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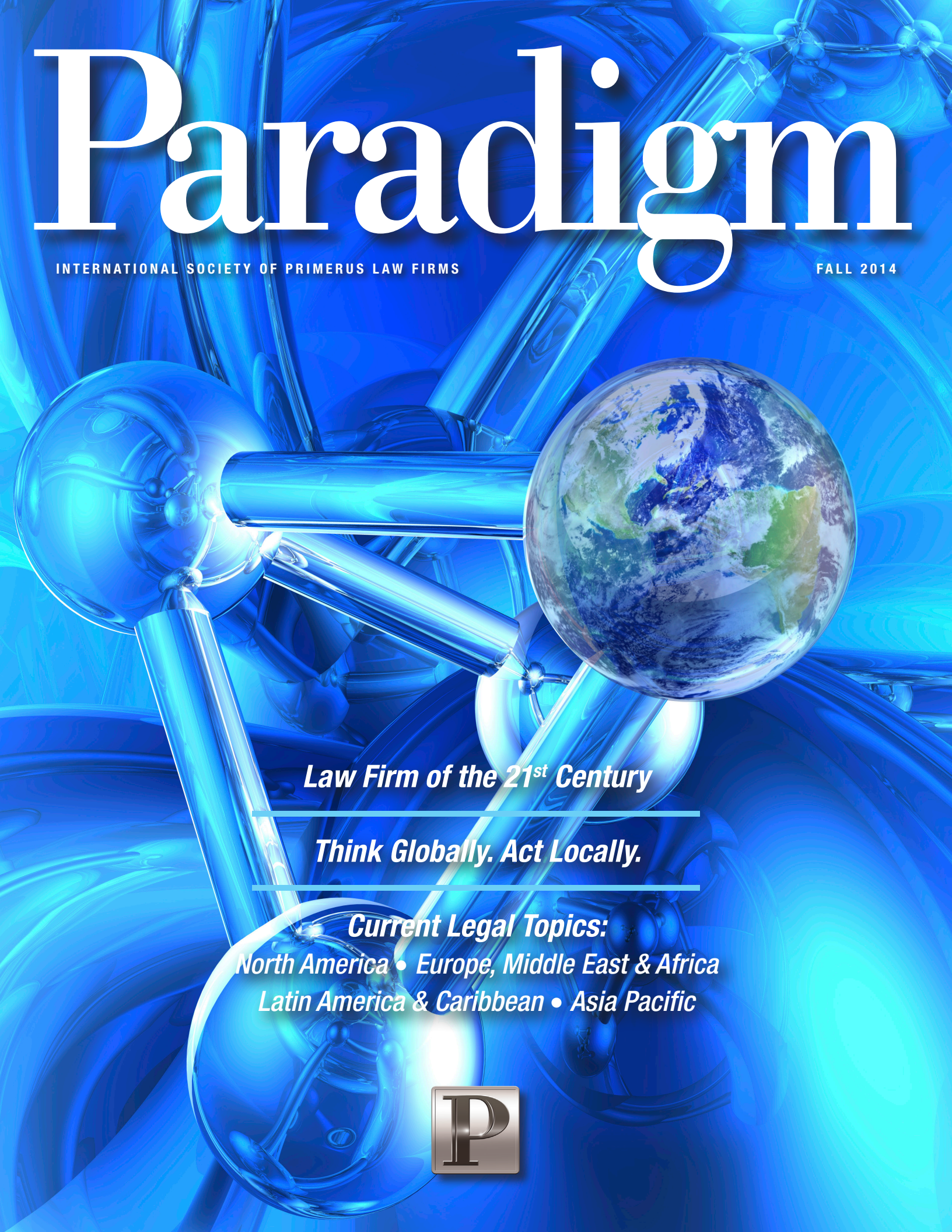

Law Firm of the 21st Century

Think Globally. Act Locally.

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Every lawyer in Primerus shares a commitment to a set of common values known as the Six Pillars:

Integrity
Excellent Work Product
Reasonable Fees
Continuing Legal Education
Civility
Community Service

For a full description of these values, please visit www.primerus.com.

About our cover

Shape and form is derived from many smaller individual pieces and abstractions. In the same way, Primerus law firms have developed a cohesive bond guided by the principles in the Six Pillars. The result is a strong society of quality law firms ready to serve clients around the world.

Scan this with your smartphone to learn more about Primerus.

Primerus
The World's Finest Law Firms

Publisher & Editor in Chief: **John C. Buchanan**
Managing Editor: **Chad Sluss**

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President's Podium

John C. Buchanan

Law Firm of the 21st Century

My wife and I took a trip earlier this year to the Galapagos Islands. In preparation for the trip, I read more about Charles Darwin and the theory of evolution, since we'd be visiting the same islands he did. A famous quote often attributed to Darwin goes something like this: "It is not the strongest of the species that survives, nor the most intelligent that survives. It is the one that is most adaptable to change." In the struggle for survival, the so-called fittest win out at the expense of their rivals because they succeed in best adapting themselves to their environment.

In the 22 years since we founded Primerus there have been many changes to the legal profession. Our start came before emails and the internet. Before globalization. Before iPhones and iPads. Before many companies missed the boat. As leaders of our businesses, we must look into the crystal ball to try to see what our world will be like over the next 10 to 20 years. And we must start now so we don't end up like companies and law firms that are no longer around.

The legal market went through a seismic shift during and following the recession of 2008. It's no coincidence that in 2009, the year immediately following the economic crisis, Primerus had one of its most successful years of growth ever, and the growth continued in the years following. Our firms were offering what clients wanted – high quality legal services for reasonable fees. Quality and value – that's it.

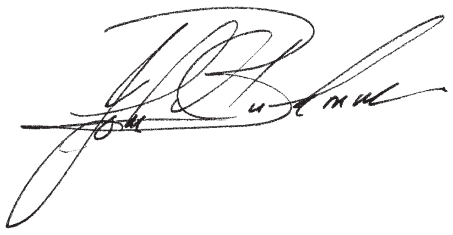
You can read more about these trends in the lead article on pages 5 through 7, for which we interviewed the lead author of the 2014 Report on the State of the Legal Market from Georgetown University Law Center and Peer Monitor. I believe the information in the report supports the fact that Primerus is on the right track and is leading the way in this industry.

The report makes it clear what clients want. They want their lawyers to provide top quality legal services, which has always been and still is, a top priority. But now, they want much more. They want their lawyers to be more responsive, more effective and efficient to keep the cost down, and they want the cost of their legal services to be more predictable.

Now that the world economies have gone global and most major companies are engaged in some form of international commerce, the time has come for a world alliance of top quality independent law firms, like Primerus, sharing very high Six Pillar standards and a common brand that clients can rely on, regardless of where their legal needs arise.

In the 22 years since we founded Primerus there have been many changes to the legal profession. Our start came before emails and the internet. Before globalization. Before iPhones and iPads. Before many companies missed the boat.

Primerus' vision is to create what I like to call the law firm of the 21st century – a revolutionary model in the delivery of legal services. The law firm of the 21st century is one that meets clients' needs for the best service and value, shares common standards of quality and integrity, shares a single language with high tech communications and personally partners with clients to meet their needs. We look forward to an exciting future at Primerus.



Think Globally. Act Locally.

You have probably heard this phrase many times. It's an environmentalist's mantra that caught on decades ago, urging citizens to consider the global impact of their choices and to take action in their own communities to help save the planet.

But Primerus thinks it has an application in the health of the legal world as well – specifically to where the current legal industry is headed and how Primerus can make a difference to clients around the world, now and in the future.

Primerus was founded in 1992 to do something about the decline in the legal profession. Armed with the Six Pillars (Integrity, Excellent Work Product, Reasonable Fees, Continuing Legal Education, Civility and Community Service), it has done just that. Now, with its 170 law firms in 40 countries, Primerus has a unique ability to bridge the local and global needs of clients around the world – offering them everything they love about having a trusted advisor at a smaller local firm, as well as global connections to vetted attorneys with the expertise to meet any legal need they encounter.

Primerus attorneys act locally, following the Six Pillars in the choices they make every day, serving their communities, and meeting the needs of their clients with personalized, quality service for reasonable fees. They also think globally, relying on their fellow Primerus members around the world as their clients' needs arise in other practice areas or jurisdictions.

And that's exactly what today's legal industry needs.

"The fact of the matter is that most smaller firms will never be able to afford the infrastructure needed to achieve nationwide or global coverage," according to James Jones, senior fellow at the Center for the Study of the Legal Profession at Georgetown Law Center. "But at the same time, clients have these needs, and increasingly even a local matter will have global implications for a client. Firms have to find a way to compete on that front and be able to offer services in a more seamless way. Organizations like Primerus offer the possibility of doing that."

According to Primerus President and Founder John C. Buchanan, the door is now wide open for a concept in law design that Primerus calls "the law firm of the 21st century."

"There is a saying I heard recently that is very appropriate to Primerus' mission of becoming the law firm of the 21st century – a new model in the delivery of very high quality legal services, at reasonable fees, anywhere in the world," he said. "The saying came from Steve Jobs, who said 'The best way to predict the future is to invent it.' I could not agree more."

Buchanan said that model includes providing high quality legal services at very reasonable fees; using the "practice group" or "boutique" model of specialists to define the size of the law firm (generally small to medium-sized firms); using the "franchise business model" to join with other law firms for marketing, branding and cost-sharing efficiencies; and allowing unlimited

expansion compared to the large firm model because there are no capital, management or conflict issues to contend with.

The New Legal Market

According to the 2014 Report on the State of the Legal Market from Georgetown University Law Center and Peer Monitor released in January, the law firm market has become much more intensely competitive over the past five years, and has shifted from a sellers' market to a buyers' market.

"Fundamental decisions about how legal services are delivered – including staffing, scheduling, strategies and how firms charge for their services – are increasingly being made by the clients, and not by the law firms," a press release about the report stated. "Clients are increasingly pushing back on these issues and more."

Jones, the lead author of the report, said clients are interested in a more efficient and cost effective delivery of legal services, creating a "golden opportunity" for smaller firms.

"This is all good news for firms the size of Primerus firms if they manage to take advantage of it," he said. To do that, firms need not just be small, but also nimble and flexible in responding to client needs.

"They must watch what's going on in the market and be ready to respond in ways that larger firms cannot," he said. "It requires a real strategic focus."

"We can pass along a lower, more flexible fee arrangement than a large firm, particularly when there's volume involved. At the same time, we can give them excellent quality."

The legal industry has, in fact, seen movement of business to smaller firms and a resulting reduction of market share for larger firms, Jones said. "This is the time (for smaller firms) to shine by trying to think creatively about how to deliver services more efficiently."

The report cites a recent survey conducted by AdvanceLaw, in which general counsel at 88 major companies were asked about their willingness to move high stakes work away from "pedigreed firms" (defined as AmLaw 20 or Magic Circle firms) to other law firms, assuming a 30 percent difference in cost. The survey showed that 74 percent would be inclined to use the "less pedigreed" firm. The survey also revealed that 57 percent of respondents found lawyers at pedigreed firms to be less responsive, while only 11 percent found them more responsive, the report said. The report also cited an Altman Weil Chief Legal Officer survey in which 40.5 percent of respondents indicated they had shifted work to lower-priced outside law firms in the previous 12 months.

"What these results suggest is that brand value – in this case the brand value of the largest and historically most prestigious firms in the legal market – may be losing some of its luster as increasingly savvy general counsel select outside law firms based on considerations of price and efficiency and not on reputation alone," the report said.

Competing with Larger Firms

Gary Stiphany, shareholder at Primerus member firm Garbett, Stiphany, Allen & Roza in Miami, Florida, has found this trend to be true at his firm, which specializes in commercial litigation, banking and finance, intellectual property and antitrust litigation, and commercial real estate and transactions. For 25 years, the firm has been the same size – in the 12- to 14-lawyer range.

"It's a new economy, and more and more we are able to compete on a value cost basis more than large firms for a simple reason – we don't carry the overhead," Stiphany said. "We can pass along a lower, more flexible fee arrangement than a large firm, particularly when there's volume involved. At the same time, we can give them excellent quality."

Stiphany said that in fact, three of the four shareholders in his firm came from

large, iconic law firms. While a large law firm was a great place to start after law school, he said, he didn't feel he was getting enough courtroom experience. "You can't read a book and learn how to try a case," he said. "It was a hard, but right, decision."

His law firm has an excellent reputation in South Florida, representing past and current clients including fashion industry greats Michael Kors, Nike, Guess, Tommy Hilfiger, Chanel and Versace.

"The best part is that when I get a call from a general counsel asking for an update on a matter, I don't have to say, 'Can I get back to you?' and talk to junior counsel," he said. "While we are very sensitive to make sure the right task gets delegated to the right level, every matter has a shareholder in charge of it and every shareholder knows his or her matters. Clients like the instantaneous feedback. We compete well, and clients are getting it. Legal budgets are being slashed across the board in every company we represent. You have to get more creative and efficient."

Jones said this kind of personal, open dialogue with clients is the biggest issue facing law firms today regarding client relations. "You have to talk to your clients," Jones said. "It's amazing the number of lawyers who don't do that… The lawyers who are the best developers of business learn how to do that – not trying to sell them something, but understanding what their issues and challenges are."

Stiphany said his firm's Primerus membership also helps them compete. "It's a well-known organization, and it's well known that only the finest firms are invited to join and are accepted," he said. "We represent corporate clients, and they have a lot of choices in law firms where they can go. You need not only exposure, but also the right kind of exposure. With Primerus, we're out there now and being shown to clients with our best foot forward."

Clients More Interested in Value than Size

Another key message of the report warns law firms against growth just for growth's sake.

"In some circumstances, growth of a law firm makes perfect sense," Jones said. "But growth for growth's sake doesn't make sense; it ought to be very strategic... Clients are interested in more efficient and cost effective delivery of legal services and in some ways, size can count against that."

The report says that once firms reach a certain size, "diseconomies of scale" become a factor. "Large firms with multiple offices – particularly ones in multiple countries – are much more difficult to manage than smaller firms. They require a much higher investment of resources to achieve uniformity in quality and service delivery and to meet the expectations of clients for efficiency, predictability and cost-effectiveness," the report says.

According to Buchanan, Primerus helps firms and clients alike avoid these pitfalls. Most Primerus firms range from 15-20 attorneys in size. Each Primerus firm around the world operates independently from one another, avoiding diseconomies of scale, and allowing for unlimited expansion compared to the large firm model by avoiding capital, management and conflict of interest issues.

But the firms and by extension, their clients, enjoy the benefits of a global alliance, including cost sharing efficiencies for marketing and branding, assurance that all members have met stringent quality standards for membership, and shared commitment to values reflected in the Six Pillars (integrity, excellent work product, reasonable fees, continuing legal education, civility and community service).

"The Primerus vision is to create a new type of world class law firm worldwide," Buchanan said. "Instead of the large law firm with many practice groups, we bring together hundreds of the best boutique law firms around the world. We share the same values and work together as one unit, partnering with clients to offer them enhanced value and high quality legal services at low costs anywhere in the world. We're thinking locally and acting globally." P

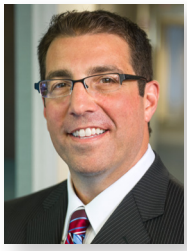
The Government is Turning Up the HEAT on Hospice Providers

According to a report issued by the Department of Health & Human Services (HHS) and the Department of Justice (DOJ), between 2005 and 2011, Medicare spending on hospice care for nursing home residents increased by 70 percent.[1] As a result of this increased spending, hospice reimbursement has come under scrutiny, particularly since the formation of the Health Care Fraud Prevention and Enforcement Action Team (HEAT) in May 2009 by HHS and the DOJ. During 2012 alone, the federal government won or negotiated over $3 billion in health care fraud judgments and settlements.[2] This article will discuss some of the publications issued by the HHS Office of Inspector General (OIG) that provide a window into where enforcement will be focused, as well as recent investigations, cases and settlements in the hospice world.

General Inpatient Care

The OIG recently released a report focusing on hospice general inpatient care (GIP), under which short-term pain control or symptom management that cannot be managed in other settings is provided in an inpatient facility (a Medicare-certified hospice inpatient unit, a hospital or a Skilled Nursing Facility (SNF)).[3] The report noted that the "Centers for Medicare & Medicaid (CMS) staff expressed concerns about possible misuse of GIP, such as care being billed for but not provided, long lengths of stay, and beneficiaries receiving care unnecessarily." Medicare paid $1.1 billion for GIP in 2011, mostly for care provided in hospice inpatient units. Twenty-three percent of hospice beneficiaries in 2011 received GIP, with one-third of the stays exceeding five days. Conversely, 27 percent of Medicare hospices did not provide any GIP, and some of these hospices did not provide any level of hospice care other than routine home care.

In the report, the OIG indicated that it is committed to further review of long lengths of stay and the use of GIP in inpatient units, and will conduct a medical record review to assess the appropriateness of GIP provided in different settings. The OIG also suggested that CMS focus on hospices that do not provide GIP to ensure those hospices are offering the necessary levels of care to beneficiaries. Moreover, the report cited that in December 2011 the DOJ reached a $2.7 million settlement in a qui tam action filed against Arkansas Hospice, Inc., for allegedly billing Medicare for GIP when beneficiaries actually received routine home care, which has a lower reimbursement rate. This settlement is a clear indication that the DOJ and OIG are serious about auditing GIP claims and joining suits to recover alleged false claims.



Drew Barnholtz

Drew Barnholtz joined Schneider, Smeltz, Ranney & LaFond in 2013. He brings his background as a former general counsel and compliance officer to focus on transactional, corporate and healthcare regulatory matters at the firm.

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Hospice Marketing Practices and Financial Relationships with Nursing Facilities

In addition to GIP, in its 2013 Work Plan, the OIG stated it will focus on hospice marketing practices and financial relationships with nursing facilities. The OIG's Office of Evaluation and Inspections (OEI) was tasked with reviewing marketing materials and practices by hospices to determine if they are overly aggressive or incorrectly define the Medicare hospice benefit and eligibility criteria. In a 2009 report, the OIG found that 82 percent of hospice claims for nursing facility beneficiaries did not meet Medicare coverage requirements.[4]

This is not a new area of concern for the OIG. The OIG issued a report in July 2011 that focused on the relationships between hospices and nursing homes.[5] The report found that almost 300 of the hospices surveyed had more than two-thirds of their beneficiaries residing in nursing facilities in 2009 (referred to as "high-percentage hospices"). The OIG pointed out in the report that 72 percent of high percentage hospices were for-profit, compared to 56 percent of all hospices, and that for-profit hospices, on average, were reimbursed 29 percent more per beneficiary than nonprofit hospices and 53 percent more per beneficiary than government-owned hospices. The OIG's recommendation was that CMS monitor high percentage hospices closely and examine whether these hospices are meeting Medicare requirements. It is clear that the OIG will be keeping a watchful eye on marketing practices targeting hospice beneficiaries, as well as on high reimbursement care administered in the hospice environment.

Recent Hospice Enforcement Actions

The increased scrutiny and examination of hospice activities referenced above has resulted in significant actions and recoveries by the DOJ and OIG. In May 2013, the DOJ filed suit against Vitas Innovative Hospice Care (Vitas), the nation's largest for-profit hospice chain, alleging false Medicare billings for hospice services. The complaint against Vitas alleged that Vitas paid employees bonuses tied to the number of patients they enrolled for crisis care services when those services were not reasonably medically necessary. The complaint further alleged that Vitas used "aggressive marketing tactics and expected their employees to increase the number of crisis care claims submitted to Medicare, without regard to whether the crisis care services were appropriate."[6] Finally, the complaint alleged that Vitas offered "intensive comfort care" services in one of its brochures and "misled patients and their families to believe that the Medicare hospice benefit would routinely cover around the clock care for hospice patients, absent the requisite acute medical symptoms resulting in brief periods of crisis."

In March 2013, Hospice of Arizona L.C., a hospice management company, agreed to pay $12 million and enter into a corporate integrity agreement to resolve allegations that Hospice of Arizona, along with its related entity and parent corporation, submitted or caused the submission of false Medicare claims for patients who were ineligible to receive end of life benefits, or for whom the hospice submitted bills at a higher reimbursement than it was entitled. The government alleged that Hospice of Arizona pressured staff to find more patients eligible for Medicare, adopted procedures that delayed and discouraged staff from discharging patients from hospice when they were no longer appropriate for such services, and did not implement an adequate compliance program that might have addressed these problems. The allegations arose under a qui tam lawsuit filed by a former Hospice of Arizona employee. The former employee who filed the underlying qui tam action received $1.8 million as her share. After reaching the settlement, Stuart F. Delery, Principal Deputy Assistant Attorney General for the DOJ's Civil Division, noted that "[T]his settlement is the result of the Justice Department's efforts to prevent misuse of the taxpayer-funded Medicare hospice program, which is intended to provide comfort and care to terminally ill persons at the end of their lives."[7]

Conclusion

It is clear that the DOJ and HHS will continue to target and pursue hospice care providers through the HEAT initiative. Hospice care providers should have strong compliance programs that address quality of care concerns, as well as implement and update their procedures for submitting claims to Medicare. Hospice care providers should also engage skilled resources to ensure hospice beneficiaries are properly enrolled and that claims are submitted for the accurate level of care. A culture of non-retaliation should be encouraged to avoid the potential for former or current employees to file qui tam lawsuits under the False Claims Act. The effects of a government investigation and whistleblower suit can be painful, not only from the payment of significant fines and negative publicity, but also the possibility of entering a corporate integrity agreement. Moreover, in certain cases, hospice providers can be excluded by HHS from Medicare or criminal indictments may be filed against the hospice provider pursuant to the federal health care fraud statute or the federal Anti-Kickback Statute. P

1 See The Department of Health and Human Services and The Department of Justice Health Care Fraud and Abuse Control Program Annual Report for Fiscal Year 2011 at 48 (Feb. 2012), *available at* http://oig.hhs.gov/publications/docs/hcfac/hcfacreport2011.pdf.

2 See The Department of Health and Human Services and The Department of Justice Health Care Fraud and Abuse Control Program Annual Report for Fiscal Year 2012 at 1 (Feb. 2013), *available at* https://oig.hhs.gov/publications/docs/hcfac/hcfacreport2012.pdf.

3 See Office of Evaluation & Inspections, Office of Inspector Gen., U.S. Dep't of Health & Human Servs., Medicare Hospice: Use of General Inpatient Care (No. OEI-02-10-00490, May 2013), *available at* https://oig.hhs.gov/oei/reports/oei-02-10-00490.pdf.

4 See Office of Evaluation & Inspections, Office of Inspector Gen., U.S. Dep't of Health & Human Servs., Medicare Hospice Care For Beneficiaries In Nursing Facilities: Compliance With Medicare Coverage Requirements (No. OEI-02-06-00221, September 2009), *available at* http://oig.hhs.gov/oei/reports/oei-02-06-00221.pdf.

5 See Office of Evaluation & Inspections, Office of Inspector Gen., U.S. Dep't of Health & Human Servs., Medicare Hospices That Focus On Nursing Facility Residents (No. OEI-02-10-00070, July 2011), *available at* https://oig.hhs.gov/oei/reports/oei-02-10-00070.pdf.

6 See *United States v. Vitas Hospice Services, LLC., et al.* Case No. 4:13 cv-00449-BCW (W.D. Mo. May, 2013).

7 See Press Release, U.S. Dep't of Justice, Office of Pub. Affairs, Hospice of Arizona and Related Entities Pay $12 Million to Resolve False Claims Act Allegations (Mar. 20, 2013), *available at* http://www.justice.gov/opa/pr/2013/March/13-civ-326.html.

Excess Insurance Policies and the Effect of Insolvency on Exhaustion Clauses and "Drop Down" Coverage

The recent economic recession in the U.S. has impacted the practice of insurance law in many ways, not the least of which has been the effect of massive insolvency on insurance coverage issues. Many self-insured companies and primary insurers fell into bankruptcy during this time creating insurance coverage issues for their excess carriers. While in bankruptcy, of course, self-insured companies and insurers were largely protected from tort claims by the automatic stay, including catastrophic claims. Often times during bankruptcy, many claimants who have been left without recovery or even unsatisfied judgments, sought redress outside of the bankruptcy court. They pursued the excess carrier by way of declaratory judgment for "drop down" coverage to cover unsatisfied claims from dollar one. Because of the recent increases in insolvencies, this issue has again come to the forefront in insurance policy drafting and insurance litigation. Excess policies vary considerably and courts rely on different policy provisions in reaching different results on this issue in various jurisdictions around the country.

The requirements and formulas that determine exhaustion of the coverage limits or retentions in the primary layer are often what determine the rights and obligations of an excess carrier in those cases. Generally, the insured's primary coverage must be exhausted by actual payment of the policy limit amount. In some cases, however, the policyholder can settle for less than the underlying policy limit, absorb the gap between the settlement and the primary limit, and then seek coverage from the excess insurer for the balance. The scenarios can vary significantly, and both decisional law as well as policy construction will ultimately determine the excess carrier's duties and obligations under each circumstance. In addition, it is important to understand that courts regularly confuse an excess carrier's obligation to pay under the excess policy following the exhaustion of the primary limits with the limits of liability section of the policy, which is what courts should rely on to determine if there is "drop down" coverage to begin with.

The Second Circuit's decision in *Zeig v. Massachusetts Bonding & Insurance Co.* is an interesting decision often cited for the proposition described above, 23 F.2d 665 (2nd Circuit 1928). The Court in *Zeig* found that construing the excess policy's exhaustion clause to mean that the plaintiff in the underlying tort claim actually had to collect the full policy limit was "unnecessarily stringent." *Id.* at 666. The court reasoned that the defendant, the excess insurer, had "no rational interest in whether the insured collected the full amount of the primary policies,

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so long as it was only called upon to pay such portion of the loss as was actually in excess of the limits of those policies." Id. The court weighed the implications of construing the exhaustion clause "[t]o require an absolute collection of the primary insurance to its full limit," finding that such interpretation would often result in "delay, promote litigation, and prevent an adjustment of disputes, which is both convenient and commendable." *Id.*

A more recent California appellate case held that *Zeig* did not apply where an excess policy had specific clauses regarding full payment by the primary layer of insurance prior to the triggering of the excess carrier's obligations. *Qualcomm, Inc. v. Certain Underwriters at Lloyd's, London.* 161 Cal. App. 4th 184, 199 (2008). The court there found that Zeig and its progeny contained "the policy rationale favoring the efficient settlement of disputes between insurers and insureds, a rationale that in our view cannot supersede plain and unambiguous policy language [citations omitted]." *Id.*

Insolvency of the primary layer of insurance can certainly affect the ability of tort claimants to collect proceeds, thereby impacting exhaustion of underlying policy limits. A Seventh Circuit case followed an Illinois state court decision in noting that "in cases of insolvency, the retained limit language means that an excess insurer is not obliged to pay costs that would otherwise be borne by the insolvent insurer, but instead is only responsible for providing coverage in excess of the underlying policy limits. *Premcor USA, Inc. v. Am. Home Assur. Co.*, 400 F.3d 523 (7th Circuit 2005) citing *Donald B. MacNeal, Inc. v. Interstate Fire & Casualty Co.*, 477 N.E.2d at 1325 (quoting Molina v. U.S. Fire Ins. Co., 574 F.2d 1176, 1178 (4th Cir. 1978)). This holding aligns with the *Zeig* decision in that excess coverage, depending on the specific policy language, only requires the excess carrier to pay anything above the primary layer's coverage amount, but not to "drop down" and cover from the first dollar owed.

Interestingly and somewhat dangerously, some courts have liberally interpreted excess policy language with the terms "collectible" or "recoverable" to require the excess insurer to drop down in the event of the primary insurer's insolvency and cover from dollar one of the primary policy. In a widely publicized Massachusetts Supreme Court case, the court resolved an ambiguity resulting from the aforementioned terms in favor of the insured, requiring an excess carrier to "drop down" to indemnify an insolvent primary insurer. *Gulezian v. Lincoln Ins. Co.*, 399 Mass. 606, 611-612 (1987). Importantly, the court there also noted that "[i]t seems likely that the [excess carrier] did not contemplate the insolvency of a scheduled underlying insurer in drafting its policy. The phenomenon of the insolvency of an insurer is not, however, so rare as to excuse that omission of attention to detail." Thus, the court does place some burden on the excess carrier to write policies with some care to avoid ambiguities resulting in an unintended coverage requirement. *See also Reserve Ins. Co. v. Pisciotta,* 640 P.2d 764, 772 (Cal. 1982); *MacNeal, supra; Lechner v. Scharrer,* 145 Wis. 2d 667 (1988). There are a number of courts across the country that have agreed in principle with *Gulezian* and its progeny and have found drop down coverage to exist under similar circumstances.

The idea behind these rulings is that when the excess carrier uses such terms as "collectible" or "recoverable" in describing the lower limit in its excess policies, from the insured's point of the view, the excess carrier will only provide excess coverage when the primary limit is collectible or recoverable, but presumably will provide primary or drop down coverage when it is not collectible or recoverable. While the excess policies containing this language do not specifically say that, courts have held that as an excess carrier, it is imperative to avoid any ambiguity that might lead the insured to believe there could be primary or "drop down" coverage by the excess carrier in the event of an insolvency. *See also Morbark Industries v. Western Employers Insurance*, 170 Michigan App. 603, 429 N.W.2d 213 (Mich. Ct. App. 1988).

Other courts have found exactly the contrary. In a Seventh Circuit ruling, the court concluded that the excess carrier "did not contract to bear the risk of the primary carrier's insolvency, nor do its premiums reflect the cost that the assumption of this risk would entail." *Zurich Ins. Co. v. Heil Co.*, 815 F.2d 1122, 1126. In *Radiator Specialty Co. v. First State Ins. Co.*, the court similarly held that "[i]t would simply make no sense to hold that an 'excess' insurer should be liable as a primary insurer due to a primary insolvency. This would impose a liability on the 'excess' insurer which is not bargained for in its premium that is based on the lesser risk which an excess carrier agrees to assume." 651 F. Supp. 439, 442 (1987).

While state and federal decisions remain split and incongruous on the issue depending on the federal circuit or the state jurisdiction, it is clear that most courts rely heavily on an interpretation of the policy language itself to determine the outcome in these declaratory judgment actions. As such, it is imperative that excess carriers employ policy language that will protect them from having to subsume the risk and cost of the underlying policy and to avoid drop down coverage from dollar one. There is no doubt that insolvencies of primary carriers and self-insured entities are not only possible but probable in this economic environment. Excess carriers who continue to incorporate ambiguous language in their policies on the lower limit of coverage open themselves up to insurance coverage litigation as well as possible indemnity exposure for large sums not contemplated by their premiums.

What Every Start-Up Company Should Know About Trademarks, Patents and Copyrights

Being sued for infringement is no way to start an enterprise! A start-up company's ability to operate, grow and prosper depends on up-front due diligence investigations and appropriate agreements regarding trademarks, patents and copyrights. Engaging in this groundwork early will safeguard against subsequent disputes.

Trademarks

Trademarks are valuable assets that protect goodwill. A trademark helps a consumer identify the source of a product or service. In an era flooded with imagery and information, it is vital to choose a brand wisely to stand out.

"What's in a Name?" – Avoiding Generic and Descriptive Marks

In order to stand out, avoid adopting generic or descriptive terms for products or services. A generic term is one that consumers identify as the common name for a product or service – think Kleenex®. Suppose you have discovered a novel way to brew beer using dewberries. You decide to brand the beer as "beer." Not so fast: trademark law would prohibit you from registering (and therefore protecting) a federal trademark for the name "beer" because it is generic, and a marketing professional would advise against it because the name "beer" is incapable of distinguishing your beer from Joe Blow's beer.

But let's say that you yearn to call your beer "Dew Beer Berry." Slow down! While "Dew Beer Berry" is stronger than the generic term, "beer," it still risks being considered descriptive in the eyes of the law and indistinguishable from other dewberry beers in the minds of the public. You are not alone – many businesses select a brand name that *describes* their product or services because they want consumers to understand what they are selling. The trouble with this is that calling dewberry beer "dew beer berry" will likely not prevent competitors from marketing their beers under the terms "dew," "beer," or "berry," because these are generic terms associated with the product, dewberry beer.

When you lose the power to prevent others from using brand names that include terms similar to your name, you begin to lose control over your reputation. Furthermore, your individuality when compared to all the other dewberry beer breweries is limited. Your brand risks looking and feeling similar to other brands trying to describe their product or service with similar names. To overcome this, avoid selecting a descriptive brand name. Save the descriptive terms for the "about us" section of your website. Think outside the box, select a unique brand name, and let your brand name serve the purpose of distinction.

The strongest trademarks are arbitrary or fanciful. They involve commonly known terms but apply them to a product or service that is unrelated – e.g., Apple® computers.

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Fanciful trademarks are made-up terms. For example, what is "IKEA" aside from the Swedish store we all know? Nothing. It is simply an amalgamation of the initials of the founder's name, his home village and a nearby village. In our hypothetical, we might try something arbitrary like Hammer Head beer or something fanciful like Dunding beer, inspired by our firm's name Dunlap Codding.

"Clear!" – Is Your Brand Name Available?

You must also clear your brand name before using it. You must have a trademark clearance search conducted to determine whether someone else is already using the same or similar name. You want to be able to answer these questions: "Can my start-up company use the proposed mark on my products or services with reasonable risk?" and "Can my mark be registered with the United States Patent and Trademark Office (USPTO)?"

A trademark search involves searching USPTO records for registered and pending marks as well as searching the Internet and many other databases for unregistered marks. If there are businesses already using a mark similar to your proposed mark (e.g., you find "Hammer Hand" used in connection with beer), there may be a conflict. It is best to uncover these risks before you invest in a particular mark. Conduct a search before you adopt a mark, or be prepared to lose money, time and a bit of your reputation when you have to re-brand.

Patents

Patents are all about creating options. Presumably, anyone can manufacture and sell a product, but manufacturing and selling "bare," that is, without proprietary rights, invites more competition. However, when a company is armed with a patent, it can limit competition. Start-ups, in particular, can benefit from patent protection; a patent allows them to break through the mass of products and services already available and gives them the ability to exclude others from using their same patented product or service.

"Shhh!" – Discuss Your Ideas Carefully

The tendency of many start-ups to share their latest venture with friends, family and potential investors must be tempered to avoid disclosing information pertinent to patentability (as well as trade secret information). Once a start-up shares its secret weapon for success (i.e., its potentially patentable product or service), the patentability clock starts ticking in the United States. After disclosing an idea to the public or offering it for sale, an inventor has ***one year*** to file a patent application. If a start-up is thinking about marketing and selling its product or service internationally, it is even more important to keep a tight lid on an invention because many non-U.S. countries do not grant inventors the one-year grace period. Instead, any single disclosure can be cited as prior art against a patent applicant and therefore destroy the chances of patenting the idea.

Sizing Up Your Asset and Assessing Risks for Infringement

Do your homework before you manufacture and unleash a product or service to ensure that someone else's rights will not prevent or limit you from operating your business. Conducting a "prior art search" is the best way to investigate the proprietary landscape. This involves searching issued patents and applications which involve technology or components similar to those that your business is attempting to commercialize.

From an offensive standpoint, prior art searches assess whether the invention has a high potential for patent protection by evaluating whether an invention is new, useful and non-obvious in light of the prior art. Prior art generally includes issued patents, published patent applications, and evidence of prior sales and use. From a defensive standpoint, prior art searches identify current patents upon which a start-up's proposed product or service could infringe, if implemented. In other words, a start-up company needs to ask itself whether it even has the right to manufacture and sell its proposed product or service and therefore whether it is truly free to operate within its vision.

Even if a prior art search does reveal a problematic patent, businesses are able to further assess high-risk patents – e.g., to determine if they are valid. In the event a determination is made that the identified patents are not valid, then the business is in a more secure position to move forward with its proposed product or service without risking infringement.

Copyrights

Third Party Work for Hire Agreements

When it comes to copyrights, we cannot emphasize enough how important it is to be aware of the work for hire doctrine and the rights of independent contractors. Typically, the owner of a creative work is who you might think it is – the author. Under the work for hire doctrine, employers own the works created by their employees within the scope of employment. The situation often not considered is one involving independent contractors. Independent contractors own the works they create unless there is a written agreement stating otherwise. Therefore, it is crucial to have documented, clear agreements in place specifying ownership of copyrightable works before the creative process begins.

Conclusion

Keeping these few items in mind can help you spot and avoid some key risks for your start-up company.

Florida Mortgage Statute of Limitations: Why It's Becoming a Problem and What We Can Do About It

Florida courts are working through a new legal issue that threatens the enforceability of mortgages there. When foreclosure cases were filed over five years ago and were later dismissed, property owners began claiming that the statute of limitations prevents their mortgage holders ("lenders") from enforcing the note and mortgage. They are fighting foreclosures and seeking to cancel mortgages with this argument. This article lays out the legal issues, explains where legal uncertainty exists, and suggests ways that mortgage documents and mortgage servicing procedures can be adapted to protect lenders, investors and servicers.

The Legal Threat

Florida's statute of limitations on foreclosures is five years. For a variety of reasons, thousands of foreclosures were filed more than five years ago and were then dismissed – either voluntarily by the lenders or by the courts. Borrowers and investors are now arguing that when those cases were filed, the full mortgage balance was accelerated, and the statute of limitations began to run against all future payments. Therefore, five years after the case was filed, the statute of limitations bars a second foreclosure action, they argue.

Borrowers and real estate investors have used this argument as both a shield and a sword. They have used it as a shield to defend against repeat foreclosures, and they have used it as a sword in quiet title lawsuits seeking to cancel mortgage liens.

Uncertainty in the Courts

Trial courts handled this issue inconsistently at first. Some canceled mortgages outright; some declined to cancel mortgages but dismissed foreclosures as time barred; and others allowed the foreclosures to continue. More recently, lenders have won important battles. Two intermediate appellate courts and several federal trial courts in Florida have ruled that mortgages cannot be canceled.

However, the war is far from over.

The first appellate court case, *U.S. Bank v. Bartram*[1], is now before the Florida Supreme Court. Four parties in the case and five *amici curiae* ("friends of the court") intend to file briefs. Of these nine, two support the bank and seven oppose the bank. A $650,000 mortgage hangs in the balance. Moreover, the result could impact thousands of similar Florida mortgages worth hundreds of millions.[2] The Florida Supreme Court has the option whether or not to hear *Bartram*. If it does, the Court could uphold, modify or reverse the lower appellate court's ruling that the mortgage is valid.

Another appellate court followed *Bartram* and explicitly ruled that mortgages cannot be canceled until five years after maturity.[3] That makes two of Florida's five District Courts of Appeal on the side of lenders. The other three districts have not published opinions on the issue.

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Muddy Waters

Even when lenders win, imprecise legal opinions leave muddy waters in their wake.

Bartram is a prime example. The appellate court ruled that dismissal of the bank's first foreclosure case did not bar a second one, but only if the second one was "a foreclosure action *for default in payments occurring after the order of dismissal* in the first foreclosure…."[4] There is no apparent basis for requiring the second case to be based on a default after the order of dismissal in the first case. Any default within five years prior to the second case is within the statute of limitations and should be a viable basis for the second case. According to *Bartram*, a borrower could start submitting regular payments immediately after dismissal of his first foreclosure case and arguably prevent a second foreclosure even though the payments are several years in arrears.

Accounting Nightmare

Another concern raised in several cases is the indication that mortgage payments delinquent more than five years are uncollectible.[5] If true, that could be an expensive loss of principal, interest and escrow advances. It could also pose an accounting nightmare as servicers struggle to make servicing platforms reflect reductions in principal balances, accrued interest accounts, and escrow accounts based on court rulings that do not match the transaction history of the loan.

Loan Documents Support Full Debt Accounting

This potential accounting nightmare should be averted in most cases if courts pay close attention to the loan documents. Fannie Mae/Freddie Mac standard residential loan documents (and the like) include "full debt" promises by the borrower. Since the borrower promises to pay the full debt with interest (not just a series of installments) courts should not deduct the amount of "time barred" installments. For example, the note in Bartram contains the following payment terms. Paragraph 1: "… I promise to pay $650,000…, plus interest…." Paragraph 3: "If on March 1, 2035, I still owe amounts under this Note, I will pay those amounts in full on that date…." The mortgage contains similar language: "Borrower shall pay when due the principal of, and interest on, the debt evidenced by the Note…." Paragraph 1.

These terms obligate the borrower to pay the full debt even where courts rule that installments more than five years old are uncollectible.

Ways to Further Strengthen Loan Documents

Some minor revisions to standard loan documents would enable the mortgage industry to exert control over future cases and reduce the room for judicial interpretation.

First, add "deceleration" clauses. Although Florida courts seem to have accepted the concept of deceleration[6], there would be less room for judicial interpretation if the loan documents contained an express *deceleration* provision, much like the express *acceleration* provision in most notes and mortgages.

This provision should state that the lender can withdraw an acceleration of the debt at any time and that acceleration is automatically withdrawn by the dismissal of any lawsuit on the note or mortgage.

Second, add express language in which the borrower promises he "will pay the full debt even if some or all of the installment payments become unenforceable by operation of law."

Ways to Strengthen Default Servicing

Default loan servicing procedures and foreclosure procedures can also be updated to help lenders.

Send notices of deceleration whenever a case is dismissed. Even if there is no express deceleration provision in the loan documents, the lender is on higher ground with a deceleration notice than without.

Lastly, servicers can instruct foreclosure counsel when they file repeat foreclosure cases to allege *two separate breach dates* in the complaint. The first date should be the contractual due date according to the note. This is important for transparency and for calculating the correct debt balance when the time for judgment arrives. The second date should be a date after dismissal of the previous case in order to meet *Bartram's* "after the order of dismissal" requirement – at least until the Florida Supreme Court speaks. The complaint should clearly state that it is being filed based on the second breach.

Conclusion

Dismissed foreclosures in Florida have raised a high stakes legal issue: Did the filing of the dismissed case accelerate all future payments so that five years later no legal action can be filed? While the tide of judicial opinion currently favors the mortgage industry, it is too early to tell how it will turn out. Nevertheless, there are concrete steps the mortgage industry can take to create more favorable conditions in future cases and leave less room for judicial interpretation. P

1 *U.S. Bank Nat. Ass'n v. Bartram*, 140 So. 3d 1007 (Fla. 5th DCA 2014).

2 One putative class plaintiff alleged there are 50,000 mortgages affected by this issue. *Torres v. Countrywide Home Loans, Inc.*, Case No. 14-20759-CIV-KMW (U.S. S.D.Fla. July 29, 2014).

3 *Evergrene Partners, Inc. v. Citibank, N.A.*, 39 Fla. L. Weekly D1342 (Fla. 4th DCA 2014)

4 *Bartram* at 1014..

5 *Id. (certified question); Isaacs v. Deutsch*, 80 So. 2d 657, 660 (Fla. 1955); *Cent. Home Trust. Co. of Elizabeth v. Lippincott*, 392 So. 2d 931, 933 (Fla. 5th DCA 1980).

6 *Singleton v. Greymar Associates*, 882 So. 2d 1004, 1008 (Fla. 2004); *Veredecia v. Bank of New York*, Case No. 13–62035–CIV, 2014 WL 3767668 (U.S. S.D.Fla. July 31, 2014).

Medicare and Liability Settlements: How to Spot Issues and Consider Medicare's Interests

When resolving a liability claim, the settling parties are required to consider Medicare's interests to avoid shifting any medical responsibility from a primary payer to Medicare. This obligation has been around since 1980, when the Medicare Secondary Payer (MSP) Act[1] was passed by Congress. However, the Centers for Medicare & Medicaid Services (CMS) have focused mostly on workers' compensation settlements, which have more clearly defined obligations for past and ongoing medical payments. But since then, the possibility of needing a Liability Medicare Set-Aside (LMSA) has seemed more of a myth than a reality. CMS did not formally acknowledge the LMSA until a 2009 update to the Medicare Secondary Payer Manual and a September 29, 2011, CMS Memorandum.[2]

Consideration of Medicare's interests is a two-step analysis of (1) medical expenses already paid by Medicare ("conditional payments"), and (2) future medical expenses which Medicare may pay (commonly referred to under the catch-all term "MSA").

Why Does It Matter?

CMS may pursue recovery from any primary payer or anyone who receives payment, directly or indirectly, from a primary payer. This opens liability to not only the insurance carrier, but also to the Medicare beneficiary, the plaintiff's attorney and even medical providers. Medicare may seek reimbursement for conditional payment liens, including double damages, taking priority over any other primary payers.[3] Medicare also has subrogation rights.[4] Medicare does not consider itself bound by the terms of settlement.

CMS may seek reimbursement or pursue subrogation when one of two things happens: (1) the medical portion of the claim settles; or (2) a final legal adjudication is reached establishing liability of a primary payer. So until the parties either settle the medical liability or resolve the matter in court, there can technically be no enforceable Medicare lien.

How Will Medicare Know?

Section 111 of the Medicare, Medicaid, and SCHIP Extension Act of 2007 (MMSEA) added certain mandatory reporting requirements for claims involving Medicare beneficiaries, including notification of how the claim is resolved. Once a claim is reported, Medicare can track related medical treatment by CPT medical codes submitted by medical providers seeking payment. If a reported claim is settled without considering Medicare's interests, particularly with regard to conditional payments, then Medicare will eventually find out and could seek reimbursement. The current penalty for failure to report under Section 111 is $1,000 per day, per claim. But regardless of mandatory reporting, the bottom line is the stakes are just too high not to consider Medicare's interests at all.

Are There Conditional Payments?

The parties must consider whether Medicare has already made any payment, conditioned upon the right to reimbursement, for medical services allegedly related to the underlying injury, for which the defendant may be deemed

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responsible by Medicare as a primary payer. Because these medical expenses have already been paid by Medicare, it necessarily involves a current Medicare beneficiary.

Upon notifying Medicare, a Rights and Responsibilities letter is issued. Within 65 days, the initial Conditional Payment Letter is sent to anyone attached to the claim. During these 65 days, the Benefits Coordination & Recovery Center (BCRC), which was previously the Medicare Secondary Payer Recovery Contractor (MSPRC), retrieves all available medical claims connected to the accident. The letter reflects the current lien amount, including dates of services, providers, and CPT codes. In some cases, medical providers may have up to 27 months to submit a bill, so conditional payments could trickle in even after settlement.

Several options are available to the Medicare beneficiary (or others with valid Consent to Release or Proof of Representation) for retrieving up-to-date conditional payment amounts, including the website MyMedicare.gov; Self Service Information Feature (866-677-7220); and the Medicare Secondary Payer Recovery Portal. The web portal allows uploading documents, requesting updates, disputing items based on relatedness, and submitting settlement information.

Beware of Medicare Advantage Plans

Some Medicare payments are actually made under Medicare Part C by a Medicare Advantage Plan. The law is unsettled, but the Third Circuit upheld a Medicare Advantage Plan's private cause of action to sue for double damages.[5] Such conditional payments may not be reflected on the Medicare Conditional Payment Letter. The beneficiary's Medicare coverage is a moving target, subject to change during open enrollment periods.

Is an MSA Needed?

No one is ever required to submit an MSA to CMS for approval. Unlike workers' compensation claims, there is currently no formal procedure for voluntary submission of liability settlements for review. Without the benefit of a formal guideline for CMS review, some best practices include consideration of the following:

- **Get an MSA proposal.** Confer with an MSA consultant regarding the need for an MSA allocation. If an MSA is appropriate, then establish an MSA account with proper funding and administration (either by self or professionally). In some situations, the circumstances may not warrant any allocation of funds, in which case a zero allocation may be appropriate. The underlying consideration is the defendant's responsibility to Medicare as a primary payer under the terms of the settlement and unique circumstances of the case. Again, with no formal submission allowed, many settling parties are relying upon the MSA proposal as the documentation of their consideration of Medicare's interests.
- **Get court approval.** In some jurisdictions, courts have been willing to consider whether the parties have properly considered Medicare's interests in approving a settlement. Sometimes the court may be willing to go so far as to determine the proper amount to be allocated towards a liability MSA.[6] Other courts may not be willing to make a finding absent Medicare's direct involvement, which typically requires a voluntary appearance.
- **Submit the LMSA to a CMS regional office.** Some CMS regional offices will routinely, albeit informally, review liability MSAs, but only on a case-by-case basis. It is believed that most regional offices now have informal, internal guidelines for reviewing liability settlements. If the amount of the settlement is substantial, CMS will likely take notice.

Are Other Options Available?

CMS has three options available exclusively for liability settlements.

- **Low Dollar Threshold ($300 Settlements).** Effective September 6, 2011, if an individual has received a settlement of $300 or less, Medicare will not recover conditional payments if the settlement is related to a physical trauma based incident (not ingestion, implantation, or exposure), no additional payments will be made, and Medicare has not already issued a recovery demand letter.
- **Certification from Treating Physician.** According to the September 30, 2011, CMS memorandum (Benson memo), if a treating physician certifies no future medical care is necessary related to the liability claim, then CMS will consider its interests protected with regard to future medicals.
- **Fixed Percentage for Conditional Payments.** Effective November 7, 2011, in liability settlements of $5,000 or less, a beneficiary who elects this option may resolve Medicare's recovery claim by paying 25 percent of the total settlement if the settlement is for a physical trauma based injury, the option is timely elected, Medicare has not already issued a recovery demand letter, and no additional payments are expected. Once elected, there is no right to appeal the fixed payment amount or request a waiver of recovery.

What Does the Future Hold?

We anticipate significant changes on the horizon. CMS published an Advance Notice of Proposed Rulemaking (ANPRM) on June 15, 2013, requesting comments on various options under consideration for liability settlements, including a voluntary submission process. The comment period has ended, but it remains unclear whether CMS may now issue a Notice of Proposed Rule Making (NPRM) or an Interim Final Rule. Additionally, once fully implemented, the Strengthening Medicare and Repaying Taxpayers (SMART) Act, will give parties important tools, including the ability to determine the exact conditional payment lien *before* a settlement is submitted. P

1 *See* 42 U.S.C. 1395y(b)(2)(A)(ii).

2 *See* ROY A. FRANCO & JEFFREY J. SIGNOR, MEDICARE SECONDARY PAYER COMPLIANCE, THE LIABILITY CASE 80 (2d ed. 2012).

3 *See* 42 U.S.C. 1395y(b)(2)(B)(iii).

4 *See* 42 U.S.C. 1395y(b)(2)(B)(iv).

5 *See In re: Avandia Mktg.*, 685 F.3d 353 (3d Cir. 2012), *cert. denied GlaxoSmithKline v. Humana Medical Plans, Inc.*, No. 12-690, 569 U.S. ___ (Apr. 15, 2013)(allowing private cause of action under 42 U.S.C. § 1395y(b)(3)(A)).

6 *Benoit v. Neustrom*, 2013 U.S. Dist. LEXIS 55971 (W.D. La. Apr. 17, 2013)

Some Employment Arbitration Issues You May Not Have Considered

Most employment lawyers advise their employer clients to have employees sign mandatory arbitration agreements, particularly with regard to discrimination and wrongful discharge claims. While this generally is considered sound advice as it avoids bad publicity, time-consuming and expensive litigation and runaway jury verdicts, did you know the following? Your client might have to pay the full cost of the arbitration if the former employee refuses to pay his share due under the arbitration agreement, or your client might find itself in court on the claims it intended to arbitrate? The arbitrator may lack the authority to issue pre-hearing subpoenas to non-parties to enable you to obtain discovery? Your client might be stuck simultaneously having to arbitrate with signatories to the agreement and litigate very similar or even identical claims against related non-signatories to the arbitration agreement? Your client may face unfair labor practice charges under the National Labor Relations Act ("NLRA" or the "Act"), if the arbitration policy precludes an employee from filing a collective or class action in arbitration? Finally, did you know an arbitrator lacks the authority to enforce an order issued during the arbitration and even the ultimate award? As a result, when a former employee still has company records or property, the employer will have to bring an action in court to compel their return. As discussed below, be careful what you wish for and choose the language you use carefully when drafting an arbitration clause in an employment agreement.

Why Are Our Officers Subject To Arbitration When They Didn't Sign An Arbitration Agreement?

It is beyond the scope of this article to discuss the law with regard to whether an arbitrator or the court decides the question of what issues and what persons (other than direct signatories) are bound by an arbitration agreement. However, keep in mind that in certain jurisdictions, incorporating the rules of the American Arbitration Association ("AAA"), JAMS or a similar body by reference in an arbitration agreement may empower the arbitrator to make this determination. This not only includes any objections with respect to the existence, scope or validity of an arbitration agreement, but also the arbitrability of any claim or counterclaim. This may result in an arbitrator deciding that officers or directors of your corporate client are proper parties to the arbitration on an unrelated third-party claim filed by a former employee, even though the officers or directors were not parties to the contract containing the arbitration provision. Moreover, if the officers or directors challenge that determination in court, various reported cases, including one from the United States Supreme Court, have held that courts under those circumstances must defer to an arbitrator's arbitrability decision. That is, courts "must" give considerable leeway to arbitrators and should set

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aside these decisions only in certain narrow circumstances, utilizing the same standard courts apply when deciding whether to confirm an arbitration award.

Why Are We In Court When We Agreed to Arbitrate?

Let's assume your employer client, as the claimant, is happy to be in arbitration rather than court. What happens if a respondent disagrees and, therefore, refuses to pay his or her share of the arbitration fees and costs? The employer should be able to obtain a default against respondent, correct? Not so fast. The arbitration body might simply suspend the proceedings. Alternatively, it might order claimant (your client) to pay respondent's share of the arbitration expenses upfront, with those outlays being dealt with as part of any final award. (See AAA Employment Arbitration R-47.) Moreover, under those circumstances, your client's refusal to pay respondent's share may also result in a finding by the arbitration body that your client waived its right to proceed in arbitration and that the matter should proceed in court (which is what your client wanted to avoid in the first place).

Why Can't We Subpoena Documents In Advance of the Hearing?

Section 7 of the Federal Arbitration Act ("FAA") deals with discovery from non-parties in arbitration. Paraphrasing, it provides that the arbitrator may summon in writing non-parties to appear at the hearing as witnesses and to bring documents with them. The question that arises is whether arbitrators may issue subpoenas to require non-parties to produce documents in advance of the hearing.

Whether a court will enforce a pre-hearing subpoena depends upon the circuit. Some courts, including the Sixth and Eighth Circuits, have held that the power to order pre-hearing document production is implicit in the power to order the production of documents at a hearing. Others, such as the Second and Third Circuits, disagree, finding that Section 7 of the FAA unambiguously limits an arbitrator's subpoena power to instances in which the non-party actually appears at the hearing. Other courts, such as in the Fourth Circuit, generally will not allow pre-hearing discovery from non-parties without a showing of hardship or special need. The bottom line is consider your circuit's law when deciding whether to include an arbitration clause in an agreement and if you should incorporate a choice of law provision. If you believe a breach of an agreement will lead to a proceeding in which you will need access to voluminous documents from non-parties to review in advance of a hearing, make sure your circuit does not allow arbitration's goals of efficiency and reduced costs to trump your discovery needs.

Why Are Unfair Labor Practice Charges Being Filed Against the Company?

Under Section 7 of the NLRA, employees have the right to engage in concerted activities for the purpose of collective bargaining or other mutual aid and protection. Therefore, employees have challenged arbitration agreements that preclude them from filing a collective or class action in arbitration by filing unfair labor practice charges pursuant to Section 8(a)(1) of the Act. While the law still remains somewhat unsettled, with most courts enforcing those provisions, NLRB judges have been finding that these class action waivers violate federal labor law under the NLRB's D.R. Horton decision and have ordered employers to cease and desist from maintaining these class or collective action waivers.

Why Can't We Get Our Documents Back Or Enjoin Our Former Employee?

When drafting an arbitration clause, be sure to have a carve-out allowing your client to go to court for injunctive relief. The 'finality rule' generally limits judicial review by a district court to final arbitration awards, but courts usually will enforce interim awards by an arbitrator to preserve the integrity of the arbitration process. (See FAA 9 U.S.C. §10(a) (1)-(3).) However, arbitrators have no power to enforce their decisions. Therefore, an interim award requiring a former employee to return the company's documents, or to abide by a non-compete agreement pending the arbitration of that claim, can only be enforced by a court willing to entertain an application prior to the conclusion of the arbitration.

Conclusion

Arbitration for employers is advantageous in a number of important and well known respects. However, there are other important issues for you and your clients to consider both when deciding whether to include an arbitration clause and when drafting the agreement. P

Third Circuit Upholds FLSA Claims Against Successor Entity

In *Thompson v. Real Estate Mortgage Network*, 2014 U.S. App. LEXIS 6150 (3d Cir. April 3, 2014), the Third Circuit Court of Appeals, in a precedential decision, joined the U.S. Courts of Appeals for the Seventh and Ninth Circuits and applied the federal common law standard to evaluate whether the plaintiff sufficiently pleaded a Fair Labor Standards Act (FLSA) successor liability claim against the company that purchased her now defunct employer. Applying this standard, the Third Circuit upheld plaintiff's FLSA claims against the successor entity.

Background

Patricia Thompson, a New Jersey resident, was hired as a mortgage underwriter by defendant Security Atlantic Mortgage Company ("Security Atlantic"). Shortly thereafter, however, she was assigned to a training class led by a representative for a different mortgage company, defendant Real Estate Mortgage Network (REMN). That employee "represented that REMN was a sister company of Security Atlantic." In February 2010, allegedly in response to an investigation being conducted by the U.S. Department of Housing and Urban Development (HUD) into Security Atlantic's mortgage practices, Thompson and many of her colleagues were asked by supervisors to fill out new job applications to work for REMN. Thompson completed the application as requested. From roughly that date forward, Thompson's paychecks were issued by REMN. Defendants characterized Security Atlantic, which is no longer in business, as "defunct." Despite Thompson's transfer to REMN, virtually no change occurred in on-site operations. Thompson and her colleagues continued to do the same work at the same location. Thompson's pay rate and direct supervisors remained the same. Thompson alleges that no employees were laid off during this transition, although some of her colleagues continued to receive paychecks from Security Atlantic.

Thompson quit in August 2010, not long after Security Atlantic's Executive Vice President told her that the company did not pay overtime to underwriters. She filed a lawsuit claiming that throughout her tenure with Security Atlantic and REMN, employees were treated as salaried workers exempt from overtime pay and were required to work more than 40 hours per week, including nights and weekends. In addition, Thompson sought to hold REMN liable for Security Atlantic's own statutory violations under theories of joint liability and successor liability.

State vs. Federal Law

One issue addressed by the Third Circuit in evaluating whether Thompson sufficiently plead her claims against either defendant was whether REMN, as an alleged successor to Security Atlantic, could be held liable for any wage-and-hour violations committed by its predecessor. In determining that issue of first impression, the Third Circuit examined whether the New Jersey state law test for successor liability applied

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or the less burdensome federal common law approach.

The parties disputed which law governed Thompson's FLSA successor liability claims. Thompson argued that, as to her FLSA claim, the court apply a federal common law standard for successor liability that has slowly gained traction in the field of labor and employment disputes over the years. The federal common law standard requires consideration of the following factors in determining whether successor liability should be imposed: "continuity of operations and work force" from the predecessor to the successor, the successor's notice of the predecessor's legal obligation, and the ability of the predecessor to provide the relief sought. By contrast, under New Jersey law, successor companies are considered legally distinct from their predecessors and do not assume any debts or obligations of the prior entity, except where: (1) the purchasing corporation expressly or impliedly agreed to assume such debts and liabilities; (2) the transaction amounts to a consolidation or merger of the seller and purchaser; (3) the purchasing corporation is merely a continuation of the selling corporation, or (4) the transaction is entered into fraudulently in order to escape responsibility for such debts and liabilities. The court agreed with Thompson that the federal law applied but found that an issue remained as to whether Thompson's allegations satisfy the federal common law standard in the case at hand.

Successor Liability

Considering the federal standard factors, the court found the allegations were enough to surmount a motion to dismiss under the federal standard. The court held that the first factor was satisfied finding that there was sufficient continuity in the operations and work force when REMN took over Security Atlantic, since essentially all aspects of employment remained the same. Second, while the complaint did not clearly allege facts that show that REMN had knowledge of Security Atlantic's FLSA violations before the transfer, the plaintiff alleged that Security Atlantic's payroll and scheduling was controlled by her supervisors who later became officers of REMN, and after the transfer, the same practices and operations continued under the same management. As to the third factor, the predecessor's "ability . . . to provide adequate relief directly," defendants have represented that Security Atlantic is now "defunct," which the court interpreted to mean that it is likely incapable of satisfying any award of damages to plaintiff. In total, the Third Circuit found these allegations were enough to surmount a motion to dismiss under the federal standard.

The court also reinstated Thompson's claims under the New Jersey Wage and Hour Law, finding that her allegations satisfied the more restrictive state law standard as well.

Implications

The trend continues for federal courts to embrace a broad view in evaluating the question of whether federal FLSA liability may be imposed upon a successor company. Employers taking on workers through corporate acquisitions or who are faced with acquiring employees from related corporate entities should consider the potential FLSA ramifications. As more federal courts find companies liable under common law successor liability principles for FLSA violations, companies should require strict review of potential successor companies' wage and hour practices for all potential mergers and acquisitions.

Non-Compete Clauses: Uses and Enforceability

In a global climate where it is common for people to hold a multitude of different occupations and work in different locations throughout a lifetime, corporations continue to make efforts to protect business interests even after an employee leaves their company. Importantly, despite even the best employee leaving on good terms, a former employee could potentially become a direct competitor, solicit clients, and use a company's trade secrets. Protecting the corporate interest can depend on the ability to enforce a non-competition clause.

A non-competition clause, or non-compete clause, is a restrictive covenant that endeavors to prevent the employee from becoming a direct competitor of the employer upon departure from a company. Certain restrictive covenants specifically bind the employee by limiting employee's ability to work in a certain geographic location, or for a specified amount of time, or within a certain field and with certain clients.

Not all non-compete clauses are enforceable. In fact, non-compete clauses are generally unpopular and are met with reluctance in the court system.[1] A non-compete clause has the negative effect of limiting a person's ability to work, thus it is scrutinized carefully. Corporations must carefully consider the parameters of the non-compete clause as too many limitations on the former employee may prove ineffective.

To find a non-compete clause valid and therefore enforceable, New York courts apply a three-part reasonableness test. The general rule to determine if an employee's non-competition clause is enforceable is if, "(1) it is no greater than is required for the protection of the legitimate interest of the employer, (2) does not impose undue hardship on the employee, and (3) is not injurious to the public."[2] Therefore, reasonableness varies and the court will look at all the case specifics before making a determination of law. To be effective, the non-compete agreement should mirror this reasonableness standard.

First, the non-compete agreement should outline the corporation's legitimate business interest. The United States District Court for the Southern District of New York has considered that an employer's legitimate interest is 1) to prevent disclosure of trade secrets or employee/client solicitation, 2) to prevent disclosure of private client information, or 3) where employee's skill and service is considered "special or unique."[3] Sometimes, New York courts determine that the restrictive covenant is unnecessary and therefore the non-compete clause is ineffective. For example, in *Last v. New York Institute of Technology*, a doctor signed an anti-competition clause stating he would not work within 10 miles of the clinic where he was assigned to work.[4] The doctor was fired after refusing to relocate elsewhere with the clinic, and he remained in the area seeing patients. Despite signing an anti-competition clause and still practicing in the same area, the Second Judicial Department determined that

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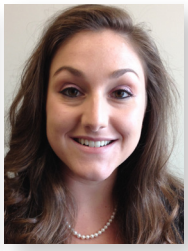

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since that employer relocated it was not in the employer's "legitimate interest" to prevent clients in the local area from receiving treatment from the doctor.

In other cases, however, New York courts have found a significant and legitimate employer interest that warrants upholding the non-compete clause. According to the Restatement Third of Employment Law § 8.07, restrictive covenants may be valid in order to protect employer's interests such as trade secrets or the misappropriation of client information.[5] For example in *Ticor Title Ins. Co. v. Cohen*, the Second Circuit Court of Appeals determined that a title insurance salesman's job was considered "unique" because he worked for the company throughout most of his career, was one of its highest paid employees, and most importantly, the pool of potential clients was very limited.[6] Given that there were limited potential clients, the court appreciated the importance of client and employee relationships in this business and considered this job as special and extraordinary. As a result of the uniqueness of the employee's services, the restrictive covenant was enforceable.

Notably, however, in instances where a personal client relationship is a result of the employee's skill, reputation and previous relationship, as opposed to the direct performance of working for the employer, a non-compete clause is not likely to be broadly applied to all of employee's client relationships.[7] According to the New York Court of Appeals in *BDO Seidman v. Hirshberg*, only if a client relationship occurred as a result of working for the employer can the employer have a legitimate interest in preventing the employee's "competitive use of a client relationship." Therefore, attempting to restrict a pre-existing employee/client relationship is not likely to be enforced by a restrictive covenant. Non-compete agreements are more likely considered reasonable and enforceable in preventing employee solicitation where the employee sold their customer accounts or business to the employer.[8]

Moreover, it is possible for a court to grant a partial enforcement of a non-compete clause or to uphold one part of a non-compete clause and not another. This can occur in cases where the employer has a legitimate, protectable business interest but the non-compete clause is too broad. In these cases, the court looks to details about the employer's conduct to see if the employer acted in good faith or if the employer tried to overreach or manipulate the employee using unequal bargaining power.[9]

Second, if the court determined that the non-compete clause is required to protect the legitimate interest of the employer, then the court proceeds to the second factor to analyze whether enforcing the non-compete clause is not overly burdensome for the employee. Although non-compete clauses must be reasonable in time and geographic scope, this does not require a specific, limited duration. The First Department in *Ashland Management Inc. v. Altair Investments NA, LLC*, upheld a non-compete agreement because it would not prevent the employees from enjoying a successful future business just because there was no end time specified on their confidentiality agreements. As long as the employee is not caused undue hardship, as was the case, the non-compete agreement still can be enforceable.

Similarly, restricting a former employee's competition inside the geographic region that includes the corporate business is likely to be found reasonable and not overly burdensome for the employee. For example, in *Innovative Networks, Inc. v. Satellite Airlines Ticketing Centers, Inc.*, the Southern District of New York determined that limiting the employee from specifically competing or misappropriating information within the whole of the continental United States, although sizeable, was reasonable given that Innovative Network Inc. monitored airline business centers throughout the country and the restriction was only to last for 12 months.[10] However, in *Ivy Mar Co., Inc. v. C.R. Seasons Ltd.*, the Eastern District of New York held that the employer's non-compete clause was unenforceable because it was unreasonable in geographic scope when the agreement restricted the employee company for six years from engaging in business anywhere on earth where the employer did business, marketed their products, or even planned to market their products.[11]

Third, the court weighs whether enforcing the non-compete clause will cause injury to the public at large. Not all restrictive covenants will be injurious to the public. Corporate restrictive covenants should not promote general anti-competition, as this is considered harmful for economic growth. For example, a non-compete agreement that is signed during the sale of a business and containing a severely restrictive burden placed on the seller, could result in the seller withdrawing from this type of business altogether. This withdrawal can be damaging to the public if the result is removing competitors, reducing a skill set in the marketplace, and minimizing competition.[12]

With the increased likelihood of worker mobility, it is crucial for counsel to construct the non-compete agreement in consideration of the three-part reasonableness standard. At the very least, the court will always look at the specifics of the non-compete clause and determine reasonableness and good will on behalf of the employer, and the resulting burden on the employee and general public. P

1 Last v. New York Institute of Technology, 219 A.D.2d 620 (2d Dep't 1995).

2 BDO Seidman v. Hirshberg, 93 N.Y.2d 382, 388–389 (1999).

3 Johnson Controls, Inc. v. A.P.T. Critical Systems, Inc., 323 F.Supp.2d 525 (S.D.N.Y. 2004).

4 Last at 219 A.D.2d 620.

5 Restatement Third of Employment § 8.07 (2010): Protectable Interests for Restrictive Covenants; See also: Restatement Second of Contracts § 188, (1981): Ancillary Restraints on Competition. See also Ashland Management Inc. v. Altair Investments NA, LLC, 59 A.D.3d 97, 103 (1st Dep't 2008) where non-compete agreements can strictly prohibit the use of any company trade secrets that are explicitly or implicitly known.

6 Ticor Title Insurance Co. v. Cohen, 173 F.3d 63 (2d Cir. 1999)

7 BDO Seidman v. Hirshberg, 93 N.Y.2d 382 (N.Y. 1999).

8 Ecolab Inc. v. Paolo, 753 F.Supp. 1100 (E.D.N.Y. 1991).

9 BDO at 394-395.

10 Innovative Networks, Inc. v. Satellite Airlines Ticketing Centers, Inc., 871 F.Supp. 709 (S.D.N.Y. 1995).

11 Ivy Mar Co., Inc. v. C.R. Seasons Ltd., 907 F.Supp 547 (E.D.N.Y. 1995).

12 Restatement Second of Contracts § 188c, (1981) Ancillary Restraints on Competition

Greater Federal Funding Helps Urban Hospitals Reach Rural and Underserved Residents

The provision of new health insurance coverage for many Americans under the 2010 Affordable Care Act, coupled with explosive advances in telecommunications technology, is greatly expanding the potential delivery of medical services by U.S. medical centers and Federally Qualified Health Centers (FQHCs) to regions otherwise underserved or unable to access medical care in the United States.

Despite the establishment of Medicare and Medicaid in July 1965, the free clinic movement in 1967, and the creation of FQHCs in 1975, the nation continues to experience existing and anticipated provider shortages in large pockets of rural and isolated areas in Alaska, throughout Appalachia, across the West, the South, and in Guam, the Northern Mariana Islands and other unincorporated territories of the U.S.

Recognizing that technology can greatly assist the expansion of access to health care, the U.S. government has stepped up efforts to fund innovative programs by providing financing in the form of grants and cooperative agreements to assist hospitals and other medical providers purchase equipment to link centers of medical excellence to those regions where such expertise is needed the most.

United States Department of Agriculture (USDA)

Telemedicine as defined by U.S. government regulation requires a telecommunications link to an end-user through the use of equipment that electronically links medical professionals at separate sites in order to exchange health care information in audio, video, graphic, or other format for the purpose of providing improved health care services (7 C.F.R. § 1703.102).

Telemedicine is a high priority for the USDA based on the unique history of the agency: in the 1930's, the Rural Electrification Administration (REA) funded electric cooperatives to bring electricity to rural communities. In 1949, the REA received authority to finance telephone service in recognition of its importance to the health and well-being of rural communities. Starting in 1995, all telecommunications networks financed by USDA were required to be broadband-capable.

Today, the USDA's Rural Utilities Service annually provides Distance Learning and Telemedicine (DLT) competitive grants from $50,000 to $500,000 to hospitals and other medical providers to enable them to purchase audio/video equipment and related technologies to provide medical advice to rural communities. The grants, which cover a three-year project period, are intended to benefit multiple "end-user" sites in different rural areas. The end-users, which often consist of local clinics and community health centers in very rural areas, use the funds to purchase telemedicine equipment to link their less populous towns and villages to urban medical centers. The urban medical centers serve as "hubs," from which specialists and other providers of medical expertise advise rural end-users on medical care. The use of telemedicine is drastically reducing consultation and travel costs for patients who, otherwise, would be required to travel hundreds and

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sometimes thousands of miles, often in poor health, to obtain the same medical advice they can now receive via live, real-time video consultation. The DLT grant offers special incentives for applicants whose telemedicine proposals contain at least one end-user site that lies within a tribal area, or within a land trust such as the Chamorro Land Trust on Guam.

Other key USDA funding opportunities for telecommunications include:

- **The Telecommunications Infrastructure Loan Program**, which provides loans to improve and build telecommunications service in rural communities (meaning with populations of less than 5,000 people).
- **The Community Connect Grant Program**, which provides grants for broadband service providers who offer broadband services in rural areas (applies to sites of less than 20,000 people). Awardees must serve an area where broadband does not exist, provide a community center with broadband access, and offer broadband service to all customers.
- **The Rural Emergency Responders Initiative**, which provides funding through the USDA Rural Development Community Facilities Program to specifically strengthen the ability of rural communities to respond to local emergencies by financing needed services and equipment.

United States Department of Health and Human Services (HHS)

While the USDA has long awarded its Distance Learning and Telemedicine (DLT) and related grants to worthy recipients in some of the most needy and underserved areas of the nation, the U.S. Health and Human Services (HHS) Office for the Advancement of Telehealth (OAT) also promotes the use of these technologies for health care delivery. OAT defines telehealth as "the use of telecommunications and information technologies to share information, and to provide clinical care, education, public health and administrative services at a distance."

Below are summaries of a few of the telemedicine programs offered by OAT:

- **The Telehealth Network Grant Program (TNGP)** funds projects that demonstrate the use of telehealth networks to improve health care services for medically underserved populations in urban, rural and frontier communities. The networks may 1) expand access to and improve the quality of health care services; 2) improve and expand the training of health care providers; and/or 3) expand and improve the quality of health information available to health care providers and their patients. The goal of the TNPG is to help communities build the human, technical and financial capacity to develop sustainable telehealth programs and networks.
- **The Telehealth Resource Center (TRC)** is a competitive grant program that provides support for the establishment and development of centers that assist health care organizations, health care networks, and health care providers in the implementation of cost-effective telehealth programs to serve rural and medically underserved areas and populations.
- **The Rural Health Network Development Planning Grant** helps rural entities plan, organize and develop health care networks. Support from the program helps health care networks become operational and develop strategies for becoming self-sustaining.
- **The Evidence-Based Tele-Emergency Network Grant Program** supports the implementation and evaluation of broad telehealth networks to deliver emergency department consultation services via telehealth to providers without emergency specialists.
- **The Agency for Healthcare Research and Quality (AHRQ)** supports the planning, implementation and evaluation of health IT and fosters the exchange of health information.

The United States Federal Communications Commission

The Federal Communications Commission (FCC) also administers a Rural Healthcare Program, which provides funds to eligible providers for telecommunications and broadband services necessary to provide increased access to health care through its Healthcare Connect Fund and affiliated programs.

- **The Healthcare Connect Fund** is based on prior FCC pilot programs to spur the development of high-capacity broadband connectivity to eligible health care providers. It encourages the formation of state and regional broadband provider networks. Under the program, eligible rural providers and those non-rural providers who are members of a consortium that has more than 50 percent rural provider sites are able to receive a 65 percent discount on all eligible expenses. Eligible expenses include broadband services and equipment, and, for consortium applicants, provider-constructed and owned network facilities.
- **Skilled Nursing Facilities** are the subject of a potential FCC pilot program to test support for broadband connections to skilled nursing facilities.

Federally funded grant programs are transforming the way in which primary care providers and specialists interact, collaborate and care for patients. Telemedicine connects primary care providers at end-sites with a multidisciplinary team of specialists at a central hub, and that single team of specialists can provide guidance to many physicians in remote areas. In turn, being able to present the nature of their patients' conditions to the specialists enables the doctors in the field to gain knowledge, expertise and confidence regarding how they can address the often complex medical conditions they perhaps must otherwise confront on their own.

Telemedicine is transforming the ways in which hospitals and other providers share medical knowledge and its application in everyday practice. In the process, physicians are providing thousands of people in remote and medically underserved communities with care they might otherwise not receive. Federal funds permit hospital CEOs to do more with less while gaining access to larger numbers of new patients.

Subpoenas, Simplified: The Impact of Revised Federal Rule of Civil Procedure 45

On December 1, 2013, significant changes to Federal Rule of Civil Procedure 45, governing subpoena practice, went into effect. The new version of Rule 45 provides simplified guidelines for how subpoenas may be issued and responded to. This article addresses several of the most substantial changes to the Rule and their impact on practitioners, parties and witnesses.

The purpose of the revisions to Rule 45, in the words of the Advisory Committee, was to "clarify and simplify the rule" and to resolve conflicts with interpretation between various courts. Although not all of the changes to the rule are major, some revisions are substantial enough that any party involved in federal civil litigation should take note.

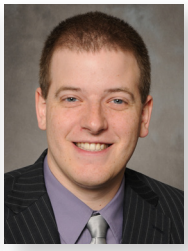
The first major alteration is found in Rule 45(a)(2), which now provides that every subpoena must be issued from the court where the action is pending. The previous guidelines often required the issuing party to issue subpoenas from the courts of the districts in which witnesses or information were located. By consolidating the place of origin of subpoenas to the court where the matter is pending, the Rule should reduce cost and confusion by permitting parties to use a single form of subpoena no matter where the witness or information is located.

Another substantial change can be found in Rule 45(b)(2), which now permits nationwide service of subpoenas. This modification permits the issuing party to serve a subpoena at any place within the U.S., eliminating the previous complex guidelines of geographical limitations and other requirements. So long as the person to whom the subpoena is addressed is located in the U.S., the issuing party may serve the subpoena on that person, even if that person is at a location where they do not normally reside or conduct business.

While these modifications make it easier for a party to issue and serve a subpoena, the Rule contains substantial protections to persons upon whom a subpoena is directed. Under Rule 45(c), a person generally can only be compelled to attend a trial, hearing or deposition within 100 miles of where the person subject to the subpoena resides, is employed, or regularly conducts business in person. It is important to note, for corporate entities that do business in other states, that while a person can be compelled to appear within 100 miles or within the state where they "transact business," that transaction must be "in person."

A subpoenaed person can be compelled to travel more than 100 miles in two situations. The first situation is if that person is a party or a party's officer. The second is if they are commanded to attend a trial *and* if the person would not incur substantial expense as a result of doing so. In both circumstances, while the 100-mile limit does not apply, the proceeding for which the person is compelled to attend *must* be within the state where the person resides, is employed, or regularly transacts business in person.

J. Mark Trimble



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Although the geographical scope of a subpoena's place of compliance has been clarified, it should be noted that the advisory committee warns that Rule 45's new revisions do not change the scope of depositions of parties and their officers, directors and managing agents. The committee notes that courts "retain their authority" pursuant to Rule 37 to control the place of party depositions and impose sanctions for failure to appear. Thus, individual parties and their officers, directors and agents must remain careful to comply with notices of depositions so as not to run the risk of a failure to appear for a deposition and subsequent sanctions made under Rule 37.

Another major element of Rule 45's revisions is found in Rule 45(d), which governs the protection of a person subject to a subpoena. Under the former version of the Rule, the district in which the subpoena was issued handled motions to quash a subpoena. Under the new rule, the issuing court is now the district in which the lawsuit is pending. The revised language of subpart (d)(3), however, states that motions to quash are to be handled in "the court for the district where compliance is required…" Thus, by way of example, if a subpoena is issued in a case pending before the District Court for the Northern District of Ohio, requiring compliance by a witness residing in the District of the Eastern District of North Carolina, a motion to quash the subpoena would be heard in the North Carolina case. Issuing parties must thus be aware that while they may issue a subpoena from the court where a case is pending, a witness seeking to quash that subpoena will have the opportunity to have their motion considered by a different court altogether.

At the same time, Rule 45's newly added subpart (f) provides that, under certain circumstances, when a court is faced with a motion concerning a subpoena that it did not issue, that motion may be transferred to the issuing court. Those circumstances include situations in which the person subject to the subpoena consents to the transfer or where the court finds "exceptional circumstances." The transfer rules apply to motions to quash, objections to a subpoena commanding the production of documents or to permit inspection, and claims of privilege. As the advisory committee notes, in order to protect nonparties, local resolution of disputes regarding subpoenas is preferred and assured by the requirement that motions be made in the Court in which compliance is required. Under certain circumstances, however, transfer to the court where the underlying action is pending is sometimes warranted. Absent such a transfer, the issuing court lacks authority to enter relief to a party challenging a subpoena. For example, in *Semex Alliance v. Elite Dairy Genomics, LLC*, 2014 WL 1576917, the U.S. District Court for the Southern District of Ohio rejected a non-party witness's attempt to quash a subpoena, noting that because the subpoena required compliance in Chicago, the U.S. District Court for the Northern District of Illinois was the court in which the motion should have been made, and without a transfer of the motion to the Southern District of Ohio, that court lacked "the power to issue the order sought." *Id, 2*.

Courts continue to take the protection of those subject to subpoenas seriously. Rule 45(d)(1) provides that parties and attorneys serving a subpoena must take reasonable steps to avoid imposing undue burden or expense on those subject to the subpoena. This obligation is substantial: as long as the duty has been violated, it is of "no consequence" that the party serving the subpoena acted in good faith. *Green v. MOBIS Alabama, LLC*, 2014 WL 2041857 (M.D. Alabama). Thus, caution must be exercised to ensure that subpoena power is not abused lest sanctions be imposed.

The changes to Rule 45 are meant to simplify the sometimes confusing requirements of the prior version. The

Rule now clearly provides guidelines for the protection of those subject to subpoenas. Further, it is now much simpler to create and serve subpoenas. These changes offer clarity to both practitioners and their clients. Parties, particularly corporate entities and their officers, directors and agents, are provided assurance that their appearance for matters cannot be compelled unnecessarily pursuant to a subpoena, and motions related to quashing or limiting the reach of a subpoena from a distant case can be brought in a local court. By being aware of Rule 45's authority and restrictions, parties and witnesses can take the necessary steps to utilize or respond to subpoenas efficiently and effectively.

New York Convention Makes Doing Business Abroad Easier

One hundred forty nine nations have adopted the New York Convention of 1958, an agreement that makes it easier for businesses to arbitrate disputes with entities around the globe. With a thorough understanding of the Convention, companies doing business abroad can reduce risk and save substantial time and money resolving disputes that cross national borders.

Many executives fear unfamiliar foreign legal practices and laws in locations unfriendly to their interests when engaging in international commerce. The New York Convention can provide a solution. Mastering the principles of this virtually universal agreement allows companies to choose the place, process and law for resolving disputes, with confidence that these choices will be respected by courts nearly everywhere in the world.

The 1958 Convention on the Recognition and Enforcement of Foreign Arbitral Awards (often called the New York Convention) creates a process for compelling arbitration and enforcing arbitration awards rendered in foreign countries or involving foreign parties. The Convention is a model of simplicity comprising a mere four pages of text (compare that to the recent trend of legislation often thousands of pages long).

Each of the 149 adopting countries has agreed to recognize written agreements to arbitrate disputes, and to compel arbitration at the request of either one of the parties (unless the contract is unenforceable or the matter is not capable of arbitration).

Once the arbitration panel makes a decision, one simply needs to submit the decision and a copy of the arbitration agreement to a court in any of 149 countries for recognition of the award. Once recognized, the award has the force and effect of a domestic judgment. This allows the prevailing party to use any and all domestic methods for enforcement and collection.

There are only a few reasons why a court may refuse to recognize an arbitration award, including invalidity of the arbitration agreement, failure to obey the arbitration procedure specified in the agreement, immaturity of the award (if it is not yet binding), or if the court determines that enforcement would be flatly contrary to the enforcing country's public policy.

These exceptions are sparingly invoked. Further, the Convention forbids countries from charging higher fees or creating procedural hurdles more onerous than are required for enforcement of domestic arbitration agreements. The spirit of the Convention is to encourage arbitration, and to keep it as simple as possible for companies to resolve foreign business disputes.

Application of the Convention in the United States is limited to commercial disputes. In the spring of 2014, the United States Supreme Court (*BG Group PLC v. Republic of Argentina*) affirmed the bedrock principles of the Convention and the great deference courts should grant arbitrator decisions. The Court held that decisions, regarding whether parties have properly followed any pre-arbitration procedure required by an agreement (for instance, conducting a

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settlement conference before proceeding with arbitration), should be made by arbitrators, not courts.

Thus, any business that signs an arbitration agreement subject to the Convention faces an uphill battle if it later attempts to resist arbitration or enforcement of an arbitral award.

While the basic principles of the Convention are straightforward and relatively easy to understand, there are a number of pitfalls that arise if an arbitration agreement is not carefully considered and properly drafted. For instance, here are a few of the mishaps we have seen:

- **Failure to specify in the agreement the law governing the arbitration**. The choice of law governs everything, most importantly, the law under which an arbitration agreement or award can be challenged in court. When drafting an arbitration agreement, we always carefully match a company's business objectives to the legal system most harmonious with those objectives.
- **Failure to understand that there are many different possible arbitration procedures, and one size does not fit all**. Some procedures are simple, quick and final. Others can be nearly as costly and time-consuming as full-blown litigation. Planning for the types of disputes that might arise and the ideal process for resolving them is a worthy investment. By selecting the right procedure, a company minimizes cost, stress and the level of disruptive havoc that business disputes can cause.
- **Failure to understand, with respect to the United States, that we have over 50 different jurisdictions and that each is different**. It is critical to consider which jurisdictions are pertinent to the arbitration contract, and which system is best suited to a company's business needs. Moreover, the language specifying the arbitration forum has to be precisely drafted, or it will not be respected by the courts. We have seen many sophisticated businesses get stuck for years in a forum they don't want because they used the wrong language in their agreement.

The New York Convention can be a powerful tool for controlling legal risk. Parties bound by a contract under the Convention can typically be compelled to arbitrate and be confident that any award can be converted into a domestic judgment in the country where enforcement is needed.

However, like any tool, effective use of the Convention requires a skilled and knowledgeable hand. The downside of its simplicity is the need for deft navigation: businesses including arbitration agreements in their transnational contracts need to have substantial discussions with experienced counsel to craft the right agreement for their unique situation. Businesses already in the midst of a dispute need counsel who are knowledgeable as to the best way of advancing their interests, or they may waste resources fighting costly battles they are likely to lose. P

Considering a Move? What You Should Know Before Expanding Your Business in Ontario

Expanding your business into Canada is a wise business decision for many reasons. Ontario and its financial center, Toronto, are its most populous city and province in Canada with about 13 million people and 2.8 million people, respectively. Ontario represents an attractive business market boasting the following:

- a well-educated and skilled workforce;
- a sound banking sector and robust capital markets;
- a simple and inexpensive incorporation process;
- minimal import restrictions;
- easy access to other North American markets; and
- a competitive and incentivized tax regime among other things.

KPMG's 2012 "Competitive Alternatives" study of international business costs confirmed Canadian business costs are among the lowest in the G7, and Forbes.com recently named Ontario a top destination for foreign direct investment in North America.

While it's certainly an appealing business decision, you will also want to consider the many other facets to operating in this new location: selecting the type of business entity, licensing and registration requirements, as well as tax and employment considerations. This article provides businesses and investors with insight into Ontario's economic structure and its business regulatory framework.

Business Presence and Form

There are several options available to foreign businesses looking to expand into Canada, each with its own benefits and drawbacks.

Licensing is the simplest method of expanding into Canada. A company can avoid establishing a physical presence by way of license agreement whereby the licensor gives specific rights in some or all of its property, usually intellectual property to the licensee. The licensee is then allowed to use the IP or other property in exchange for a fee or royalty.

Establishing a physical presence can also be avoided by selling goods using an agency or distributor agreement. These methods differ in that an agent will act on behalf of the foreign business, whereas a distributor will buy goods from the foreign business and offer them for re-sale.

Another alternative is to open a foreign branch office. This can have certain tax advantages, as Canadian losses can be claimed by the parent company in its home jurisdiction. However, it also means the foreign company will be subject to Canadian income tax on the income and liabilities incurred by the Canadian branch.

A foreign company can also incorporate a Canadian subsidiary. Companies can be incorporated at either the provincial or federal level. For most purposes, federal and provincial business corporations are able to conduct business anywhere within Canada

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and abroad, but, differing rights and obligations do exist.

An unlimited liability corporation (ULC) is a special type of corporation that currently only exists in three of Canada's provinces: Alberta, British Columbia and Nova Scotia (not Ontario). Unlike limited liability corporations (LLCs), the shareholders of a ULC can be personally liable for any liabilities of the company. However, ULCs also allow some flow-through tax benefits to shareholders.

Foreign corporations may also consider operating in Canada through a sole-proprietorship, a partnership or by purchasing an existing Canadian business.

Business Registrations

There are registration requirements for businesses operating in Canada. A corporation incorporated in a jurisdiction outside of Canada must obtain an Extra-Provincial License to carry on business in Ontario. "Carrying on business" is defined broadly and covers most business/commercial activities.

Under the Ontario *Business Names Act*, if a business uses a name that differs from the individual's name (in the case of a sole proprietorship), the names of the partners (in the case of a partnership), or from its corporate name (if a corporation), it must register that name in Ontario. This registration is for administration purposes, and does not grant any trademark rights or protections.

Businesses are also required to obtain a business number from the Canada Revenue Agency. Employers may also

be required to pay the Ontario Employer Health Tax and report the earnings of employees working in Ontario and pay Workplace Safety Insurance Board insurance premiums.

Taxes

Everyone with income from a taxable source in Canada is required to file a Canadian tax return and pay income tax. Thankfully, Canada has a progressive tax system. Sole proprietors and partners in a partnership are taxed at the individual level. Canadian corporations pay a flat rate of income tax. The current federal corporate tax rate is 15 percent and the Ontario corporate tax rate is 11.5 percent, with a combined rate of 26.5 percent.[1] However, tax treaties between Canada and the foreign jurisdiction may reduce tax owed.

In addition to income tax, a business operating in Ontario may incur taxes such as:

- Capital gains tax on the sale or 'disposition' of an asset;
- Provincial land transfer tax of approximately 1.5 percent of the fair market value of any real property bought or sold in Ontario (certain municipalities such as Toronto also levy a tax in addition to the provincial tax);
- Contributions on behalf of employees for payroll-related expenditures such as employment Insurance and the Canada Pension Plan;
- Withholding taxes in the case of non-residents; and
- A 25 percent branch tax for non-resident foreign corporations that carry on business in Canada through a branch.

Employees

The information in this section relates to non-unionized employees and their employers in Ontario, and does not apply to independent contractors.

The Employment Standards Act ("ESA") and its regulations provide standards for employee wages, hours of work, overtime entitlement, vacation entitlement and leave of absence entitlements among other things. Some employees may be exempt from particular standards, depending on the nature of the employment.

We normally recommend that employers enter into a written employment agreement with their employees, and make the signing of the agreement a condition of any job offer.

Employers must also comply with legislation designed to protect employees from physical harm (the Ontario's Occupational Health and Safety Act) and from discrimination (the Ontario's Human Rights Code). In general, employers cannot discriminate against employees (or prospective employees) based on protected traits, and must also accommodate employees with disabilities.

Termination of Employment

The concept of "at will" employment does not exist in Canada. Employees are either employed for a specific period of time or for an indefinite period. If individuals are employed on an indefinite basis, they must generally be given notice (or pay in lieu of notice), if their employment is terminated without cause.

Whether or not an employee is entitled to receive notice of termination or other compensation depends on the circumstances of the termination. There are two categories of termination: with cause and without cause.

"Without cause" means the termination is not a result of any specific charge or problem with the employee. An employee may also be considered to have been terminated without cause if they are constructively dismissed. Constructive dismissal occurs when an employer unilaterally changes a material term of a person's employment without consent from the employee, or permission in the employment agreement.

Compensation for this type of termination is established by the employee's written employment agreement or by the common law and the ESA if there is no such agreement. In general, the ESA provides for a minimum amount of notice (or pay in lieu of notice). In some cases, the employer may also be required to pay severance in addition to termination pay. A court may also extend the reasonable notice period beyond the ESA minimums based on the employees' age, length of employment, nature of work, and other circumstantial factors.

An employee may only be terminated for "cause" if they have committed significant misconduct. Employee's dismissed with cause are not entitled to any notice or compensation. We caution employers to seek legal counsel before terminating someone's employment when they believe there is cause for termination.

Conclusion

If you have made the decision to establish a business in Ontario or to expand your existing business into Ontario, we congratulate you on embarking on this exciting journey. We hope the topics discussed here have provided you with a basic understanding of some of the key legal issues to be considered when operating a business in Ontario.

1 Canada Revenue Agency. Corporation Tax Rates. <URL: http://www.cra-arc.gc.ca/tx/bsnss/tpcs/crprtns/rts-eng.html>

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Dealing with Diplomatic Immunity

Diplomats and diplomatic buildings enjoy diplomatic immunity and inviolability. That's how countries show that they respect each other's sovereignty and independence. It also allows them to maintain international relations without having to fear their representatives will be pressured by legal proceedings or arrests. These privileges are far reaching: Julian Assange, the internationally wanted founder of WikiLeaks, has been living in the Ecuadorian Embassy in London for two years now, in a building the British police are not allowed to enter.

Based on our experience as lawyers for several foreign missions in the Netherlands, in this article I will provide guidance on legal disputes involving diplomats.

When a foreign diplomat whose speeding caused a fatal car accident in the land he was posted to in 2013 avoided prosecution by invoking immunity, and then quickly returned to the sending state, the local court could not do anything to stop him. This caused much indignation. Therefore, more and more governments are taking measures against abuses of immunity, for instance by withdrawing parking permits or tax-free fuel cards and by publishing a blacklist of diplomats refusing to pay their fines.

What are the consequences of diplomatic immunity for citizens dealing with diplomatic institutions and diplomats? Can rules governing the relations between countries be invoked in the case of commercial transactions? Everyone dealing with diplomats or diplomatic institutions can be faced with the limits of diplomatic immunity and inviolability. This may involve buying, selling and leasing real estate, delivery of goods, and employment in an Embassy or Consulate.

Diplomatic Immunity and Inviolability

Diplomatic immunity means that Embassies, Consulates and diplomats and members of their family are not subject to the legal authority of the host country. Though the laws and regulations of the receiving state are not applicable to them, they are expected to observe common rules. In addition, the court does not have jurisdiction either. Furthermore, diplomats do not have to pay taxes.

In addition to immunity, there is also inviolability. This means the premises of diplomatic missions must not be entered, they must not be searched, property must not be seized and persons must not be arrested by the host country.

These and other rules on diplomatic relations are specified in the Vienna Conventions of 1961 (on Diplomatic Relations) and of 1963 (on Consular Relations), which have been ratified by most countries. In addition, there are also the *United Nations Convention on Jurisdictional Immunities of States and Their Property* and the *European Convention on State Immunity*. They have been ratified by fewer countries but can be used by courts as an indication of what is regarded as customary international law in cases that are not governed, or in less detail, by the Vienna Conventions.

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Not all actions performed by the diplomatic service are subject to immunity. A distinction is made between official activities (*acta iure imperii*) and personal activities (*acta iure gestionis*). Only official activities are subject to immunity. Thus, if a foreign Embassy in Washington places a lunch order with a catering service operating in the neighborhood, the catering service can take legal action if the bill remains unpaid. Not all countries make this distinction, however, and some are convinced that all activities by diplomats are covered by immunity.

The level of diplomatic immunity may differ according to the function and status of the diplomat. Leading diplomats enjoy the highest degree of immunity, whereas technical, clerical and consular staff generally enjoy functional immunity, i.e. only for activities in connection with the performance of their official duties. An Embassy janitor will rarely be able to appeal to immunity in a private dispute. However, for reasons of national security this may be entirely different for security staff members.

Commercial Contracts and Real Estate

Representatives of Embassies and Consulates may conclude commercial contracts on behalf of the missions. Does state immunity apply to such commercial contracts as well? That mainly depends on the reason for the conclusion of the contract. Concluding a commercial contract will, in principle, not be qualified as an official act. The contract will thus fall under the *acta iure gestionis* and state immunity does in principle not apply. However, commercial contracts can also contribute to preserving the Embassy or Consulate and as a result, fall under the *acta iure imperii*. Purchasing or leasing an Embassy building or residence of the ambassador or senior diplomats belong to the latter category. However, if an economic attaché decides to build a real estate portfolio in his temporary place of residence, immunity will not apply. In the event the real estate is meant as accommodation for diplomats, the portfolio may however well be covered by immunity.

Employment Law and Social Security

Employment law is an area of limited immunity. According to customary international law, concluding an employment contract falls under the *acta iure gestionis* and immunity does not apply. This paragraph is not applicable if the employee has the nationality of the sending state or his or her common place of residence is not in the receiving state. Professional diplomats usually fall under these exceptions.

If a dispute arises regarding the employment contract of locally recruited support staff, the court of the host country can render a judgment on it. An exception is if the Embassy refers to its own national security. Obviously, the court cannot check whether this plea was made justly without violating state immunity.

Mandatory social security insurance is closely connected with employment law. Mandatory social security insurance is not a tax and therefore, fees must be paid. In the event one is subject to the mandatory social security insurance, one also has to fulfill the obligations of social security insurance such as reintegration rules in the event of sickness. These rules can differ from country to country.

Disputes with Diplomats

What happens if the Embassy or Consulate does not fulfill its obligations? In principle, in the event of *acta iure gestionis*, the law of obligations of the host country will apply. In this case, if it turns out that a settlement cannot be reached, legal proceedings against the Embassy can be launched if necessary. If an Embassy appears at a court session and does not immediately invoke immunity, it is considered to have waived its immunity. If the claimant wins the lawsuit, the matter will not necessarily be over. The buildings and bank accounts of Embassies are inviolable and therefore not subject to execution.

However, a state is expected to cooperate when it comes to the enforcement of a judgment. After all, diplomatic relations are based on mutual respect. If an Embassy refuses to fulfill its obligations, the claimant does not have any legal coercive measures. An option may be to report the refusal to comply with a judgment to the Ministry of Foreign Affairs that maintains relations with the diplomatic community.

Conclusion

State and diplomatic immunity is not absolute but subject to limitations. However, even if there is no diplomatic immunity involved, inviolability may still apply. When disputes involving immunity arise, it is advisable to get assistance from a lawyer who is experienced in dealing with these complex matters. P

CEAC – A New Option for Dispute Resolution Clauses in China Related Contracts

The Chinese European Arbitration Centre (CEAC) in Hamburg, Germany, specializes in China related disputes. Founded in September 2008 with the joint support of the Hamburg Bar, the Hamburg Chamber of Commerce and the Hamburg State, as well as law firms from around the globe, CEAC has received ten cases since June 2012. CEAC handles cases from all parts of the world. Its arbitration rules are based on the neutral arbitration rules of the United Nations Commission on International Trade Law, adapted to the needs of China related arbitration.

I. The Practical Need of Arbitration Clauses in China Related Contracts

In international contract negotiations, usually each party is most satisfied when it can impose its own conditions, rely on its own law and provide for the competence of the courts at its seat. Often this simply does not work, because the business partner may have a similar concept in mind with different conditions, another state law and a distinct dispute resolution mechanism. In the case of contract negotiations with a Chinese party, e.g. about a joint venture, a transaction or sale of goods, the Chinese party is likely to have Chinese law and the competence of Chinese courts in mind, while its international partner, e.g. a company from New York, might prefer New York law and the competence of New York courts. How is such a conflict resolved?

Regarding substantive law, the parties might settle on the choice of the law of a neutral state or, less risky and less costly[1], on the neutral *UNIDROIT Principles of International Commercial Contracts* (UNIDROIT PICC), which have been created over the past decades by the neutral international organization UNIDROIT, comprising 63 member states including the U.S. and China[2]. They provide a bridge between anglo-saxon U.S. law and Chinese law, which is based on continental (German) law.

With respect to the best possible dispute resolution mechanism, counsel of both parties will soon find out that any choice of jurisdiction clause is only of limited value. The reason is that enforcement of Chinese state judgments in the United States (or other jurisdictions of the world) or of U.S. judgments (or other foreign state judgments) in China are difficult and sometimes even impossible as there is no international treaty basis for enforcement. As a result, both counsel would look for an arbitration clause in order to create a functioning tool for the enforcement of rights, if necessary, by using the international enforceability of arbitration awards under the *New York Convention on the Recognition and Enforcement of Arbitral Awards (New York Convention)*[3]. China acceded to this convention in 1987.

With respect to the choice of the adequate arbitration regime, the perspective is likely to be different. Each party will prefer the choice of the rules of

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a local or national arbitration institution of its home jurisdiction, e.g. the US AAA-rules[4] or the Arbitration Rules of the Chinese International Economic and Trade Arbitration Commission[5].

II. The CEAC Rules as a Pragmatic, Neutral Solution

It is at this stage that the alternative option of choosing the Arbitration Rules of the CEAC (CEAC Rules)[6], becomes a more suitable solution. They have been specifically designed for such an occasion for three reasons.

First, they are tailor-made for the Chinese market. They include a number of details which are the result of discussions with Chinese experts involved in making and controlling the rules. For example, the CEAC Rules ensure that any wording of the arbitration clause referring to arbitration under the CEAC Rules will always be interpreted as referring to *institutional* arbitration administered by CEAC[7]. As *ad hoc* arbitration is not a common concept in China[8], this enhances the chances of enforcement of an award in China. The Chinese judge in charge of an enforcement of a CEAC award under the New York Convention will thereby relate to a form of arbitration which is known to him.[9]

Second, they reflect a concept of intensified neutrality which is the basis for their international acceptability, also in China.

- Hamburg, CEAC's seat in the north of Germany, is acceptable to Chinese merchants as Hamburg is the sister city of Shanghai[10], hosts over 400 Chinese companies and is considered by many Chinese as a "gateway to Europe."
- They are the result of a worldwide legal dialogue and are based on the neutral arbitration rules of UNCITRAL, the Commission on International Trade Law of the United Nations[11].
- The international team involved in creating the rules or the administration of arbitrations, includes members from China, Europe and the world (e.g. Brazil, U.S.). This concerns the case management, the appointing authority and the advisory boards of CEAC, the arbitration centre, and its shareholder, the NGO Chinese European Legal Association (CELA).
- The legal environment of the CEAC Rules is neutral. It is based on instruments which the state of China was involved in making. Even the German arbitration law (which comes into play in the worst case scenario of a legal battle over a CEAC case[12]) is based on the UNCITRAL Model Arbitration Law. The CEAC choice of law clause[13] proposes, on an optional basis, to choose the United Convention of the International Sale of Goods or the UNIDROIT Principles of International Commercial Contracts as a neutral set of rules.

Third, the CEAC Rules include a number of pragmatic adaptations to the underlying UNCITRAL Arbitration Rules, designed for ad hoc arbitrations, in order to create a secure ground for the case administration by CEAC as an institution. Such adaptations relate, for example, to communication (filing, sending of copies to CEAC) or to costs (e.g. VAT issues).

III. The CEAC Rules in Practice

Since 2008, the CEAC Rules have been accepted by many parties from around the globe. CEAC Ambassadors in Algeria, Argentina, Colombia, Hong Kong, Switzerland and as well as CEAC and CELA events in over 30 cities and 19 jurisdictions around the globe help to promote the rules. The Willem C. Vis International Commercial Arbitration Moot has based its 2013 problem on a case which is to be decided under the CEAC Rules.

The first cases mainly relate to alleged contract violations in the energy or, for example, the shipping industry. Some of the cases concern disputes between Chinese and European companies (from Germany, Italy or Spain). Other cases are due to disputes between German companies and companies from Western Europe, Canada or Israel. In these cases the relation to the Chinese market is indirect, e.g. by one of the companies being a subsidiary of a Chinese company.

The total dollar amount of CEAC administered disputes already reaches over 80 million USD (ca. 60 mio. euro). For more information see www.ceac-arbitration.com and www.cela-hamburg.com.

1 *Bonell*, in: An International Restatement of Contract Law, 3rd edition 2004, p. 26 et seq.; *Vogenauer* in: Vogenauer/Kleinheisterkamp, Commentary on the UNIDROIT Principles of International Commercial Contracts (PICC), Oxford 2009, Introduction, marginal No. 21; *Brödermann*, The impact of the UNIDROIT Principles on international contract and arbitration practice - The experience of a German lawyer -, Uniform Law Review 2011, p. 589 et seq.

2 *See* www.UNIDROIT.org.

3 Dated 10 June 1958; and entered into force on 7 June 1959, 330 U.N.T.S. 38 (1959).

4 Arbitration Rules of the American Arbitration Association, *see* www.adr.org.

5 *See* generally on arbitration in China *Kun Fan*, Arbitration in China. A Legal and cultural analysis (2013), p. 119 et seq. (on CIETAC).

6 For a detailed description of the CEAC Rules see e.g. *Brödermann*, The Chinese European Arbitration Centre, Journal of International Arbitration (J.Int.Arb.) 2013, 303-327.

7 Art. 1A CEAC Rules.

8 *Kun Fan*, Arbitration in China (op. cit. note 5), p. 40 et seq.

9 For further examples, see *Brödermann, op. cit.*, J.Int.Arb. 2013, p. 303, 318-319.

10 Hamburg is also sister city to Chicago, Dar-es-Salaam, Dresden, León, Marseille, Osaka, Prague, and St. Petersburg.

11 http://www.uncitral.org/pdf/english/texts/arbitration/arb-rules/arb-rules.pdf

12 Book 10 (Arbitration Proceedings) of the German Civil Procedure Act (*Zivilprozessordnung*) which contains, in its §§ 1025 et seq., the German arbitration law.

13 Art. 35 CEAC Rules.

The Italian FCPA: A Little Known Issue for Foreign Companies Operating in Italy?

Over the last years the United States and many other countries around the world have been creating provisions aiming to hold corporations liable for committing criminal offenses for their own advantage. Principally, these provisions seek to prevent corrupt practices and similar offenses and lead to the adoption of dispositions set out by the Organisation for Economic Co-operation and Development (OECD) Convention on Combating Bribery of Foreign Public Officials in International Business Transactions, known also as the OECD Anti-Bribery Convention (Paris, December 1997).

The Italian Republic followed this legislative trend by adopting in 2001 Decree No. 231 concerning the "administrative liability of legal entities deriving from the commission of criminal offenses" (hereinafter the "Decree"). As a result of this Decree, criminal sanctions are now applicable against companies, not just against individuals. Companies, whether resident or non-resident, conducting business within the Italian territory, are thus liable for not only severe pecuniary sanctions but, even more seriously, debarment which leads to the forced suspension of business activities.

This is an additional liability, separate from the specific individual liability of the person committing the criminal offenses and also separate from ordinary liability for damages.

This risk arises (in broad terms) whenever a criminal offense is committed by an individual in the interest of a company (however minimal). One of the main differences between Italian law and similar laws in other countries is that the Italian system aims to sanction a far wider range of criminal offenses than the "usual" bribery or corruption (e.g. environmental criminal offenses, criminal offenses regarding the health and the safety of workers, computer and IT crimes, immigration-related criminal offenses, corporate criminal offenses and so on[1] – which shall hereinafter be referred to collectively as "231 offenses").

The three conditions for corporate liability under the Decree are as follows:

(a) a 231 offense committed by representatives, directors or managers of the company or by one of its operative units ("managers"), including those individuals who are responsible for the *de facto* management and control of the company or by individuals subject to their direction or supervision ("non-managerial employees");

(b) a connection between the offense and the company's interests, or the company's advantage. The company is not liable if it can be proved that the individual acted in his own interests or for the interests of a third party;

(c) "organizational negligence" on the part of the company.

The sanctions provided for company liability are, first, fines (up to 1.5 million euros) and the forfeiture of all

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profits deriving from the commission of the crime. These fines apply upon the ascertainment of corporate liability. Moreover, in some cases, the following debarments are also applicable: suspension of business activities, suspension or revocation of the authorizations, concessions, licences or permits related to the crime, prohibition from entering into contractual agreements with the Italian public administration, exclusion from all government concessions, grants, loans or subsidies, and possible revocation of those granted previously, and, finally, prohibition from advertising goods or services. These sanctions are applied only upon certain conditions, however. If a "restraining" sanction is applied, the judgment may be published.

Moreover, debarments may also be imposed as a precautionary measure, on the basis of the presumption of serious evidence of the company's liability and even while a trial is still pending. Alternatively, an official receiver for the company may be appointed by the court.

The Decree provides, on certain conditions, for the exemption of companies from the liability. In this regard, it is necessary to distinguish between a criminal offense committed (A) by managers or (B) by employees subject to their direction (this due to the different presumptions forming the basis of company liability).

In case A, in order to avoid any liability, the company must provide evidence of the following facts:

(1) the managing body has adopted and efficiently created, before the commission of any 231 offense, an appropriate management, organization and control model ("231 Model") in order to prevent the commission of such offenses;

(2) the task of controlling the full functioning and the implementation of the 231 Model and of keeping it up to date has been assigned to an independent Supervisory Board with appropriate auditing and surveillance powers[2];

(3) the Supervisory Board has duly and effectively complied with its duties;

(4) the individual committing the offense has eluded, with intent to commit fraud, the provisions of 231 Model and the policies implemented by the company in order to carry out the 231 Model.

In case B, in order to avoid liability, the company must be able to prove that it has duly controlled and supervised the actions of its non-managerial employees. Thus the liability of the company may be excluded when, notwithstanding the failure to comply on the part of the non-managerial employees of the obligations of direction or supervision imposed on them, the company has adopted an efficient preventive 231 Model.

The enforcement of these provisions has caused a certain amount of both economic and credibility damage to a number of well-known companies (including ThyssenKrupp, Morgan Stanley, Bank of America, Credit Suisse and Citibank). Moreover, the lack of a 231 Model and of an independent and efficient Supervisory Board may be considered as a hint of an overall lack of proper corporate control systems, if not of the propensity of the company to commit violations other than 231 offenses.

This particular trend, together with the range of offenses sanctioned by Italian law (a range wider, as mentioned above, than similar laws in other countries), must be carefully evaluated by foreign companies doing business in Italy, in order to draft a 231 Model that provides appropriate protection, which – while it may be based on similar organizational models already used by the foreign corporation – must reflect the somewhat different realities in Italy and, as such, requires attention to certain specific areas.

1 As of May 15, 2014, the criminal offenses which may lead to administrative liability for companies number approximately 130. Moreover, the number of such criminal offenses has been increasing each year.

2 A company's 231 Model must be periodically updated and verified, and must provide for a suitable disciplinary system (in the event of any violation). The supervisory board must exercise its powers of control and initiative even with respect to the levels of implementation and efficiency of the Model in question.

Paying with Bitcoins: How Your Business Can Gain Traction

What are Bitcoins?

Bitcoins (commonly abbreviated as BTC) are an internationally used cryptocurrency. They are created and transferred within a decentralized peer-to-peer computer network. New Bitcoins are created through the solution of complex arithmetical problems by computers in the Bitcoin network (so called mining). As the Bitcoin software is open-source, basically everybody can have access to it.

There is no single entity – like a central bank – controlling the network or generating the Bitcoins. And, unlike central bank money, there is a limitation in the total amount of Bitcoins that can be created. The program restricts the number of Bitcoins to 21 million. At the end of 2013, approximately 12 million Bitcoins were created. Because Bitcoins are divisible, it is possible to transfer smaller units than one Bitcoin. Several Bitcoin exchanges make it possible to buy and sell Bitcoins.

The software was made publicly available in 2009, but Bitcoins needed time to gain public interest. Now, more and more people are possessing and trading Bitcoins and the number of goods and services which can be purchased with Bitcoins is increasing.

Independence from a central bank and thus from politics, and the limitation to 21 million units in total are the most heard positive arguments in the ongoing discussion, while critics point out that there are also great risks at hand. For instance, unless Bitcoins have a broader acceptance as a method of payment, a high amount of speculation remains, resulting in a very high volatility.

For merchants, there are two interesting aspects in using Bitcoins as a method of payment. Firstly, transaction fees are optional and – by now – very low, especially compared to the fees of credit cards. Secondly, refunds are not possible in the Bitcoin system. Furthermore, due to the current media awareness, there is a significant marketing advantage.

Regulatory Issues in the Bitcoin Business

Before starting a Bitcoin related business, it is important to know the laws and regulations you must follow. Due to their increasing popularity, Bitcoins came under the scope of the financial authorities, who are now setting the rules for Bitcoin businesses. If people want to start a business in the German market or a business focusing on the German market, they should follow the opinion of the German Federal Financial Supervisory Authority (Bundesanstalt für Finanzdienstleistungsaufsicht, BaFin).

BaFin stated that Bitcoins are not e-money within the meaning of the German Payment Services Supervision Act because there is no central issuer who establishes claims against himself by issuing the Bitcoins.

Neither do Bitcoins qualify as a foreign currency nor as foreign banknotes and coins because they are not legal tender.

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Anka Hakert practices tax law and the law of nonprofit organizations. With her special focus on value added tax matters, she regularly holds lectures concerning tax matters of Bitcoin businesses. Anka makes sure that clients interested in trading or using Bitcoins are well prepared when it comes to tax issues. She has more than 15 years of professional experience as a German attorney.

Eike Weerda practices banking and capital markets law. He advises clients regarding regulatory issues in banking and finance matters. He is an expert on Bitcoins and regulatory issues surrounding Bitcoin businesses. He also has extensive experience in the area of securities law where he counsels private and institutional investors.

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However, BaFin rates Bitcoins as a financial instrument in the form of units of account pursuant to the German Banking Act, i.e. as units of value not denominated for legal tender, which is at least comparable to foreign currencies.

BaFin concluded that taking Bitcoins as a substitute currency for cash or scriptural money in currencies of legal tender to participate in the economy does not need an authorization. In general, the same is true for the sale of mined or acquired Bitcoins or their purchase.

When accepting Bitcoins as payment, a company still provides no banking transactions or financial service. The mere participation in the existing market of Bitcoins does not need an authorization.

Although, things might get difficult when interposing a Bitcoins-payment-provider, who himself may need an authorization.

However, an authorization requirement will arise if additional circumstances appear. That is the case if a special contribution is paid to sustain, foster or create the market. E.g., if people advertise on the market that they regularly purchase and sell Bitcoins, this then qualifies as proprietary trading subject to authorization pursuant to the German Banking Act. The same normally applies for mining pools.

As far as Bitcoins becoming the object of trade themselves, there are several authorization elements that may be relevant, e.g. principal broking services, the multilateral trading system, investment and contract broking, as well as proprietary trading.

Tax Issues

As mentioned above, Bitcoins and other cryptographic currencies are not legal tender and can also not be classified as e-money, as the BaFin clarified in December 2013.

Besides the income tax effects of Bitcoin transactions, the value-added tax treatment of Bitcoins is of particular interest to companies. It will be particularly troublesome for companies accepting Bitcoins as a means of payment if the tax authorities treat the later sale of Bitcoins via a trading platform as a service subject to value-added tax.

Whether this way of handling such transactions is correct, is at least questionable. First of all, according to a judgment of the European Court of Justice, the pure purchase and sale of securities in a company is not at all a business activity and thus not taxable. Transactions with Bitcoins could in this respect be considered similar. Regarding tax exemption in connection with Bitcoin transactions, the German Federal Ministry of Finance has already expressed its first opinion in 2013: The trading of Bitcoins and the procurement of Bitcoin sales is not exempted from the value-added tax, according to Section 4 no. 8b of the German Value-Added Tax Act, since Bitcoins are not legal tender. In individual cases, however, tax exemption may result from Section 4 no. 8c of the German Value-Added Tax Act, according to a September 2013 statement of the German Federal Ministry of Finance.

All this relates to the question of tax exemption as a second step of the examination of a VAT liability. Only in the case of an actual delivery or other service according to Section 1 (1) of the German Value-Added Tax Act, which is subject to value-added tax, the question arises, whether the transaction is according to Section 4 tax exempt or not.

Unlike the sale of Bitcoins, transactions, which are used merely for the pure payment of a fee, should not be subject to value-added tax according to a statement by the German Federal Ministry of Finance in September 2013. Therefore, the use of Bitcoins as a means of payment is not taxable according to Section 1(1) of the German Value-Added Tax Act. Assuming first, Bitcoins are ordinary assets and not money, and second, in a "payment process," Bitcoins are exchanged for other goods and services (which normally triggers value-added tax on both sides), this statement is surprising at first glance. The value-added tax law in many cases does not, however, strictly follow the income tax law. Therefore, it may be correct to treat Bitcoins at least as a "fee" for value-added tax purposes. In fact, the entrepreneur, who uses Bitcoins as a form of payment, pursues no economic interests beyond the pure payment of a fee. In 1969, the German Federal Finance Court already decided that in such a case no value-added tax accrues.

A statement of the Finance Ministry on April 23, 2014, shocked all companies. It was announced that besides the trade of bitcoins, also the use of Bitcoins must be considered a taxable service for which no tax exemption is applicable. This recent statement contradicts the announcement of September 2013. Back then, the Ministry said that the mere payment of remuneration is not delivery or other service, so that the use of Bitcoins as a means of payment is not subject to VAT at all. However, given the recent statement, entrepreneurs have to worry that the tax authorities will impose value-added tax on all transactions with bitcoins, including the use of Bitcoins as a form of payment.

So it is urgently needed that the value-added tax treatment of Bitcoin transactions be clarified in a satisfactory manner.

Conclusion

Bitcoins are a new, innovative and fast spreading technology with enormous potential. Due to its novelty, not all legal matters are settled at the moment. Everyone who is interested in implementing Bitcoins in his or her business case or starting one on the cryptocurrency should get extensive legal advice on the regulatory and tax issues concerning Bitcoins in the targeted jurisdiction. It remains to be seen, how regulatory institutions will assess Bitcoin transactions and Bitcoin trading in the future.

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Energy Reform in Mexico

In December 2013, the most important constitutional reform on energy in Mexico in several decades was published in the Official Journal of the Federation. This reform intends to implement radical changes by promoting competition in a sector that has been historically characterized by the concentration of productive activities in the hands of the Mexican government since the 1930s. This sector began to open up to private investment just two decades ago.

This holds true for the hydrocarbon industry, given that oil production has always dominated public debate in Mexico. Nevertheless, it is also the case that the electricity sector is quietly undergoing its greatest transformation since its nationalization in 1960. Since then, and until the 2013 reform, the generation, transformation, transmission, distribution and sale of electrical energy for public consumption has been the exclusive province of the federal government. By means of a creative constitutional interpretation, the reforms to the 1992 Public Service Electrical Energy Act broadened the opportunities for self-supply and gave way to a vigorous framework for the independent production of electricity, among other achievements. However, such reforms did not allow the generation of electrical energy for sale between private parties.

As a result of the alarming financial situation faced by the public utility Federal Electricity Commission (*Comisión Federal de Electricidad, CFE*), the opacity, politicization and cross-subsidization in determining electricity fees, the lack of investment in networks and the urgency to meet ambitious goals in the reduction of greenhouse gases, the need for a far reaching reform became indispensable. In their respective initiatives, Mexico's President and the senators of the National Action Party (*Partido Acción Nacional, PAN*) proposed to move toward an institutional framework that would allow for the creation of a true electricity market.

The result is a model in which planning and control of the national electricity system will continue to rest in the hands of the federal government by means of an operator that is independent of other parties in the industry, specifically, the CFE. Electricity transmission and distribution will be considered public utility services, which will also be entrusted to the State, and the remaining activities in the electricity industry will be opened to participation from private industry, in accordance with the terms established by the new laws. Nevertheless, all of the above activities will continue to be subject to oversight by the Energy Regulatory Commission (*Comisión Reguladora de Energía, CRE*) with renewed autonomy for such an agency.

Thus, although much work remains in order to bring about a duly integrated legal framework, we now have a solid constitutional basis from which to work. To begin with, on April 30, the President submitted to Congress the bills of the regulatory statutes which will contain the detailed rules of the new model. Subsequently, presidential

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regulations will be forthcoming, which will provide due observance of the law at the administrative level. Next, general administrative provisions will be issued by the regulatory agency. Lastly, we will see the specific permits and contracts. The path will consist of pursuing effective competitive conditions and promoting strong regulations as needed in accordance with the model conceived by the substantive and transitory articles of the constitutional reform.

Meanwhile, those working on the energy reform's regulations should consider the following:

1. The tenth transitory article, paragraph (c) of the decree of constitutional reforms grants the CRE the power to regulate the generation of electricity and wheeling fees for the transmission and distribution of electricity. There is no room for confusion: the Department of Finance and Public Credit should no longer determine the fees that the CFE charges for its network services or for electricity as a product. Finally, a technical specialized regulatory agency will be in charge of such work based on a meticulous cost analysis. Nevertheless, the CFE will continue to be a dominant player in the generation and marketing of electricity, and the regulations should treat it as such if we desire a strong market to flourish in the mid-term. Furthermore, consumer subsidies should be granted to those who truly need them in accordance with energy and social policy, and not as a result of regulatory considerations.
2. Paragraph (a) of the eleventh transitory article leaves the Department of Energy (*Secretaría de Energía*, SENER) as coordinator of the sector and grants it the power to establish the terms of the strict legal separation that will be required to promote open access and efficient operation of the electricity sector, and to oversee compliance. The intent was for SENER to construct the so-called "Chinese walls." Nevertheless, such a mandate will be exhausted when the rules for the operation of at least two State-owned companies are established: the first one in charge of the generation and marketing of electricity, and the second in charge of transmission and distribution. As a result, responsibility for the true and effective regulation of open access to the network should belong to the CRE through the issuance of terms and conditions and economic regulation of electricity transmission and distribution services, and the approval of the rules for dispatch and other instruments to be applied by the new system's independent operator.
3. The National Energy Control Center (*Centro Nacional de Control de Energía*, CENACE) will play a key role in the new model. As an independent operator, it will ensure that the CFE does not unduly discriminate in providing access to the electricity grid for its own generation purposes. The basis for this is found in transitory article sixteen, subsection (b) of the reform decree. In any case, since the CENACE is being created as a decentralized organism, as part of the Federal Public Administration, it must be ensured that the various interested parties participating in the industry have a voice according to the international best practices.
4. The law shall regulate the procedures for contracting so that individuals may participate in the financing, installation, maintenance, management, operation and expansion of transmission and distribution infrastructure. Perhaps a permits system would have been more appropriate to encourage private participation in these activities, as had been proposed by the PAN. Given that there was not much success in the drafting of the eleventh transitory article of the decree for constitutional reform, the law must be very clear on the scope of the exclusivity of the State in transmission and distribution, and what activities will be done "on behalf of the nation," in addition to what should be understood by operation and management for hiring purposes. At issue is how to establish the appropriate incentives to grow the infrastructure of the national electricity system, particularly to develop the enormous potential for renewable energy.
5. A big question is what kind of obligations with respect to clean energy and reduction of pollutants will be established under the law for participants in the electricity industry, as ordered by the seventeenth transitory of the reform decree. Hopefully, the drafters are thinking of what has been called in the United States "renewable portfolio standards," by means of which various states force suppliers to provide a certain percentage of their electricity from renewable sources. In a best case scenario, this could be accompanied by strict federal controls on emissions of greenhouse gases and the corresponding emissions rights markets which help to optimize the energy mix as a whole. The mature technology of some renewable energy, such as wind and, more recently, solar photovoltaic, suggests that subsidies may not be required in Mexico (on the contrary, the new framework seems to encourage abandoning prevalent general subsidies on gasoline, diesel and propane).

In its electricity sector restructuring, Mexico is at least 20 years behind most countries in the Organization for Economic Cooperation and Development (OECD). Mexico should use this lag in implementation to its advantage and learn lessons from the international experience of other countries that have already reformed their electricity sectors. For now, Congress will be in charge of building a good electricity market with strong regulations aimed at benefiting the end consumer and regulations which presuppose that the electric industry is the industry that most contributes to climate change. P

Seychelles International Business Companies Compliance Requirements

Given the latest amendments to the Seychelles International Business Companies Act of 1994, we would like to summarize those requirements, which every international business company (IBC) incorporated in the Republic of Seychelles must comply with.

First, every IBC must have a registered office in Seychelles, according to Section 38 of the IBC Act. Also, in Section 39 the provision indicates that every IBC must have a registered agent in Seychelles, which is licensed to provide international corporate services under the International Corporate Services Act 2003. The agent must have a non-fiduciary role and act as the IBC's point of contact in Seychelles.

According to Section 28 of the IBC Act, an IBC must keep a Share Register (Register of Members), which must contain the following information (at minimum):

- the name and address of each shareholder;
- the number of each class and series of shares held by each shareholder;
- the date on which the name of each member was entered in the register; and
- the date on which any person ceased to be a member.

This Share Register must be kept at its registered office in Seychelles, and may be in electronic or other data storage form (i.e. a PDF or Microsoft Word copy is sufficient).

A penalty of US$100 and an additional penalty of US$25 for each day that the violation continues may be imposed on those IBCs that do not keep the above-mentioned Share Register, as well as on the IBC's Directors, who knowingly permit these violations.

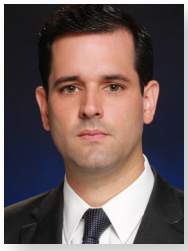
Also, Section 65(2)-(7) of the IBC Act establishes that Seychelles IBCs must keep a Register of Directors, which must contain the following information (at minimum):

- the name and address of each director and other officer of the company;
- the date on which each person whose name is entered in the register was appointed as a director or other officer of the company;
- the date on which each person named as a director ceased to be a director or other officer of the company.

As well as the Share Register, the Register of Directors must be kept at the IBC's registered office in Seychelles, and may be in electronic or other data storage form (i.e. a PDF or Microsoft Word copy is sufficient).

In addition, the same penalty of US$100 and an additional penalty of US$25 for each day that the violation continues may be imposed on those IBCs that do not keep the above-mentioned Share Register, as well as on the IBC's Directors, who knowingly permit these violations.

Furthermore, an IBC is required to keep, inside or outside of Seychelles as the directors shall determine, minutes



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of all meetings and copies of all written consent resolutions of directors and members ("minutes and resolutions").

When these minutes and resolutions are not kept at its registered office in Seychelles, the Registered Agent must be notified in writing of the physical address where they are; and in case this location changes, the company must inform its Seychelles Registered Agent in writing of the physical address of the new location of the minutes and resolutions within 14 days of the change of location.

For this, a penalty of US$25 for each day that the violations continues may be imposed on those IBCs that do not keep their minutes and resolutions according to the Act, as well as on the IBC's Directors, who knowingly permit these violations.

The amendments now also regulate, under Section 65(1) of the IBC Act, the Keeping of Accounting Records while the company is active and seven years from the completion of the transactions or operations to which they each relate (*understanding as accounting records all the documents relating to the company's assets and liabilities, company receipts and expenditure and sales, purchases and other transactions to which the company is a party – for example, bank statements, receipts, title documents, agreements, vouchers, etc*); and it obliges IBCs to keep or cause to be kept proper accounting records that:

(a) are sufficient to show and correctly explain the company's transactions;

(b) enable the financial position of the company to be determined with reasonable accuracy at any time; and

(c) allow for accounts of the company to be prepared (notwithstanding that an IBC is not required under the IBC Act to prepare accounts).

As well as the Minutes and Resolutions, the IBC is required to keep, inside or outside of Seychelles, as the directors shall determine, its accounting records. And, when these accounting records are not kept at its registered office in Seychelles, the Registered Agent must be notified in writing of the physical address where they are. In case this location changes, the company must inform its Seychelles Registered Agent in writing of the physical address of the new location of the minutes and resolutions within 14 days of the change of location.

In addition, although these accounting records are permitted to be kept outside of Seychelles, law requires that they can be made available by the IBC on request in Seychelles through the IBC's Registered Agent. This would apply, for example, if there is a legal request for information made by the Seychelles governmental authorities or courts.

As well as with the Registered Agent and Registered Office in Seychelles provision, an IBC which violates the account record-keeping requirements under the IBC Act is liable to a penalty of US$100 and an additional penalty of US$25 for each day during which a violation continues. A director of an IBC who knowingly permits the violation is also liable for a penalty of US$100 and an additional penalty of US$25 for each day during which a violation continues.

On the other hand, according to Section 119 of the IBC Act; every IBC must, by December 31 of every year, furnish only to its Seychelles Registered Agent a return in the form of a written declaration (the "Annual Return") that provides to the effect that:

(a) the company is keeping accounting records in accordance with the IBC Act and that such records can be made available through its Registered Agent in Seychelles; and

(b) the company's Share Register located at the Seychelles registered office is complete and up-to-date.

This Annual Return, according to the Registrar's Guidelines, may be made and submitted on the company's annual renewal date, provided that in every year, the Annual Return is submitted to its Seychelles Registered Agent by no later than December 31.

The same penalty as for the accounting records keeping applies if this requirement is violated.

Finally, pursuant to amendments to the IBC Act made by the International Business Companies (Amendment) Act 2013 (the "Amendments"), IBCs are no longer permitted to issue bearer shares.

In this regard, an IBC that has any issued and outstanding bearer shares is required to recall and cancel such bearer shares by June 16, 2014 (six months after the Amendments went into effect) and to issue registered shares in substitution for the cancelled bearer shares. That being said, any bearer shares that have not been recalled and cancelled by June 16, 2014, will be deemed null and void and have no legal effect. P

Public Private Partnerships in Developing Countries: Concept, Characteristics and Mechanisms for Implementation in Colombia

Public Private Partnerships (PPPs) or Public Private Associations (PPAs), are a mechanism by which the private sector delivers a public service (utilities, infrastructure, etc.) in alliance with the public sector, interested in fulfilling its goals by sharing risks, responsibilities and benefits.

Nevertheless the term "shared risks" usually means the risk is passed to the private sector rather than shared. To this point, one must bear in mind that the public sector in developing countries has, among other things, limited resources, unqualified human personnel and inefficient management systems. On the other hand, the private sector has know-how, experience, competence, innovation, and well-trained people.

In summary, PPPs are considered a useful tool to integrate and help the public sector fulfill its social functions and to attract foreign investment, thus improving the economy in developing countries.

The key elements according to author Peter Snelson[1], to promote and implement PPPs in emerging economies, are as follows:

- **Maximizing value for money**: Delivery by the private sector is designed to maximize efficiency and innovation as well as minimize costs and time overrun.
- **Reducing public debt or off-balance-sheet financing**: Allows the reduction of public sector borrowing and enables the procurement of services that are consistent with policies to drive economic development; in this case construction or reconstruction of infrastructure triggers economic growth, which is a tool for poverty reduction.
- **Strengthening infrastructure and public utilities**: This can be achieved by providing services that would not otherwise be available within existing public budgets of developing countries.
- **Financing tool for emerging countries**: Becomes a suitable tool to finance their development, establishing the legal mechanisms to secure the correct use of resources, whether public or private, to be invested in infrastructure, housing and utilities systems projects.

PPPs under Colombian Law

PPPs are enshrined in Act 1508 of 2012, regulated by National Decree 1467 of 2012 and modified through Act 1682 of 2013.

Public Private Partnerships are defined, in Article 1° of Act 1508 of 2012, as follows: "*The Public Private Associations are an instrument to bind private equity, that materialize in a contract between a public/state entity and a natural person or legal private entity, for the provision of public goods and its related services, that involves the retention and transfer of risks between the parties and the mechanisms of payment, related to the availability and level of service of the infrastructure and/or service.*"[2]

Regarding the legal definition, it is possible to say that PPPs in Colombia are

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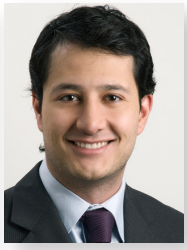

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considered contracts between public and private sectors for building infrastructure or providing public utilities. Through this legal instrument, the Colombian Government expects to sustain the growth rate of the Colombian economy and promote and enhance private sector participation, trying to overcome infrastructure and public utilities deficiencies and gaps with respect to other emerging economies.

Key Issues and Concerns before Undertaking a PPP Project

There are some key issues that must be analyzed and considered before any PPP is undertaken:

- **Project settlement**: The project must be justified and all real options must be evaluated.
- **Legal certainty**: Clear and fair rules for the parties involved in the PPP and its future contractors are essential for the project's success.
- **Technical viability and flexibility**: In order to achieve suitable and ideal value for money and innovation, it is necessary to ease the procurement requirements and permits to carry on the project activities.
- **Financial feasibility and investment attraction**: The project must be lucrative in order to facilitate the private sector participation which will allow the PPPs to have better financial conditions.
- **Public sector commitment**: The state, department or municipality involved in the project must be committed to carry out the aforementioned tasks during the entire process, working in harmony and joining efforts with the private sector in order to achieve the PPP's objectives.

PPP Structure Challenges and Trust as an Ideal Solution

Today, the main challenges to PPP projects in Colombia are commercial risk and uncertainty.

The private sector is not in a position to undertake large investments without significant debt financing from financial institutions (usually 30 percent equity and 70 percent debt). Lenders generally have specific concerns, as they lend money against known commercial risks and usually are afraid of assuming legal and political risks associated with the project.

For the purpose of addressing these issues, trusts can be implemented as tools not only for the administration of the public sector resources, but also to control the way they are invested.

To control uncertainty, the PPP´s trust can include the following provisions and regulations:

- **Framework**: Establish a strong legal framework for lenders regarding the use of resources by the person or people in charge of the project.
- **Guarantees**: Settle guarantees linked to the resources delivered – preference, payment and other kind of guarantees. Stipulate that it will be the trust, not the persons chosen by the government, who will be in charge of the development of the project, or the one who is going to own the goods required for its development.

  As a result, all the assets-rights of the contract and all the goods acquired to fulfil the obligations linked to it will be owned by the trust.
- **Government**: It is possible to create an internal organization in which banks and institutional lenders could have a seat. From there, they will be able to monitor the project and the way the resources are being invested.
- **Clear rules for dissolution or liquidation of the trust**: It allows the regulation of a complete framework to protect the investor's interests through the allocation of the trust assets in case of liquidation.

In Colombia it is possible to find good examples of such trusts. On one hand, some urban projects were implemented by the private sector for the development of nearly 35,000 housing solutions where trusts were used to administrate the resources and to regulate the participation of the public sector. Additionally, during the last two years, the current government used trusts as a mechanism to administrate almost 2 billion dollars with the objective of building another 100,000 housing solutions; currently at least 30,000 of these housing solutions have been delivered to their final beneficiaries.

It can be concluded that to the extent a legal regime provides a cohesive and clear structure for the grant of concessions, lenders will be encouraged to provide financial support to PPP projects. The legal regime should recognize the lender's interest in establishing effective security over the project and in ensuring effective enforcement remedies. Trusts could play an essential role considering that within its internal regulation, investors, project managers and the public sector are able to create the necessary environment to enhance their participation, secure their rights and develop the projects effectively.

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2 Free authors translation.

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Investment via Limited Partnership Falls out of Double Tax Treaty

The 2014 G-20 Heads of Government Summit in Australia follows other 2014 G-20 meetings in Australia, including meetings of finance ministers, trade ministers and central bank governors. On the agenda is the contribution of trade agreements towards economic growth. Australia is a party to free trade agreements with the United States, New Zealand and Korea, and it recently concluded an economic partnership agreement with Japan.

These treaties, along with applicable double tax treaties, form an important part of the framework for cross border dealings. They also increase uniformity of treatment, but some differences remain.

This article focuses on the 2014 Australian full Federal Court decision in Commissioner of Taxation v Resources Capital Fund III LP, which involved consideration of the Australian/United States double taxation treaty, as well as principles for valuation of business components.

Background

The Resources Capital Fund III Limited Partnership (RCF) was a Cayman Islands limited partnership with a Cayman Islands general partner. Almost all of the limited partners were U.S. residents. The partnership invested in an Australian company, St. Barbara Mines Limited (SBML). RCF sold the shares in SBML for a gain of over $58 million. The Australian tax authorities wished to tax that gain on the basis that the sale resulted in a capital gain liable for tax in Australia.

At this point it is important to note that with some exceptions (including for certain venture capital limited and management partnerships), corporate limited partnerships are treated as taxable entities under Australian law even though for United States tax purposes they may be regarded as tax transparent (i.e. the partners rather than the partnership being assessed to tax).

The Australian Taxation Office (ATO) assessed RCF under Division 855 of the Australian Income Tax Assessment Act 1997, which applied Australian tax to a foreign resident on a capital gain on the sale of shares in an Australian company only if the shares were an "indirect Australian real estate property interest," which in turn required that the shares constitute a greater than 10 percent interest in the company and that the sum of the market value of the company's assets that are taxable Australian real property (TARP) must exceed the market value of the company's non-TARP assets. TARP assets include real property and mining rights in Australia.

Note that a different regime would apply where the foreign resident has used an Australian permanent establishment.

The Valuation Issue

The assets of SBML included mining rights (which constituted TARP), and mining information together with the plant and equipment (which was not TARP).

Selwyn Black

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The trial judge suggested that the correct valuation approach was to value separately each category of assets as if it was the only asset offered for sale in a transaction. However on appeal the full Federal Court preferred to measure the market value of the individual assets on the basis that they "are to be ascertained as if they were offered for sale as a bundle, not as if they were offered for sale on a stand alone basis." This meant that a hypothetical purchaser of the TARP assets might expect to acquire the mining information and the plant and equipment for less than their production or acquisition costs and without material delay. This reflects the reality that information and plant will generally be sold to the purchaser of the relevant mine. The result was that the TARP assets exceeded the non-TARP for a least one relevant date, and the transaction was taxable, subject to the application of the U.S./Australia double tax treaty.

Double Tax Treaty Issue

The general Australian tax laws are subject to inconsistent provisions of relevant double tax treaties. The U.S. limited partners may have had the benefit of protection under the U.S./Australia double tax treaty if the relevant tax payer was a U.S. resident. As noted, for U.S. purposes the limited partnership was regarded as fiscally transparent (i.e. a pass through situation). However, with some exceptions, Australian tax law treats a corporate limited partnership as a separate taxpayer, generally taxed as if it was a company, so that apart from the treaty Australian tax law would treat the taxpayer as a Cayman Islands limited partnership rather than looking through to the U.S. limited partners.

The trial judge paid heavy regard to the OECD commentary on the model tax treaty on which the Australia/U.S. double tax treaty was based, to find that the U.S. limited partners were the relevant taxpayers, and accordingly protected by the double tax treaty.

On appeal the full Federal Court said that the Australia/U.S. double tax treaty did not apply because RCF (i.e. the taxpayer assessed, being the Cayman Islands limited partnership rather than the partners), was neither a resident of the United States nor a resident of Australia.

Subject to any further appeal or change in the law, one consequence is that where there are TARP assets (e.g. mining rights or real estate), a non-Australian investor should consider investing directly from an entity in a treaty jurisdiction, to reduce the risk of double tax. In addition, other structures and specific advice should be considered. While the context here is Australia/U.S., similar issues may occur under other double tax treaties where there is an interposed entity or structure, even a fiscally transparent one, with a domicile different to the parties of the treaty.

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Fighting for Justice

On Monday morning the week of Thanksgiving 2013, Marie, a client of Primerus member firm Lewis Johs Avallone Aviles, arrived at the firm's New York City office with her 17-year-old son, Alex, carrying tubs filled with food. One by one, they presented dishes in a traditional Haitian Thanksgiving feast – four kinds of pasta, salmon, turkey, rice, fish, pie and much more.

It was the only payment this mother could offer to the firm, whose Special Education Group had worked tirelessly to gain her son access to a state funded

school for students with Autism – a right afforded to him under the federal Individuals with Disabilities Education Act (IDEA).

According to Eileen Libutti, managing partner of the firm's New York City office, every member of the firm's Manhattan office sat around the table feasting. "This one woman who didn't have much money managed to bring us all together as a community in a way we don't often get to. For every lunch that week, we were eating leftovers. On Wednesday, you were eating things that you hadn't gotten to on Monday," Libutti said. "We were able to assist a very motivated single mom to effect lasting change on her son's education, self-esteem and transition to adulthood. She also left a lasting impression on us and taught us to take a moment to be thankful and experience joy."

The Lewis Johs Special Education Group has helped many families of students with disabilities obtain the free and appropriate public education that they are entitled to under IDEA. Libutti, a founding member of the group, and her colleague Maggie Cowley, said that often language barriers and financial need put families at a disadvantage in dealing with the New York City Department of Education (DOE) to secure a proper education for children with learning and developmental disabilities.

"Lewis Johs has been very supportive of us taking these cases that scream out for justice," Libutti said.

Marie came to them seeking a state-approved school for her son, Alex, who Libutti and Cowley described as a non-verbal gentle giant who likes to cook and loves animals. In January 2014, Libutti and her team prevailed in a hearing, securing Alex a placement at the Westchester Exceptional Children's School, Libutti said.

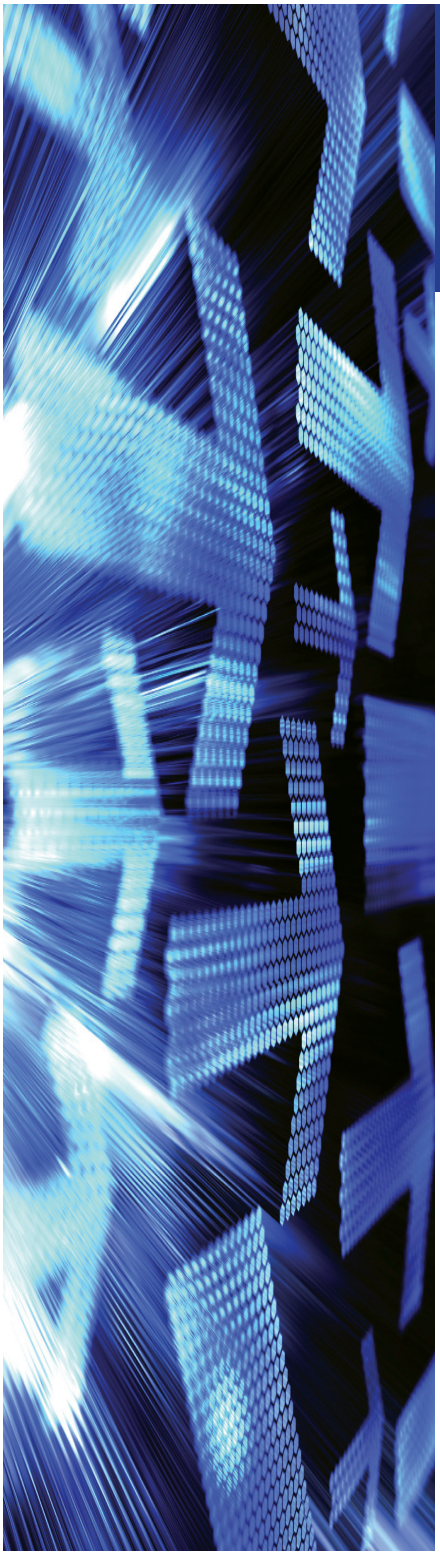
Libutti and Cowley bring to Alex's case, and others, not only deep knowledge and experience, but also personal passion. As a child, after seeing "Children of a Lesser God," Libutti dreamed of being a lawyer for the hearing impaired. Now, as a mother of 8-year-old twins, she draws fulfillment not only from helping the students, but also their parents. "We have seen some extraordinary mommies and daddies and all they want is what's appropriate for their child to learn," she said. "To help them avoid that feeling of desperation is pretty rewarding."

Cowley went to law school, forever changed by a childhood memory. As a teenager, she was diagnosed with a hip deformity which required multiple surgeries and confined her to a wheelchair for about six months. "That feeling of how badly you want to do things for yourself stuck with me," Cowley said. "I wrote on my application to law school about how I wanted to fight for people with disabilities."

Another founding member of the group, Jennifer Frankola, was a former full time public school teacher, and therefore understands and appreciates the needs of students and their families, as well as the complexities of the education system.

Now, Libutti, Frankola and Cowley dedicate their talents to representing families in need as much as possible.


Lewis Johs Avallone Aviles, LLP
Counsellors at Law



2014-2015 Calendar of Events

Scan this with your smartphone to learn more about Primerus.

September 18-19, 2014 – Primerus Defense Institute Professional Liability and Insurance Coverage and Bad Faith Seminar
Chicago, Illinois

October 9-12, 2014 – Primerus Global Conference
Monterey, California

October 28-31, 2014 – Association of Corporate Counsel Annual Meeting
New Orleans, Louisiana – *Primerus will be a corporate sponsor*

November 5-7, 2014 – Professional Liability Underwriting Society International Conference
Las Vegas, Nevada – *Primerus is a corporate member*

February 18-21, 2015 – Primerus Consumer Law Institute Winter Conference
Indian Wells, California

February 19-20, 2015 – Primerus Defense Institute Transportation Seminar
San Diego, California

March 18-20, 2015 – Primerus Young Lawyers Section Boot Camp
San Diego, California

April 23-26, 2015 – Primerus Defense Institute Convocation
Amelia Island, Florida

Plans for additional events in 2014-15 are underway. For updates please visit the Primerus events calendar at www.primerus.com/events.

For additional information, please contact Chad Sluss, Senior Vice President of Services, at 800.968.2211 or csluss@primerus.com.

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