.* distinguish the collection of funds due on a debt and the foreclosure of a security interest in real property, holding the latter is not debt collection activity under the FCCPA or its federal counterpart, the Fair Debt Collection Practices Act (FDCPA).

In *Freire v. Aldridge Connors, LLP*, a Florida district court held that a mortgage foreclosure action will constitute debt collection activity only when the complaint also seeks to collect on the note, that is, independently demands payment on the underlying debt. Most recently, in *Reese v. Ellis, Painter, Ratterree & Adams, LLP*, the Eleventh Circuit reiterated the difference between a promissory note (which evidences a debt and specifies terms under which one party will pay money to another) and a security interest (not a promise to pay a debt, but an interest in collateral that a lender can take if a debtor does not fulfill a payment obligation). Thus, the FCCPA does not apply to strictly *in rem* mortgage foreclosure actions, and nothing in Section 559.715 indicates that the notice required is a condition precedent to foreclosing on a security interest.

As a practical matter, welcome letters are typically sent to mortgagors when their servicer changes and such letters will satisfy the alleged condition and avoid the argument. Where a welcome letter has not been sent or is unavailable, the best offense to a Section 559.715 defense is not to demand payment of the underlying debt in the mortgage foreclosure complaint.

THE BEST OFFENSE TO A SECTION 559.715 DEFENSE IS NOT TO DEMAND PAYMENT OF THE UNDERLYING DEBT IN THE MORTGAGE FORECLOSURE COMPLAINT.

CFPB Proposes Regulating Nonbank Auto Finance Companies

BY ELIZABETH M. BOHN

On September 16, the Consumer Financial Protection Bureau (CFPB) issued and requested comment on a proposed rule that would, for the first time, subject nonbank auto finance companies to federal regulation and oversight. The proposed rule would use the CFPB's power under Dodd-Frank to define and regulate "larger participants" that provide consumer financial products and services. In announcing the proposal, the CFPB said it sought to create the means for it to fight loan discrimination across the auto finance market after uncovering auto-lending discrimination at supervised banks.

Specifically, the rule would amend the regulation defining larger participants of certain consumer financial product and service markets by adding a section defining "larger participants" of the auto finance market. The auto finance market would include extension of credit for consumer automobile (defined as a "self-propelled vehicle primarily used for personal, family, or household purposes for on-road transportation") purchases and leases, purchases of auto loans and leases (i.e. indirect auto lenders), and auto loan refinancings.

Larger participants subject to regulation would be defined to include nonbank auto finance companies that make, acquire, or refinance 10,000 or more loans or leases annually. The CFPB estimates this represents approximately 38 auto finance companies responsible for originating 90 percent of nonbank auto loans and leases. Proposed nonbank participants would include (1) specialty finance companies, such as subprime auto lenders, (2) "captive" nonbanks (generally owned by auto manufacturers), and (3) Buy Here Pay Here finance companies. The rule would not apply to depository institutions and credit unions that engage in automobile financing and are already subject to the CFPB's supervisory authority.

Several federal consumer protection financial laws already apply to automobile financing including the Truth in Lending Act, the Fair Credit Reporting Act, the Consumer Leasing Act, the Equal Credit Opportunity Act, and the Gramm-Leach-Bliley Act. I**f adopted, the proposed rule would also subject auto finance contracts and leases to Dodd-Frank's prohibition on unfair, deceptive, or abusive acts or practices (UDAAP).** The proposal states that the CFPB would examine whether larger participants of the auto finance market engage in UDAAPs, noting that conduct that does not violate an express prohibition of another federal consumer financial law may nonetheless constitute a UDAAP.

The comments period on the proposed rule expired on December 8. The full text may be found here: http://files.consumerfinance.gov/f/201409_cfpb_proposed-rule_lp-v_auto-financing.pdf.

Reflecting the firm's commitment to creating an inclusive and diverse workplace, Carlton Fields Jorden Burt received a perfect score – 100 percent rating – on the Human Rights Campaign 2015 Corporate Equality Index for the sixth consecutive year. Carlton Fields Jorden Burt is one of 89 law firms in the country that scored 100 percent. To achieve a perfect score and the distinction of "Best Places to Work for LGBT Equality," law firms/companies must have fully-inclusive equal employment opportunity policies, provide equal employment benefits, demonstrate organizational LGBT competency, evidence their commitment to equality publicly, and exercise responsible citizenship.

Carlton Fields Jorden Burt is pleased to announce the firm has been included in the 14th Annual *BTI Client Service A-Team 2015* report, a designation limited to law firms that deliver unparalleled client service. This is the only law firm ranking that identifies top law firms for client service through a national survey of corporate counsel. The research is independent and unbiased. Only the client decides which law firms are best at driving superior client relationships. The interviews revealed that Carlton Fields Jorden Burt is in the top 20 percent for delivering better client service to the world's largest clients.

Florida Chief Justice Jorge Labarga issued an administrative order on November 24, 2014 establishing the Florida Commission on Access to Civil Justice. The 27-member commission includes two Carlton Fields Jorden Burt Tampa shareholders: **Kathleen S. McLeroy** and **Gwynne A. Young**. Other members include leaders from all three branches of Florida government, The Florida Bar, The Florida Bar Foundation, civil legal aid providers, the business community, and other stakeholders. Members of the commission will work in a coordinated effort to identify and remove economic barriers to civil justice.

The prestigious Defense Research Institute, the leading organization of defense attorneys and in-house counsel, appointed Miami shareholder **Leonor Lagomasino** to the position of Vice-Chair of DRI's Life, Health and Disability Litigation Committee. Lagomasino's appointment is for a one-year term that began at the conclusion of DRI's Annual Meeting in October.

Miami shareholder **Paul A. Calli** was appointed Chair of The Florida Bar Grievance Committee "I" for the 11th Judicial Circuit, serving Miami-Dade County. His term as Chair will expire in 2015. The Florida Bar's Grievance Committees are comprised of attorney and non-attorney volunteers who review complaints against members of The Florida Bar. They are charged with deciding whether there is probable cause to believe a lawyer has violated professional conduct rules imposed by the Florida Supreme Court and whether discipline against the lawyer is warranted.

Miami shareholer **John A. Camp** was elected to the Board of Directors of the Lawyers' Committee for Civil Rights Under Law. Members of the Board of Directors are elevated from the Board of Trustees and demonstrate a high level of commitment to the Lawyers' Committee's mission and goals. The Lawyers' Committee is a nonpartisan, nonprofit organization, formed to enlist the private bar's leadership and resources in combating racial discrimination and the resulting inequality of opportunity.

A group of four lawyers joined Carlton Fields Jorden Burt in the Hartford office. They practice in the firm's national Real Estate and Commercial Finance Practice Group in close collaboration with the firm's Insurance Industry and Practice Groups. The team includes shareholders **Frank A. Appicelli**, **R. Jeffrey Smith**, and **H. Scott Miller**, and of counsel **Kate S. D'Agostino**.

Carlton Fields Jorden Burt also welcomes the following new attorneys to the firm: of counsel **John "Jack" E. Clabby** (Business Litigation, Tampa), and associates **Stephanie E. Ambs** (Bankruptcy & Creditors' Rights, Tampa) and **James E. Parker-Flynn** (Government Law & Consulting, Tallahassee).

On the Move

Carlton Fields Jorden Burt relocated its Los Angeles office to Century Park, 2000 Avenue of the Stars, Suite 530, North Tower, Los Angeles, CA 90067.

In addition to the move, Carlton Fields Jorden Burt welcomed four new attorneys to the Los Angeles office. **Thomas H. Godwin** joined as a shareholder bringing with him **Valerie D. Escalante** and **Kate S. Shin**. Additionally, **Jee H. Lee** joined the firm from his clerkship with the United States District Court. All four attorneys practice in the Business Litigation section of the firm's National Trial Practice Group.

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