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SEEKING LIBERTY & JUSTICE

# ANTITRUST NEWS

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## The Chair's Comments

As another Bar Association year draws to a close, I want to thank all those who have contributed to the work of the Antitrust Section this year. As one of the smaller sections in the North Carolina Bar Association, we cannot and do not take your membership and participation for granted. We know that you have numerous choices in allocating your professional development dollars, and we appreciate the choice you have made. To demonstrate our appreciation, we strive hard to respond to the feedback that the section receives from its members.



Don Esposito, Jr.

One example of this is our recent annual CLE program, "*The Changing Dynamics of Antitrust Law: From Local to Global*," held in May in Charleston, South Carolina. As many of you may know, for the past several years, we have sponsored or co-sponsored CLE programs that were intended to, and did, actually appeal beyond our section's membership to a broad range of the Bar Association at large. For instance, the section recently offered programs focusing on Chapter 75 and complex litigation in the North Carolina Business

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## The Supreme Court Steps Into the Chapter 75 Fray

### Walker v. Fleetwood Homes

BY CLINT PINYAN

Over recent years, North Carolina's antitrust and trade regulation bar has watched two developments with great interest. One is the growing attempt, through both legislation and litigation, to define conduct in a variety of industries as *per se* unfair and deceptive trade practices, with resulting treble damages remedies. The second is the intense debate over the unresolved question of who, other than a direct purchaser of an item, can bring unfair and deceptive trade practices claims related to the purchase of that item.

Those developments have largely played out without the input of the North Carolina Supreme Court, leaving substantial questions about what the high court would do when presented with these issues. The Supreme Court shed some light on these topics in December 2007, when it decided **Walker v. Fleetwood Homes, Inc.**, 362 N.C. 63, 653 S.E.2d 393 (2007). That opinion seemingly answered certain questions about these issues, but it left other questions unresolved.

#### Background of Walker

**Walker** concerned claims brought by a father and his adult daughter for defects in a manufactured home built by Fleetwood Homes. The purchase was what is referred to in the industry as a "buy for" transaction. The daughter selected the home and was to live in it, but she was disabled and could not qualify for credit. Instead, her father financed and bought the home on her behalf – a fact that was apparently known by the retailer but not disclosed on the documents provided to Fleetwood Homes. The purchase documents

solely disclosed the father as the buyer.

The home had numerous defects, which Fleetwood Homes did not correct. The daughter never lived in the home, and the plaintiffs attempted to rescind the purchase. Those attempts were rebuffed.

The plaintiffs sued Fleetwood Homes, as well as the retailer and finance company. The claims against the retailer and finance company were resolved before trial, and the causes of actions against Fleetwood Homes were whittled down. The plaintiffs ultimately went to trial against Fleetwood Homes on the father's claims for breach of warranty and both plaintiffs' claims for unfair and deceptive trade practices.

As the case was tried, the unfair and deceptive trade practices claims almost exclusively piggybacked on the provisions of the North Carolina Manufactured Housing Board Act (the "Act") and its regulations. Therefore, to understand the unfair and deceptive trade practice claims, one must understand the Act.

The Act is an occupational licensing statute that establishes the Manufactured Housing Board and requires certain members of the manufactured housing industry to be licensed by the Board. As with other occupational licensing statutes, the Act provides for conditions of licensure, including requiring licensees to comply with certain professional standards. Among those standards, it provides that a license may be denied, suspended or revoked, or the licensee may be fined, if the licensee has employed "unfair methods of competition" or committed

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## Comments *from page 1*

Court. All the while, at least a portion of our membership was vocal about our section's obligation to provide programs focused on antitrust issues that no other section could or would. We heard you, and we did so this year. This year's CLE attracted speakers the like of Commissioner Tom Rosch of the Federal Trade Commission and our own Matt Sawchak of Ellis & Winters (listed in alphabetical order, of course, Matt). We were also privileged to have prominent Charleston attorney Robert Brunson of Nelson Mullins Riley & Scarborough speak about recent development in South Carolina antitrust law. We are proud to be able to organize and sponsor such an insightful and thought-provoking program.

Another example: the section recognizes that it would not exist – and the practice of antitrust and trade regulation law in North Carolina would be vastly different – if not for

the vision of a few dedicated individuals who have contributed so much to North Carolina and the Bar Association in this area. It therefore gives me great pleasure to report that, at its Annual Meeting, the section approved the creation of a Distinguished Service Award to recognize such individuals. The Distinguished Service Award will be given biannually at the section's Annual Meeting in the spring, with the first such award to be given in the spring of 2009. Look for nomination forms and other information to be distributed in the fall.

Finally, I would be remiss if I did not recognize and thank this year's Section officers and committee chairs: Jon Heyl; Clint Pinyan; Jennifer Van Zant; Mitch Armbruster; George Sanderson; Bill Mayberry; Lawrence Moore; Pamela Shores; Hal Kitchin & Lisa Garrison. You have made it a pleasure to serve this year as the Section's Chair, and I personally appreciate your many contributions. ■

## Chapter 75 *from page 1*

“unfair or deceptive acts or practices.” G.S. Section 143-143.13(a)(7).

In framing the disciplinary provisions in the Act, the General Assembly did not define what constituted an “unfair method of competition” or “unfair or deceptive act or practice.” Instead, the agency adopted regulations that define some of the industry practices that constitute unfair practices that can give rise to discipline under G.S. Section 143-143.13. Those include “failure to perform repairs, alterations and/or additions completely or in a workmanlike and competent manner” and “repeated failure to respond promptly to consumer complaints and inquiries.” 11 N.C.A.C. 8 .0907(1) and (4).

Like other occupational licensing statutes, the principal purpose of the Act is to regulate the conduct of its licensees through the regulator's ability to revoke, suspend or otherwise discipline a licensee. But, unlike other occupational licensing statutes, the Act provides a private right of action for “any buyer of a manufactured home” who has suffered any loss or damage from any violation of the Act. G.S. Section 143-143.12(c). Pursuant to this provision, injured buyers can recover against the bond that licensees are required to provide.

The Walker plaintiffs tied their unfair and deceptive trade practices claims closely

to these regulatory provisions. They submitted verdict forms asking the jury to find that Fleetwood Homes violated the regulatory provisions, copying the regulations almost verbatim. There were no other issues submitted to the jury that asked them to find any other conduct by Fleetwood Homes to support the G.S. Section 75-1.1 claim.

The jury returned a verdict finding that Fleetwood Homes had acted in violation of the regulations and finding that both plaintiffs were entitled to damages. Based on those jury findings, the Superior Court entered judgment for both plaintiffs. It pointed to the two jury responses that found regulatory violations and held that those acts “are specifically delineated and defined as unfair and deceptive commercial acts or practices” by the agency charged with licensing members of the manufactured housing industry.

The Court of Appeals affirmed the judgment's conclusion that Fleetwood Homes was liable to both plaintiffs on their G.S. Section 75-1.1 claims, but it remanded for a new trial on damages. Judge Jackson dissented from the Court of Appeals' decision as to the daughter's claim. Judge Jackson would have held that the daughter lacked standing as an indirect purchaser, whether that standing was based on G.S. Section 75-16 or on

the private right of action contained in the Act itself, G.S. Section 143-143.12(c). With that background, the Supreme Court took up the case.

### Regulations as the Basis for a Section 75-1.1 Claim

Before the Supreme Court, the principal issue on the merits was whether, and in what fashion, a violation of the manufactured housing regulations could give rise to a claim under G.S. Section 75-1.1. The plaintiffs contended that, by passing G.S. Section 143-143.13, the General Assembly had intended to proscribe unfair and deceptive trade practices in the manufactured housing industry. They further contended that the Manufactured Housing Board's regulations defined the standard of practice in the industry – including specifically defining certain conduct related to repairs and responses to customer complaints – as unfair and deceptive trade practices. They thus argued that violation of the regulations constituted a *per se* violation of G.S. Section 75-1.1 or that, at a minimum, the Superior Court properly concluded that, on the facts of this case, the regulatory violations constituted violations of G.S. Section 75-1.1.

In contrast, Fleetwood Homes argued that it was improper and dangerous to allow a private plaintiff to leverage regulations promulgated for the purpose of license disciplinary proceedings into a *per se* claim under Section 75-1.1 and a corresponding treble damage remedy. It further argued that violations of these particular regulations governing repairs and responses to complaints amounted simply to variations on a breach of warranty claim. Fleetwood Homes argued that its violation of these regulations did not give rise to liability under G.S. Section 75-1.1 at all, let alone *per se* liability under the statute.

The *Walker* case arose against the backdrop of legislative expansion of the number of statutes whose violations constitute *per se* violations of G.S. Section 75-1.1. In recent years, the General Assembly has been quite active in enhancing private enforcement of a wide range of statutes by specifically providing that violations of those provisions are also *per se* violations of Chapter 75. This burgeoning legislative growth in unfair trade practice law was well-chronicled by Don Esposito in “Legislative Expansion of the Scope of North Carolina’s Unfair Trade Practices Act” in the March 2005 *Antitrust News*.

But the vast majority of those statutes are quite different from the Manufactured Housing Board Act at issue in *Walker*. In the lion’s share of such statutes, the General Assembly has described a specific industry practice that it views as *per se* “unfair and deceptive.” Most often, the General Assembly has made explicit its intention to create a Section 75 remedy for the violation. *See, e.g.*, G.S. Section 25A-44 (Retail Installment Sales Act violation); G.S. Section 42A-10 (vacation rental agreement violation).

The Manufactured Housing Board Act stands in stark contrast to those statutes. It is an example of a small handful of occupational licensing statutes that (1) allow the occupational licensing board to take disciplinary action against licensees who engage in unfair or deceptive trade practices but (2) do not go on to explicitly define the scope of the conduct that the General Assembly views as unfair or deceptive. The Act also makes no attempt to link a violation of this licensing statute to a cause of action under Chapter 75. Other examples of such statutes include the Motor Vehicle Dealers and Manufacturers Licensing Law, G.S. Section 20-294(6), the Mortgage Lending Act, G.S. Section 53-243.12(m), and the state check-cashing license provisions, G.S. Section 53-283(5).

As a matter of professional governance, these statutes have certain salutary benefits. These statutes give the occupational licensing agencies the latitude to define – whether by regulation or by administrative case law – what sorts of practices are so unfair that discipline of a licensee is justified. They thus permit the agencies to employ their expertise about industry standards – expertise often not shared by members of the General Assembly – and to do so in fact-specific ways that the General Assembly could not in passing statutes of general applicability.

Specifically with respect to the Manufactured Housing Board Act, the agency employed its experience in the industry to determine that “failure to perform repairs, alterations and/or additions completely or in a workmanlike and competent manner” and “repeated failure to respond promptly to consumer complaints and inquiries” were unfair practices that would justify discipline on a license. 11 N.C.A.C. 8.0907(1) and (4). But, could the agency’s definition of that practice as unfair and deceptive give rise to treble damage liability?

That was the question before the court.

The *Walker* court ruled that violations of the Manufactured Housing Board regulations were not *per se* Section 75-1.1 violations. In doing so, it rejected more broadly the argument “that a violation of a licensing regulation is a UDTP [unfair and deceptive trade practice] as a matter of law.” 362 N.C. at 71, 653 S.E.2d at 399. But the *Walker* court went on to rule that violations of the Manufactured Housing Board regulations “may be evidence of a UDTP” and “are potentially relevant to any claim that defendant violated § 75-1.1.” *Id.*

Applying those principles to the *Walker* case, the Supreme Court ruled that, because the jury had been given a special verdict form with interrogatories that “were derived nearly verbatim from a licensure regulation, and violations of this regulation by themselves are insufficient to prove a UDTP claim,” the verdict form was insufficient to provide the court a basis to find a violation of G.S. Section 75-1.1. *Id.* at 72, 653 S.E.2d at 399. The Supreme Court therefore vacated the finding of Section 75-1.1 liability and remanded to the Superior Court for a new trial where it “may submit to the jury additional interrogatories seeking information which, if found by the jury, may be sufficient to support a finding of fact that defendant committed a UDTP.” *Id.*, 653 S.E.2d at 400.

The *Walker* decision leaves open some questions – both practical and legal. The interesting practical question is exactly what additional interrogatories the *Walker* plaintiffs would need to include in a special verdict form in order to support a finding of a violation of Section 75-1.1. Some might argue that, even if there were no Manufactured Housing Board regulations at all, jury findings that the defendant had “failed to perform repairs, alterations and/or additions completely or in a workmanlike and competent manner” and “repeatedly failed to respond promptly to consumer complaints and inquiries” would themselves constitute Section 75-1.1 violations. On the other hand, some might argue – as Fleetwood Homes did – that these sorts of interrogatories simply constitute a finding that Fleetwood Homes breached a warranty, which is insufficient to give rise to Section 75-1.1 liability. The Supreme Court gave no guidance about what more the jury must find in order to support a determination that

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Fleetwood Homes violated Section 75-1.1, and the court pointedly declined to address Fleetwood Homes' argument that the conduct in this case simply amounted to a breach of warranty. Therefore, it is not at all clear what sort of jury interrogatories, over and above the interrogatories finding regulatory violations, plaintiffs will need to offer to establish a Section 75 violation in this and other cases that seek to piggyback on similar regulations.

The appellate courts will soon have the occasion to flesh out this practical issue. When *Walker* was remanded, the Superior Court did not hold a new trial at all. Instead, it used the same special verdict form and jury interrogatories that had been answered by the jury at the initial trial as the basis for a new judgment for the plaintiffs. The trial court found again that Fleetwood Homes had committed a Section 75-1.1 violation. Fleetwood Homes has appealed the judgment. It will likely contend that the Supreme Court required additional jury findings above and beyond a finding of a regulatory violation in order to constitute a Section 75-1.1 violation and there were no such additional findings here, where the Superior Court entered judgment based on the same verdict form that the Supreme Court had rejected.

Moreover, the *Walker* decision leaves open certain legal questions about the interaction between regulations and unfair and deceptive trade practices law. To be sure, the *Walker* court took a broad stance against basing Chapter 75 claims exclusively on the violation of occupational licensing regulations. It drew a sharp distinction between certain statutory violations, which in some cases have been held to give rise to *per se* Chapter 75 claims, and licensing regulation violations, which it indicated could not constitute *per se* Chapter 75 violations.

One open question may occur with respect to certain regulations where (like the Manufactured Housing Board regulations), the agency has defined particular conduct that it considers to be unfair and deceptive, but (unlike the Manufactured Housing Board regulations) the underlying statute does provide a private right of action for unfair and deceptive trade practices. That situation currently exists with certain insurance regulations. The Department of Insurance has defined certain conduct to constitute an

unfair and deceptive trade practice, *see, e.g.*, 11 N.C.A.C. 4 .0314 through 4 .0318, 4 .0422, 12 .0561, 12 .1018, and it has done so pursuant to its authority to enforce a statute (G.S. Section 58-63-10) whose violation can constitute a *per se* Chapter 75 violation. Can violation of one of those insurance regulations give rise to *per se* Chapter 75 liability?

The *Walker* decision could be read to support either position. The *Walker* court did attempt to draw the line between statutes and regulations as a basis for a Chapter 75 violation. The court did not evidence any willingness to permit plaintiffs to try Chapter 75 claims simply by providing the jury with interrogatories tracking the language of regulations, regardless of the nature of the regulations. On the other hand, the Supreme Court did find it significant that the Manufactured Housing Board regulations were not adopted pursuant to a statute whose violation itself constitutes a Chapter 75 violation. In the insurance context, where the General Assembly did intend to create *per se* UDTP liability for statutory violations, would the courts permit the agency to promulgate regulations interpreting those statutes that themselves gave rise to *per se* UDTP liability? The Supreme Court could arguably view such a claim very differently than the one before it in *Walker*.

One additional open question after *Walker* may be how the court would react if, in the course of a disciplinary proceeding, there were an agency finding that a licensee committed acts that constituted unfair and deceptive trade practices under a regulation such as the one at issue here. Would such a finding give rise to Section 75-1.1 liability as a matter of law, whether as a matter of the decision establishing a *per se* violation or as a matter of *res judicata*?

Presumably the courts would hold that an agency finding of an unfair and deceptive trade practice under a regulation such as those at issue in *Walker* cannot give rise to *per se* Chapter 75 liability. If there must be something more than a finding of a violation of a licensing regulation (as the *Walker* court held), then the fact that an agency has found a violation, rather than a jury, should not matter – the jury must find something more to support a Section 75-1.1 claim. However, the bar should watch for that and other applications of the *Walker* decision to shake

out over the coming years.

### Indirect Purchaser Claims

The bar's interest in the *Walker* decision on the merits paled in light of its anticipation of the court's decision on the preliminary issue of who had standing to bring those claims. Based on the dissent in the Court of Appeals, the Supreme Court considered the question of whether the daughter could maintain an action when she had not been the direct purchaser of the home, but instead had her father purchase the home on her behalf as a "buy for" purchase. In addressing this issue, the Supreme Court took its first foray into the heated debate over indirect purchaser standing. It addressed the two issues raised by the dissent in the Court of Appeals: First, whether the daughter's standing was governed, not by Section 75-16, but instead by the narrower private right of action under Section 143-143.12(c). And, second, whether the daughter had standing if the general Section 75-16 standing provision applied.

In its brief, Fleetwood Homes focused exclusively on the first of these arguments. Fleetwood Homes argued that, because the plaintiffs were relying upon violations of the Manufactured Housing Board regulations to establish their claims, they had standing only if they could state a private right of action under the Manufactured Housing Board Act itself, Section 143-143.12(c). That section limits the private right of action on a surety bond to "buyers," which was defined in the statute in a way to exclude the daughter. Indeed, Fleetwood Homes did not independently discuss whether the daughter had standing under the language of Section 75-16.

The *Walker* court rejected Fleetwood Homes' argument that Section 75-16 did not apply. The court ruled that the Manufactured Housing Board Act right of action was not an exclusive remedy. Because the daughter was proceeding under Section 75-16, her standing was determined by that statute, rather than the Manufactured Housing Board Act.

This holding is not surprising in light of the *Walker* court's decision on the merits. As outlined above, the *Walker* court distanced the plaintiffs' Section 75-1.1 claim from the Manufactured Housing Board regulations by holding that its Section 75-1.1 claim required the jury to make additional findings over and above a violation of those regula-

tions. Because the court analyzed the Section 75-1.1 claim on its own merits, separate from the issue of the regulatory violations, it is natural that the court would analyze the issue of standing under Section 75 as well. The **Walker** court then addressed the issue of much more general interest – whether indirect purchasers have standing to bring a claim under the language of Section 75-16 – an issue that Fleetwood Homes had not argued. The court thus provided some guidance on an issue that has been percolating for more than three decades. Some background is in order.

The federal and state courts have taken different sides of the indirect purchaser debate into which the **Walker** court waded. In **Illinois Brick Co. v. Illinois**, 431 U.S. 720 (1977), the U.S. Supreme Court held that indirect purchasers do not have claims under the Clayton Act. The **Illinois Brick** court ruled that, where there was an alleged price fixing conspiracy among concrete block manufacturers, an action could be maintained only by their direct purchasers (masonry subcontractors) rather than by their indirect purchasers (owners of the buildings built with the concrete blocks). Although the language of the Clayton Act provides an action for “[a]ny person who shall be injured in his business or property,” the court reasoned that providing an action for indirect purchasers would risk duplicative recovery for both direct and indirect purchasers. Furthermore, even if there were no duplicative recovery, creating such an action would pose insuperable problems in managing litigation, proving damages and apportioning damages between direct and indirect purchasers.

In **Hyde v. Abbott Laboratories, Inc.**, 123 N.C. App. 572, 473 S.E.2d 680 (1996), the North Carolina Court of Appeals had the opportunity to interpret the similar provision of Section 16 of Chapter 75, which provides a private right of action for violations of both the state law antitrust provisions and the Unfair and Deceptive Trade Practices Act. The claims in **Hyde** were similar to those in **Illinois Brick**: indirect purchasers (infant formula consumers) maintained that a price fixing conspiracy among manufacturers had affected the price that was passed through the direct purchasers (retailers) to the consumers. Notwithstanding the similarity of the claims, the Court of Appeals rejected **Illinois Brick** as a matter of state law and determined that G.S. Section 75-16 provides a private right of action to both direct and indirect purchasers.

It did so even though the court did not find any significant difference between the language of G.S. Section 75-16 and Section 4 of the Clayton Act, which both provide an action to “any person” injured by a violation. In so ruling, North Carolina joined most other states, which allow some form of indirect purchaser antitrust claims.

The decade after **Hyde** has been marked by both substantial uncertainty and significant efforts to pull the law related to indirect purchasers in opposite directions. Those developments are chronicled in previous articles in the *Antitrust News*, most thoroughly in Henry L. Kitchen Jr., “An Update on Indirect Purchaser Litigation Under North Carolina Law” in the March 2006 issue, and Jason D. Evans, “Indirect Purchaser Antitrust Actions in N.C. Seven Years After **Hyde v. Abbott Laboratories, Inc.**” in the June 2003 issue. Those articles are commended for a more complete description of the lay of the land. While there have been efforts to move the law in each direction, the predominant trend appears to have been toward permitting more actions by indirect purchasers. At the federal level, the rumblings about overruling **Illinois Brick** crystallized last year with the recommendations of the Antitrust Modernization Commission that Congress overrule **Illinois Brick** and allow actions by indirect purchasers.

In **Walker**, the Supreme Court took its first look at this issue and took a stand on the side of expansive indirect purchaser standing, at least in the factual scenario presented in that case. At length, the **Walker** court discussed the reasoning of the Court of Appeals both in **Hyde** and in the decision below in **Walker**. It adopted the Court of Appeals’ reasoning that the language of Section 75-16 providing a cause of action to “any person” injured is broad and, in order to promote the remedial purposes of Section 75-16, is to be interpreted broadly enough to cover indirect purchasers such as the daughter in **Walker**.

Plaintiffs will contend that **Walker** has settled the indirect purchaser argument under Section 75, once and for all. And certainly the Supreme Court has indicated its willingness to adopt the **Hyde** principles.

But those arguing against indirect purchaser standing are not completely without hope. In presenting **Walker** to the Supreme Court, Fleetwood Homes did not dispute that the daughter would have standing under the language of Section 75-16. Therefore, the issue of how to interpret Section 75-16 was

not fully presented to the Supreme Court by the litigants. The Supreme Court could take a different view if the issue were more completely joined.

Moreover, the Supreme Court’s analysis focused on the unusual facts of **Walker**. The Supreme Court reasoned that the daughter had standing because she was the real consumer in the transaction. The father never intended to play any role except sign for a loan so that his daughter could buy a home.

This scenario does not present the ills of the usual **Illinois Brick** fact pattern, where class action claims are brought by both the intermediate consumers of the raw product (e.g., concrete bricks, rubber) and the ultimate consumer of the finished products (e.g., buildings, tires). In such a case, the courts have legitimate concerns about trying to manage litigation and to unscramble the egg to apportion damages between the two sets of consumers who consume different products (raw vs. finished) at different stages of the manufacturing process. Comparatively, it is easy to manage litigation and apportion damages in a case like **Walker**, where there are two plaintiffs who both simultaneously purchase a finished product as part of the same transaction. Therefore, defendants in the typical **Illinois Brick** context will certainly continue to argue that the Section 75-16 holding in **Walker** is distinguishable and that Section 75-16 does not provide indirect purchaser standing in other factual situations.

As with the issue on the merits, although the Supreme Court has lifted some of the fog surrounding standing under Chapter 75, there will be litigants who attempt to flesh out the precise contours of the **Walker** decision. ■

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# Trimming Back the Spread of the UDTPA

BY BRAD KUTROW

*This article originally appeared in Volume 20 Issue 3 of the Business Lawyer, published by the Corporate Counsel Section of the North Carolina Bar Association in March 2008.*

Claims under the Unfair and Deceptive Trade Practices Act (UDTPA), N.C.G.S. § 75-1.1, are the kudzu of business litigation in North Carolina. Since its adoption in 1969, the UDTPA has spread from its consumer-protection roots so wildly that it now is asserted in virtually every type of commercial dispute. The UDTPA's treble damages and attorneys' fees provisions allow plaintiffs to boost the amounts at stake, making the potential exposure and recovery in each case more than three times higher than it would be if only compensatory damages were sought. The result is that risk-averse defendants settle more cases and take fewer to jury trials.

In recent years, however, courts have found some ways to cut back the sprawling coverage of the UDTPA. A number of 2007 decisions, including several from the North Carolina Business Court, illustrate this trend and provide additional guidance for business lawyers who need to plead or defend UDTPA claims.

## Scope of the UDTPA

The UDTPA was originally based on language in the Federal Trade Commission (FTC) Act, under which the FTC acts to protect consumer interests. The UDTPA regulates "commerce," now defined by case law to include "all business activities, however denominated." This broad definition supports the UDTPA's application to both commercial and consumer transactions. Our Supreme Court has held that while the UDTPA was "clearly intended to benefit consumers," it also protects "businesses in appropriate contexts." *HAJMM Co. v. House of Raeford Farms, Inc.*, 328 N.C. 578, 592, 403 S.E.2d 483, 492 (1991).

As the case law developed, two important types of cases were fenced off from the UDTPA: securities transactions and employer-employee relations. The U.S. Court of

Appeals for the Fourth Circuit and later the North Carolina Supreme Court held that securities transactions were already subject to comprehensive federal and state regulation, so that the General Assembly could not have intended to have the UDTPA create "overlapping supervision, enforcement, and liability" in that area. *HAJMM* at 593, 402 S.E.2d at 492-93. Courts also concluded that employer-employee relations were outside the "intended scope" of the UDTPA. Because the UDTPA was enacted to promote fairness in dealings between buyers and sellers, courts concluded that it was not meant to cover typical employer-employee disputes. See *Buie v. Daniel Int'l Corp.*, 56 N.C. App. 445, 448, 289 S.E.2d 118, 119, *disc. rev. denied*, 305 N.C. 759, 292 S.E.2d 574 (1982). Such disputes were deemed not "in commerce."

In addition, courts routinely dismissed UDTPA claims that were asserted in simple breach of contract cases. Again following the Fourth Circuit's lead, North Carolina appellate courts held that "a mere breach of contract, even if intentional, is not sufficiently unfair or deceptive" to support a UDTPA claim. *Branch Banking & Trust Co. v. Thompson*, 107 N.C. App. 53, 62, 418 S.E.2d 694, 700 (1992). However, a plaintiff who could show "substantial aggravating circumstances attending the breach" could recover under the UDTPA and win treble damages. *Id.* (quoting *Bartolomeo v. S.B. Thomas, Inc.*, 889 F.2d 530, 535 (4<sup>th</sup> Cir. 1989)).

UDTPA claims are still pled in virtually every case where there is some basis to allege an "aggravating circumstance" accompanying a breach of contract, or where some aspect of an employment dispute arguably affects commerce more broadly. The *prima facie* elements of UDTPA are, simply stated, that:

- (1) the defendant committed an unfair or deceptive trade practice;
- (2) the action in question was in or affecting commerce, and
- (3) the act proximately caused injury to the plaintiff.

*Oberlin Capital, L.P. v. Slavin*, 147 N.C. App. 52, 62, 554 S.E.2d 840, 848 (2001). The cases also provide that, before a practice can be declared unfair or deceptive, it must be deemed to take place "in commerce" as that term has been defined in earlier decisions. *Id.* Because of the UDTPA's broad language and the absence of any statutory defenses, claims of unfair and deceptive practices continue to be asserted in all kinds of business disputes.

## Trends in 2007 Decisions: Trimming Back the UDTPA

Last year, courts applied some of these precedents to new situations and found themselves cutting back on the UDTPA in several areas. In particular, the North Carolina Business Court has further defined the parameters of UDTPA claims.

**Capital Raising and other "Extraordinary Events" in Corporate Life.** As discussed above, the North Carolina Supreme Court held soon after the UDTPA was enacted that it did not apply to securities cases already governed by state and federal statutes. In the 1991 *HAJMM* decision, the court extended this rule to other capital-raising instruments like revolving fund certificates, holding that they were not "in or affecting commerce" as that term was meant in the statute. *HAJMM*, 328 N.C. at 594-95, 403 S.E.2d at 493. The *HAJMM* court held that the term "business activities" in the statute was intended to connote "the manner in which businesses conduct their regular, day-to-day activities, or affairs, such as the purchase and sale of goods, or whatever other activities the business regularly engages in and for which it is organized." It held that issuance, redemption, and transfers of securities were "extraordinary events," not "a business activity of the issuing enterprise," and thus were not subject to the UDTPA.

Ten years later, in *Oberlin Capital, L.P. v. Slavin*, the North Carolina Court of Appeals addressed a UDTPA claim arising from a loan and security agreement in which the plaintiff agreed to loan the defendant \$1.5 million in return for the right to purchase

stock in the future. The court held that the loan agreement was “primarily a capital-raising device” and affirmed the dismissal of its UDTPA claim. **Oberlin Capital**, 147 N.C. App. 52, 62, 554 S.E.2d 840, 848.

In 2007, the North Carolina Business Court got several chances to apply these precedents. In **Latigo Investments II, L.L.C. v. Waddell & Reed Fin., Inc.**, 2007 NCBC 17, 2007 WL 2570753 (N.C. Super. Ct. May 22, 2007), Business Court Judge Albert Diaz dismissed a UDTPA claim that alleged misrepresentations in connection with promised financing for a business acquisition. The **Latigo** plaintiffs owned MB2 Motorsports, L.L.C., a company which owned and operated NASCAR teams. As part of negotiations for a capital infusion into MB2, they were provided a letter from defendant Waddell & Reed attesting to an investor’s ability to provide the needed capital. The financing never materialized, and the plaintiffs were forced to sell their interest in MB2 on unfavorable terms in order to obtain financing for it elsewhere. Judge Diaz reviewed the holdings in **HAJMM** and **Oberlin** and concluded that, despite plaintiffs’ efforts to characterize it otherwise, the proposed financing was a “capital raising transaction” outside the scope of the UDTPA.

Judge Diaz noted that in **HAJMM**, Justice Mark Martin’s dissent had argued that there was no textual basis in the UDTPA for the view that “commerce” meant only day-to-day business activities rather than capital-raising transactions, which the **HAJMM** majority viewed as extraordinary events in a corporation’s life. “Were I writing on a clean slate,” Judge Diaz said, the UDTPA claim would not survive, because “like Justice Martin, I find no logical basis for excluding misrepresentations made in the context of capital raising transactions from the reach of what is intended to be a broad remedial statute.” *Id.* at 47, 2007 WL 2570753 at \*4. Constrained by the appellate precedents in **HAJMM** and **Oberlin**, however, he ruled that misrepresentations arising from a capital-raising transaction were not actionable.

Notably, Judge Diaz rejected the plaintiffs’ contention that the **HAJMM** precedent should apply only to the parties to the transaction itself, and not to third parties whose involvement was ancillary. What mattered under **HAJMM**, he said, was not “who is a party to the transaction,” but “what is the

purpose of the transaction.” *Id.* at 46, 2007 WL 2570753 at \*4.

Soon thereafter, Judge Diaz issued another decision that turned on the “extraordinary event” line of cases. **Lawrence v. UMLIC-Five Corp.**, 2007 NCBC 20, 2007 WL 2570256 (N.C. Super. Ct. June 18, 2007) was brought by Texas plaintiffs who had successfully sued the defendant UMLIC-Five Corporation in Texas. During the latter stages of their Texas case, the Lawrences discovered that UMLIC-Five (a North Carolina corporation) had been in dissolution for several years. UMLIC-Five then abandoned its defense in Texas, and the Lawrences obtained a \$3.8 million judgment there. The Lawrences then sued UMLIC-Five in North Carolina on various tort theories and statutory claims, including UDTPA. Judge Diaz dismissed the UDTPA claim because (1) the dissolution of a corporation is “an extraordinary event falling outside of an entity’s day-to-day business activities,” and (2) because the plaintiffs’ alleged injury did not arise from competition between the parties or consumption of goods or services in North Carolina and thus did not have a substantial “in-state effect on North Carolina trade or commerce.”

Finally, **Fliehr v. Storick**, also decided by Judge Diaz, arose from the plaintiffs’ relationship with their longtime insurance agent and financial advisor, defendant Storick. The plaintiff (better known by his professional name, “Nature Boy” Ric Flair) and his former wife asserted a host of claims against Storick, several insurance companies, and other individuals and companies involved in various investments and businesses that the Fliehrs alleged had cost them money. Citing **HAJMM**, Judge Diaz granted a partial dismissal of claims against one group of defendants, holding “misconduct arising from a merger of business entities is not the type of ‘regular, day-to-day’ business activity that is the principal focus of [the UDTPA].” **Fliehr v. Storick**, No. 07-CVS-1393 (N.C. Super. Ct., Mecklenburg County, Dec. 3, 2007) (Order on BWIRTHIT/Quickel Motion to Dismiss) (available at [www.ncbusinesscourt.net](http://www.ncbusinesscourt.net)). Other claims in the **Fliehr** case remain pending.

**Overlapping State Statutes, Regulations and Enforcement.** In July 2007, the North Carolina Court of Appeals again considered when a state statute or regulatory scheme will bar UDTPA claims in **State v. Ridgeway Brands Mfg., L.L.C.**, 646

S.E.2d 790 (N.C. App. 2007). The case arose in the context of the master settlement agreement between the State of North Carolina and the major American cigarette manufacturers, and turned on a statute enacted in 2005 following the settlement. The new statute, N.C.G.S. Section 66-291, requires manufacturers not participating in the master settlement to place certain funds in escrow, based on their sales. The attorney general sued Ridgeway for failing to place amounts in escrow and for civil penalties. In addition to pleading violations of Section 66-291, the state asserted that Ridgeway had violated the UDTPA, Section 75-1.1. The Court of Appeals held that application of both the UDTPA and Section 66-291 would create unnecessary and overlapping supervision, enforcement, and liability, citing **HAJMM**, and affirmed the lower court’s dismissal of the UDTPA claim. 646 S.E.2d 790, 798.

In another 2007 case where a government entity was the plaintiff, **Wake Co. v. Hotels.com, L.P.**, 2007 NCBC 35, 2007 WL 4125456 (N.C. Super. Ct. Nov. 19, 2007), Business Court Judge Diaz held that the UDTPA’s coverage was not so broad as to provide the government with a treble damages remedy in what he found was a “garden-variety” tax dispute. Several North Carolina counties had sued the owners of the Hotels.com and other travel Web sites, alleging that they failed to pay all the occupancy taxes owed on rooms booked through their sites. The defendants purchased blocks of hotels at discount rates, then resold them at higher rates via the Web sites. The defendants allegedly “charge and collect the Occupancy Tax from consumers based on the higher rate, but only remit amounts to each County based on the discounted rates paid to the hotel owners, thereby pocketing the difference.” *Id.* at 3-5, 2007 WL 4125456 at \*1.

Judge Diaz found that the counties’ claim, apart from an allegation that consumers were being misled by the travel sites about their liability for occupancy tax, amounted to “an ordinary, garden-variety failure to pay a tax.” He concluded that the UDTPA was not intended to provide a treble damages remedy in every tax dispute between the government and a taxpayer. He also held that the counties lacked standing to assert claims on behalf of any misled consumers; Chapter 75 gives such authority

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only to the attorney general.

Perhaps most importantly, Judge Diaz concluded that the existing criminal and civil penalties available for failure to remit occupancy taxes constituted an “extensive regulatory regime.” To allow the counties to pursue UDTPA violations on top of those civil and criminal penalties would violate HAJMM’s teaching against overlapping supervision, enforcement and liability. He therefore dismissed the counties’ UDTPA claim. *Id.* at 76-83, 2007 WL 4125456 at \*10-11.

**New Focus on “Internal Corporate Affairs” as Outside the Scope of the UDTPA.** Meanwhile, the Business Court and federal courts continued in 2007 to address cases that arose from internal corporate squabbles and sometimes involved disgruntled ex-employees.

In *Schlieper v. Johnson*, 2007 NCBC 29, 2007 WL 2580120 (N.C. Super. Ct. Aug. 31, 2007), Business Court Judge Ben Tennille addressed a variety of claims asserted by former employees of a re-insurance business. The plaintiffs, Schlieper and Pyrtle, had worked with the individual defendant, Johnson, in several companies. Johnson started a new company, Axiom, and offered Schlieper and Pyrtle employment there pursuant to “Letters of Understanding.” Part of their compensation was a percentage share of Axiom’s net profits, although neither had an equity ownership stake in Axiom itself. They were both allowed to participate in a “Phantom Stock Plan.” When Axiom’s assets were sold to another re-insurance company, Schlieper and Pyrtle disputed the amounts they received from Axiom following a “Phantom Sales Calculation” and the termination of their Letters of Understanding.

Judge Tennille compared the plaintiffs’ UDTPA claim to the key North Carolina Supreme Court precedents. While noting that the UDTPA “does not normally extend to run-of-the-mill employment disputes,” citing *Dalton v. Camp*, 353 N.C. 647, 656, 548 S.E.2d 704, 710 (2001), he observed that “[t]here are cases in which an employment dispute affects commerce in such a way as to give rise to a Chapter 75 claim,” pointing to *Sara Lee Corp. v. Carter*, 351 N.C. 27, 33, 519 S.E.2d 308, 317 (1999). *Schlieper*, 2007 NCBC 29 at 46; 2007 WL 2580120 at \*9. Summaries of these two cases illustrate how the UDTPA has been applied to employer-employee disputes:

- **Sara Lee:** A Sara Lee employee, with the

responsibility of purchasing computer hardware and services, created four business entities to which he steered Sara Lee’s business. He charged Sara Lee excessive prices for goods and services while concealing his involvement with the businesses. Because he had engaged in “buyer-seller relations in a business setting” with Sara Lee, a UDTPA verdict against him was affirmed.

- **Dalton:** A furniture company employee, who produced an employee newspaper as part of his job, formed a publishing business and obtained a contract to produce the employee newspaper, then resigned. The Supreme Court distinguished *Dalton* from *Sara Lee* on the ground that the *Sara Lee* defendant had been a purchasing agent who served his employer “in the capacity of . . . a buyer or a seller,” while the employee in *Dalton* had no buyer/seller relationship with his employer (at least while he was employed). Accordingly, no valid UDTPA claim arose.

Turning back to the facts of the case and the parties before him, Judge Tennille concluded that “the dispute that arose between them remained internal to Axiom,” and focused on the amount of compensation due the plaintiff under the terms of their employment and the “Letters of Understanding.” He rejected the plaintiffs’ argument that they were business partners rather than mere employees, pointing out that they had only a “phantom stock interest. They had no equity stake in Axiom, no votes to cast, and no risk of loss.”

Finally, Judge Tennille observed that the UDTPA was enacted to protect consumers, not to regulate the internal operations of businesses. “The statute was not meant to apply to the internal affairs of business associations. The law is replete with mechanisms to address those types of disputes, and section 75-1.1 need not be stretched beyond its intended purpose to accommodate them.” 2007 NCBC 29, 48-53; 2007 WL 2580120 at \*10-11.

Another intra-corporate dispute, *Anderson v. Dobson*, produced multiple federal court actions and resulted in several published opinions from the Western District of North Carolina. The basic issue was who owned stock in SmartBand Technologies, Inc., a firm formed to commercialize technologies invented and patented by the plaintiff, Anderson. After a falling-out among Anderson and other sharehold-

ers, Anderson allegedly “abandoned his duties to SmartBand” and focused attention on a new company he had formed. Then, acting as majority shareholder, Anderson removed the defendants as SmartBand directors and, acting as sole director, fired them. During the struggle over control of SmartBand, the other directors issued additional stock to dilute Anderson’s control. Anderson then alleged that the new stock certificates had been fraudulently issued and backdated.

District Judge Lacy Thornburg surveyed the corporate wreckage and entered a declaratory judgment and permanent injunction sorting out the parties’ legal rights. He then addressed Anderson’s remaining UDTPA claim. He, like Judge Tennille, noted that while the UDTPA has been applied to certain business relationships, its original intent was to benefit consumers. Judge Thornburg held: “The acts complained of . . . relate to internal corporate relationships and disputes between the private parties. They concern the question of disputed corporate control, the validity of corporate stock, etc.; the consuming public was not involved. There was no buyer-seller commercial market or public stock market of any kind involved. The provisions of Section 75-1.1 simply do not apply to this litigation.” *Anderson v. Dobson*, 2007 WL 4059515 (W.D.N.C. Nov. 13, 2007), at \* 3; *see also Anderson v. Dobson*, 2007 WL 2462675 (W.D.N.C. March 22, 2007) (Howell, Mag. J.) (providing additional factual background and recommending dismissal of UDTPA claim).

A Virginia federal court also found itself drawn into the thick kudzu of the UDTPA in a case brought by a government contracting firm whose business included what was described as “irregular warfare.” *SRA Int’l, Inc. v. McLean*, 2007 WL 4766697 (E.D. Va. Dec. 6, 2007) was initially filed by SRA against a former employee, McLean. McLean responded by asserting counterclaims for breach of his employment agreement, two counts of slander and violation of the UDTPA. He alleged that SRA engaged in unlawful business practices because its employees made slanderous or otherwise unfair or deceptive statements to third parties in Virginia and North Carolina following his departure from SRA.

District Judge Claude M. Hilton determined that, because some of the

allegedly slanderous statements were made to McLean himself, they were not “in or affecting commerce” as the UDTPA requires. Other statements were simply made by SRA employees to other SRA employees, and likewise were not “in or affecting commerce.” While some statements were allegedly made by SRA to third parties, they concerned McLean’s alleged violation of his employment agreement, misappropriation of trade secrets, events in the litigation, and statements of opinion. Judge Hilton deemed them not “unfair” or “deceptive,” meaning they were not “immoral, unethical, oppressive, unscrupulous . . . substantially injurious to consumers [or] amount[ing] to an inequitable assertion of [SRA’s] power or position.” *Id.* at \*2.

In a case involving criticism of an employee by (rather than to) third parties, **Esposito v. Talbert & Bright, Inc.**, 181 N.C. App. 742, 641 S.E.2d 695 (2007), the North Carolina Court of Appeals affirmed the dismissal of a UDTPA claim. Esposito worked for the North Carolina Department of Transportation (NCDOT) employed as project manager at the Brunswick County Airport. Talbert & Bright, an engineering firm, served as consulting engineer for the airport project. When a Talbert & Bright manager complained about Esposito to his superiors, he was placed on administrative leave and later terminated.

The Court of Appeals focused closely on the elements of UDTPA, concluding that even if the engineering firm’s statements or actions were unfair or deceptive practices that proximately caused an injury to Esposito, they were not “in or affecting commerce” because there was no evidence that “they had any impact beyond his employment relationship with NCDOT.” It affirmed the trial court’s summary judgment for Talbert & Bright on that claim and a related civil conspiracy claim.

**Proximate Cause: Another Potential Limit on UDTPA.** One other noteworthy 2007 case took a strict view in analyzing the application of the UDTPA to a consumer class action against a car dealership. **Pope v. TT of Lake Norman, L.L.C. d/b/a Lake Norman Dodge**, 505 F. Supp. 2d 309, 310-12 (2007). The dealership sold a product called “Etch” with all of its new vehicles. “Etch” consists of an identifying number acid-etched on the vehicle’s windows, carrying with it a \$5,000 guarantee payable to the owner if the Etch number did not deter theft and if the stolen car was not recovered with-

in 30 days. Lake Norman Dodge added an Etch cost of \$349 to the price of every vehicle sold. Pope, a Dodge buyer who was seeking to represent a class, alleged that Etch was insurance, not a product, and that the dealership’s failure to characterize it as insurance resulted in the miscalculation of his “amount financed” and “finance charge,” as well as violated various state and federal statutory disclosure requirements.

Judge Graham Mullen dismissed Pope’s UDTPA claim. His opinion looked first at a North Carolina Attorney General’s opinion, which held Etch to be a warranty rather than insurance. The opinion observed that there was no misrepresentation because the charge for Etch was fully disclosed and the dealership personnel had told Pope accurately that it was not optional but was included on every car. Even though Pope was required to sign a form that stated incorrectly that the purchase of Etch was not required to buy the car, Judge Mullen held that such a mis-statement was not sufficient to allege proximate cause of an actual injury: “Plaintiffs knew that the Defendant’s policy was to require Etch in every deal, and they purchased it anyway.” In Judge Mullen’s view, that precluded Pope from claiming that the mis-statement caused his actual injury and barred his UDTPA claim.

Failure to establish proximate cause is rarely a basis for dismissal of tort or UDTPA claims. Judge Mullen’s opinion seems, however, to indicate that when a plaintiff claiming misrepresentation as the basis for a UDTPA claim has access to the truth, the plaintiff cannot make a UDTPA claim.

## Potential Developments in UDTPA Jurisprudence

While these 2007 decisions came from

different courts and judges, they support some conclusions about the direction UDTPA case law may take:

- Courts seem increasingly attentive to potential conflicts between legislatively-enacted regulatory schemes and “overlapping” damages actions seeking to privately enforce the UDTPA. When private enforcement seems likely to undermine or contravene such a regulatory regime, courts are willing to bar a private UDTPA claim. This amounts to an implied restriction on the private right of action that generally exists under the UDTPA.

- Courts are also skeptical of litigants’ efforts to use the UDTPA and its formidable treble damages and attorneys’ fees remedies in intra-corporate disputes. Where the dispute principally concerns a single business entity and its owners, it is not “in commerce” as that statutory element is now understood. This is particularly clear in employment-related disputes.

- The UDTPA seems to be firmly rooted and thriving in business-against-business litigation, even when the potential benefits for consumers are attenuated or non-existent. It would likely take legislative action to eradicate it in that area. Absent such action, corporate litigants will continue to plead UDTPA violations on the premise that any business dispute is “in commerce” and therefore within the UDTPA’s coverage. ■

BRAD KUTROW IS A PARTNER IN THE CHARLOTTE OFFICE OF MCGUIREWOODS LLP. HIS PRACTICE FOCUSES ON COMPLEX BUSINESS LITIGATION, INCLUDING BUSINESS TORTS AND UDTPA CLAIMS, AND PRODUCTS LIABILITY.

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