EXPECTFOCUS®

VOLUME III SUMMER 2011

Start Making Sense

Working through the maze of laws, regulations, and rules

JORDEN BURT®

EXPECTFOCUS® Vol. III SUMMER 2011

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

The content of EXPECTFOCUS® is for informational purposes only and is not legal advice or opinion. EXPECTFOCUS® does not create an attorney-client relationship with Jorden Burt LLP or any of its lawyers.

Editorial Board
Jo Cicchetti
Denise Fee
Rollie Goss
Markham Leventhal

Editor
Michael Kentoff

Production Editor
Moira Demyan

Graphics and Design
Frances Liebold

Industry Group Editors

Life Insurance & Health Care Groups
Jason Gould

Property & Casualty
Irma Solares
John Pitblado

Reinsurance
Anthony Cicchetti

Securities
Tom Lauerman

Consumer Finance & Banking
Farrokh Jhabvala

Subscriptions
Changes in address or requests for subscription information should be submitted to:

Moira Demyan
mfd@jordenusa.com

Copyright © 2011 Jorden Burt LLP. All rights reserved. No part of this publication may be reproduced by any means, electronic or mechanical, including photocopying, imaging, facsimile transmission, recording, or through any information storage and retrieval system, without permission in writing from Jorden Burt LLP. EXPECTFOCUS® is a registered trademark of Jorden Burt LLP.

The Pros and Cons of Cloud Computing

BY DIANE DUHAIME

Not everyone likely agrees on the definition of cloud computing ("the cloud"). Some contend that cloud computing is nothing new; it is merely applying a marketing term to something that has already been done by technology providers for many years.

Cloud computing, in general, provides user access to data storage, applications software and/or other technology services through shared configurable resources, but without the user organization (1) necessarily knowing the location or configuration of those resources or (2) having to invest in acquiring, managing, and maintaining its own computing resources. The blog, Hacking Alert, aptly frames the cloud's fundamental concept: "[i]f you only need milk, would you buy a cow?"

The use of cloud computing has expanded rapidly, with no end in sight; it is typically less expensive for implementing new computing solutions than traditional methods. The cloud provider may have complete control over the user organization's servers, software applications and data. In trading control for efficiency, the user organization is faced with a variety of advantages and disadvantages in adopting cloud computing, including:

Pros	Cons
Cost savings based on not having to acquire and maintain own information technology infrastructure (costs are typically categorized as operational expenses, not capital expenses).	Increased risk of information security and data privacy breaches.
Ability to access applications from virtually anywhere and from any device via an Internet connection.	Increased risk that user organization will not have an awareness of and/or the ability to assess the precise nature of such breaches.
Ability to increase or decrease the provision of resources depending on demand (scalability).	Limitations on ability to ensure compliance with all laws applicable to the user organization's business, including the laws of other countries with regard to data that is located outside of the U.S. or flows across borders.
Increased reliability where cloud computing platform is uniform and appropriately configured for business continuity and disaster recovery.	Risk that the user organization will not have access to and control of data at any time for any purpose, including for compliance with electronic discovery and litigation hold requirements.

While this article presents only a treetop view of cloud computing benefits and drawbacks, it gives a glimpse into the myriad issues involved in moving to the cloud. Moreover, with the trend towards adopting cloud computing, user organizations are revisiting their information technology contract language to address the benefits and risks that are attendant to the specific cloud computing arrangement they are seeking to obtain from the cloud provider.

CONTENTS

IN THE SPOTLIGHT

The Pros and Cons of Cloud Computing 2

LIFE INSURANCE

Settlements Reached in Annuity Class Actions 4
New Attack on Indexed Annuities 4
Annuity Class Action Dismissed 5
Regulators Juggle Swaps Deadlines 5
Retained Asset Account Initiatives 6
Third Circuit Rules on Discretionary Authority 7
Updated Guidance on Deferred Annuity Partial Exchanges 7

HEALTHCARE

Court Certifies ERISA RAA Class Action 8
Insurance Providers May be Sued Under ERISA § 502(a)(1)(B) 8

PROPERTY & CASUALTY

Insurer Properly Invoked Appraisal Clause 9
Fifth Circuit Holds Overhead & Profit Costs Unattainable 9
Insurer Has Broad Discretion to Settle 9

REINSURANCE

Reinsurer Must Demonstrate Late Notice Prejudice in PA 10
Solvent Scheme of Arrangement Survives Challenge 10
Courts Say "Go Ask the Arbitrators" 11
Nailing Down the Arbitration Process 11

SECURITIES

SEC Breaks Silence on Indexed Products 12
Tips on Preparing SAR Narratives 12
NY High Court Eyes Martin Act Preemption 13
BD Compensation Disclosure 13
High Court Addresses Rule 10b-5 14
Persons with Compliance Responsibilities May Blow Dodd-Frank Whistle 14
Regulators Warn About Structured Notes 15
FINRA Officials Can Have Their Cake and Eat it Too 15

CONSUMER FINANCE & BANKING

Third Circuit: TCPA Does Not Divest Federal Court of Jurisdiction Under CAFA 16
Seventh Circuit: CAFA Jurisdiction Solid Unless Recovery Estimate is "Legally Impossible" 16
Supreme Court Clarifies Rule 23(b)(2) in *Wal-Mart v. Dukes* 17
Individualized Damages Calculations Sink (b)(2) Class 17
Arbitration Round-Up 18

NOTEWORTHY

Should Companies Obtain .xxx Domain Name Registrations? 19
Expanded Generic Top-Level Domain Registration Program 19

Settlements Reached in Annuity Class Actions

BY ROLLIE GOSS

Class settlements have been reached in annuity disputes recently by American National, Conseco and American Equity. Interestingly, all three cases were pending in courts in the State of California. While none of the settlements include a claims process, some contain relief gradations based upon factors that may be viewed as a proxy for a claim process. For example, the American Equity settlement provides greater relief for class members who purchased through a particular agent while the American National settlement provides greater relief for those who purchased a particular product. These scenarios might be viewed as informal subclasses. The Conseco settlement requires that class members complete and return a claim form to receive a certain benefit. As an alternative to a formal claim process, these settlement structures may be used to obtain more relief for class members who may have suffered particular harm, while providing less relief to class members who suffered lesser or different injuries.

Recent settlements provide a wide range of relief

The level of relief in these settlements – most of which consists of credits to annuity values if an annuity is in force and modest payments where the annuities are no longer in force – has varied considerably perhaps due, in part, to the procedural posture of the cases. For example, the court in the American National case entered a partial summary judgment against the company and American Equity suffered an adverse verdict in the first stage of a trial.

Recently, there has been a noticeable intersection of class action lawsuits and regulatory examinations. Accordingly, a few class settlements have settled claims from both civil class actions and regulatory proceedings together, while several reported opinions have addressed the extent to which a civil settlement could essentially preclude regulators from pursuing individualized remediation or rescission claims on behalf of purchasers who participated in class settlements. Given an increase in the level of collaborative market conduct examinations by groups of states, we expect to see heightened interest in such issues.

New Attack on Indexed Annuities

BY TODD WILLIS

The plaintiffs' bar recently filed a class action attacking indexed annuities in Illinois federal court. The lawsuit, brought on behalf of all purchasers of indexed annuities from North American Company of Life and Health Insurance, contains many recycled allegations, including assertions that the insurer's fraudulent scheme works by a) incentivizing sales agents with large undisclosed commissions, b) offering 'bonuses' that are recouped through surrender charges or by increased pricing spreads, and c) applying a charge in the market value adjustment formula that takes an additional percentage of the amount withdrawn regardless of the interest rate environment.

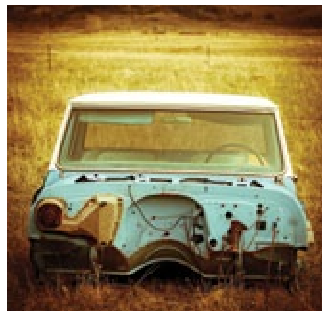
A new, aggressive strategy?

However, the complaint also contains the more novel allegation that the insurer developed a scheme to bypass the "prospective test" under Standard Nonforfeiture Law for Individual Deferred Annuities (SNFLIDA), which prohibits certain surrender penalties for deferred annuities that have "optional" maturity dates. According to plaintiffs, the insurer sold "fixed" maturity date contracts that did not permit annuitization until, in some cases, the annuitant turned 115 years old. Plaintiffs then assert that the company attempted to "skirt" the SNFLIDA "prospective test" requirement by relying on a company practice that permits annuitization at much younger ages thereby creating "optional" maturity date contracts, and conclude that if the insurer's "practice were reflected in the contractual language…," the contracts "would not pass the SNFLIDA prospective test." **In short, plaintiffs allege that the insurer's alleged conduct harms "policyholders because it directly leads to lower credited rates to persisting policyholders, insufficient nonforfeiture guarantees for surrendering policyholders, longer periods of time during which [the insurer] extracts its steep product spreads, and less liquidity."** Given the potential for any adverse decision or settlement to have a ripple effect, Jorden Burt will continue to monitor this case.

Indexed Annuity Class Action Dismissed

BY JASON GOULD

A Nevada federal court recently handed a resounding victory to the defendants in a putative class action alleging wrongdoing in how an indexed annuity's index values are captured. Plaintiffs in *Rivera v. Allianz Life Ins. Co. of North America, et al.* had filed a putative class action complaint in Nevada state court last November, alleging breach of contract and consumer fraud in connection with their purchases of index annuity policies. Plaintiffs alleged that certain language in their Statements of Understanding (SOUs) was contradictory and fraudulent because it stated that the index value would be captured on **each contract's "monthiversary,"** while the policies defined the "initial index value" as the value of the index at the end of the **last business day** before the start of a monthly term. Defendants removed the action and moved to dismiss the complaint, and plaintiffs moved to remand.



Putative class action goes nowhere

The court first denied plaintiffs' motion to remand, rejecting plaintiffs' contention that the securities exception to the Class Action Fairness Act applied because the claims concerning capturing of index values involved securities. The court held that **the securities exception did not apply "by any reasonable reading of the statutory language**" because none of plaintiffs' claims involved securities "except as to the effect of a stock index" which "clearly does not meet the criteria for the exception." The next day, the court issued an order dismissing one of the named Allianz defendants, finding that plaintiffs' collectivized allegations had failed to comply with Federal Rule of Civil Procedure 9(b) because they failed to allege any facts specific to that entity. And the following day, the court granted the remaining defendants' motions to dismiss the complaint for failure to state a claim and dismissed the action.

The court found that the "SOUs are **clearly not part of the Policy contract, and even if they were, there is no inconsistency between the SOU, which states *when* the value would be captured, and the annuity Policy, which stated *how* it would be captured."** The court also held, among other things, that the lawsuit was barred under the doctrine of claim preclusion because the plaintiffs were members of a previously certified class action "that fully litigated to final judgment the merits of claims arising from these particular annuity purchases and in which Allianz prevailed." Jorden Burt represented the Allianz defendants in the action.

Regulators Juggle Dodd-Frank Swaps Deadlines

BY TOM LAUERMAN

The CFTC and SEC (the Commissions) must adopt a large number of regulations to implement the regulatory scheme that Dodd-Frank establishes for swaps and security-based swaps (collectively, swaps).

Dodd-Frank is likely to keep regulators busy

Recently, for example, the Commissions issued a joint proposal to clarify the circumstances under which financial products, including insurance contracts, would or would not be swaps. Under the proposal, most insurance contracts would not be swaps. This is highly significant, because Dodd-Frank's regulatory scheme for swaps is largely incompatible with insurance regulation. Indeed, Dodd-Frank specifically prohibits states from regulating swaps as insurance. The comment period on this joint proposal ended on July 22 and the Commissions have not yet taken final action.

The fact that the Commissions have not yet taken final action on this and other important measures to implement Dodd-Frank's regulatory scheme for swaps has caused numerous problems. Among other things, Dodd-Frank made July 16, 2011 the date on which swaps are generally required to begin complying with the new regulatory scheme, which has in many cases proved impossible or impractical. For example, issuers of some of the insurance and other financial products addressed in the above-mentioned joint proposal do not yet know even whether those products will be considered to be swaps for this purpose.

The Commissions have each promulgated temporary exemptions and taken other actions to ameliorate such problems. For example, shortly before the July 16 deadline, the CFTC issued an order that, among other things, provides a temporary exemption from requirements under the Commodity Exchange Act that go into effect on that date but that depend on the definition of swap. This CFTC relief extends until the earlier of the date the CFTC takes final action on the definition or December 31, 2011.

Regulatory Roundup: Retained Asset Account Initiatives

BY ANN BLACK & KAREN BENSON

States continue efforts to adopt requirements on the use of retained asset accounts (RAAs). Also, the NAIC Market Conduct Examination Standards (D) Working Group adopted a new claims standard for Chapter 19 of the Market Regulation Handbook to ensure that consumers receive the disclosure on the available settlement options. NCOIL proposes to amend its Beneficiaries' Bill of Rights to require that insurers perform sweeps to find deceased insureds and RAA holders. While several states have proposed RAA legislation, most are issuing an RAA regulation, order, bulletin, or opinion, as reflected below (as of August 3, 2011).

States with RAA Legislation or Law		States with RAA Regulation	States with RAA Order, Bulletin or Opinion	
Alabama¥	New Jersey	Maryland	Arkansas	Maryland
Alaska	New York±~	New Jersey^	Colorado~	Montana~
California±~	Oregon@	North Carolina~	Connecticut~	Nebraska~
Connecticut¥	Pennsylvania		Delaware~	Nevada~
Indiana*«	Rhode Island*@		Florida	New Hampshire~
Kentucky*@	Texas#		Illinois~	New Jersey~
Maryland*«	Virginia*~		Iowa~	New York
Nevada~			Kansas~	North Dakota~
			Kentucky~	Ohio~
			Maine~	West Virginia~

* RAA legislation adopted
^ RAA regulation proposed
± State has multiple bills
~ NAIC Sample Bulletin or prior version
@ NCOIL Beneficiaries' Bill of Rights
« NCOIL based disclosure
¥ NCOIL based but no filing requirement
\# NCOIL based but no inactive account requirement

Most RAA requirements focus on required disclosure to consumers based on the NAIC RAA Sample Bulletin (NAIC Bulletin) or NCOIL Beneficiaries' Bill of Rights. Other notable requirements include:

- Requiring written consent from the policyholder or beneficiary to use an RAA (AK, CT, NJ, PA, OR, and TX),
- Prohibiting RAAs as the sole mode of settlement (MD and PA),
- Requiring all interest earned on RAA funds (less reasonable administrative expenses) to be paid to the claimant (NJ), and
- Banning the use of RAAs (NY).

Moreover, California and Indiana allow an RAA to be the default option if disclosed whereas Pennsylvania and Texas do not. Maryland establishes an exemption for the RAA disclosure requirements, and Oregon creates a private right of action for beneficiaries. Additionally, some states with an RAA Order, Bulletin or Opinion impose additional requirements from the NAIC Bulletin. Kentucky, Kansas, Maryland, and Nevada (as well as non-NAIC Bulletin states Florida and New York) require participation in an RAA to be by opt-in.

Save the Date

The ALI-ABA Conference on Life Insurance Company Products will be held November 3-4, 2011 at the Hamilton Crowne Plaza in Washington, DC. Co-chaired by **Richard Choi**, partner in the Washington office, the conference will address recent Dodd-Frank issues, the Volcker Rule, multi-state market conduct issues, including retained asset accounts and unclaimed insurance benefits, the new Federal Insurance Office, as well as other recent legislative, regulatory, and compliance developments relevant to organizations and individuals involved with these products. **Josephine Cicchetti** and **Gary Cohen**, also partners in the Washington office, serve on the faculty. For more information and to register, visit www.ali-aba.org.

Third Circuit Joins Circuit Split On Whether "Satisfactory To Us" Grants Insurer Discretionary Authority

BY JOHN BLACK

The Third Circuit Court of Appeals recently addressed, in *Viera v. Life Ins. Co. of N. Am.*, whether certain language in an accidental death and dismemberment policy granted the insurer discretionary authority to determine eligibility.

Third Circuit: discretionary authority must not be ambiguous

According to the Supreme Court, a denial of benefits challenged under ERISA is to be reviewed under a de novo standard unless the benefit plan gives the administrator discretionary authority to determine eligibility. If so, the decision should be reviewed under an abuse-of-discretion or arbitrary and capricious standard. In *Viera*, the Third Circuit specifically analyzed whether the terms of the plan ("Written or authorized electronic proof of loss satisfactory to Us must be given to Us at Our office….") gave LICONA discretionary authority, noting that the other circuits have split as to whether "Satisfactory to Us" language is sufficient to grant discretion. The First, Fourth, Sixth, Eighth, Tenth, and Eleventh Circuits have held that such language does indeed grant discretionary authority to a claims administrator, while the Second, Seventh, and Ninth Circuits have taken the opposite view.

The Third Circuit ultimately sided with the Second, Seventh, and Ninth Circuits, holding that "Satisfactory to Us" language was ambiguous, and that the ambiguity should be resolved in favor of the insured. In particular, **the court explained that the language was not clear whether the "form" must be satisfactory to LICONA or whether the proof of loss must be "substantively and subjectively" satisfactory to LICONA**. In reversing and remanding the matter to district court the Third Circuit noted that in order to avoid the default of de novo review, the policy must contain language explicitly granting discretion to the insurer.

Scribner, Hall & Thompson, LLP

Updated Guidance Released on Partial Exchanges of Deferred Annuity Contracts

BY JACKIE ALLEN

In recently released Rev. Proc. 2011-38, 2011-30 I.R.B., the IRS provides guidance on the tax treatment of partial exchanges of non-qualified deferred annuity contracts under I.R.C. § 72 and I.R.C. § 1035, which simplifies prior guidance and takes into account new partial annuitization rules under I.R.C. § 72(a)(2). A direct transfer of a portion of the cash surrender value of an existing annuity contract for a second annuity contract (a partial exchange), regardless of whether the two annuity contracts are issued by the same or different companies, will be treated as a tax-free exchange if no amount is withdrawn from or received under either the original contract or the new contract during the 180 days beginning with the date of transfer. For these purposes, an amount withdrawn from or received under an annuity involved in a partial exchange will not apply to an annuity for a period of 10 years or more or during one or more lives. The revenue procedure clarifies that a subsequent partial exchange will not be viewed as an amount received under either the original contract or the new contract if the subsequent exchange qualifies as tax-free under I.R.C. § 1035, and that there will be no aggregation of the original contract with a second contract (i.e., the contracts will be treated as separate annuity contracts).

Unlike prior guidance, the new revenue procedure does not make the enumerated I.R.C. § 72(q) conditions automatic exceptions for amounts withdrawn or received under an annuity during the specified waiting period. The eliminated exceptions will be missed by contract owners who are 59-1/2 years or older.

Court Certifies ERISA Retained Asset Account Class Action

BY KRISTIN SHEPARD

The plaintiff in *Otte v. Life Insurance Company of North America* brought an action on behalf of approximately 100,000 beneficiaries of an estimated 5,000 employer-sponsored group life insurance plans underwritten by CIGNA-subsidiaries. Plan benefits were issued through a CIGNAssurance Retained Asset Account (RAA). Plaintiff alleged that this violated ERISA's fiduciary duty and anti-self-dealing provisions and moved for class certification under Federal Rule of Civil Procedure Rule 23(b)(3).

Defendants opposed, asserting that material differences in the benefits payment provisions of the approximately 5,000 plans and Summary Plan Descriptions (SPDs) applicable to the class, as well as the existence of individualized statute of limitations defenses as to each class member, undermined Rule 23(a)'s typicality and adequacy requirements, and Rule 23(b)(3)'s predominance and superiority requirements.

In its June 10, 2011 opinion, the Massachusetts federal district court noted in dicta that the RAA was "no more than an IOU" which failed to transfer the funds out of an ERISA plan and thereby failed to discharge the defendants' fiduciary obligations. Thus, **the class could be certified irrespective of any differences in the language of the 5,000 plans and SPDs at issue**. The court, however, troubled by the existence of individualized statute of limitations defenses, "provisionally certif[ied]" two subclasses: (1) those whose benefits were paid into RAAs within three years of the filing of the complaint and thus plainly within the applicable three-year limitations period, and (2) the remaining class members. As to the latter sub-class, the court appeared to shift from plaintiff the burden of satisfying Rule 23's requirements by finding that a "brief period of discovery should establish whether the second sub-class can survive the commonality test and whether a suitable representative of the sub-class can be identified." The court's provisional certification is difficult to reconcile with the rigorous analysis followed by the Supreme Court in *Wal-Mart v. Dukes*.

Insurance Providers May Be Sued For Plan Benefits Under ERISA § 502(a)(1)(B)

BY ROBIN SANDERS

In a recent en banc decision, *Cyr v. Reliance Standard Life Insurance Company*, the Ninth Circuit Court of Appeals overruled its own precedent by holding that an insurer, which was not a plan administrator, may be sued for plan benefits under ERISA § 502(a)(1)(B). Reliance provided long term disability insurance to participants of an employee welfare benefit plan, but was not the plan administrator. Reliance did, however, control plan benefit distribution by deciding who qualified for LTD benefits. Plaintiff Cyr sued Reliance because it declined to pay increased LTD benefits she alleged were owed.

The universe of those who may be sued under ERISA § 502(a)(1)(B) may be limitless

The district court held that even though Reliance was neither the plan itself nor plan administrator, it could be sued under ERISA § 502(a)(1)(B). Eventually, plaintiff was successful in obtaining the disputed benefits, attorney's fees and costs, and Reliance appealed to the Ninth Circuit. In response to the limited issue of whether Reliance could be sued for benefits, the Ninth Circuit held that ERISA § 502(a)(1)(B) claims need not be limited to claims against benefit plans or their plan administrators. Instead, the court relied on the Supreme Court's *Harris Trust & Savings Bank v. Salomon Smith Barney, Inc.* decision, which included discussion about who could be sued for a breach of fiduciary duty under § 502(a)(3). As the Supreme Court found in *Harris Trust*, while ***§ 502(a) includes the universe of the parties who may sue for relief under ERISA, it does not identify the universe of parties who may be sued.*** Thus, the court concluded that insurance providers who are not plan administrators may be sued for benefits.

Insurer Properly Invoked Appraisal Clause

BY JONATHAN STERLING

Appraisal clauses are commonly featured in property insurance policies and provide a means to resolve disputes about the amount of loss for a covered claim. Recently the Texas Supreme Court addressed the following question concerning the enforcement of such clauses: "When the parties disagree, but neither seeks appraisal until one has filed suit, has the party demanding appraisal waived its right to insist on the contractual procedure?"

In *In re Universal Underwriters,* a car dealership suffered hail damage to its buildings and filed a claim with its insurer, Universal Underwriters (Universal). After Universal inspected the property and made payment, the dealership requested a re-inspection. This request was granted and resulted in an additional payment by Universal. No further demands or inquiries were made by the dealership. Four months later, the dealership filed suit, claiming the policy was breached. Universal responded by invoking the policy's appraisal clause in order to resolve the dispute over the value of the damaged property. Under the clause, each party was to select a disinterested appraiser, and if those two appraisers could not agree, they would submit their differences to an umpire. Universal moved to compel appraisal under this clause.

The dealership argued that Universal had waived its right to compel appraisal by waiting eight months from the date of re-inspection. The trial court agreed and denied Universal's motion. The Texas Supreme Court granted a writ of mandamus and ordered the trial court to grant Universal's motion to compel appraisal, finding that **the length of delay should have been measured from the date that the parties reached an impasse**, which was the date on which suit was filed. The court found there was no unreasonable delay from the lawsuit filing until the date of the motion to compel appraisal. Even if there had been an unreasonable delay, the court held, the dealership would have to show that it was prejudiced by the delay.

Fifth Circuit Holds Overhead & Profit Costs Unattainable If House Is Sold Unrepaired

BY SCOTT BYERS

The Fifth Circuit Court of Appeals recently reversed a Louisiana district court's grant of overhead and profit costs under a National Flood Insurance Program policy, holding that the district court improperly awarded overhead and profit costs to policyholders who sold their home unrepaired.

In *Dwyer v. Fidelity National Property & Casualty Insurance, Co.*, plaintiffs sued Fidelity claiming that it failed to properly pay flood insurance benefits after Hurricane Katrina destroyed their house. Before repairing the flood damage, plaintiffs sold their home. The district court found in favor of the plaintiffs and awarded more than $55,000 to the plaintiffs for overhead and profit costs. The Fifth Circuit reversed, finding that "[o]verhead and profit is a pass-through cost intended to reimburse homeowners for the expense of using a general contractor. **Since the [plaintiffs] sold their home unrepaired, they never incurred and will never incur the cost of a general contractor."** Consequently, the court held that the plaintiffs are not entitled to overhead and profit costs.

Insurer Has Broad Discretion to Settle–Even Over Its Insured's Objection

BY JOHN PITBLADO

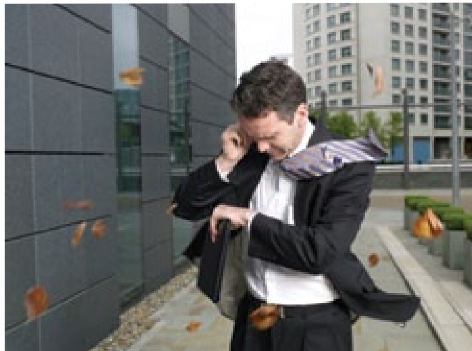
Dr. Mohan Papudesu was a defendant in a wrongful-death lawsuit. His insurer, Medical Malpractice Joint Underwriting Association of Rhode Island (MMJUA), settled the case for $500,000. Dr. Papudesu objected to the settlement because he believed he would win at trial, because the settlement adversely affected his reputation and caused his malpractice insurance premiums to rise. MMJUA asserted that it had unfettered discretion to settle the case and pointed to the following policy language as support for its position: **"[t]he company may make such investigation and settlement of any claim or suit as it deems expedient."**

Dr. Papudesu filed suit against MMJUA, and the trial court in Rhode Island agreed with MMJUA that its actions were proper. The Rhode Island Supreme Court, in *Papudesu v. Medical Malpractice Joint Underwriting Association of Rhode Island*, concluded that the above-referenced language is: "of pellucid clarity; it vests full discretion in the insurer with respect to the issue of settlement."

Reinsurer Must Demonstrate Prejudice To Prevail On Late Notice Defense

BY JOHN PITBLADO

Global Reinsurance and Pacific Employers Insurance were parties to a facultative reinsurance agreement, whereby Global agreed to reinsure an umbrella policy that Pacific had issued to Buffalo Forge Company. In 2009 – eight years after Pacific first received notice of multiple asbestos-related lawsuits against Buffalo Forge – Pacific submitted a claim to Global for $559,072.67. Global denied the claim, contending that coverage was barred under the agreement's notice provision, which required that Pacific "promptly provide [Global] with a definitive statement of loss." Pacific then sued Global in Pennsylvania federal court.



Late notice defense requires more than mere tardiness

Responding to Global's motion for summary judgment in *Pacific Employers Insurance Co. v. Global Reinsurance Corp. of America*, Pacific contended that, under Pennsylvania law, late notice does not preclude coverage unless prejudice from the delay can be demonstrated. Global argued that New York law applied, under which late notice bars coverage without requiring a showing of prejudice. Global also asserted that the same was true under Pennsylvania law, so no conflict was present. The court denied summary judgment, holding that, notwithstanding Pacific's failure to comply with the notice requirement, (1) Pennsylvania law should apply because the insured risk was located in Pennsylvania (where Pacific's offices were located, and from where it paid claims under the primary policy), and because payment by Global to Pacific would have been received in Pacific's Pennsylvania office, and (2) **under Pennsylvania law, prejudice must be demonstrated to prevail on a late notice defense**.

Solvent Scheme of Arrangement Survives Initial Constitutional Challenge

BY ROLLIE GOSS

For some years, companies in the United Kingdom have utilized a statutory process called ***solvent schemes of arrangement***. These schemes amount to what in the United States is called a "cram down" voluntary reorganization of financially distressed, but solvent, debtors. They impose upon creditors reductions in the amount owed to them outside the U.S. Bankruptcy Code. Rhode Island adopted a similar statutory scheme, which became effective in 2004. The constitutionality of such a scheme in the United States has long been questioned, but stood unaddressed because no companies had, until recently, attempted to use the Rhode Island statute.

GTE Reinsurance Company, in runoff since 1990, proposed a commutation plan under the Rhode Island statute regarding its remaining potential property-casualty related liabilities and, in 2010, initiated a proceeding in the Rhode Island Superior Court to implement the plan. Two of GTE's cedents objected. One challenged Rhode Island's Voluntary Restructuring of Solvent Insurers Act as unconstitutional under the Contract Clause and Due Process Clause of the Rhode Island and federal Constitutions. The court rejected the challenges, crediting the large majority of cedents that voted in favor of the plan, and noting that, **while some rights under the contracts between the objectors and GTE would be impaired by the commutation, they would not be "substantially impaired"** – the standard for a constitutional contract clause challenge. The court also found the Act had a legitimate public purpose and employed reasonable and necessary means to carry out that purpose. It rejected the due process argument for essentially the same reasons, noting that a "Contract Clause inquiry is more searching than the rational basis review employed in a due process challenge." Expect to see further court involvement in these issues, whether in an appeal of this case or otherwise.

Courts Say "Go Ask The Arbitrators"

BY BEN SEESSEL

Two recent cases illustrate the courts' view that procedural matters concerning the arbitration process are confined to the arbitrators' bailiwick.

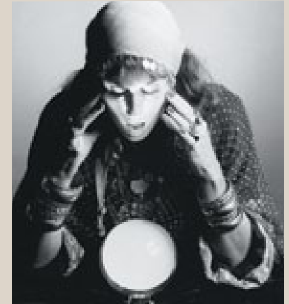
Courts: Procedural issues are for the ears of arbitrators

In *Allstate Insurance Co. v. Liberty Mutual Insurance Co.*, the U.S. District Court for the District of Massachusetts denied reinsurer Allstate's motion to compel two separate arbitrations. Instead, the court granted ceding insurer Liberty Mutual's cross-motion to compel Allstate to select an umpire to complete an arbitration panel that, in turn, would decide how many arbitration proceedings should be held. Allstate, having filed two arbitration demands based on distinct issues, sought to compel two separate arbitrations. The court denied Allstate's request, reasoning that the court's job was to determine the validity and scope of the arbitration provision, while the **arbitrators should decide procedural questions related to the arbitration, including whether to consolidate the separately requested proceedings**.

The U.S. District Court for the Southern District of New York likewise held, in *Munich Reinsurance America, Inc. v. National Casualty Co.*, that the interpretation of a treaty's "act-as-one" provision is a procedural issue for the arbitrators to decide. National Casualty was one of several reinsurers providing reinsurance to Munich Re under a single treaty. National Casualty and another reinsurer, Wausau, denied claims submitted by Munich Re. The treaty provided that disputes would be arbitrated and that if more than one reinsurer was involved in the same dispute, all reinsurers would act as one party. Wausau refused to submit to arbitration, however, and National Casualty took the position that the treaty's "act-as-one" clause prohibited the arbitration from going forward without Wausau as a party. Munich Re successfully moved to compel. The court held that **whether the "act-as-one" provision prohibited an independent arbitration against National Casualty was a threshold procedural issue for the arbitrators to decide**.

Treaty Tips: Nailing Down the Arbitration Process

BY ANTHONY CICCHETTI



Lesson: It pays to address the foreseeable

A companion article in this section demonstrates that appropriate focus on the arbitration provisions of a reinsurance agreement can do much to advance timely and efficient dispute resolution. For example, the dispute resolved in the Allstate/Liberty Mutual case could have been avoided had the parties addressed consolidation in their agreement. Similarly, the parties in the Munich Re/National Casualty matter could have provided contractually for contingencies in the event the "act-as-one" mandate was not honored by all reinsurers.

The benefits of addressing reasonably foreseeable events apply equally to the most basic elements of arbitration, such as selection of the arbitration panel. In *Northwestern National Insurance Co. v. Insco, Ltd.*, the reinsurance agreement provided that each party would appoint one arbitrator, with the two party-appointed arbitrators then selecting a neutral umpire. The agreement did not prescribe a method for replacing an arbitrator. When reinsurer Insco's arbitrator resigned, Northwestern petitioned the court to appoint an ARIAS-certified arbitrator to fill the void. Two weeks later, however, Insco gave notice that it had appointed an ARIAS-certified arbitrator of its own choosing. Although the court recognized that Section 5 of the Federal Arbitration Act authorized it to appoint a replacement arbitrator when an arbitration agreement does not specifically provide a method for doing so, it denied Northwestern's petition. The court concluded that allowing Insco to appoint a replacement was consistent with the intent of the reinsurance agreement and the underlying goal of arbitration by a mutually acceptable panel. The court also determined that manipulation of the arbitration process was not a concern under the circumstances presented.

This end result and underlying reasoning are sound. Nevertheless, one must recognize that the time and expense of this litigation could have been avoided had the reinsurance agreement included a simple sentence addressing the method for selecting replacement arbitrators.

SEC Breaks Silence on Indexed Products

BY GARY COHEN

The SEC's Office of Investor Education and Advocacy has placed on its website (*www.investor.gov*) an Investor Bulletin providing information on features of indexed annuities. The Investor Bulletin, which principally provides information concerning the computation of the index-linked interest rate and potential limitations on an individual investor's realization of the full interest rate, states that "you should understand how each feature works and what impact … it may have on the annuity's potential return." In addition, the Bulletin contains numerous warnings, such as "you can lose money" and "[c]ircumstances may arise where the insurance company is unable to pay its obligations."

The Bulletin does not refer to the status of indexed annuities (or indexed life insurance) as securities or insurance. Some observers find this curious, since the SEC has not yet announced how it will administer the Harkin Amendment's conditions for the treatment of an indexed product as insurance rather than as a security. **Moreover, as some indexed products are currently registered with the SEC as securities, the Bulletin seems to stop short of providing a full picture to investors.**

Those seeking clarity might be a little frustrated with the Investor Bulletin

The Bulletin's genesis is something of a mystery. One view is that SEC Chairman Mary Schapiro originated the Bulletin, given her stated view, while head of FINRA, that indexed annuities should be treated as securities. The Bulletin concludes with a statement that "[i]t is neither a legal interpretation nor a statement of SEC policy."

See "Regulators Warn About Structured Notes with Principal Protection" on page 15 about a joint Investor Alert that the Office of Investor Education and Advocacy and FINRA have recently issued concerning a type of security that has many similarities to indexed annuities.

Tips on Preparing SAR Narratives

BY KAREN BENSON

In its current issue of The SAR Activity Review – Trends, Tips & Issues, the Treasury Department's Financial Crimes Enforcement Network (FinCEN) published extensive guidance to assist financial institutions, including broker-dealers and mutual funds, in filing suspicious activity reports (SARs). The guidance focuses on activity related to foreign corruption, but it could be easily applied to other types of suspicious activity.

Among other things, the guidance lays out the "5 Ws" that FinCEN believes are the key elements for writing an effective SAR narrative:

- who conducted the activity, including pertinent relationships (e.g., a senior political figure and/or his family members and close associates),
- what instruments were used (e.g., wires, cashiers' checks, etc.),
- where the activity occurred (e.g., the jurisdiction(s) where the subjects of the report, and relevant accounts, were located),
- when the activity took place, and
- why the filer believes the activity was suspicious (e.g., news reports discussing potential corruption, large incoming wire amounts, potential structuring, etc.).

Additionally, the guidance provides examples of an "effective" and "less effective" SAR narrative. According to the guidance, an SAR narrative is less effective in achieving its law enforcement objectives if it lacks details such as pertinent account numbers, names associated with the accounts or types of products or services utilized by the account holder, or relevant transactional information (e.g., dollar amounts that alerted the filer to potential suspicious activity). **FinCEN emphasizes that an effective SAR narrative should contain a complete account of the suspicious activity and follow a chronological order.**

By referring to this new FinCEN guidance, many filers will be able to significantly improve the narrative portion of the SARs they prepare.

New York High Court Eyes Martin Act Preemption

BY BEN SEESSEL

New York's "blue sky" law, the Martin Act, has been a substantial impediment to certain types of private legal actions involving securities. This may be about to change.

Will the court creatively interpret New York "blue sky" law?

Most courts, including the federal Second Circuit Court of Appeals, have held that the Martin Act preempts common law claims involving securities transactions that do not require scienter. The New York Court of Appeals, however, is currently reviewing a contrary holding by the First Department of the Appellate Division, *Assured Guaranty (UK) Ltd. v. J.P. Morgan Investment Management*.

In *Assured Guaranty*, plaintiff alleged that investment manager J.P. Morgan committed a breach of fiduciary duty and gross negligence by over-exposing a reinsurer's reserves to risky mortgage-backed securities. The trial court granted J.P. Morgan's motion to dismiss, holding that the breach of fiduciary duty and gross negligence claims were preempted by the Martin Act. The Appellate Division reversed, noting the general rule that a remedy provided by statute is cumulative unless specifically made exclusive. Further, the court interpreted prior state court decisions on Martin Act preemption very narrowly, pointing to a recent amicus brief submitted by the New York Attorney General in another case, in which the Attorney General argued that the Martin Act was "intended to supplement, rather than supplant existing causes of action."

BD Compensation Disclosure: Goodbye Prospectus, Hello Point of Sale

BY MARILYN SPONZO

Proposed FINRA Rule 2341, which will replace current NASD Rule 2830 regarding investment company securities, imposes new point-of-sale cash compensation disclosure requirements on broker-dealers, while simultaneously eliminating Rule 2830's prospectus disclosure requirement for such arrangements. The proposed rule, currently pending before the SEC, will become effective within 365 days after SEC approval.

The disclosure provisions of the proposed rule apply to any broker-dealer that has, within the previous calendar year, received or entered into an arrangement to receive cash compensation from an offeror, other than sales charges and service fees disclosed in the prospectus fee table. Supplementary information accompanying the rule defines cash compensation to include revenue-sharing arrangements, whether based on assets under management, shares sold, or another formula.

A broker-dealer participating in these arrangements must prominently disclose them, and also state that they may influence the selection of investment company securities that the broker-dealer offers or recommends. As to a broker-dealer's customers at the time Rule 2341 becomes effective, the disclosure must be provided prior to the customer's next investment company securities purchase from the broker-dealer, except that it need not be provided earlier than 90 days after the effective date. The disclosure must be provided to new customers prior to their first such purchase after the effective date.

The proposed rule also requires that the broker-dealer disclosure include a prominent reference or hyperlink to a webpage or toll-free number providing more information on the arrangements, including: 1) offeror names; 2) a narrative description of the additional cash compensation and any services provided in exchange; and 3) if applicable, a narrative description and names of any preferred investment company sponsors recommended to customers as a result of additional cash compensation. This information must be updated annually, within 90 days after calendar year end, or whenever it becomes materially inaccurate.

High Court Addresses Rule 10b-5

BY GLENN MERTEN

The Supreme Court recently issued two opinions regarding rule 10b-5. In *Erica P. John Fund, Inc. v. Halliburton Company*, the Court resolved a conflict among the Circuits as to whether "loss causation" is required to be proved at the class certification stage in a Rule 10b-5 putative class action. The Fifth Circuit Court of Appeals had determined that in order to invoke the fraud-on-the-market presumption of reliance, the plaintiff must establish that a decline in a security's value was caused by the correction of a prior misleading statement and could not be explained by other market factors. A unanimous Court vacated the decision and remanded for further proceedings, holding that "[l]oss causation has no logical connection to the facts necessary to establish the efficient market predicate to the fraud-on-the-market theory."

In *Janus Capital Group, Inc. v. First Derivative Traders*, the Court considered whether statements in a mutual fund's prospectus could be attributed to the fund's investment adviser. The Fourth Circuit Court of Appeals had held that the adviser, "by participating in the writing and dissemination of the prospectuses, made the misleading statements contained in the documents." In an opinion authored by Justice Thomas, a five-justice majority held that "[f]or the purposes of Rule 10b-5, the maker of a statement is the person or entity with ultimate authority over the statement…[o]ne who prepares or published a statement on behalf of another is not its maker." Since the mutual fund was the entity that filed the prospectuses with the SEC, its investment adviser generally could not be deemed to have "made" any statements in the prospectuses.

Persons with Compliance Responsibilities May Blow Dodd-Frank Whistle

BY EDDIE KIRTLEY

The SEC recently adopted detailed rules implementing the Dodd-Frank Act's program of hefty bounty awards for whistleblowers who provide the agency with original information about securities law violations resulting in sanctions in excess of $1 million.

The new rules impose special limitations on the receipt of bounties by certain persons who have explicit or implicit compliance responsibilities with a company, including, for example:

- any officer or director who is informed by any other person about allegations of misconduct,
- any officer or director who learns such information as a result of the company's whistleblower hotline or other corporate mechanisms for identifying potential violations, and
- any employee whose principal duties involve compliance or internal audit responsibilities.

Under the rules' limitations, such individuals can receive a bounty for information they disclose to the SEC, but only if:

- they have a reasonable basis to believe that such disclosure is required to prevent the company from acting in a manner likely to cause substantial injury to the financial interest or property of the company or investors,
- they have a reasonable basis to believe that the company is engaging in conduct that will impede an investigation of the misconduct, or
- 120 days have passed since the company had notice of the information.

Company personnel with compliance responsibilities will often possess the most complete information about an alleged violation, and the prospect of a whistleblower bounty will, in many cases, provide such personnel with a substantial incentive to inform the SEC before the company or another person does so. Moreover, the above-described limitations generally leave such individuals free to inform the SEC at the end of the 120-day period, if not before.

Regulators Warn About Structured Notes with Principal Protection

BY ANN FURMAN

In June, FINRA and the SEC Office of Investor Education and Advocacy jointly issued an Investor Alert entitled *Structured Notes with Principal Protection: Note the Terms of Your Investment.* The joint Investor Alert seeks to explain to investors how these products work and what risks they may entail.

The term "structured note with principal protection" refers to any structured product that combines features of a bond with a derivative component and that offers a full or partial return of principal at maturity. For example, the promised return of principal could resemble a zero coupon bond, which pays no interest until maturity, while the derivative component promises a return linked to the S&P 500, or other underlying index, asset, or benchmark.

The Investor Alert warns investors that some of these products offer only partial principal protection – for example 10% rather than 100% return – and states that investors typically will receive principal protection from the issuer only if they hold the note until maturity – typically ranging up to 10 years from issuance. The Investor Alert also addresses fees, costs, tradeoffs, and taxes, and provides a list of questions to ask before investing in these products.

Meanwhile, FINRA officials have made public statements admonishing broker-dealers to fully understand, effectively supervise, and offer robust training concerning these products. FINRA's warnings follow settlement of an enforcement matter alleging that certain advisers misled clients about the complex "principal protection" feature of structured notes by Lehman Brothers Holdings Inc. that were sold a few months before the firm collapsed.

Also, see "SEC Breaks Silence on Indexed Products" in this section about an Investor Bulletin that the Office of Investor Education and Advocacy recently issued concerning certain insurance products that can have many features similar to structured notes with principal protection.

FINRA Officials Can Have Their Cake and Eat it Too

BY TOM LAUERMAN

The Second Circuit Court of Appeals has recently affirmed that FINRA and its officers are entitled to absolute immunity from private suits for damages resulting from the discharge of their regulatory responsibilities. The plaintiffs in *Standard Investment Chartered, Inc. v. NASD* were broker-dealer firms who alleged that proxy materials distributed in 2006 by FINRA (when it was still the NASD) were misleading. The proxy materials sought approval of bylaw amendments in connection with the then-proposed consolidation of the NASD with the regulatory arm of the NYSE to form FINRA. The plaintiffs complained of misrepresentations in the proxy materials concerning a one-time "special member payment" that was made to firms in connection with the consolidation.

For FINRA officers, life is pretty sweet

Because of its quasi-governmental nature as a self-regulatory organization, FINRA and its officers are absolutely immune from suit where the alleged misconduct concerns such things as bylaw amendments that are within FINRA's role as regulator. The court found it significant that FINRA cannot alter its bylaws without approval from the SEC after a notice and comment period.

Nevertheless, FINRA is a private company that has not been shy about emphasizing its similarity to non-governmental entities when criticized for the high compensation levels of certain FINRA personnel. FINRA has emphasized that such personnel perform functions that more closely resemble those of the entities that FINRA regulates than lower-compensated functions that are characteristic of government agencies.

In some respects, FINRA and its officers seem to have the best of both worlds.

Third Circuit: TCPA Does Not Divest Federal Court of Jurisdiction Under CAFA

BY LARA GRILLO

In *Landsman & Funk PC v. Skinder-Straus Associates*, a split Third Circuit Court of Appeals panel on a consolidated appeal of three class actions held that the Class Action Fairness Act (CAFA) provides diversity jurisdiction over plaintiffs' private Telephone Consumer Protection Act (TCPA) claims. The TCPA provides a private right of action for recipients of unsolicited facsimiles with statutory damages of $500 per violation. Based on allegations that defendants sent over 10,000 unsolicited fax advertisements in violation of the TCPA, plaintiffs requested over $5 million in damages. The court held that, although under Third Circuit precedent the TCPA divested the district court of *federal question* jurisdiction over the claims, the district court could exercise *diversity* jurisdiction under CAFA, which provides federal courts with original jurisdiction over class actions with minimal diversity and an aggregate amount in controversy exceeding $5 million. The court found that each of the three cases under appellate review met the CAFA criteria. Relying on the Second Circuit's 2006 opinion in *Gottlieb v. Carnival Corporation*, the court concluded that "it would take a 'clear and definitive' directive from Congress to persuade us 'to remove a party's entitlement to a federal forum based on diversity,'" and that the TCPA did not contain such a clear directive. The concurring opinion agreed that diversity jurisdiction existed, but believed that the same rationale supported the conclusion that federal courts could also exercise federal question jurisdiction over TCPA claims. The dissent believed that Congress clearly designated the "courts of that State" as the forum for all TCPA claims, therefore, federal courts could not entertain the claims. On May 17, 2011, the Court granted petitions for rehearing en banc.

Telephone consumer act trumped by CAFA

Seventh Circuit: CAFA Jurisdiction Solid Unless Recovery Estimate is "Legally Impossible"

BY MICHAEL SHUE

In *Back Doctors v. Metropolitan Property and Casualty Insurance Co.*, a group of medical providers brought a state-court class action against Metropolitan Property and Casualty, which removed the action to federal court under the Class Action Fairness Act (CAFA). The district court remanded, holding that doubts are construed against removal because it is disfavored, and finding that the insurer had not established "a reasonable probability" that the amount in controversy exceeds $5 million because the complaint did not seek punitive damages or allege wanton or malicious conduct.

The Seventh Circuit Court of Appeals vacated the remand order, rejected the district court's application of a "reasonable probability" standard, and held that the correct test for determining whether the amount in controversy requirement has been met is whether "recovery of an amount exceeding the jurisdictional minimum is legally impossible." The panel stated that "when a plaintiff does not tie its own hands, the defendant is entitled to present a good-faith estimate of the stakes. If that estimate exceeds the jurisdictional minimum, it controls and allows removal unless recovery exceeding the jurisdictional minimum would be legally impossible." The Seventh Circuit found it instructive that the complaint did not affirmatively disclaim punitive damages, and was persuaded by the medical providers' failure to cite a single Illinois case holding that an omission of punitive damages allegations from a complaint makes a punitive award impossible. The panel also rejected the district court's contention that there are presumptions against federal jurisdiction or removal, holding that CAFA "must be implemented according to its terms, rather than in a manner that disfavors removal of large-stakes, multi-state class actions."

Seventh Circuit: "[D]efendant is entitled to present a good-faith estimate of the stakes"

Supreme Court Clarifies Rule 23(b)(2) In *Wal-Mart v. Dukes*

JONATHAN HART

In the potentially landmark decision, *Wal-Mart Stores, Inc. v. Dukes*, the Supreme Court, on June 20, 2011, held that claims for monetary relief cannot be certified under Rule 23(b)(2) where "the monetary relief is not incidental to the injunctive or declaratory relief." In *Dukes*, the district court and Ninth Circuit Court of Appeals approved the certification of a Rule 23(b)(2) class of female employees of Wal-Mart who sought injunctive and declaratory relief and backpay under Title VII. The Court analyzed the history and structure of Rule 23(b) and concluded that sub-part (b)(2) "does not authorize class certification when each class member would be entitled to an individualized award of monetary damages." It added that Wal-Mart was "entitled to litigate its statutory defenses to individual claims" for backpay and "the necessity of that litigation will prevent backpay from being 'incidental' to the class-wide injunction." **The Court expressly rejected the argument that monetary claims were proper in a (b)(2) class as long as they do not "predominate" over the injunctive and declaratory relief**, explaining that the protections of Rule 23(b)(3) cannot be nullified "whenever a plaintiff class, at its option, combines its monetary claims with a request – even a 'predominating request' – for an injunction." Citing the Fifth Circuit Court of Appeals' decision in *Allison v. Citgo Petroleum Corp.*, the Court left open the question of whether monetary claims that are "incidental" to the injunctive relief could ever be certified under (b)(2), finding that in this case the damages clearly were not incidental.

Are monetary damages available any longer under Rule 23(b)(2)?

Individualized Damages Calculations Sink (b)(2) Class In Seventh Circuit

MICHAEL WOLGIN

In what turned out to be a preview of the U.S. Supreme Court's *Wal-Mart v. Dukes* decision, the Seventh Circuit Court of Appeal, in *Randall v. Rolls-Royce Corp.*, affirmed the denial of certification of a class of more than 500 female employees of Rolls-Royce who alleged they were underpaid and under-promoted on the basis of gender. Despite seeking primarily monetary relief, which is characteristic of 23(b)(3) classes, plaintiffs presented their requested relief as an injunction under Rule 23(b)(2), which governs a class in which "final injunctive relief or corresponding declaratory relief is appropriate respecting the class as a whole." In its March 30, 2011 decision, the Seventh Circuit explained that it may be "easier" to establish the requisite adequacy of the class representatives in a (b)(2) class because "usually there is less variance in injunctive relief" than in a (b)(3) class seeking damages. But the court rejected the claim that a (b)(2) class could be maintained in this case, where "the equitable relief is mainly monetary." **Rule 23(b)(2), the court stressed, envisions a class remedy of "final" injunctive relief**, which would not apply here, where "calculating the amount of back pay to which the members of the class would be entitled if the plaintiffs prevailed would require 500 separate hearings." The court further explained that it "is only when the primary relief sought is injunctive," and where monetary relief (if sought) is "mechanically computable," that (b)(2) is applicable.

Individual variations in back pay claims fatal to class

Arbitration Roundup

BY LANDON CLAYMAN

After being directed by the U.S. Supreme Court to reconsider its decision in light of the Court's *Stolt-Nielsen* decision, the U.S. Court of Appeals for the Second Circuit reached the same result on the second go-around in *In re American Express Merchants' Litigation*, ruling that a class action waiver provision in the arbitration clause of a card acceptance agreement was unenforceable. The Second Circuit ruled that it would be prohibitively expensive for the plaintiffs to bring their federal antitrust claims on an individual basis, and therefore it refused to enforce the class action waiver provision because it would have deprived the plaintiffs of substantive rights under the antitrust statutes. However, **the Court of Appeals emphasized that it was not holding that class action waivers in arbitration agreements are per se unenforceable**, and that each case must be considered on its own merits, governed by a "healthy regard" for the liberal federal policy favoring arbitration. Moreover, despite its ruling that the class action waiver was unenforceable, the Second Circuit noted that the *Stolt-Nielsen* decision precluded it from granting relief ordering class-wide arbitration.

Class action waivers continue to attract a good deal of judicial scrutiny

The U.S. Supreme Court continues to exhibit interest in cases presenting arbitration issues, and recently it granted certiorari to review two arbitration matters next term. One of the matters, concerning whether a party resisting arbitration must show prejudice in order to establish a waiver by the other party of the right to arbitrate, has been dismissed by stipulation of the parties. In the other matter, the Court is postured to review *Greenwood v. Compucredit Corp.*, in which the Ninth Circuit Court of Appeals invalidated an arbitration agreement based upon its holding that the federal Credit Repair Organization Act specifically prohibits agreements that disallow a consumer's right to sue in court for violations of the Act.

Congratulations!

Richard Ovelmen, partner in the Miami office, spoke on June 24, 2011 at the Florida Bar Annual Convention at the Florida Bar's Annual Review of U.S. Supreme Court First Amendment Decisions, which addressed opinions handed down during the 2010 Term. A recent Jorden Burt victory, *Sorrell v. IMS Health*, was discussed by the panel. Mr. Ovelmen also spoke about the *IMS Health* decision on a live webcast from Washington, D.C. on July 19, 2011.

Jorden Burt is pleased to announce that **John Herrington**, associate in the Connecticut office, has been appointed to serve on the Connecticut Advisory Committee to the U.S. Commission on Civil Rights.

Jorden Burt is also pleased to announce that **Diane Duhaime**, a partner in the firm's Connecticut office, has been selected by the Connecticut Bar Foundation as a James W. Cooper Fellow. Fellow selection requires demonstrated superior legal ability and devotion to the welfare of the community, state, and nation. Further information about the Fellows Program and its mission is located at http://cbf.ctbar.org/.

Come September, Should Financial Services Companies Obtain .xxx Domain Name Registrations?

BY DIANE DUHAIME & JOHN HERRINGTON

The recent approval by the Internet Corporation for Assigned Names and Numbers (ICANN) of a new .xxx sponsored top-level domain (TLD) for the online adult entertainment industry or those supplying products to such industry (the sponsored community) creates a risk that names, service marks and/or trademarks of financial services companies may be used as part of a .xxx web site address for sexually explicit material. According to ICM Registry LLC, the registry for the .xxx sponsored TLD:

- beginning on September 7, 2011, owners of national trademark or service mark registrations who are not members of the sponsored community, will have a period of 30 days within which to make an opt-out application to reserve .xxx domain names, in order to block their nationally registered marks from being used by others as .xxx domain names (Sunrise B),
- during the same 30-day period, qualifying members of the sponsored community may make an opt-in application for corresponding .xxx domain names (Sunrise A), and
- once the Sunrise period ends, the .xxx domain names will be available on a first come first served basis; therefore, many trademark owners "will take a prevention is better than cure approach" by making applications during the Sunrise period.

The cost for an opted out .xxx domain name registration is reportedly expected to be in the range of $200 to $300 for a period of ten (10) years. On the other hand, **the filing fee for seeking a transfer of a single domain name registration under the ICANN Uniform Domain Name Dispute Resolution Policy (UDRP) is approximately $1,300 for a single arbitration panelist**. Thus, it apparently will be more cost effective to acquire the opt-out .xxx domain name registration in the first instance, and financial services companies interested in protecting their registered marks against potential unauthorized uses in the .xxx TLD, would be wise to consider filing applications within the aforesaid Sunrise period.

Will Your Company Participate in the Expanded Generic Top-Level Domain Registration Program?

BY DIANE DUHAIME & JOHN HERRINGTON

As we reported in the Fall 2008 issue of Expect Focus, the Board of Directors of the Internet Corporation for Assigned Names and Numbers (ICANN) first approved the concept of expanding the system for registering a generic top-level domain (gTLD) in June of that year. On June 20, 2011, ICANN finally approved a new plan to implement the drastically expanded gTLD registration program.

The current domain name system includes 22 gTLDs, and most U.S. companies already own domain name registrations that end in .com, .net, .org, .info, .biz, .mobi and/or .us. The new gTLD registration system will allow the registration of gTLDs in any language or script, limited only by registrant creativity. For example, the expanded system will accommodate the addition of *company names*, such as Ford, IBM, Chase; *trademarks*, such as GATORADE, HP, DOLBY; *city and state names*, whether or not abbreviated, such as NYC, LA, Wisconsin, WI, London, Berlin; and *names of target markets or communities*, such as finance, insurance, reinsurance, money, savings, retirement, investments, travel, books.

The initial 90-day application period for registration under the expanded gTLD registration program will run from January 12, 2012 to April 12, 2012. The application fee will be approximately $185,000 (additional fees may be required during the application evaluation process), and the annual fee will be approximately $25,000. ICANN anticipates the evaluation process for each application will take between 9 and 20 months.

This expanded gTLD registration program will dramatically increase the number of available domain names. Therefore, **businesses, governmental entities, associations, educational institutions, individuals and others should consider not only whether to participate in the new expanded gTLD registration program, but also, whether to implement additional measures to effectively monitor the unauthorized uses of their trademarks** in order to combat trademark infringement and cybersquatting.

JORDEN BURT LLP is the premier national legal boutique providing litigation services and counseling to the financial services sector. The firm serves clients in seven key industries:

- Life Insurance
- Health Care
- Property & Casualty Insurance
- Reinsurance
- Investment Companies & Advisers
- Securities
- Consumer Finance & Banking

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

SOUTHEAST
Suite 500
777 Brickell Avenue
Miami, FL 33131–2803
305.371.2600
Fax: 305.372.9928

WASHINGTON, D.C.
Suite 400 East
1025 Thomas Jefferson St., N.W.
Washington, D.C. 20007–5208
202.965.8100
Fax: 202.965.8104

NORTHEAST
Suite 301
175 Powder Forest Drive
Simsbury, CT 06089–9658
860.392.5000
Fax: 860.392.5058