EXPECT FOCUS®

LEGAL ISSUES AND DEVELOPMENTS FROM CARLTON FIELDS JORDEN BURT

CARLTON FIELDS JORDEN BURT

VOLUME I | WINTER 2015

PROTECTING TRADEMARKS IN CUBA

How Soon Is Too Soon?

INSIDE: WHAT SUCCESSFUL WHISTLEBLOWERS HAVE IN COMMON • THE BIG DEAL ABOUT BIG DATA • HEALTH CARE AND ENCRYPTION • JURY INSTRUCTION TIPS

EXPECTFOCUS®, Volume I, Winter 2015

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Editor
Michael Kentoff

Production Editor
Lauriell Webb

Copy Editor
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Layout
Frances Liebold

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Life Insurance
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Health Care
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Securities
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Subscriptions

Changes in address or requests for subscription information should be submitted to: **Lauriell Webb, lwebb@CFJBLaw.com**.

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NEWS & NOTES

Is your Company Ready to Comply with Encryption of Individually Identifiable Health Information?

BY DIANE DUHAIME & MATTHEW KOHEN

New Jersey's new data privacy standard, signed into law as S. 562 by Gov. Chris Christie on January 9, requires health insurance carriers that are authorized to issue health benefit plans in New Jersey to protect individually identifiable health information through encryption or "by any other method or technology rendering the information unreadable, undecipherable, or otherwise unusable by an unauthorized person." In addition to all other penalties provided by law, violating the statute shall mean a fine of not more than $10,000 for the first violation, and not more than $20,000 for all subsequent violations. This law was passed in the wake of a series of data breach incidents involving stolen laptops containing the unencrypted health information of nearly one million New Jersey residents.

New Jersey's encryption requirement, which becomes effective on August 1, 2015, is more stringent than the Health Insurance Portability and Accountability Act of 1996 (HIPAA), which requires health plans, health insurance carriers, and business associates (among others) to implement administrative, physical, and technical safeguards that reasonably and appropriately protect the confidentiality, integrity, and availability of electronic protected health information, and implement encryption of such information whenever deemed appropriate. Notwithstanding, encryption of electronic protected health information is already the standard for many HIPAA covered entities and business associates. Therefore, the encryption requirements imposed by this New Jersey statute may not result in practical changes for all that many health insurance carriers issuing plans in New Jersey.

New Jersey's new encryption requirement is more stringent than HIPAA.

Of note, this New Jersey law, like many other data privacy laws with encryption provisions, does not address the fact that: (a) some entities employ encryption solutions that use simple algorithms and/or have other issues that make the data susceptible to unauthorized access; and (b) rendering the information "unreadable, undecipherable, or otherwise unusable" is an impossible goal because even the best encryption in the world can only make it extremely difficult to do these things – no one has ever made it impossible.

Privacy law practitioners now group New Jersey, Massachusetts, and Nevada together as states with information security requirements that are more rigorous than those imposed by federal or other states' laws.

STOLI Schemers Must Make Good on Damages Caused

BY ANTHONY CICCHETTI

Followers of stranger-originated life insurance (STOLI) issues have likely read over the last few years about *Ohio National Life Assurance Corp. v. Davis* and the favorable results the insurer obtained in its action against STOLI transaction participants. After a previous decision allowed Ohio National to retain premium payments it received on four of the five insurance policies at issue, the insurer more recently prevailed in large part on a motion for judgment on damages.

For schemers, deceit = damages

The court first held that the defendants who conspired to procure policies absent an insurable interest were jointly and severally liable to Ohio National for the $120,271 in commissions paid to the agent. The defendants sought to evade this liability by arguing that the insurer profited overall because it would retain aggregate premiums in excess of commissions paid. The court rejected any notion of off-set, reasoning that two distinct injuries were present, with each resulting in separate damages. The first injury – paying commissions for an insurance policy that was void *ab initio* – resulted in monetary damages in the amount of the commissions. Incurring the risk of paying death benefits constituted the insurer's second injury, for which retention of premiums was the appropriate compensation.

The court also granted Ohio National's motion to recover certain attorneys' fees and costs. Because the defendants' unlawful acts caused the insurer to become involved in litigation with third parties (the policyholders) to obtain declaratory judgments that the policies were void *ab initio*, the insurer was deemed entitled to damages for expenses incurred in that litigation, which amounted to $605,395. Ohio National, however, lost on its motion for punitive damages. Emphasizing the absence of evidence that the defendants harmed, or intended to harm, the insureds, the court concluded that the defendants' deceptive conduct was not sufficiently outrageous to support punitive damages.

At the State Level, Is a Fixed-Index Annuity a Security?

BY JASON BROST

The so-called Harkin Amendment to the Dodd-Frank Act was intended to keep fixed-index annuities outside the SEC's jurisdiction. But the issue remains unsettled on the state level. For example, an Illinois state court recently upheld a determination by that state's Securities Department that a fixed-index annuity is a security under Illinois law, again raising concerns about such products' regulatory treatment.

In April, the Illinois Securities Department found that Richard Lee Van Dyke, an insurance producer and registered investment adviser representative, advised clients to surrender existing fixed-index annuities to purchase new fixed-index annuities, transactions the Department found unsuitable and not in the clients' best interests. The Department also determined that the fixed-index annuities, while exempt from registration with the Department, were securities subject to the Illinois Securities Act.

Van Dyke challenged this order in circuit court, arguing that the fixed-index annuities were insurance contracts properly regulated by the Department of Insurance and that the Securities Department lacked jurisdiction to regulate his activities regarding those products. In December, in *Van Dyke v. White*, the court upheld all of the Department's determinations. The *Van Dyke* decision is consistent with a prior ruling, *In re Senior Financial Strategies*, wherein the court upheld a 2012 determination by the Department that a fixed-index annuity was subject to state security law. **The court did not engage in any substantive analysis of the issue in either case, so it is difficult**

to determine whether all fixed-index annuities will be treated as securities by Illinois or, if only a subset, how such a subset can be identified.

Van Dyke filed a notice of appeal, raising hopes that an appellate court will have the opportunity to clarify the law on this topic.

FSOC's Designation of Nonbank SIFIs: More New Developments

BY MICHAEL VALERIO

The end-of-year holidays failed to slow the pace of developments surrounding the Financial Stability Oversight Council's (FSOC) process for designating nonbank Systemically Important Financial Institutions (SIFIs) for Federal Reserve supervision and enhanced prudential standards.

In November 2014, the United States Government Accountability Office (GAO) issued a report regarding its audit of FSOC's SIFI decision-making process to the Ranking Member of the Senate Committee on Banking, Housing, and Urban Affairs. The report identified several key areas in which GAO concluded that FSOC could enhance the accountability and transparency of its designation process to "bolster public and market confidence in the process and also help FSOC achieve its intended goals."

Unfortunately, GAO's recommendations came too late for MetLife. On December 18, following a non-public hearing conducted in response to MetLife's administrative challenge to FSOC's preliminary SIFI determination, FSOC issued its final designation of MetLife as a nonbank SIFI. Notably, FSOC's independent voting member with insurance expertise dissented from the designation. The non-voting insurance commissioner representative on FSOC also opposed the designation.

Undeterred, on January 13, MetLife filed a first-of-its-kind court challenge to FSOC's SIFI determination in D.C. federal district court, alleging that, among the "numerous critical errors" in FSOC's rationale for the SIFI designation, **"FSOC failed to understand, or give meaningful weight to, the comprehensive state insurance regulatory regime that supervises every aspect of MetLife's U.S. insurance business, despite statutory and regulatory requirements that direct [FSOC] to consider existing regulatory scrutiny."** MetLife seeks declaratory and injunctive relief overturning the designation based on FSOC's alleged violations of the Dodd-Frank Act, the Administrative Procedure Act, and MetLife's constitutional due process rights. MetLife also asserts that FSOC's determination and certain authorizing provisions of the Dodd-Frank Act violate the constitutional separation of powers.

Meanwhile, amid pressure from certain Congressional and industry circles, FSOC announced in February that it had adopted a series of changes to its designation process, effective immediately, including notifying financial firms under SIFI consideration earlier in the process and allowing the primary regulators of subject firms to participate in the process. Stay tuned.

The Big Deal About Big Data: What Life Insurers Must Know

BY CHRISTINE STODDARD

Big data and predictive analytics, which forecast future outcomes based on past occurrences, allow companies to examine large stores of data and uncover patterns that can be used to gain a competitive advantage. Long-used in the financial services industry by banks, credit card companies, investors, and even property and casualty insurers, big data has only recently gained traction in the life and annuity industry.

While very few life insurance companies reported using big data just a few years ago, according to recent reports, 90 percent now use predictive analytics.

For life insurers, predictive analytics provide valuable insights into areas such as consumer behavior, life expectancy, and investment risks, and ultimately inform everything from marketing and product development to underwriting and claims assessment. Analytics enable insurers to more accurately acquire and retain customers, predict lapses, and root out fraud. As a result, big data's popularity in the industry has skyrocketed: while very few life insurance companies reported using big data just a few years ago, according to recent reports, 90 percent now use predictive analytics to implement streamlined processes, increase sales, reduce costs, and generally improve their businesses.

While big data can provide a competitive edge in the insurance market, it is a double-edged sword, as regulators are also increasingly using such techniques. In laying out its 2015 regulatory priorities, FINRA stated that data mining and predictive analytics are being used to identify risks posed by particular individuals and businesses, with this information then used to make faster and more targeted determinations about examinations and enforcement.

Similarly, the SEC announced that 2015 will bring augmented use of big data analytics to identify potential compliance issues and illegal activity. Like FINRA, the SEC will use analytics to examine the activities of registrants and companies and to target its examinations and investigations. Thus, life insurers must be astute as to both sides of the big data coin because big data will only continue to become a bigger deal in the industry.

Protecting the Data Lode: NAIC Addresses Cybersecurity

BY ANTHONY CICCHETTI

With cyber-attacks and data breaches making frequent headlines, the NAIC in November 2014 took steps to promote protection of insurance industry information by creating the **Cybersecurity (EX) Task Force**. The task force will report and make recommendations to the Executive Committee regarding protection of information housed in insurance departments and the NAIC, protection of consumer information collected by insurers, and cyber-liability policies issued in the marketplace. The task force will initially operate to meet the following adopted charges:

- Monitor developments in the area of cybersecurity.
- Advise, report, and make recommendations to the Executive (EX) Committee on cybersecurity issues.
- Coordinate activities with NAIC standing committees and their task forces and working groups regarding cybersecurity issues.
- Represent the NAIC and communicate with other entities/groups, including sharing information, as appropriate, on cybersecurity issues.
- Perform such other tasks as may be assigned by the Executive (EX) Committee relating to the area of cybersecurity.

First Circuit's RAA-Friendly Ruling Stands

BY MICHAEL VALERIO

The class plaintiffs' challenge to a group life insurer's use of so-called retained asset accounts (RAAs) in *Merrimon v. Unum Life Insurance Company of America* has come to an unsuccessful end.

On January 26, the United States Supreme Court denied the *Merrimon* plaintiffs' petition for a writ of certiorari seeking review of the First Circuit Court of Appeals' July 2014 decision affirming that the defendant insurer's general account funds, which backed the RAAs, were not "plan assets" and thus could not be the object of an ERISA "prohibited transaction" claim. Also left undisturbed was the First Circuit's holding that Unum did not breach any alleged fiduciary duties under ERISA by virtue of its use of RAAs as a means to disburse death benefits under employer-sponsored benefit plans funded by group life insurance policies that Unum issued to the plans. This follows last year's *Edmonson v. Lincoln National Life* decision wherein the Supreme Court denied a petition seeking review of the Third Circuit's affirmance of summary judgment in favor of another life insurer in a similar ERISA RAA class action.

RAAs operate much like interest-bearing checking accounts. Upon approval of a life insurance beneficiary's claim, the insurance company provides the beneficiary with a draft book issued by an intermediary bank from which the beneficiary can choose to write a single draft in the entire amount of the benefit, draw the account down via multiple drafts over time, or do nothing, in which case the account continues to accrue interest at a guaranteed rate. In *Merrimon*, the named plaintiff life insurance beneficiaries alleged that Unum earned more on the "retained assets" backing the RAAs than the one percent guaranteed rate Unum credited to the plaintiffs and other class members through their RAAs, and that by retaining the alleged difference, Unum violated ERISA by: (1) self-dealing in plan assets in violation of ERISA Section 406(b); and (2) violating Unum's fiduciary duty of loyalty owed to plan beneficiaries under ERISA Section 404(a).

The unanimous panel affirmed summary judgment in favor of the insurer, reversed summary judgment in favor of insureds, and vacated a $12 million judgment.

The unanimous First Circuit panel affirmed the trial court's summary judgment ruling in favor of Unum on the Section 406(b) claim, reversed the trial court's grant of summary judgment in favor of the plaintiffs on the Section 404(a) claim, and vacated a $12 million judgment in favor of the plaintiff class following a bench trial. In light of the Supreme Court's petition denial, the First Circuit's RAA-friendly rulings will stand.

Morgan Stanley Agrees to Resolution of Multi-State Unclaimed Property Audit

BY JEE LEE & STEPHANIE FICHERA

The California State Controller announced an Audit Resolution Agreement with Morgan Stanley on December 23, 2014, which sets forth the terms and conditions for finalizing and resolving an unclaimed property audit that Verus Financial LLC is conducting of the company. Thirty-four states, in addition to California, are participating in the audit.

The Agreement follows settlements between the Controller and several life insurance carriers regarding their use of the Death Master File to identify deceased insureds and escheatable life insurance benefits, and signals an expansion of state regulators' and auditors' focus beyond unclaimed life insurance benefits. Morgan Stanley reportedly approached the Controller to enter into a similar agreement.

The Agreement will require Morgan Stanley to identify and escheat to the State lost or abandoned brokerage services or customer service accounts, including employee stock plan accounts, retail brokerage accounts, and retirement accounts. The audit's scope is broad and encompasses "property maintained in, related to, or originating from all brokerage services or customer accounts at" Morgan Stanley that were reportable, or potentially reportable, as unclaimed property on or before December 31, 2014.

The Agreement expressly excludes: (i) property of owners and beneficiaries who live in non-signatory states; (ii) education and health savings-related accounts; (iii) property related to employment-based defined benefit plans; (iv) property previously escheated or that becomes escheatable on or after January 1, 2015; and (v) property that Morgan Stanley transferred to a third party prior to commencement of the audit and no longer controls.

The Agreement sets forth detailed provisions for determining when accounts become escheatable. **Non-retirement accounts generally become escheatable when dividends or distributions related to the account have been unclaimed by the account owner, mailings have been discontinued to the account owner or returned to Morgan Stanley as undeliverable, and/or there has been no owner-generated activity on the account during the dormancy period.** The dormancy period begins on the date the first unclaimed distribution was issued or on the date of receipt of the last piece of returned mail. The standards for determining whether a retirement account is escheatable vary depending on the type of account and whether the owner is deceased. Generally, property in a retirement account is escheatable if there has been no owner-generated activity regarding the account during the dormancy period, which begins on the date that distributions from the account must commence in order to avoid a tax penalty.

NCOIL Revises Unclaimed Property Model Act

BY WHITNEY FORE

The National Conference of Insurance Legislators (NCOIL) recently adopted an enhanced Model Unclaimed Life Insurance Benefits Act to address particular concerns regarding the Social Security Death Master File (the DMF). The first iteration of that Model Act was passed by NCOIL in 2011 and subsequently adopted by 15 states.

The updated model requires life insurers to search, "on at least a semi-annual basis, by using the full Death Master File once and thereafter using the Death Master File update files for future comparisons." **The previous model, by contrast, required life insurers to search the full DMF twice a year.** The revised model also includes new definitions. "Knowledge of death," for example, has been defined by the Act to mean either receipt of an original or valid copy of a certified death certificate, or a DMF match validated by the insurer.

The amendments also clarify the model's substantive provisions. The model provides that contractual interest is payable to beneficiaries or owners, or to the state in the event of escheat, but that interest payable only under the state's statutory interest law will not escheat to the state as unclaimed property. Violations of the Act constitute a violation of the state's Unfair Trade Practices Act (UTPA), though the drafters noted that "care should be taken … to ensure consistency across [the] two statutes" when the state's UTPA requires that the act be a pattern or practice prior to finding a violation. Finally, the revised model provides that the act will take effect no less than one year after the date signed into law.

Rep. George Keiser (ND), Unclaimed Property Task Force Co-Chair, stated that the "updated model evidences successful compromise between differing, often opposing, perspectives, including those of life insurers, regulators, unclaimed property officials and consumer representatives."

Jury Instructions – Avoiding Landmines and Preserving Error

BY CRISTINA ALONSO

The jury instructions and verdict form are often treated as an afterthought relegated to an associate just before trial when lead counsel is focused on opening statements and presenting evidence. Don't let this happen. The importance of having clear jury instructions, objections, and rulings thereon cannot be overstated. Jury instructions are often reviewed *de novo*, because they involve questions of law, so it is vital for counsel to preserve all potential issues related to the instructions and verdict form.

The relevant jurisdiction's standard or pattern instructions are a good place to begin when drafting jury instructions; trial courts will usually use these instructions unless it is shown that they do not accurately describe the current state of the law or are otherwise insufficient. Where standard instructions fail to adequately state the law regarding claims or defenses, or if counsel wishes to argue that a change in the law is appropriate based on some authority, special instructions should be submitted. Once a first draft of jury instructions is complete, counsel must compare them to the verdict form to ensure consistency.

It is critical to explain to the court on the record how the language of the other side's requested instructions is deficient.

At the charge conference, do not be afraid to object and where appropriate, to reject suggestions from the court that instructions have been agreed upon. A specific objection to the failure to give your requested instruction may be required to preserve an issue for appellate review. Likewise, an objection to the other party's requested instruction may not suffice—counsel may be required to request a correct instruction. At a minimum, the objections must be specific enough to raise the points counsel would want to assert on appeal. For example, when taking the position that a requested instruction does not correctly state the law, counsel must explain why. It is also critical to explain to the court *on the record* how the language of the other side's requested instruction is either legally inaccurate or not supported by the evidence.

Be sure the record reflects that the trial court ruled on all of your instructions, what all the rulings are, and any reasons given for granting or denying a requested instruction. At the conclusion of the charge conference and again before the jury deliberates, be sure to renew your objections to the instructions and verdict form as given to the extent they deviate from what you requested. Lastly, be sure that all instructions are filed and the record is complete.

Neither Side Folds on FINRA CARDS Proposal

BY WHITNEY FORE

The Comprehensive Automated Risk Data System (CARDS) proposed by the Financial Industry Regulatory Authority (FINRA) to regularly collect customer account data from various broker-dealers and clearing firms and allow FINRA to more efficiently detect dangerous product sales practices and industry trends continues to draw stiff opposition.

According to FINRA, CARDS "would … reduce present regulatory costs and burdens on firms by reducing the need for manual, partial, overlapping and one-time regulatory report generation for the information required to be reported." However, the Securities Industry and Financial Markets Association (SIFMA), the principal broker-dealer trade association, submitted a comment letter on December 1, 2014 strongly opposing FINRA's most recent iteration of its CARDS proposal. Later in the month, SIFMA also published the results of an investor survey it commissioned concerning the proposal.

A very large percentage of investors who took the survey:

- believed that CARDS's risks outweigh the benefits, even if their data is kept anonymous, because it will create a single location that hackers and cyber-terrorists can target, putting investors' account activity balances and money movements at risk; and,
- trusted their financial professionals or firms much more than the government to keep their financial information safe.

Such fears about the danger of cyber-attacks on personal data can only have been reinforced by the recent cyber-attack on Sony Pictures Entertainment. Indeed, in an interview, one SIFMA executive was quoted as follows: "[t]he Sony hacking incident gives everyone a real-life, real-time reminder of what we've been saying in our comment letters over the last year or so...If the bad guys break into FINRA, they've got everything."

At least for now, however, FINRA is keeping CARDS very much on the table.

Feds Dig for Disguised Fund Distribution Fees

BY KYLE WHITEHEAD

A nearly two-year SEC sweep examination of mutual funds' payments for distribution and other services appears to have concluded. Now, the question is what, if any, enforcement or other action the SEC will take.

Mutual funds can make expenditures that are primarily intended to promote the distribution of fund shares only pursuant to written "Rule 12b-1" plans. However, when investors purchase mutual fund shares through broker-dealers and other intermediaries that use "omnibus accounts" and provide administrative services to the funds (e.g., "sub-transfer agent services"), a question arises whether any payments the funds make to the intermediaries are for distribution services, administrative services, or partially for each.

In a 1998 letter to the Investment Company Institute, SEC staff discussed payments that mutual funds make, either directly or through their investment advisers, to "mutual fund supermarket" intermediaries. The letter warned fund boards to monitor to determine that any such payments that a fund considers to be for non-distribution services (and thus are not paid pursuant to a Rule 12b-1 plan) are reasonable in relation to the value of those services to the fund and its shareholders.

More recently, under the heading "Payments for Distribution in Guise," the SEC's published 2013 and 2014 examination priorities focused on "the wide variety of payments" made to intermediaries. The SEC also recently expressed concern that the 1998 letter's guidance is not being followed.

Accordingly, mutual funds would be well advised to consider whether all of their payments to intermediaries, and related disclosures are consistent with Rule 12b-1 and applicable guidance.

SEC 2015 Budget Impacts Investment Management Industry

BY SCOTT SHINE

This past December, President Obama signed an appropriations bill that provides an $11.8 million budget increase for the SEC's Division of Economic and Risk Analysis (DERA) intended to bolster the agency's cost-benefit analysis used in rulemaking. This action comes after multiple SEC rules have been stricken by the D.C. Circuit for failure to adequately consider their effect on efficiency, competition, and capital formation, as required by law. DERA's budget increase will likely enhance its role in many upcoming regulatory initiatives, including those mentioned mentioned in "FSOC Presses SEC on Money Managers' Systemic Risks" on page 14.

Nevertheless, the SEC's overall 2015 fiscal year budget increase fell about $200 million short of the President's request. Rick A. Fleming, the SEC's "Investor Advocate," is among the dissatisfied, having recommended, in reports to Congress, that sufficient resources be provided to enable the SEC to conduct an adequate number of investment adviser examinations. In 2014 the SEC examined only 10 percent of advisers.

Although the SEC's 2015 appropriation does not provide the funds he recommended, Mr. Fleming's most recent report states that his office will seek to identify potential efficiencies or other funding mechanisms to help enhance the SEC's oversight of investment advisers. However, in recent years the SEC has already exploited many of the most obvious potential efficiencies, and agreement on other funding mechanisms (including charging advisers "user fees" or requiring them to pay third parties to conduct examinations) has so far proved elusive.

Accordingly, although this year the SEC is expected to add personnel who will be available to examine investment advisers, it has indicated that, absent further budget increases, the percentage of advisers examined each year is likely to remain around 10 percent.

The SEC has already exploited many of the most obvious potential efficiencies, and agreement on other funding mechanisms has so far proved elusive.

What Successful Whistleblowers Have in Common

BY ED ZAHAREWICZ

As required by the Dodd-Frank Act, the SEC makes monetary awards to eligible individuals who voluntarily provide original information that leads to successful SEC enforcement actions resulting in monetary sanctions over $1 million, and successful related actions. In its 2014 Annual Report to Congress on the Dodd-Frank Whistleblower Program, the SEC recently shed some light on the nature of successful whistleblowers.

One striking takeaway from the report is that **only a very small percentage of whistleblowers ever receive a monetary award**. Since the program's inception in August 2011, the SEC has received 10,193 whistleblower tips, including 3,620 tips during the SEC's 2014 fiscal year. While the number of tips has increased each year, there have been only 14 whistleblower awards, involving 10 or fewer SEC enforcement matters. Nine of the awards came in the 2014 fiscal year.

According to the report, the whistleblowers who received awards:

- identified *specific* individuals involved in *specific* transactions evidencing, or *specific* documents (or the *specific* locations of documents) substantiating, the whistleblower's fraud allegations;
- alleged misconduct that was relatively current or ongoing; and
- provided additional information or assistance to the SEC staff during the course of its investigation.

More than 40 percent of the individuals who received awards were current or former company employees. Of these, more than 80 percent raised their concerns internally before reporting to the SEC. Twenty percent of the award recipients were contractors, consultants (or solicited to act as consultants) for the company committing the fraud. The remaining award recipients obtained their information "because they were investors who had been victims of the fraud, or were professionals working in the same or similar industry, or had a personal relationship with one of the defendants."

More Insider Trading Clarity for Money Managers

BY JOHN CLABBY

It is plainly illegal to bribe a corporate insider for non-public information and then trade that company's stock. But what if the briber shares that information with a money manager, who then trades on that inside information, knowing that it is non-public but ignorant of the bribe?

According to the U.S. Attorney for the Southern District of New York, as recently argued in *United States v.*

Newman, this would, indeed, constitute a crime. The Second Circuit disagreed, however, and overturned the convictions of two former hedge fund managers charged with making $72 million off trades in the stocks of technology companies Dell and NVIDIA.

At trial, the government accused Todd Newman and Anthony Chiasson of trading on tips received from their employees, members of a "cohort of analysts" who shared with each other non-public information obtained from corporate insiders. The trial judge rejected a defense jury instruction that would have required the government to prove that Newman and Chiasson knew that the Dell and NVIDIA insiders received a personal benefit in exchange for the disclosure.

The appellate court reversed, holding that **"to sustain a conviction for insider trading, the Government must prove beyond a reasonable doubt that the tippee knew that an insider disclosed confidential information *and* that he did so in exchange for a personal benefit."** For added measure, the court found insufficient evidence that the corporate insiders even received a "personal benefit" in exchange for the information.

The government has requested a rehearing and a rehearing *en banc.* For now, however, this decision can provide some comfort—at least in the Second Circuit—to money managers who do not know the circumstances under which information about an issuer was divulged or, perhaps, even whether the information must be regarded as nonpublic.

Defendants Challenge SEC's Increased Use of Administrative Forum

BY NATALIE A. NAPIERALA

The Dodd-Frank Act expanded the SEC's jurisdiction to compel administrative hearings and to seek sanctions and remedies similar to those in federal court. The Commission's recent policy of commencing more enforcement proceedings before its own "home court"—rather than in federal courts—has provoked concern and criticism.

Defendants have alleged that proceedings in the SEC's administrative forum deprive them of their constitutional right to due process, e.g., that they are unable to adequately prepare and conduct their defense, because:

- hearing schedules typically are expedited;
- defendants generally cannot compel testimony at depositions or hearings;
- other discovery is more restricted; and
- the application of the federal rules of evidence and civil procedure is limited.

Other constitutional arguments include a violation of defendants' Seventh Amendment right to a jury trial or of Article II restrictions on executive power.

In recently denying the SEC's motion to dismiss a defendant's claim that the SEC's decision to sue him (but not multiple other defendants) in an administrative forum violated the equal protection clause, U.S. District Judge Jed Rakoff is among those who have expressed constitutional concerns.

Is the SEC taking unfair "home court" advantage?

While the SEC insists that it is motivated by the administrative forum's greater efficiency and streamlined process, the Commission's success rate before an administrative law judge (ALJ) is demonstrably greater than that before federal courts or juries. The SEC contends, however, that administrative proceedings—held before expert and experienced ALJs—are fair, constitutional, and subject to two levels of appeal.

The few federal courts addressing defendants' challenges have generally dismissed such suits for, among other reasons, lack of subject matter jurisdiction. Continued constitutional challenges can be expected and, at some point, a ruling by a federal appeals court.

FSOC Presses SEC on Money Managers' Systemic Risks

BY TOM LAUERMAN

The SEC is stepping lively to preserve a role in formulating any additional requirements for money managers—such as mutual funds and investment advisers—to limit perceived risks to the financial system.

Although the Dodd-Frank Act gives the FSOC authority to impose such requirements, money managers have strenuously argued that they do not present such "systemic" risks, and many in Congress agree. (*See* "Mutual Funds Get Congressional Help Against FSOC" in the Spring 2014 edition of *Expect Focus*.) Nevertheless, SEC Chair Mary Jo White, who is an *ex officio* member of the FSOC, gave a speech on December 11 detailing major SEC initiatives that would help reduce any systemic risks that money managers present. These include:

- Enhancing controls on risks resulting from the composition of investment portfolios. For example, SEC officials have indicated that a group of 10 SEC staffers are hard at work on a white paper that addresses the risks presented by exchange-traded funds (ETFs)—particularly those that make extensive use of derivatives—including the risk of increased financial volatility.
- Enhancing data reporting, which would improve regulators' ability to evaluate any systemic risks.
- Improving transition planning and stress testing.

Nevertheless, **just one week after Chair White's speech, the FSOC voted unanimously to request input from the public on many of the same types of issues pertaining to money managers as are included within the SEC's initiatives**. Chair White observed that the FSOC's effort is a "constructive complement" that may produce information useful to the SEC's work. Similarly, the FSOC stated that it intends to consider the impact of the SEC's initiatives in reducing any risks to U.S. financial stability.

Although the SEC and FSOC therefore appear to be embracing, it may feel to the SEC more like a bear hug.

Court Rejects Attenuated Argument of Automobile Insurer Liability

BY ZACHARY D. LUDENS

Just how attenuated is *too* attenuated for a driver's conduct outside the vehicle to be covered by the auto policy covering the vehicle? In *Hough v. McKiernan*, the Supreme Court of Rhode Island drew the line at about two-to-three car lengths from the vehicle, holding that the driver's conduct, after exiting the vehicle and knocking a pedestrian to the ground, was not sufficiently connected with his use of the vehicle to trigger coverage.

On the evening of February 22, 2006, a group of friends gathered for a party at one of their homes. One friend asked another to borrow his pickup truck. The owner declined, but the friend still "borrowed" the truck anyway. When the owner of the pickup truck found out, he borrowed another friend's car to search for his own pickup. This car was owned by the friend's grandmother and insured by the same.

As the pickup owner searched for his own pickup—with three of his friends in the vehicle—the car passed by two young men on foot. At this point, the pickup owner rolled down the car window and yelled what he considered to be "funny jokes" about the young men's mothers. The pickup owner further circled around the young men a few times, flashing his high beams at them.

When the pickup owner and friends later located his pickup, he parked approximately two-to-three car lengths in front of it. Coincidentally, at that time, the two pedestrians who had earlier been harassed approached the pickup and conversed with the friend that had borrowed it. One of them flicked a cigarette, which struck the pickup owner. Incensed, the pickup owner got out of the car, pursued the young man, and punched him in the chest. The young man collapsed to the pavement, and the assailant and his friends left the scene in the insured vehicle, without checking to see if he needed medical attention. As a result of hitting his head on the pavement, the young man sustained a subdural hematoma and required multiple surgeries and months of treatment.

The injured pedestrian sued, and coverage was sought under the auto policy covering the vehicle, under the theory that the car enabled the incident to happen, as it provided transport to the scene of the incident, "facilitated a series of drive-bys that would have been very unlikely had the [pickup owner] been on foot," and enabled the pickup owner to "have passengers with him who were 'egging him on.'" The Supreme Court of Rhode Island, however, found that this theory was a bridge too far, and held that this was not an accident arising from use of the vehicle.

The court found plaintiff's theory of liability was a bridge too far.

Florida Supreme Court Thwarts Attempt to Circumvent "Exclusive Remedy" Provision

BY JOHN HERRINGTON

Most states limit a worker's remedies for work-related injuries to a workers' compensation claim against the employer. Such "exclusive remedy" provisions codify a longstanding compromise whereby employers trade liability, regardless of fault, for protection from large tort awards, and employees surrender a cause of action in return for swift but limited financial benefits.

Plaintiffs' attorneys and like-minded reformers seeking to challenge exclusive remedy provisions have made some progress in recent years. For instance, in August 2014, a judge in Miami-Dade County, Florida ruled that Florida's workers' compensation statutes were "unconstitutional" on their face because they no longer provided adequate benefits to injured workers in exchange for them giving up their constitutional rights to pursue civil litigation. In *Padgett v. State of Florida*, which is currently on appeal, the trial judge declared that statutory changes in Florida had eroded benefits for injured workers to the point that it was no longer a "grand bargain" for the injured workers.

In *Morales v. Zenith Ins. Co.*, however, the Florida Supreme Court recently rejected an attempt to evade the exclusive remedy provisions of Florida's workers' compensation law, holding that the challenged provisions barred the estate of a worker killed on the job from collecting a $9.5 million wrongful death judgment against the deceased worker's former boss and insurer.

Santana Morales was crushed to death by a palm tree while working as a landscaper for Lawns Nursery and Irrigation Designs, Inc. The employer maintained a "Workers' Compensation and Employers Liability Insurance Policy" with Zenith Insurance Co., which provided two types of coverage: (1) workers' compensation insurance under Part I and (2) employer liability insurance under Part II.

Soon after Morales's death, his surviving spouse entered into a workers' compensation settlement agreement with Zenith. As required by Florida's workers compensation laws, this settlement agreement included a release that barred the estate from pursuing any other tort claims against either the employer or the employer's insurer.

Nonetheless, the Morales estate had also filed a separate wrongful death action against Lawns Nursery and eventually obtained a $9.25 million judgment. When Zenith refused to pay the default judgment, the estate sued Zenith for a breach of the employer's employment liability policy. The district court ultimately dismissed the wrongful death suit, ruling that the workers' compensation exclusion barred the estate from filing a civil negligence action.

On appeal, the estate argued that the exclusive remedy did not apply to its wrongful death suit because the estate had already received a default judgment, and the second civil case was brought not under the original theory of negligence, but rather to enforce the default judgment. The Eleventh Circuit Court of Appeals, certified the issue to the Florida Supreme Court, which concluded that, **since both the exclusive remedy and the settlement release should have precluded the estate from filing a civil negligence action in the first place, it was not entitled to collect the judgment.**

In so holding, the court reinforced the longstanding concept that workers' compensation benefits are the "exclusive remedy" for work-related injuries in Florida.

Policy Language Aside, Insurer is Obligated to Pay in California

BY K. RENEE SCHIMKAT

A California appellate court found that an insurer's delay in resolving and denying a claim under a commercial property liability insurance policy excused the property owner from satisfying a condition precedent to coverage, namely, repairing the damage at issue in order to recover the replacement cost for the loss. The court also approved of a lost business income award to the insured, despite the insured's failure to conduct any business at the property as the policy required.

WORK INJURY CLAIM FORM

In *Stephens & Stephens XII v. Fireman's Fund Insurance Co.*, a commercial warehouse was burglarized over a period of time, though coverage was added by Fireman's Fund only days before the theft was discovered. The insured notified Fireman's Fund of the theft, but Fireman's Fund neither accepted nor denied coverage for the loss, concerned the damage was too extensive to have occurred in the brief period of the policy's coverage. Fireman's Fund eventually denied coverage, but not until nearly five years after the incident and barely a month before trial. The jury awarded the insured more than $2 million for the replacement cost of the damage to the property, though the insured had never repaired the property, and an additional $2 million in lost business income. The trial court granted the insurer JNOV, finding the insured was required to (a) complete the repairs before it could receive their replacement cost, and (b) conduct business at the property before it could receive a lost business income award.

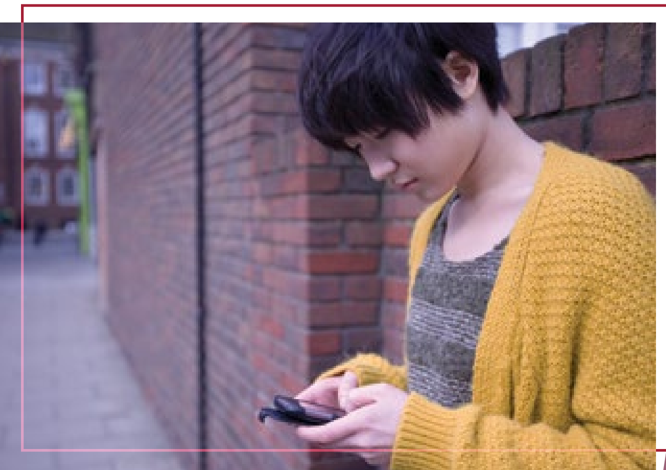
The insurer's delay in resolving or denying the claim "materially hinder[ed]" the insured's ability to repair the property

The appellate court disagreed, holding the insured's failure to complete the repairs did not preclude it from obtaining reimbursement for that cost once the condition precedent was satisfied. Though the insured was not entitled to an immediate award for the costs of repairing the damage, it was entitled to "a conditional judgment awarding these costs if the repairs are actually made." The insurer's delay in resolving or denying the claim "materially hinder[ed]" the insured's ability to repair the property and, therefore, such "procedural obstacles to obtaining the replacement cost value should be excused." The appellate court also approved of the jury's award for lost business income, reasoning the award could be properly construed as an award for lost rent under the policy.

Florida Court of Appeal: Photos on Facebook are Fair Game in Discovery

BY JONATHAN C. STERLING

Discovery of social media is often appropriately considered in any case where evidence or admissions tending to disprove the other party's case is potentially available. Although social media has long been firmly rooted in our daily lives, no single rule has developed regarding discoverability of social media postings in litigation. Many courts, in fact, craft discovery orders tailored to the facts of the case and nature of the claims, but remain reluctant to order blanket disclosure of social media accounts.



In January 2015, however, Florida's 4th District Court of Appeal did exactly that. In *Nucci v. Target Corp., et al*, the plaintiff sued Target, claiming that she slipped and fell on the floor of one of their stores. Target obtained what it alleged were post-accident surveillance videos showing plaintiff carrying heavy items and performing other physical acts, and moved to compel disclosure of any photographs of plaintiff posted on her Facebook profile beginning two years before the date of the accident. The plaintiff responded that, because her Facebook page had, since its creation, been on a privacy setting blocking access to the general public, she maintained a reasonable expectation of privacy in the photos. She also argued that the request was overbroad and would violate the federal Stored Communications Act (SCA).

The trial court granted Target's motion and plaintiff appealled. Affirming the trial court, the appellate court found that the photos were "powerfully relevant to the damage issues in the lawsuit," particularly in concert with the post-accident surveillance footage. The appellate court further noted that because of the requested discovery's electronic format, production would not be onerous. Plaintiff's privacy interest in the photos was, said the court, "minimal," because the very nature of social media is to share information that can be freely accessed and shared by others. Finally, the appellate court rejected the plaintiff's SCA argument because the statute prevents only providers, not end-users, of communications from divulging private communications.

Use of Prior Servicer's Records at Trial Depends on Proper Foundation

BY ALANA ZORRILLA-GASTON & MERRICK L. "RICK" GROSS

Mortgage servicing duties are routinely transferred, requiring lenders, servicers and financial institutions to rely on the prior servicer's business records to prove their cases against borrowers – specifically, to prove the amount of the debt due at trial, since the assignee's records necessarily include and are based on the predecessor's records. Such records may also be used to demonstrate possession of the original note prior to the filing of the complaint, and other essential elements of a foreclosure case that go to standing.

Several recent Florida appellate court decisions, however, have given borrowers some ammunition to counter reliance on prior servicer's records. For example, in both *Hunter v. Aurora Loan Services, LLC* and *Yang v. Sebastian Lakes Condo. Ass'n, Inc.*, the court found the prior servicer's records should have been excluded because the witness lacked sufficient personal knowledge to rely on a prior servicer's records.

Nonetheless, reliance on a prior servicers' business records is still permissible with the proper foundation. For example, the court in *Bank of New York, as Trustee v. Calloway*, found the lender's witness sufficiently confirmed the trustworthiness of the third-party business records at issue by testifying that the prior servicer's records had been reviewed for accuracy prior to integrating them into the plaintiff's own records. The court further held that the circumstances of the loan transfer itself could have been sufficient to establish trustworthiness given the business relationships and common practices inherent among lending institutions acquiring and selling loans.

The pivotal difference in the cases: the foundation laid by the lender or loan servicer's trial witness. Therefore, preparation of the trial witness to lay the appropriate foundation for reliance on a prior servicer's business records is key. With sufficient training regarding the policies and procedures in place to ensure the accuracy of records transferred from a prior servicer, a trial witness should be able to lay the proper foundation to allow the witness to rely on a prior servicer's records.

New CFPB Consent Orders Point to Growing Indirect Regulation of Title Insurance

BY KELLY CRUZ-BROWN & ROBERT SCHMIDLIN

The Dodd-Frank Act of 2010 granted rule-making authority under the Real Estate Settlement Procedures Act (RESPA) to the CFPB and, with respect to entities under its jurisdiction, generally granted authority to the CFPB to supervise and enforce compliance with RESPA and its implementing regulations. CFPB supervisory jurisdiction includes residential mortgage originators, brokers, and servicers and other large participants in the consumer financial services market, however; CFPB does not have authority over insurers,

including title insurers. However, as we reported in the last issue, new regulations promulgated by the CFPB have been resulting in the indirect regulation of title insurance.

In addition to those regulations, recent and aggressive RESPA enforcement actions by CFPB against title insurance agents and settlement service providers are giving rise to concerns that the CFPB is extending its authority to areas not contemplated under Dodd-Frank. **Such actions could impact how title insurers operate in the marketplace and potentially allow CFPB to supplant a space in which state insurance regulators have traditionally maintained authority.**

The CFPB has made its mark on RESPA enforcement against the title industry in three actions directly against title insurance agents in 2014, in which Realty South and its TitleSouth, LLC affiliate, Stonebridge Title Services, Inc. and Lighthouse Title, Inc., entering into consent orders and levying fines in connection with alleged RESPA violations for affiliated business arrangement disclosures, payment of referral fees and marketing service agreements, respectively. The Consent orders announced by the CFPB in January 2015, highlight the role Genuine Title LLC was alleged to play in violations of RESPA related to marketing services and commission payments. While there has been considerable analysis and debate of CFPB's interpretation of RESPA as applied to the 2014 actions, there is no question as to CFPB's intent to establish itself in the enforcement arena.

While no title insurers were cited by CFPB in these actions, **CFPB's willingness to use RESPA as a tool to extend its authority over title insurance agencies has implications for title insurers, especially with respect to agency, audit, and compliance programs**. Title insurers who own title agencies, are engaged in joint ventures, or are service providers to mortgage originators are at the greatest risk of impact by CFPB's maturing view of its jurisdiction. They should take note of the agency's recent enforcement actions and work to align their controls and business practices in anticipation of further activity by the CFPB.

CFPB to Regulate Prepaid Debit Cards

BY ELLEN LYONS

The CFPB plans to amend Regulation E (implementing the Electronic Funds Transfer Act) and Regulation Z (implementing TILA) to cover prepaid financial products including prepaid debit cards issued by a financial institution that may be used at unaffiliated merchants. These products are called prepaid "cards," but can also refer to an app or key fob that allows access to prepaid funds. Currently prepaid products are not subject to cost disclosure, period statements, or loss/theft limitations; though some financial institutions do provide these services.

The Federal Reserve, as the predecessor to CFPB, declined to regulate prepaid products in 2006 because the market for prepaid products was small. Since then, however, consumers have embraced prepaid products—with some using prepaid debit cards to replace bank accounts. Now, CFPB plans to extend regulations that already govern credit cards to prepaid debit cards.

The proposed amendments will require the issuers of prepaid debit cards to:

- provide cost disclosures prior to the time the cards are loaded with funds;
- provide either periodic statements or website access to account balances and transactions;
- timely investigate and resolve complaints about incorrect charges; and
- limit consumer losses when their cards are lost or stolen.

To encourage comparison shopping, issuers will also be required to post their card agreements on their websites.

Many prepaid debit cards now have credit card features, such as the ability to generate an overdraft. If a prepaid debit card has credit card features, the proposed regulations will require the issuers to consider a consumer's ability to repay an overdraft prior to issuing a card, provide monthly billing statements, give a 21-day grace period for payment, charge "reasonable and proportionate" late fees; and limit fees and interest charges to 25 percent of the credit limit.

Under the proposed regulations, CFPB would require an issuer to wait 30 days from the registration of a prepaid debit product to offer credit features on the card. The issuer could not apply reloaded funds to pay the credit portion of the account without customer consent, and the issuer couldn't take funds from the prepaid account more than once monthly or less than 21 days after mailing the periodic statement. If not extended, the comment period for these proposed regulations, ends on March 23, 2015.

Stripping of Unsecured Second Mortgages in Chapter 7 Bankruptcies in the Crosshairs

BY CHRISTOPHER PAOLINI & MICHAEL WINSTON

Since its 1989 opinion in *Folendore v. Small Business Admin.*, the Eleventh Circuit Court of Appeals has allowed debtors to completely strip off and void wholly unsecured junior liens in Chapter 7 bankruptcies under Section 506(d) of the Bankruptcy Code. Complete lien stripping forever prevents creditors from seeking relief against a debtor's collateral if it is underwater, even if the property value later increases. Since Chapter 7 debtors are also discharged of personal liability, subordinate debt is, in such cases, rendered worthless.

That may soon change.

The Eleventh Circuit's position on lien stripping conflicts with that of the Fourth, Sixth, and Seventh Circuits – the only federal Courts of Appeal to have addressed the issue. Now the Supreme Court appears ready to resolve the conflict, accepting *certiorari* review of two Eleventh Circuit cases dealing with the issue.

Most commentators expect the Supreme Court to side with the Fourth, Sixth, and Seventh Circuits and hold unsecured junior liens may not be stripped in Chapter 7 cases; it has, after all, already held, post-*Folendore*, that debtors may not partially strip down undersecured subordinate liens, reasoning that if a claim "is secured by a lien with recourse to the underlying collateral, [it cannot be stripped under] § 506(d)… [because] the creditor's lien stays with the real property until foreclosure [as this] is what was bargained for by the mortgagor and the mortgagee."

Even the Eleventh Circuit has signaled it may reconsider the issue. In a recent opinion affirming the stripping of an unsecured second mortgage, the panel acknowledged that the Supreme Court has "rejected the reasoning of [its prior holding in] *Folendore*" but noted the court was bound by the prior panel precedent rule until reversed on appeal *en banc* or by the Supreme Court. The court then invited the creditor to seek *en banc* review of its own decision.

In response, debtors in the Eleventh Circuit have expedited their efforts to strip off underwater subordinate debt before the Supreme Court addresses the issue. Some debtors are even attempting to reopen long dormant cases to seek such relief. In such instances, home equity lenders and other debt holders, who have historically abandoned subordinate claims given the grim prospects of recovery, should reevaluate their position. Loans once considered worthless may be given new life by the Supreme Court in the coming months. Until a final ruling on the issue is reached, creditors should seek to stay enforcement of orders allowing subordinate liens to be stripped in Chapter 7 cases.

Eleventh Circuit Says No to Mooting Class Actions with Individual Offers of Judgment

BY ELIZABETH BOHN & AARON WEISS

Serving a Rule 68 offer of judgment for maximum individual statutory damages before the filing of a class certification motion was once a common strategy used to moot putative class actions alleging claims for violations of the Telephone Consumer Protection Act (TCPA), and Fair Debt Collection Practices Act (FDCPA) which had been approved by several Florida district courts.

For example, in *Keim v. MidAtlantic, LLC*, and *Stein v. Buccaneers, Ltd. Partnership*, putative class actions alleging TCPA violations in the form of unsolicited commercial text messages and faxed advertisements respectively, Florida district courts in the Southern and Middle Districts granted the defendants' motions to dismiss the plaintiffs' claims as moot based on offers of maximum statutory damages to the representative plaintiffs. The practice also appeared to be permitted in the Eleventh Circuit Court of Appeals, based on its 2012 decision in *Zinni v. ER Solutions*. In *Zinni*, an FDCPA case, the Eleventh Circuit reversed a dismissal based on mootness after maximum relief was offered based on the fact that the defendant failed to serve a formal Rule 68 offer of judgment. This had been interpreted by lower courts as indicating that claims could be mooted by service of a formal offer of judgment.

However, in December, the Eleventh Circuit reversed both the *Stein* and *Keim* decisions, joining the Third, Fifth, Ninth, and Tenth Circuits to hold that a Rule 68 offer of judgment may not be used to moot a potential class action in the Eleventh Circuit. Specifically, the court held that a plaintiff's individual claim is not subject to dismissal based on mootness as a result of service of a Rule 68 offer of judgment that is not accepted, and, that an offer that does moot a named plaintiff's individual claim does not moot a class action, even if the offer comes before the plaintiff has moved to certify a class.

The reversal of *Stein* and *Keim* has far-reaching strategy implications for class actions based on violations of the TCPA, FDCPA, and other consumer statutes with maximum statutory damages, as it prevents forcibly "picking off" an individual plaintiff by seeking dismissal based on mootness after service of an offer of judgment for maximum statutory damages. While it will still be possible to settle with an individual plaintiff before a motion for class cert is filed, the decision will likely result in increased defense and settlement costs.

New Regulations Likely to Yield New Theories

BY TENIKKA L. JONES & ZACHARY D. LUDENS

The plaintiffs' bar, drawing inspiration from the Consumer Financial Protection Bureau (CFPB) regulations that took effect in early 2014, have begun to pursue new theories of liability under old causes of action. The new theories illustrate real conflicts between the new regulations and existing consumer protection laws, such as the Fair Credit Reporting Act (FCRA) and the Fair Debt Collection Practices Act (FDCPA). Covered entities subject to CFPB regulation thus face a Hobson's choice: Follow the new regulations and risk violating other existing laws, or face enforcement actions for failing to follow the new CFPB regulations.

For example, CFPB Amendments to the RESPA Regulation X contain detailed new requirements for acknowledging and responding to notices from home mortgage borrowers alleging errors related to their mortgage loan. However, these provisions conflict with existing FCRA provisions for consumer debt dispute resolution. And while amendments to TILA Regulation Z require mortgage servicers to send regular periodic statements, the FDCPA prohibits "debt collectors" from contacting a "debtor" regarding a "debt" if they know the debtor is represented by counsel, or if they have received a "cease communication" request from the debtor regarding the debt.

Once the conflict with the FDCPA became apparent in October 2013, the CFPB issued guidance that a servicer that is considered a "debt collector" does not violate the statute by sending the periodic statement notwithstanding that a "cease communication" request has been received. **This, however, did not resolve conflicts with state debt collection statutes, such as the Florida Consumer Collection Practices Act, that are broader and may be more protective than the FDCPA.**

Additionally, claims now being brought under the revised RESPA Regulation X based on alleged inaccurate reporting of information concerning a home mortgage borrower's loan account to consumer reporting agencies, appear to infringe on FCRA authority, and have created uncertainty regarding whether FCRA regulations control. Given the complex regulatory and litigation landscape, some confusion was inevitable as was a series of splintered and conflicting lower court decisions. Clarity is unlikely until appellate courts start deciding the issues.

King v. Burwell: Setting the Tone for Health Care Politics

BY T.J. FERRANTE

In 2015, the Affordable Care Act (ACA) will face new challenges in a Republican-controlled Congress, and continued challenges in the courts. The Supreme Court recently granted a writ of certiorari to review a Fourth Circuit Court of Appeals decision upholding a regulation by the Internal Revenue Service, permitting the government to subsidize health insurance on either a federal or state created exchange. A Court decision to restrict the subsidies to state exchanges could make health insurance unaffordable for millions of Americans, threatening the viability of the law's entire health insurance program. Oral arguments were held on March 4.

Background

The ACA expands coverage to the uninsured using two mechanisms: expansion of Medicaid and creation of regulated insurance exchanges, where the government would subsidize premiums for lower income individuals.

Several lawsuits in multiple jurisdictions have addressed a May 2012 IRS rule, which provides that health insurance premium tax credits are available to certain Americans if they obtain coverage through a federal or state exchange. The plain language of ACA Section 1401 provides health insurance "tax credits" to certain taxpayers who enroll in a qualified health plan "through an Exchange established by the State." Challengers to the IRS rule contend that this wording prohibits the federal government from providing financial assistance to individuals if their state does not run its own exchange, instead relying on the federal exchange. The government points to other ACA provisions that show broader legislative intent, supporting its contention that tax credits are meant for all qualified taxpayers nationwide.

Two major cases frame the debate. In *Halbig v. Burwell*, a three-member panel of the Court of Appeals for the District of Columbia issued a decision supporting the plaintiff's assertion that the subsidy is only for individuals who purchased insurance through a state exchange. In *King v. Burwell*, however, the Fourth Circuit upheld the IRS regulation granting subsidies for all qualified individuals regardless of whether they purchased insurance on a state or federal exchange, as a "permissible exercise of the agency's discretion."

Implications of a Supreme Court Ruling

If the Supreme Court sides with the Administration, the status quo would be preserved, with ACA subsidies continuing. However, if the Supreme Court rules in favor of the challengers, the subsidy program would be restricted to individuals who purchase insurance through a state operated exchange. Either choice carries far-reaching ramifications.

First, **a decision against the government might nullify the employer mandate in states that use the federal exchange**. There are two major penalties under the employer mandate. The first is assessed against employers that do not offer coverage. However, this penalty only applies if at least one of the affected employees receives a subsidy from a public exchange. If, as a result of a Supreme Court ruling, there are no subsidies, then there would be no employer penalties. The other major penalty applies when an employer offers coverage that is unaffordable for some employees. Any employee who only has access to unaffordable employer-offered coverage is eligible for subsidies in a public exchange—and if the employee gets a subsidy, the employer owes a penalty. Again, with no possibility of subsidies, there is no employer penalty for providing unaffordable coverage.

Second, **a victory for the challengers also would deny federal tax subsidies to individuals in the 34 affected states**. Without subsidies, many individuals would be unable to afford to purchase health insurance policies. Without affordable coverage, many individuals would be exempted from the ACA's individual mandate.

Enrollees who are unable or unwilling to pay the full cost of their insurance premiums would have their coverage terminated. Those who retain insurance are likely to be sicker than those who drop coverage. This may result in skewed risk pools, exposing insurers to large, unanticipated losses.

With a decision expected in mid-2015, *King v. Burwell* could redefine the ACA and health care politics in 2015 and beyond.

State Law Claims Based on HIPAA Guideline Violations are Not Preempted by HIPAA

BY GAVRILA A. BROTZ

Though the Health Insurance Portability and Accountability Act of 1996 (HIPAA) precludes a private right of action in the event of a breach of confidentiality, recent decisions have found that claims based on such breaches under state laws are not preempted by HIPAA, even where failure to comply with HIPAA guidelines is a basis for such claims. In *Byrne v. Avery Center*, the Connecticut Supreme Court recently cited a growing body of case law in holding that common law claims for negligence were not preempted by HIPAA, even where violations of HIPAA's protections were alleged in support of those claims. In 2012's *R.K. v. St. Mary's Medical Center*, The Supreme Court of Appeals of West Virginia noted "the absence of a plethora of precedent on the issue of HIPAA preemption of state-law claims" before arriving at a similar result. The confidential nature of the protected health information disclosed in both *Byrne* and *R.K.* was dramatic. The information disclosed related to the patients' estranged partners, causing emotional distress through the disclosure of, respectively, a pregnancy and psychiatric records. Following the disclosures, the patients sued the health care facilities for negligence and infliction of emotional distress. In each case, the defendant facilities argued that disclosure of protected health information was governed by HIPAA, which provides no private right of action, and which "supersede[s] any contrary provision of State law."

However, both courts held that state law claims allowing for a private right of action are not "contrary" to HIPAA because it is possible to comply with both HIPAA and state law private rights of action for disclosures of confidential information. Neither does the allowance of a private cause of action create an "obstacle" to HIPAA's goals of establishing disincentives to wrongfully disclose a patient's health care record. As the *Byrne* court noted, state causes of action are not ordinarily preempted solely because they impose liability over and above that authorized by federal law. Though HIPAA provides criminal penalties for such disclosures, these decisions found that this remedy does not occupy the same field of relief of those provided by private causes of action.

While recognizing that a plaintiff cannot assert an express cause of action for a HIPAA violation, the Connecticut and West Virginia Supreme Courts held that **violations of HIPAA can be used as evidence of the appropriate standard of care that was not met to support negligence claims.** Reversing a trial court decision, the Connecticut Supreme Court in Byrne determined that "a complaint alleging a violation of a federal statute as an element of a state cause of action, when Congress has determined that there should be no private, federal cause of action for the violation," is not necessarily preempted by that federal statute. Rather, the Byrne court relied on the increasing number of federal and sister state court decisions holding that a HIPAA violation may be used either as the basis for a claim or as the standard of care to support other tort claims.

Meet the ACA's Employer Mandate

BY RYAN WIERENGA & JON GATTO

After several delays, the Affordable Care Act's "employer mandate" has begun to take effect. Under the mandate, employers with more than 50 fulltime employees (Large Employers) must offer affordable, minimum essential coverage (Coverage) to all fulltime employees. Such Coverage must cost less than 9.5 percent of annual household income and must pay for at least 60 percent of covered services. Large Employers also must comply with new Internal Revenue Service reporting requirements for the 2015 tax year.

The mandate became effective for Large Employers with 100 or more fulltime employees on January 1, 2015, and will do so for other Large Employers beginning January 1, 2016.

If a Large Employer with more than 100 fulltime employees does not offer Coverage to at least 70 percent of its fulltime employees in 2015, and any of its fulltime employees receives subsidized coverage through a health insurance exchange, then the Large Employer will owe a penalty of $2,000 per year for each fulltime employee after the first 80 fulltime employees. **In 2016, the percentage of fulltime employees who must receive Coverage will increase to 95 percent, and the penalty will apply to each fulltime employee after the first 30 fulltime employees.**

A recent bill passed by the House of Representatives may complicate the mandate's implementation. That bill, which President Obama has threatened to veto, would raise the requisite number of hours per week for an employee to be considered fulltime from 30 to 40. If the bill becomes law, it may incentivize employers to keep employees under the new 40-hour threshold.

Although the mandate applies only to Large Employers with more than 100 fulltime employees in 2015, all Large Employers presently must file IRS Forms 1094-C and 1095-C for the 2015 tax year.

A Modern Game of Hide and Go Seek? Some Lessons Learned Following Sony and Other Widely-Publicized Data Breaches

BY DIANE DUHAIME & ZACHARY D. LUDENS

While the recent hack of Sony was prominent news because of the celebrity ties and potential geo-political implications, other prominent cyber-attacks over the last few months are enough to give any company pause. The January 2015 hacks of Swiss bank BCGE and American health insurer Anthem show us, once again, that any company could be next.

There is always the risk that an inside job could lead to the unauthorized disclosure of private, proprietary, and/or highly confidential information, including personal health information—any of which may result in lost business, reputational harm, regulatory actions, and/or civil lawsuits, such as the class action lawsuit filed in January 2015 against Sony Pictures by former employees alleging violations of the California Confidentiality in Medical Information Act.

Sony succeeded in getting a good portion of its hacked material (e.g., movie scripts) removed from various websites—but this was primarily because the hacked material is protected under U.S. copyright laws, and thus was promptly removed by the websites pursuant to the take-down provisions of the Digital Millennium Copyright Act (DMCA). What other laws might be of use to a company following a data security breach, especially when the information does not fall under the DMCA? Consider the following federal statutes:

- Computer Fraud and Abuse Act (CFAA): The CFAA broadly prohibits unauthorized systems access, including by employees that exceed their authorized access. It provides for civil and criminal liability; however, a civil action requires a showing that the violation caused “loss” (as defined in the CFAA) aggregating at least $5,000 in value.
- Electronic Communications Privacy Act (ECPA): The ECPA provides for civil and criminal liability for unauthorized systems access, including any electronic communications (*e.g.*, emails) disseminated after such access, and allows for compensatory, statutory, and punitive damages, and reasonable attorneys’ fees and costs.
- Stored Communications Act (SCA) of the ECPA: Under the SCA, it is a crime to intentionally access emails or other electronically stored communications without authorization, or to intentionally exceed authorized access to such communications. In a civil action, the SCA provides for compensatory, statutory, and punitive damages, and reasonable attorney’s fee and costs.

In addition, state computer crime and state trade secret statutes could afford protection and relief to companies that experience a data security breach. However, in an increasingly interconnected world, it is possible that the laws of more than one state would be applicable in a particular instance.

One fact remains true: being proactive before any data security breach is the best protection for limiting repercussions following a data security breach. This includes the implementation of a comprehensive written information security plan that outlines the necessary steps and contacts for recovering and limiting the spread of accessed information, and pursuing hackers, as well as frequently testing the plan for opportunities to improve its effectiveness.

Banks Take Notice: The Sunrise Period for .bank Registrations is Coming Soon

BY DIANE DUHAIME

The sunrise period for .bank is currently scheduled to take place between May 18 and June 16, 2015. Only trademark holders who have obtained verification of their bank’s trademarks with the Trademark Clearinghouse (TMCH) may purchase .bank domain names during the sunrise period. In other words, during the sunrise period, such trademark owners may apply to register one or more domain names that are an exact match to their verified marks. After the sunrise period, other eligible members of the general public will have an opportunity to purchase .bank domain names.

Financial and Merchant Industries Group and Obama Administration to Address Privacy Concerns

BY DIANE DUHAIME & MATTHEW KOHEN

On behalf of its 19 participating trade association members from the merchant and financial services industries, the Merchant Financial Cyber Partnership (MFCP) announced "8 Next Steps" to protect customers and their sensitive data from the ever-growing host of cyberthreats. The 8 Next Steps are as follows:

1. Establishing a formal administrative link and protocols for information sharing between merchants and financial services institutions;
2. Holding threat information sharing forums;
3. Hosting exercises that simulate significant cyber attacks;
4. Implementing and refining the National Institute of Standards and Technology's Cybersecurity Framework for developing a listing of leading cybersecurity practices;
5. Developing formal breach notification response programs;
6. Outlining recommendations for merchants, issuers, acquirers, and processors to collaborate in developing technology standards to combat cyber threats to payment systems;
7. Outlining technological and other principles for protecting payment systems; and
8. Proposing tailored, effective legislation in support of cyberthreat information sharing.

The essence of these principles has been echoed by policymakers in the United States and other countries. President Obama, during his most recent State of the Union address, stated that he intends to propose comprehensive federal legislation regarding data privacy and cybersecurity. Many are hopeful that federal legislation will mean a single data privacy breach law that will obviate the need to meet the differing obligations under state and federal data privacy laws and regulations. Depending on the precise language of the federal legislation ultimately enacted, it is possible that a single federal data privacy breach notification law could actually result in a heavier compliance burden on businesses than exists today.

MFCP members include the American Bankers Association, American Hotel and Lodging Association, Financial Services Forum, International Council of Shopping Centers, and the National Retail Federation. All industry stakeholders will want to stay abreast of the MFCP developments, as well as the ever-changing state, federal, and foreign data privacy and cybersecurity legal landscapes.

Up, Up, and Away: Insurance Market for Commercial Drones Set to Take Off

BY BRUCE J. BERMAN & ZACHARY D. LUDENS

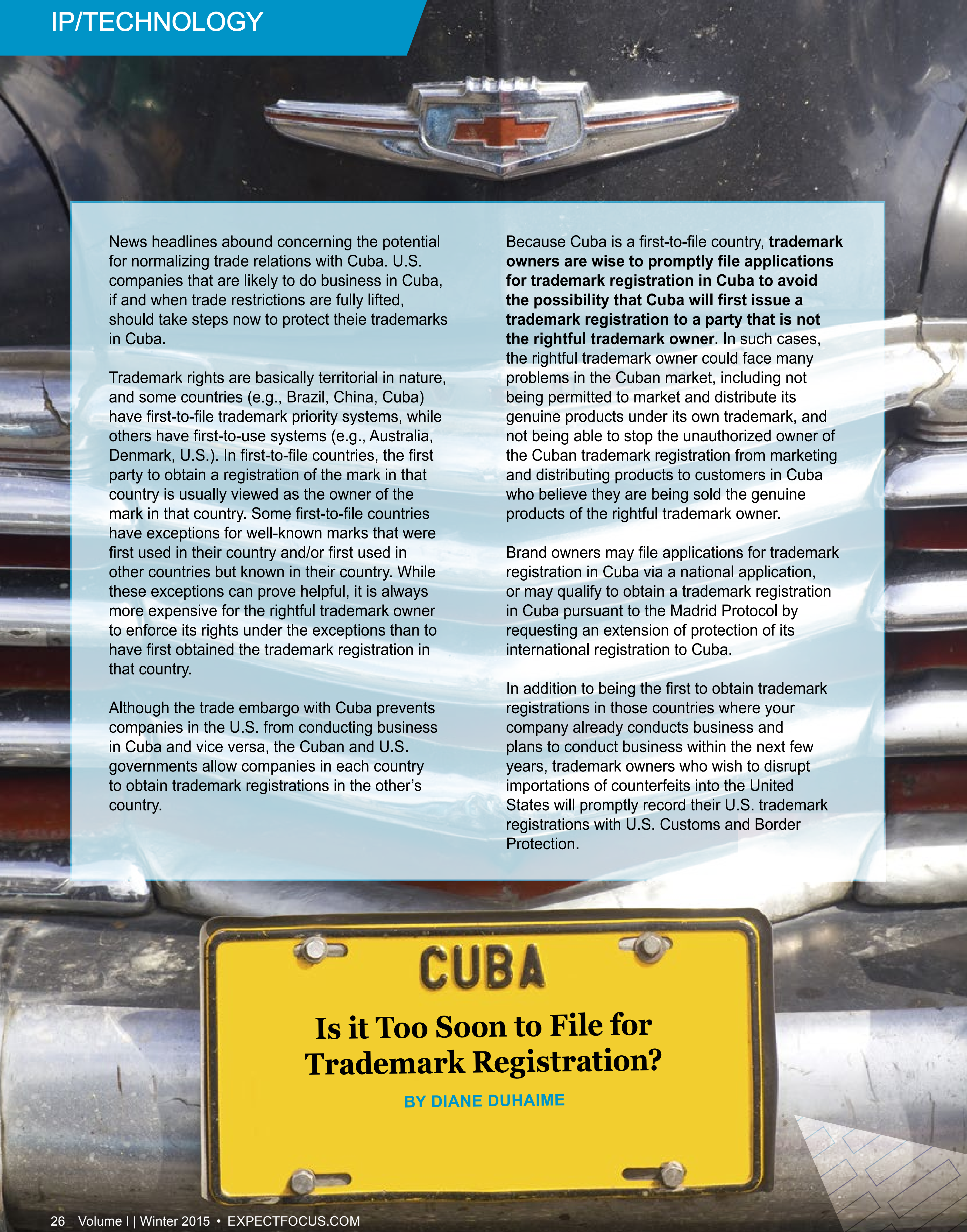
Unmanned Aerial Vehicles (UAVs or Drones) have been in the news increasingly over the past decade. While it began, primarily, with the federal government's use of Drones through the military and federal law enforcement agencies, Amazon's conceptual announcement of Prime Air in December 2013 started a whole new conversation. Since Amazon's announcement, the Federal Aviation Administration has notably granted a handful of exemptions, allowing corporations in industries such as agriculture, construction, film, and real estate to begin to operate Drones commercially.

As of drafting, the FAA reports having received more than 200 UAV exemption requests from commercial entities. Although the FAA is currently in the rule promulgation process with regard to Drones, the boom in requests for exemptions confirms that Drones are coming, and in volume. In fact, there have already been news reports of UAV activity around airports disrupting commercial airport and aircraft operations and traffic, and potentially endangering the public. Consequently, **a colossal demand for Drone insurance is on the horizon.**

The FAA estimates that close to 30,000 Drones will be used commercially by the year 2020. These estimates include a price tag of nearly $100 billion in investment. With this large of an investment and exposure to loss developing, so too is the insurance market for Drones.

Although the amount and breadth of Drone insurance policies will vary based on industry, the intended usage, size of the device, and qualifications of the operator, a specialty market has started to emerge. But, because this industry is so new, it comes with a great deal of uncertainty. For instance, how much liability would a "typical" Drone accident result in?

One thing is certain: as the usage of Drones increases exponentially over the next decade, those property and casualty carriers that were prepared are set to capitalize. Are you ready for the Drone takeoff?



Is it Too Soon to File for Trademark Registration?

BY DIANE DUHAIME

News headlines abound concerning the potential for normalizing trade relations with Cuba. U.S. companies that are likely to do business in Cuba, if and when trade restrictions are fully lifted, should take steps now to protect theie trademarks in Cuba.

Trademark rights are basically territorial in nature, and some countries (e.g., Brazil, China, Cuba) have first-to-file trademark priority systems, while others have first-to-use systems (e.g., Australia, Denmark, U.S.). In first-to-file countries, the first party to obtain a registration of the mark in that country is usually viewed as the owner of the mark in that country. Some first-to-file countries have exceptions for well-known marks that were first used in their country and/or first used in other countries but known in their country. While these exceptions can prove helpful, it is always more expensive for the rightful trademark owner to enforce its rights under the exceptions than to have first obtained the trademark registration in that country.

Although the trade embargo with Cuba prevents companies in the U.S. from conducting business in Cuba and vice versa, the Cuban and U.S. governments allow companies in each country to obtain trademark registrations in the other's country.

Because Cuba is a first-to-file country, **trademark owners are wise to promptly file applications for trademark registration in Cuba to avoid the possibility that Cuba will first issue a trademark registration to a party that is not the rightful trademark owner**. In such cases, the rightful trademark owner could face many problems in the Cuban market, including not being permitted to market and distribute its genuine products under its own trademark, and not being able to stop the unauthorized owner of the Cuban trademark registration from marketing and distributing products to customers in Cuba who believe they are being sold the genuine products of the rightful trademark owner.

Brand owners may file applications for trademark registration in Cuba via a national application, or may qualify to obtain a trademark registration in Cuba pursuant to the Madrid Protocol by requesting an extension of protection of its international registration to Cuba.

In addition to being the first to obtain trademark registrations in those countries where your company already conducts business and plans to conduct business within the next few years, trademark owners who wish to disrupt importations of counterfeits into the United States will promptly record their U.S. trademark registrations with U.S. Customs and Border Protection.

Following President Obama's recent announcement that the United States will establish diplomatic ties with Cuba, many businesses are questioning how their operations and opportunities may be impacted. There will likely be significant implications for businesses operating in various industries, particularly finance, health care, insurance, banking, telecommunications, construction, and manufacturing.

Carlton Fields Jorden Burt's Cuba Team is monitoring developments and is prepared to help individuals and companies take advantage of these opportunities as the commercial relations between Cuba and the United States continue to normalize.

Carlton Fields Jorden Burt is 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 firms for client service through a national survey of corporate counsel.

Additionally, Washington, D.C. and Miami Shareholder **Frank G. Burt** was nominated by corporate counsel for the second year in a row as a "Client Service All-Star" in BTI Consulting Group's 2015 survey. The survey identifies lawyers who demonstrate superior client focus and legal skills; deliver outstanding results and outsized value; have an unmatched business understanding; and provide innovative thought leadership to their clients' business and legal objectives.

Carlton Fields Jorden Burt launched its first-ever mobile app, CFJBLaw, developed for the Android and Apple platforms. The app allows for easy access to search for attorneys, office locations, industries and practices, blogs and other important information about the firm. The app is available for download in the AppStore and in Google Play.

Carlton Fields Jorden Burt relaunched its "Classified: The Class Action Blog" with a new and improved look and features. The blog now has an updated interface with improved navigation and is mobile responsive and easy to access from a smartphone or tablet.

Shareholders **Steven J. Brodie** and **Amy E. Furness** were named co-managing shareholders of the firm's Miami office. Brodie and Furness succeed Miami Shareholder Charles M. Rosenberg. With longstanding commitments to the firm and to the greater Miami business, education, and legal communities, Brodie and Furness bring a wealth of talent to their new positions.

Hartford Shareholder **Diane Duhaime**, recently earned the designation of Certified Information Privacy Professional (CIPP/US), the global standard in privacy certification, through the International Association of Privacy Professionals (IAPP). Duhaime received her CIPP/US designation upon passing both the Certification Foundation and CIPP/US examinations.

Washington, D.C. Shareholder **Shaunda Patterson-Strachan** will serve as the firm's 2015 Leadership Council on Legal Diversity (LCLD) Fellow. The Fellows program was created by the LCLD to identify, train, and advance the next generation of leaders in the legal profession.

Eleven attorneys throughout the firm were elected shareholders during Carlton Fields Jorden Burt's 2015 All-Attorney Meeting held on January 29-30,2015. Congratulations to the following newly elected shareholders: **Jacob R. Hathorn** (Financial Services and Insurance Litigation, Hartford), **John C. Pitblado** (Financial Services and Insurance Litigation, Hartford), **Paul Ray Borr** (Business Litigation, Miami), **Gavrila A. Brotz** (Business Litigation, Miami), **Olga M. Vieira** (Products and Toxic Torts Liability, Miami), **April Y. Walker** (Business Litigation, Orlando), **William "Ty" Giltinan** (Intellectual Property, Tampa), **Kevin P. McCoy** (Business Litigation, Tampa), **Scott P. Pence** (Real Estate and Commercial Finance, Tampa), **Kristen Reilly** (Financial Services and Insurance Litigation, Washington, D.C.), and **Alana E. Zorrilla-Gaston** (Business Litigation, West Palm Beach).

Miami Shareholder **Aaron S. Weiss** was recently appointed by Chief Judge K. Michael Moore to serve on the Ad Hoc Committee on Rules and Procedures of the Southern District of Florida. This committee is charged with preparing an annual report to the Court regarding proposed amendments to the Local Rules of the district.

Tampa Shareholder **Kevin McCoy** was selected to serve as Chair-Elect for Bay Area Legal Services' (BALS) Board of Directors. BALS is a nonprofit, public interest law firm that provides civil legal assistance to low-income residents in the Tampa Bay region.

CARLTON FIELDS JORDEN BURT serves business clients in key industries across the country and around the globe. Through our core practices, we help our clients grow their businesses and protect their vital interests. The firm serves clients in nine key industries:

- Insurance
- Health Care
- Technology
- Consumer Finance
- Construction
- Telecommunications
- Securities
- Real Estate
- Manufacturing and Raw Materials

For more information, visit our website at www.CFJBLaw.com.

Atlanta
One Atlantic Center
1201 W. Peachtree Street | Suite 3000
Atlanta, Georgia 30309-3455
404.815.3400 | fax 404.815.3415

Hartford
One State Street | Suite 1800
Hartford, Connecticut 06103-3102
860.392.5000 | fax 860.392.5058

Los Angeles*
2000 Avenue of the Stars
Suite 530, North Tower
Los Angeles, California 90067-4707
310.843.6300 | fax 310.843.6301

Miami
Miami Tower
100 S.E. Second Street | Suite 4200
Miami, Florida 33131-2113
305.530.0050 | fax 305.530.0055

New York
Chrysler Building
405 Lexington Avenue | 29th Floor
New York, New York 10174-0002
212.785.2577 | fax 212.785.5203

Orlando
CNL Center at City Commons
450 S. Orange Avenue | Suite 500
Orlando, Florida 32801-3370
407.849.0300 | fax 407.648.9099

Tallahassee
215 S. Monroe Street | Suite 500
Tallahassee, Florida 32301-1866
850.224.1585 | fax 850.222.0398

Tampa
Corporate Center Three at International Plaza
4221 W. Boy Scout Boulevard | Suite 1000
Tampa, Florida 33607-5780
813.223.7000 | fax 813.229.4133

Washington, DC
1025 Thomas Jefferson Street, NW
Suite 400 East
Washington, DC 20007-5208
202.965.8100 | fax 202.965.8104

West Palm Beach
CityPlace Tower
525 Okeechobee Boulevard | Suite 1200
West Palm Beach, Florida 33401-6350
561.659.7070 | fax 561.659.7368

* Carlton Fields Jorden Burt practices law in California through Carlton Fields Jorden Burt, LLP.

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PROTECTING TRADEMARKS IN CUBA

How Soon Is Too Soon?

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