

BUSINESS AFFAIRS

**Entertainment Industry Outlook:
1990 and Beyond**

by Michael I. Yanover

Introduction:

This past year has witnessed an unprecedented number of transactions among entertainment and entertainment-related companies. Such transactions, which total over \$19 billion, include: the acquisition by Ronald O. Perelman's The Andrews Group of New World Entertainment Inc.; the acquisition by Carolco Pictures Inc. of De Laurentiis Entertainment Group Inc.; the failed acquisition by Quintex Entertainment Inc. of United Artists; the

acquisition by Sony Corp. of Guber-Peters Entertainment Co. and Columbia Pictures Entertainment Inc.; and the merger of Time Inc. and Warner Communications Inc. Although some of these transactions were merely "deal" driven, others demonstrate the emergence of market forces which are beginning, and which will continue through the 1990's, to reshape the entertainment industry.

Harold Vogel, in his authoritative text of 1986, entitled *Entertainment Industry Economics*, explains that the entertainment industry operates much like a "cottage" industry. By this he means that it is "highly fragmented in both physical organizational structure and mental disposition." Mr. Vogel predicts that it will remain as a cottage industry "if only because many small, privately owned service firms and production units are frequently much more efficient than the behemoth studios." Although Mr. Vogel accurately describes the present state

of affairs, this cottage industry structure may be changing as the market restructures itself in an attempt to build "barriers to entry."

Building Barriers to Entry:

Michael Porter, corporate strategist and management consultant, explains in *Competitive Strategy* that, "[a] barrier to entry can be created by... [making it more difficult] to secure distribution... [such that] [t]he more limited the wholesale or retail channels for a product are and the more existing competitors have these tied up, obviously the tougher entry into the industry will be." Steps towards the building of barriers to distribution channels in the entertainment industry were taken during the 1980's when studios achieved vertical integration through the acquisition of theater circuits. Such acquisitions were clearly driven by the need to ensure

accessibility to retail markets, rather than the desire to increase revenues as exhibitors. More recent steps are best exemplified by the mega-merger of Warner and Time and the decision by Paramount Communications Inc. (formerly Gulf & Western Inc.) to spend over \$3 billion acquiring entertainment companies. Both of these moves represent the expectation of a further internationalization of the entertainment industry - especially in light of the removal of the European Common Market's trade barriers in 1992 - and of economies of scale which may be achieved through the consolidation of distribution channels. The net result of such transactions will undoubtedly be the construction of virtually impenetrable distribution channels providing access to all markets in all nations.

Given such an evolution, the survival of independent distributors, or even "major" distributors, is questionable. The fate of the independent distributor may be best

exemplified by a company called Vestron Inc. Vestron operated initially as a video distributor. Its strategy was simple-it established itself very early on as a strong player in a niche market by purchasing the video rights, through "pre- sales," to several high potential feature films, such as "Platoon." As the majors entered the video market and slowly strangled Vestron's access to such films, Vestron decided to integrate backwards by producing and distributing its own feature films. Today, Vestron, unable to compete as a major film distributor and unable to feed its distribution machine with successful feature films, has admitted defeat by putting itself on the block for sale. This scenario may be equally applicable in the future to those majors forced to compete against international juggernauts like Paramount and Time Warner.

Michael Porter states that, in an industry where barriers to entry increase, consolidation becomes more

likely. In fact, in most mature industries where barriers to entry are strong there emerge three or four dominant firms which control a vast majority of the market share. A good example of this is the soft-drink industry, in which soft-drinks produced by Coca-Cola, Pepsi and 7-Up are responsible for more than 70% of that industry's revenue.

As access to distribution channels becomes more difficult, the entertainment industry will come under increasing pressure to consolidate. Both independent and major distributors which are slow to establish themselves as dominant players may be forced to either sell out or fold. In anticipation of such a choice, one major distributor, Twentieth Century-Fox Film Corporation (which is owned by Rupert Murdoch's News Corp.), has shown great foresight by establishing both the Fox television network, for the U.S. market, and Sky Channel, for the European market.

Sony Corp. and the JVC/Victor Company of Japan, Ltd. have demonstrated an altogether different strategy. In an attempt to build barriers to entry to the home video market, they have decided to integrate backwards into film production and distribution. Sony's acquisition of Columbia and JVC's \$100 million joint venture with Hollywood producer, Lawrence Gordon, will undoubtedly provide them with both greater control over the home video market and increased sales of home video equipment. Other companies appear to be less well poised for the future, and have yet to develop any clear strategy.

An Increased Need for Product:

While the entertainment industry consolidates, the need for product will probably increase. This need will be prompted both by further technological advances and

by further deregulation of international markets. At the same time, the tremendous overhead costs of operating large distribution channels will cause entertainment industry executives to distribute more product in order to decrease the risk of loss by any one film—since overhead costs are divided among whatever films are distributed. As a result, the number of independently produced films acquired by studios, known as "pick-ups," will probably increase in order to meet the high demand for product.

The increased need for product coupled with, what many view as, the inability of ever-expanding bureaucratic giants to produce fresh new films provides a rather optimistic outlook for independent production companies. One independent production company, which has enjoyed tremendous success as the producer of films such as "Major League," is Morgan Creek. The likelihood of success for independent producers is also increased by the fact that there exists no "product

branding" in the entertainment industry. That is, consumers do not respond, either favorably or unfavorably, to a film based on its producer as they do with other products, such as soft-drinks.

Conclusion:

The consolidation of the entertainment industry will likely continue as international markets deregulate and the industry attempts to build barriers to entry through virtually impenetrable distribution channels. At the same time, the probability of success for independent distributors will decrease dramatically.

However, with this consolidation will come the need for more product. As a result, both the number of "pick-ups" and the likelihood of success for independent production companies should increase. Although the structure of the industry will undergo dramatic changes, the

1990's should prove to be the entertainment industry's most prosperous and exciting years ever.

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LEGAL AFFAIRS

**International Tax Planning for Artists
in the Entertainment Industry
(Part 2)**

by Bruce M. Stiglitz

C. Problems of United States Artists Going Abroad

1. United States Actors, Actresses and Athletes

a. Foreign Counsel

United States tax counsel should consult with foreign tax counsel in the country or countries where the artist plans to work in order to determine: (a) what foreign income tax withholding rates will be applicable; (b) whether an income tax treaty will prevent withholding, since our treaty partner might interpret the treaty differently than we do; (c) whether withholding will be on the gross income (sometimes including travel expense reimbursements) or whether an allowance will be made for expenses (and, if expenses are allowed, which expenses are customarily allowable in each country); and (d)

whether social security or medical taxes are applicable and, if so, the amount of such taxes, which party is responsible for such taxes if the agreement is silent on the question, whether there is a ceiling on the amounts to which such taxes apply, and whether a totalization agreement prevents the imposition of such taxes if a proper claim for exemption is made.¹⁵ Sweden, for example, imposes employment taxes of 37% on the employer (in addition to a top 72% rate of income tax imposed on the employee) with no ceiling on the amount of salary to which the tax applies, but, fortunately, this tax doesn't apply to foreign artists who pay only a flat 30% tax.

Any applicable tax treaty and totalization agreement should be reviewed, as well as the internal tax laws of the foreign country, so as to determine whether the artist should work individually or through a United States loan-out company. In some instances, producers hire

United States artists through foreign companies to avoid United States FICA taxes, and these foreign companies then re-lend the artist's services, without charge, to the foreign production company, which will often avoid foreign payroll taxes in the country where the work will be done.

In some instances, guild considerations will dictate whether a foreign or domestic entity will employ the artist.

b. Foreign Tax Credit Planning

If there will be taxes withheld in a foreign country, the American artist should work in that country either individually or through an S corporation so that he will individually obtain a foreign tax credit in the United States for any foreign taxes withheld. (Some countries, such as England, issue the withholding slips to the individual artist, even though the tax is withheld from the fee paid

to the artist's loan-out company. This is because the English tax is imposed by statute on the individual, even though that tax is withheld from the payment to his loan-out corporation.)

Tax counsel should determine whether there is a limitation on the maximum amount of compensation that is subject to any applicable social security or medical taxes and whether the imposition of such tax will be affected by whether the artist works for a United States loan-out company, as an independent contractor, for a foreign loan-out company, or directly for the foreign production company. Totalization agreements often restrict a foreign country's ability to impose social security taxes on United States persons covered by the United States social security system if he is not employed by a local company. If a country imposes a social security or medical tax without any ceiling (e.g., 10% in England), such a tax will be very significant when imposed on the

total fee of an important artist. The part of such tax imposed on the employee should qualify for a foreign tax credit in the United States, subject to the applicable limitations on tax credits. See Treas. Reg. Sec. 1.901-2(a)(2)(ii)(C). (However, some countries, such as England, will not give credit for U.S. FICA taxes.) See IRC Sec. 904 regarding the limitations imposed on foreign tax credits. However, if a loan-out company is used and if it must pay the employer's share of such tax, no credit would be allowed to the artist for such tax.

Foreign tax credits can be claimed on either the cash or accrual method, irrespective of the accounting method used by the artist generally. IRC 905(a). The selection of which method to use can be very important. For example, if a foreign tax credit can only be used at the time of accrual, the credit might be lost if the taxpayer checks the box on his return saying "cash method" and if

a foreign tax deficiency is assessed after it is too late to amend the return for the year when the tax was incurred.

In some countries (e.g., England), social security taxes can be avoided if the artist is not present for an extended period of time, while in other countries (e.g., Italy) such taxes are imposed (unless exemption is claimed under a totalization agreement) even if the artist is only present for a very short period.

In each instance, counsel should consider what tax applications and reports will be handled by the promoter for the artist, what matters the artist must retain a local accountant or attorney to handle for him, and how long in advance of the tour this work must be done.

c. Foreign Earned Income Tax Exclusion

If the artist is traveling to a foreign country for as long as six months, his United States tax advisor should

consult foreign tax counsel to determine whether the artist will be deemed to be a resident of that foreign country for that year, and, if so, whether the artist will be taxed on his worldwide income by that foreign country for the year when he is deemed to be a resident there for tax purposes.

In many cases, it will be advantageous for an artist to claim a foreign income exclusion under IRC Secs. 911(a)(1) and 911(b)(2)(A) and a foreign housing allowance under IRC Secs. 911(a)(2) and 911(c). However, in some high tax jurisdictions, the foreign tax credit may be so reduced as a result of claiming these "benefits" that the artist would be better off electing to forego them. See Treas. Reg. Sec. 1.911-6(a) and Form 2555.n16

With regard to extensions of time in which to file U.S. tax returns when an American artist is abroad, see T.D. 8241, 1989-14 irb 18.

d. Using Treaties to Avoid Foreign Taxes

If an artist intends to use a loan-out company, he should be careful that his loan-out company does not have an office or other permanent establishment in the foreign country. Local counsel should be asked what constitutes a permanent establishment under local law (and then any applicable tax treaty should be reviewed to see if any more restrictive tests are applied). For example, the IRS has ruled that the owner of a racehorse that runs more than once in the United States has a permanent establishment. See Rev. Rul. 60-249, 1960-2 CB 264. At one time, Canadian revenue agents took the position that a musician's instrument constituted a permanent establishment! Often it is best if the foreign production company does not give the artist or his loan-out company the exclusive use of an office, because that

office (e.g., with the artist's name on the door) could possibly constitute a permanent establishment of the artist's company. If work is being done in certain countries, it is advisable for the officers and directors of the United States loan-out company to remain in the United States so the company will not be considered to be managed there and, in such cases, the artist should resign as an officer and director before working in that foreign country.

In some countries, tax treaty protection will not be available if the United States artist owns the loan-out company (for example, Japan, France, Germany and Belgium). The artist may be able to avoid this problem if he works for a company owned by the producer, assuming that there is sufficient trust between the parties, or possibly even by the artist's business manager. However, if the artist has an S company and if the withholding rate is low (e.g., 10% in Japan), then it may be best

to pay the withholding and claim a credit for that tax in the U.S. For some countries (e.g., Japan) the withholding rate is lower if you work for a U.S. company than if you are employed directly by a Japanese company. In some instances, there are advantages to using a company formed in a Common Market country rather than in the United States. If there is a significant amount of money involved and if a foreign tax credit cannot be fully utilized in the United States, foreign tax counsel familiar with the problems of entertainers should be consulted. Good foreign corporate tax counsel, who does not regularly work in the entertainment industry, may not be very effective in tax planning for an artist.

Actors and actresses are treated as employees in the United States, and not as independent contractors. However, many foreign countries will treat an actor as an independent contractor if the agreement so provides. Depending upon the income tax treaty and the

totalization agreement between the United States and the country in question, it may be advisable for an artist to be retained by the foreign production company as an independent contractor, rather than to work as an employee of a United States loan-out company that furnishes his services to the foreign production company.

e. Minimizing Foreign Taxes

In some high-tax jurisdictions (e.g., Australia), full United States credit may not be available for the foreign tax. In such countries, in addition to obtaining the benefit of maximum allowable deductions, tax planning often must be done to allocate as much of the income from the project as possible to other foreign jurisdictions which have lower tax rates or which would impose no tax. (The allocation of income to the United States will be of some help, but it will not be as effective as an allocation

to another foreign jurisdiction in reducing the total tax burden because an allocation of services to the U.S. will not increase the amount of foreign source income, and hence it will not increase the IRC Sec. 904 limitation on the amount of foreign taxes for which tax credits can be used in the United States.) This allocation of income away from a high-tax jurisdiction can be accomplished by a number of methods, often including the following:

(a) In some cases, income can be allocated away from a high-tax jurisdiction by the payment of a "release fee" or a "holding fee" to the artist's United States loan-out company. A release fee is paid to release the artist from his exclusive employment agreement and hence allow the artist to be employed directly by the foreign production company. This release fee may, if properly structured and if reasonable in amount, be able to reduce taxes in certain high-tax jurisdictions, and these fees may still constitute foreign source income under United

States tax law so as to increase the amount of foreign taxes for which credit can be used in the United States. A holding fee is a fee paid to keep the artist available until the producer decides whether to hire him. See generally IRC Sec. 861(a)(3) and the authorities cited at Prentice- Hall Federal Taxes Para. 30,044, regarding the source of income from different types of services.

(b) In other cases, the artist's name and likeness can be licensed for use throughout the world in connection with the motion picture, and this license fee can result in the allocation of some income to other foreign countries which will not impose tax.

(c) In some instances, it will be appropriate to allocate some income to rehearsal services and/or to post-production and publicity services, rather than allocating all income to the actual filming which may be done in the high tax jurisdiction.

There are problems in drafting agreements that involve these devices because the producer will want the compensation to accrue and be earned during the period of filming - not during the "holding period" or the period when the artist's name and likeness are used. Counsel must consider how to allocate overtime payments (e.g., when shooting is not finished on schedule). There is no perfect solution to this problem.

If total foreign taxes will not exceed the IRC Sec. 904 limitation on the available United States foreign tax credit, there may be no point in spending legal fees to do complex tax planning to reduce foreign taxes. Note that excess tax credits can generally be carried back two years and forward five years. IRC Sec. 904(c).

f. Tax Indemnities

When appropriate from a business viewpoint, a tax indemnity should be requested when an artist works in a jurisdiction which might impose taxes in excess of the amount which will be creditable against the artist's United States tax. When an artist is able to obtain a tax indemnity from a responsible party, issues to be negotiated include:

(a) Whether the indemnifying party will pay the artist's United States income tax on the tax reimbursement itself (this is usually obtainable, if obtainable at all, only for a very important star). Note that there may be an argument that, in some fact situations, the amount paid under a tax indemnity might not be subject to tax. See PLR 8748072 (September 3, 1987) and Shop Talk, November 1988, *J. Taxation* at p. 367;

(b) To what extent will the artist be permitted to shelter his compensation from United States tax so that he cannot use the foreign tax credit, and still be reimbursed for

the foreign tax (many indemnities only protect against foreign taxes in excess of the maximum of 28%);

(c) Who will have control over the preparation of foreign and domestic tax returns and foreign and domestic tax litigation and who will pay the accounting and legal costs. Many tax indemnities are conditioned on the artist filing proper and timely foreign and domestic tax returns;

(d) When will the tax indemnity be paid (i.e., will the indemnity be payable before the foreign tax must be paid so the artist does not have to first pay the foreign tax with his own funds and then seek reimbursement);

(e) Who will be responsible to pay the indemnity (i.e., an indemnity from a "shell" production company may not be worth much) and, if the production company is not creditworthy, will the indemnity be secured by a letter of credit;

(f) Will the artist be permitted to use a C corporation (which will preclude effective use of the foreign tax credit for most withholding taxes) and still obtain a tax indemnity; and

(g) Under what circumstances (e.g., illness, transportation strikes, etc.) will the artist be permitted to stay in the foreign jurisdiction longer than is required by the production schedule, and will the artist be permitted to rent a house or take other action that would increase the risk that he would be deemed to have established residence in the foreign country. See generally, Moore, *The Filmed Entertainment Industry*, BNA Tax Management, Inc. (1988), 2004 for some typical tax indemnity provisions.

2. United States Writers, Directors and Producers

Many of the provisions discussed above, regarding actors, actresses and athletes working abroad, are also applicable to United States writers, producers and directors working abroad. However, there are a few situations in which non-performing artists have a more advantageous tax position, as described below. For example:

Most countries do not apply the "artists and athletes" clauses of their tax treaties to writers, producers, directors and other non-performing artists, and hence United States writers, producers and directors can more often avoid foreign taxes than can United States performing artists. (But this isn't always true - e.g., France treats a film director as a performing artist.)

Writers, producers and, to some degree, directors, can control where they will work, and hence a substantial part of their compensation often can be allocated to the United States or to low-tax or no-tax foreign

jurisdictions. Actors must do most of their work when the picture is being filmed.

3. United States Singers, Musicians and Other Touring Artists

a. Local Income Tax Issues

The American artist's counsel should work with the foreign promoter of the show in each country to determine the approximate amount of foreign taxes that will be withheld in that country. The foreign promoter is often more knowledgeable than is foreign tax counsel as to the practical ways to reduce withholding tax (e.g., by allocating some of the fee to a separate company that pays for travel and/or production costs). Nonetheless, if the artist will not be able to obtain full credit in the United States for foreign withholding taxes, the artist's United

States tax counsel should consider speaking to foreign tax counsel (as well as to the promoter) in each country where significant foreign taxes are being withheld in order to determine whether these withholdings can be further reduced by proper planning, and also to be sure that the promoter's suggestions are appropriate and not unreasonably aggressive.

Methods of reducing foreign tax withholding in some countries include: (1) having the promoter pay more of the expenses of the tour and reducing the artists fee by an equal amount; (2) changing the place of incorporation and/or place of management of (or the ownership and/or officers and directors of) the company putting on the show in that country; and (3) creating a joint venture between the promoter and the company putting on the tour instead of just paying a fee (e.g., in Ireland, this approach will avoid VAT on the artist's fee). Agreements should specify who will bear the VAT, social security

and similar taxes imposed with respect to the artist's fee. VAT often is not imposed on an artist's fee, and, where it is imposed (e.g., in England), it can often be recouped.

The promoter and foreign tax counsel should be asked whether the withholding will be on the gross income, or whether a deduction is allowable for expenses, and, if expenses are deductible, whether related-party fees are deductible. In some countries, total fees of up to 30% are allowed, even if paid to an affiliated company.

In some countries, it will make a difference as to whether the expenses are paid: (1) by the artist's company; or (2) by the promoter and then subtracted from the artist's fee. However, many countries treat any expenses paid by the promoter as having been first paid by the promoter to the artist, and then as having been paid by the artist for purposes of withholding.

In some countries (e.g., Italy), it is necessary to use a separate contract (and sometimes, even to pay a

separate company - possibly a company not owned by the artist) for lights, sound, travel and other production costs in order to avoid foreign withholding on that part of the funds that represents the cost of producing the show.

We usually find it advisable to speak briefly with foreign tax counsel before and after talking to the promoter if substantial monies are involved. In that way, we learn what questions to ask the promoter and then, after we obtain practical methods of reducing tax from the promoter, we consult foreign tax counsel to be sure that no appropriate tax-savings ideas were overlooked, and also to be sure that the promoter's ideas are not so aggressive as to get the artist in trouble.

Withholding rules applicable to band members should be reviewed. In some countries, there is a relatively small amount (\$3,000 to \$20,000) that will not be taxed each year if paid directly by the foreign promoter to the

band members, and not to the star's company. In some countries (e.g., England), the tax authorities usually will not grant the exemption to musicians early in the year because the band member might return to the country later in the year and exceed the above limits on excludible income. It may be advisable to have band members paid by the promoter in those cases where the band member can use the tax credit but where the star cannot (or vice versa if the star can use the credit and the band members cannot). United States withholding and FICA taxes can also be affected by whether the band members and crew are paid by the United States company owned by the American star, by a foreign company owned by the American star or a related party, or by the foreign promoter. In each case, they could either be paid as employees, or one might try to characterize them as independent contractors. Often, FICA savings are not sufficiently important to involve tax counsel in planning,

but these issues should not be overlooked if there are many employees. Tax counsel should inquire as to the residence of the band members. The star may be American, but some members of the band are often Canadian or English, and this will affect the availability of treaty protection for these musicians.

In some countries (not ordinarily in Western Europe, Japan, Australia, New Zealand or Canada), the foreign promoters will make payment to the artist in the United States, free of withholding, and these promoters will either avoid or absorb local taxes, if any. Local tax counsel should be consulted as to whether such practices will cause the artist to have a problem with the local tax authorities. In the more sophisticated countries, this is more likely to occur on merchandising payments than on performance fees. If merchandising royalties or sponsorship fees are being paid, such payments may constitute the type of royalties that are treated differently than

performance fees under local tax law and under applicable tax treaties. There may be some room for planning if there is any flexibility as to how monies are allocated between these categories of income if both types of income are paid by the same company.

Under the typical United States income tax treaty or exchange of tax information agreements, the foreign country is empowered to obtain from the IRS copies of all documents and bank statements relating to a project, and they often do so. Our firm has have recently received such requests from Australia and from the United Kingdom. Accordingly, there should be no "side letters" or correspondence which would cause embarrassment to any of the parties if they should fall into the hands of foreign revenue authorities. See *United States v. Philip G. Stuart*, 109 S.Ct. 1183 (1989). See generally, Patton, "How the IRS obtains International Tax Information," World Trade Institute at New York City, 5/8/89.

b. Reducing VAT

Rules relating to value added taxes ("VAT"), as well as rules on withholding and social security taxes, should be discussed with local counsel and with the promoter. In the United Kingdom, fees paid to an independent contractor (e.g., possibly the director of a film) will be subject to VAT and there is a question as to who will pay the VAT and how the fee should be structured so any VAT that is paid can later be recovered when the film is "exported". A decision must be made as to whether the United States company should register for VAT in the foreign country so it can, in some situations, recoup the VAT that is paid. We generally use different tax counsel (often in the same firm) for VAT issues than for withholding issues, because income tax advisors are often not knowledgeable on VAT issues.

In some countries, the burden of VAT on hotel and restaurant bills can be avoided by having these bills paid by the promoter and subtracted from the artist's fee. This is because the promoter may be able to recoup the VAT if he pays the hotel and restaurant bills (e.g., this can be done in Austria and West Germany). In some countries, VAT can be recouped on hotel bills but not on restaurant bills. The way the promoter recoups this VAT is by offsetting the VAT imposed on the hotel and restaurant bills against the VAT that the promoter collects on ticket sales, turning only the net amount over to the government. However, this cannot be done in most countries, either because there is no VAT on hotel and restaurant bills, or alternatively because VAT on hotel and/or restaurant bills cannot be recouped by offsetting it against the VAT charged on ticket sales.

In Ireland, VAT is imposed on the entire fee paid to the artist's company at the rate of 25%, but, by using a

properly worded joint venture arrangement between the artist's company and the promoter, the VAT can be avoided because the "fee" is treated as a division of the joint venture's profits which is not subject to VAT.

4. United States Artists Changing Residence/Citizenship

If an artist who is a United States resident and/or citizen is planning to become a nonresident alien, there are special tax problems and planning opportunities as demonstrated by the example set forth below.

Example:

A British artist, who had been resident in the United States for ten years, decided to return to England. He had accumulated a substantial pension benefit in the United States and he owned a home here that he intended to sell at a large profit.

Because of effective planning, the artist sold the house before giving up his United States residence, and hence he was able to replace it, without paying United States tax, with a home in England. (Note that if the artist later sells his English home, he will still pay no tax on the gain because England does not tax the gain on one's principal residence.) The tax-free sale and replacement of his principal residence is allowed under IRC Sec. 1034 only to United States citizens or residents. See Treas. Reg. Secs 1.1445- 9T and 1.897-6T(a)(5). See generally, Gatesman and Stewart, "Income Tax Planning for the Departing Resident Alien Taxpayer," *The International Tax Journal*, p. 135 (Spring 1986).

This artist was also able to avoid both United States and United Kingdom tax on his pension benefits (i.e., by taking distribution of his pension plan in a lump sum after he ceased to be a United States resident and after he returned to England). This is because the United

States/United Kingdom tax treaty precludes the United States from imposing tax on pensions paid to a resident of the United Kingdom. See PLR 8934025 (May 25, 1989). However, for some reason, England does not tax lump sum pension distributions under its internal laws!

Note that if the artist had reversed the order in which he liquidated these two assets (i.e., if he had taken his pension distribution while he was still a United States resident, and then sold his house after he returned to England), the income from both assets would have been taxed in the United States, instead of neither being taxed. This example demonstrates the need to plan in advance.

Before giving up his United States residence, a foreign artist, until recently, was able to avoid tax on the disposition of his United States real estate investments by entering into a like-kind property exchange under IRC Sec. 1031 for property located outside the United

States. See Rev. Rul. 68-363, 1968-2 CB 336. United States tax on the gain from the later sale of the foreign properties acquired in the IRC Sec. 1031 exchange might have been avoided if the properties are sold when the artist is no longer a United States citizen or resident. However, this planning opportunity has been ended by tax legislation passed by Congress in November 1989, disallowing such tax-free exchanges into foreign real estate. IRC Sec. 1031(h), as amended by the Revenue Reconciliation Act of 1989, Secs. 7601(a).

United States citizens who are going to a high tax jurisdiction (e.g., France) to reside should consider placing their investments, copyrights, film interests and similar assets in S corporations and/or in grantor trusts. In this way, it may be possible to avoid having the new country of residence impose tax on the artist's worldwide investment income under circumstances where a complete credit against the artist's United States tax may

not be available. Also, the departing American artist should consider selling his assets to a grantor trust because such a sale should be ignored for United States tax purposes. See Rev. Rul. 85-13, 1985-1 CB 184. But it might give the artist a new tax basis for the asset in the high-tax jurisdiction to which the artist will move.

There are special tax planning opportunities and problems for United States citizens who renounce their United States citizenship. See, IRC Sec. 877 relating to income taxes and IRC Sec. 2107 relating to estate taxes but these rules are applicable only with respect to certain specified items (often United States source income) and only for ten years after expatriation. Therefore, if an artist earned money by making films abroad, United States tax would cease when the artist gives up his citizenship without the 10 year delay. United States citizens who live in the United States will not ordinarily wish to give up their citizenship and move to another country to

save taxes. However, if an artist has lived abroad for many years and has closer ties to another country, he might be interested in changing his citizenship, especially if a large tax savings would result.

A United States artist living abroad and married to a nonresident alien can, in some situations, reduce income and death taxes by channeling business opportunities to his spouse. Also, interest-free loans of up to about \$1,100,000 can divert income of about \$100,000 per year (i.e., 9% on \$1,100,000) to a foreign spouse and still be within the gift tax limitations of IRC Sec. 2523(i). See Rev. Proc. 85-46, 1985-2 CB 507; Eileen D. Cohen, 92 T.C. No. 65 (1989); and the discussion of this in Part II of this article.

Another tax planning opportunity arises in connection with pension plans. If an artist who is a United States resident plans to move to another country, and if the artist has accumulated a pension plan, he should consider

how the country to which he is moving will tax that pension. For example, if the artist takes a distribution of the pension plan and then rolls it into another pension plan or an IRA account, the country to which he is moving might consider that he has a tax basis for his pension benefits equal to the amount that he contributed to the new pension plan, even though, in the United States, the "rollover" was tax free. Arranging such a "rollover" before the artist moves to another country might avoid tax on a substantial part of the pension distributions after the move since the new country might tax the pension as an annuity or as a trust, allowing the artist to recoup his tax basis without the payment of tax. On the other hand, the country to which the artist is moving might treat an IRA account as a "grantor trust" and tax the artist on the income from the IRA account currently, whether or not he takes a distribution and hence it might be best to "roll" the benefits into a corporate plan. There is often a

difference in this tax treatment as between an IRA, a Keogh Plan and a corporate plan. In Australia, the tax authorities will give credit for your tax basis in the pension account, but only after you first take out all of the income from that trust, and therefore, if you are only taking out the income currently, this will be of no help to you since you will be fully taxable on the income. However, if you were to divide the IRA account into several separate IRA accounts or pension trusts, taking out the entire income of one account plus some principal from that account in each year, then you would pay Australian tax at 46% only on the amount of income taken from that account and you would take out some of the principal tax free so as to keep the average tax rate down to 28% so that full credit will be available. This example shows the need to consider how to deal with an artist's pension plan before he becomes resident of a country which has rules on the taxation of pension plans

that might be different than the rules applicable in the United States.

There can also be problems with pension plans if an artist is moving to the United States from another country. For example, Australia will tax an artist on the accumulated benefits of certain pension plans at the time an Australian resident ceases to be a resident of Australia. Australia feels that if an artist has accumulated the pension benefits while he was a resident of Australia, and if he then is about to become a non-resident where Australia will not again be able to tax these benefits, they then impose the tax at the time he leaves. Canada has a similar rule as to appreciated assets for people who have resided there for over five years. Therefore, whenever an artist is changing his residence (whether from the United States to another country, or from another country) the effect of this change on his IRA and pension account should be considered and planning should be done so as

to minimize taxes in both the country he is leaving and the country he is moving to.

5. Use of Foreign Corporations by United States Artists

In most instances, foreign corporations are no longer useful as a tool for American artists to defer tax on their foreign earnings. Even if the Subpart F and Foreign Personal Holding Company rules can be avoided, the new Passive Foreign Investment Company ("PFIC") provisions in IRC Sec. 1291 et seq. will usually make it uneconomic for an artist to use a foreign company to defer United States tax on services income. A deferred compensation agreement, even with an unrelated party, might be taxed as a PFIC under these new rules. See also IRC Sec. 1014(b)(5) regarding the tax basis of inherited stock of a Foreign Personal Holding Company.

It can, in some situations, still be advantageous for an active film production and/or distribution company to use a foreign company to defer tax on foreign source income if the company can avoid being a FPHC or a PFIC. However, with the current maximum federal tax rate of 28%, many producers and distributors have decided not to deal with the costs, risks (e.g., the branch profits tax exposure under IRC Sec. 884) and complexities of using a foreign structure.

D. Update: Sargent Case

The Tax Court recently held in *Sargent v. Commissioner*, 93 T.C. No. 48 (November 13, 1989), that members of the Minnesota North Stars hockey team, who attempted to render services through loan-out companies, would be viewed as employees of the team, rather than the loan-out companies. The court based its

decision on the substantial control the team could exert over its players.

Though the case did not involve international tax planning issues, it impacts on the use of loan-out companies by foreign team athletes, as well as potentially foreign entertainers, such as actors. Without express reference, the case essentially adopts the position asserted by the internal Revenue Service in the 1974 "Lend-A-Star" rulings (Rev. Rul. 74-330, 1974-2 CB 278 and Rev. Rul. 74-331, 1974-2 CB 281) under which a foreign entertainer's loan-out company is to be ignored where the person contracting with the loan-out company can exercise sufficient control over the entertainer to qualify the entertainer as an employee of the contracting party. These rulings were discussed in the first installment of this article last month.

The nature of team sports suggests that the Sargent case should be limited to team players. Furthermore, the

Tax Court in Sargent merely distinguished, rather than overruled, cases in which it had accepted the separate existence of loan-out companies. Nonetheless, the Internal Revenue Service may well seek to give the case broader application and may become even more aggressive in attacking the use of loan-out companies in the entertainment industry generally.

NOTES

15. Italy, for example will withhold 20% income tax on United States citizens performing in Italy, but Italy's totalization agreement with the United States will avoid Italian social security taxes if proper forms are filed in Italy. The artist should request a certificate of coverage from the Social Security Administration, International Policy Staff, Room 1104, West Highrise, 6401 Security Blvd., Baltimore, Maryland 21235, certifying that he is

covered by the United States social security system. That form must then be given to the Italian withholding agent.

16. If decisions are being made on the basis of available tax credits, projections should be prepared that will reflect the amount of the credit that can be used. For example, the deductions for living expenses "away from home" can also be affected by the decision to use the earned income exclusion. See IRC Sec. 911(d)(1). Also, the Tax Reform Act of 1986 imposed new restrictions on foreign tax credits by dividing income into different foreign tax credit "baskets," so that a foreign tax imposed on one category of income cannot be used to offset United States tax imposed on other categories of income. See IRC Sec. 904(d).

Bruce Stiglitz is a partner in the Los Angeles office of the law firm of Loeb and Loeb. The author wishes to

express his appreciation to Paul A. Sczudlo of Loeb and Loeb for his valuable input regarding these international tax issues. Copyright 1989 by Bruce M. Stiglitz. [ELR 11:7:5]

RECENT CASES

\$3 million damage award to producer of "Cross Country" in breach of contract case against United Artists is affirmed

As previously reported (ELR 9:7:11), a Federal District Court (S.D.N.Y. 1989-1-11) affirmed a judgment awarding (Country) Productions damages in the amount of about \$2.2 million plus about \$870,000 in prejudgment interest in the company's breach of contract action against United Artists Corporation.

United Artists' stated reason for repudiating a contract to purchase and distribute the Filmline-produced work entitled "Cross Country" was that the film unacceptably varied from "an approved screenplay." The District Court found that United Artists sought to avoid a financial commitment to the film, and that although the company had a right to terminate its contract with Filmline prior to filming, United Artists waived that right by failing to exercise it in a timely fashion.

Federal Court of Appeals Judge Mahoney stated that even on the assumption that Filmline may have breached the parties' contract, and that United Artists therefore was entitled to terminate the contract, United Artists' notice of termination did not conform to the terms of the contract and was ineffective under New York law. The contract contained an explicit requirement that Filmline was to be given an opportunity to cure a breach or default within thirty days of receiving notice of the breach.

The District Court did not find that United Artists' failure to give Filmline an opportunity to cure was "a fatal defect" under New York law because it did not appear that Filmline had the "artistic or financial" capacity to revise the screenplay as requested. But Judge Mahoney concluded that on the basis of the record, New York courts would apply the "clear New York rule requiring termination of a contract in accordance with its terms;" Judge Mahoney did not find it necessary to resolve the waiver issue.

Filmline (Cross-Country) Productions, Inc. v. United Artists Corporation, 865 F.2d 513 (2d Cir. 1989) [ELR 11:7:14]

Proteus Books wins reinstatement of verdict that Cherry Lane Music is liable for breach of "due professional skill and competence" contract provision, but damages issue is remanded

As described in ELR 10:7:11, one of the provisions in a 1983 contract signed by Proteus Books Limited and Cherry Lane Music Co. required Cherry Lane to distribute Proteus' books to American book, music and record stores with 'due professional skill and competence.'

Proteus sued Cherry Lane in 1985, and a Federal District Court jury returned a verdict awarding Proteus about \$2.8 million on the company's claim that Cherry Lane breached its contractual standard of care; about \$317,000 on the claim that Cherry Lane breached an oral agreement to pay Proteus by bills of exchange; \$120,000 on the claim that Cherry Lane breached a

minimum sales agreement; and \$177,000 on the claim that Cherry Lane converted Proteus' inventory.

The District Court granted Cherry Lane's motion for judgment notwithstanding the verdict as to the first two claims, but denied the motion as to the third and fourth claims.

After reviewing the transactions of the parties, Federal Court of Appeals Judge Meskill stated that the District Court correctly held that the phrase "due professional skill and competence" was ambiguous as a matter of law, and properly instructed the jury to construe the phrase most strongly against Proteus, its author. Nevertheless, the evidence presented was sufficient for the jury to issue a verdict on behalf of Proteus, stated Judge Meskill. However, the damage award to the company on the claim was "unreasonable and unfounded." It was observed that Proteus had been in existence for only two years when die company filed its action against Cherry

Lane and its sales performance in the United States was "consistently poor." Furthermore, Proteus did not prove with reasonable certainty a basis for anticipating profits in the amount awarded by the jury.

The court, accordingly, vacated the judgment notwithstanding the verdict as to liability on the breach of contract claim for failure to exercise "due professional skill and competence," and remanded the matter to the District Court for a retrial on the issue of damages.

Judge Meskill affirmed the District Court's decision granting judgment notwithstanding the verdict to Cherry Lane with respect to Proteus' claim that Cherry Lane breached its agreement to pay Proteus by bills of exchange.

In turning to the claim that Cherry Lane breached a March 29, 1985 agreement guaranteeing Proteus sales of \$85,000 per month for six months in return for Proteus' guarantee of four new titles per month on a timely

basis, Judge Meskill rejected Cherry Lane's argument that Proteus did not deliver the required books on time each month. The court found that there was sufficient evidence to support the jury's damage award of \$120,000, and that Cherry Lane was not entitled to judgment notwithstanding the verdict on this claim, nor on the conversion claim.

Proteus Books Limited v. Cherry Lane Music Company, Inc., 873 F.2d 502 (2d Cir. 1989) [ELR 11:7:14]

Hustler magazine prevails in libel actions brought by three anti-pornography activists, because derogatory statements were protected expressions of opinion

In March 1989, the United States Supreme Court let stand, without comment, two rulings by a Federal Court

of Appeals in California in which the court dismissed the libel actions brought by antipornography activists Peggy Ault and Dorchen Leidholdt against Hustler magazine.

The April 1985 issue of Hustler included an article featuring Ault as "Asshole of the Month." A small photograph of Ault in a less-than-flattering setting accompanied the article. The article criticized Ault's anti-pornography activities, and included several derogatory references to Ault.

When Ault sued Hustler, the District Court dismissed the claims for libel and intentional infliction of emotional distress as barred by the statute of limitations. The court also found a lack of personal jurisdiction over Larry Flynt and L.F.P., Inc. Ault's third amended complaint realleged all four forms of invasion of privacy. The District Court dismissed the complaint and imposed sanctions on Ault and her attorney for filing frivolous claims.

Federal Court of Appeals Judge Tang held that the challenged statements in the Hustler article were protected expressions of opinion. The pornographic nature of the magazine created a context which "rob[bed] the statements of defamatory meaning." It was observed that Hustler's readers most likely would not consider the statements in the article as facts about Ault's personal reasons for opposing pornography, and that the monthly feature article often focused on opponents of pornography.

In all, the article was constitutionally protected opinion, thus foreclosing Ault's claims for libel, for invasion of privacy by placing her in a false light and for intentional infliction of emotional distress. The District Court's dismissal of these claims therefore was affirmed, albeit on different grounds.

The dismissal of Ault's claim of public disclosure of private facts also was affirmed - Ault did not

successfully allege the publication of any true private facts. And Ault did not prevail on her claim of wrongful appropriation. The court observed that Hustler did not use Ault's photograph for its own commercial gain, but to accompany a newsworthy article.

Judge Tang concluded by reversing the imposition of sanctions and attorney fees, stating that since Ault had "clearly suffered a grievous assault to her human dignity we do not wish to endorse sanctions which can only serve to chill zealous advocacy."

Dorchen Leidholdt, a founding member of the organization Woman Against Pornography, was "vilified in graphic terms" in Hustler's June 1985 "Asshole of the Month" column. A Federal District Court dismissed Leidholdt's causes of action for libel, false light invasion of privacy, and intentional infliction of emotional distress.

Federal Court of Appeals Judge Fletcher found that the column, as in *Ault*, was an expression of opinion in an important public debate, and affirmed the dismissal of Leidholdt's claims, including claims for the misappropriation of Leidholdt's image, and the public disclosure of private facts.

In a third proceeding, antipornography activist Andrea Dworkin cited derogatory statements published in the February, March, and December 1984 issues of *Hustler* as the basis for her complaint alleging libel, invasion of privacy, intentional infliction of emotional injury, and the denial of her constitutional rights; the complaint sought \$50 million in actual damages and \$100 million in punitive damages.

The District Court granted *Hustler's* motion for summary judgment as to Dworkin's libel claim on the ground that the articles in issue could not reasonably be understood as expressing statements of fact about Dworkin,

and on the ground that even if the articles contained false statements of fact, Dworkin had presented no evidence of malice.

Federal Court of Appeals Judge Cynthia Holcomb Hall stated that Ault and Leidholdt were "squarely in point," and agreed with the District Court that the Hustler articles consisted of privileged opinion. Judge Hall commented that "ludicrous statements are much less insidious and debilitating than falsities that bear the ring of truth. We have little doubt that the outrageous and the outlandish will be recognized for what they are."

Judge Hall also held that Dworkin was not entitled to recover on any privacy theory recognized by the applicable law, i.e., section 51 of the New York Civil Rights Law; that recovery was not available on an implied private cause of action based on a Wyoming criminal statute (Wyoming being the original site of the instant litigation); and that the civil rights claim was properly

dismissed because Hustler magazine and Larry Flynt did not engage in state action.

Ault v. Hustler Magazine, Inc., 860 F.2d 877 (9th Cir. 1988); Leidholdt v. L.F.P. Inc., 860 F.2d 890 (9th Cir. 1988) [ELR 11:7:15]

Sponsor of Boston Marathon wins summary judgment in service mark infringement action against unauthorized distributor of merchandise

A Federal Court of Appeals has reversed a District Court decision and has granted a motion for summary judgment sought by the Boston Athletic Association, the operator and sponsor of the Boston Marathon, in a service mark infringement action against Mark Sullivan.

The association claimed that Sullivan was engaged in the unauthorized sale of T-shirts and other items bearing the "Boston Marathon" service mark and its unicorn logo. Judge Bownes rejected Sullivan's claim that the service mark had become generic, noted that the association's failure to register its mark was not dispositive, and stated that a mark provides protection not only for the product or service to which it is originally applied but also to related items or services.

Judge Bownes, after agreeing with the District Court that the association had valid and enforceable marks for the relevant time period, addressed the factors to be weighed in assessing the likelihood of confusion. It was found that the meaning of the marks in issue was identical; that the parties offered "virtually" the same goods for sale; and that the seasonal sales of the shirts and other wearing apparel occurred in the same outlets via the same advertising methods to casual purchasers

among the general public. The evidence indicated that some individuals actually were confused as to the sponsor of Sullivan's shirts. And the court found that the actions taken by Sullivan and his companies showed their intent "to trade on [the association's] sponsorship and management of the Boston Marathon."

Other factors considered by the court were that the service marks were "strong" marks in view of their use for a long period of time before registration, and in view of the fact that the Boston Marathon is one of the oldest and most prestigious marathons in the country. The court found that it was established that the purchasing public was likely to confuse Sullivan's shirts with those of the association.

Judge Bownes next considered the question of whether the public was likely to believe that the sponsor of the Boston Marathon produced, licensed or endorsed Sullivan's shirts. Whether or not purchasers happened to

know that the sponsor of the Boston Marathon was an organization called the Boston Athletic Association would be irrelevant to this "likelihood of confusion" analysis, stated the court, because in order to establish infringement in a promotional goods case, a party generally must show that prospective purchasers are in fact likely to be confused or misled into thinking that the allegedly infringing product was produced, licensed or otherwise sponsored by the party seeking relief.

Relevant case law cited by the court included the decisions in *University of Georgia Athletic Association v. Laite*, 756 F.2d 1535 (11th Cir. 1985; ELR 7:1:11); *Warner Bros. v. Gay Toys, Inc.*, 658 F.2d 76 (2d Cir. 1981), decision on appeal after remand, 724 F.2d 327 (2d Cir. 1982; ELR 3:16:5; 5:5:10), and *Processed Plastic Co. v. Warner Communications, Inc.*, 675 F.2d 852 (7th Cir. 1982; ELR 41:10:4). On the basis of these cases, and given the undisputed facts that Sullivan

intentionally referred to the Boston Marathon on his shirts, and that purchasers were likely to buy the shirts because of that reference, the court stated that it was "fair to presume that purchasers are likely to be confused about the shirt's source or sponsorship." In the absence of evidence rebutting the presumption of a likelihood of confusion, the court held that the association was entitled to enjoin the manufacture and sale of Sullivan's shirts.

In Judge Bownes' view, "when a manufacturer intentionally uses another's mark as a means of establishing a link in consumers' minds with the other's enterprise, and directly profits from that link, there is an unmistakable aura of deception." Unless it is shown that there is in fact no likelihood of such confusion or deception about the product's connection to the trademark holder, such a use can be enjoined.

The judgment of the District Court was reversed, accordingly, and Sullivan and his companies were permanently enjoined from manufacturing or selling goods displaying the name "Boston Marathon" or any other confusingly similar design.

Boston Athletic Association v. Sullivan, 867 F.2d 22 (1st Cir. 1989) [ELR 11:7:16]

Article author succeeds in copyright infringement action against former collaborator who copied article without consent, because joint authorship of prior works did not make collaborator a co-owner of author's derivative article

Dr. Heidi Weissmann and Dr. Leonard Freeman co-authored several papers based on their research on

various aspects of nuclear medicine. In 1985, Weissmann published an article concerning a relatively new diagnostic technique; the article was derived from previous papers jointly written by the doctors during the course of a seven year professional relationship.

In 1987, Freeman planned to use Weissman's article in a review course; Freeman deleted Weissmann's name from the article and replaced it with his own, and added three words to the title. In response to a request by Weissmann, the article was removed from the packet of course materials.

A Federal District Court in New York concluded that Freeman's use of the article did not violate the copyright law, finding that Freeman was a joint author and therefore a co-owner of any copyright Weissmann acquired in the article. The court also found that the new matter contained in the article was "too trivial" to qualify for protection as a derivative work, and that even if

Freeman were not a joint author of the allegedly infringed work, and even if the new matter in the article was copyrightable, Freeman's purported use of the article was a fair use.

Federal Court of Appeals Judge Richard J. Cardamone first noted that Freeman had conceded that he did not assist in preparing the article in issue, and that the District Court based its finding of co-ownership of the copyright in the article on the "mistaken view" that the joint authorship of the prior existing works automatically made the two joint authors co-owners of the derivative work. Judge Cardamone observed that the District Court's approach "would convert all derivative works based upon jointly authored works into joint works regardless of whether there had been any joint labor on the subsequent version." Such an approach would "eviscerate" the independent copyright protection that attaches to a derivative work that is wholly independent of

the protection afforded the preexisting work, stated the court, and it was plain error for the District Court to rule, as a matter of law, that Freeman's joint authorship of the prior works made him a joint author with Weissmann in the derivative work.

Judge Cardamone proceeded to find that Freeman acquired no interest in the article beyond those rights which he had as coauthor in the prior joint material incorporated into the article. Furthermore, there was no evidence that the doctors intended their prior work to be "forever indivisible," or that Freeman intended to contribute to a derivative work. There was "substantial and uncontroverted" evidence, however, that Weissmann intended the article to be her own individual work, and the District Court's finding of fact that Freeman's co-authorship of the preexisting works also made him a joint author of the 1985 article was clearly erroneous.

Judge Cardamone also questioned the District Court's failure to find that Weissmann, by selecting and rearranging material from prior works and adding to that material, produced a work of original authorship warranting copyright protection. The court described several new elements added by Weissmann to the existing prior joint work. Although many of the elements consisted of portions of prior works, the Copyright Act "expressly protects the selection of subject matter and content from underlying works, as well as the rearrangement of pre-existing material taken from those works," stated Judge Cardamone. The article was a "new and original" treatment of material and was entitled to copyright protection as a derivative work.

Judge Cardamone next commented on certain equitable considerations present in the instant case, pointing out that Freeman not only neglected to credit Weissmann for her authorship of the article, but "actually attempted to

pass off the work as his own, substituting his name as author in place of hers. Adding insult to injury, he then distributed copies of her work, but modified the title slightly to one of his own devising." Freeman's conduct, stated the court "severely undermines his right to claim the equitable defense of fair use."

Notwithstanding the above comments, Judge Cardamone reviewed the statutory fair use factors, and found that when such factors were considered in the context of scholarly scientific research and publication, they weighed against Freeman's right to invoke the fair use defense in the infringement action.

The court concluded that Weissmann's article was an individually-authored, copyrightable, derivative work, and that Freeman's use of the work was not a fair use. The District Court's decision, accordingly, was reversed, and remanded with directions that judgment be entered in favor of Weissmann.

Federal Court of Appeals Judge Pierce concurred in the court's opinion, differing with Judge Cardamone only with respect to noting that the fact that Freeman was not the author of any of the new material included in Weissmann's article did not, of itself, preclude that work from being "joint." If Weissmann had intended the work to be joint, Freeman could have been deemed a joint author "simply by virtue of his contributions to the earlier work..." Judge Pierce also would have found relevant to the question of Weissmann's intent, although not dispositive, the parties' past willingness to have their works "absorbed" into a common syllabus.

Judge Lombard dissented from the court's opinion, and would have voted to affirm the judgment of the District Court.

Weissmann v. Freeman, 868 F.2d 1313 (2d Cir. 1989)
[ELR 11:7:17]

New Jersey appellate court upholds finding granting Nancy Piscopo an interest in former husband's celebrity goodwill

A New Jersey appellate court has upheld a trial court ruling (ELR 11:3:12) including Joe Piscopo's "celebrity goodwill" as marital property subject to equitable distribution in the divorce proceeding between the comedian and Nancy Piscopo.

An accountant appointed by the trial court judge calculated Joe Piscopo's celebrity goodwill by taking twenty-five percent of the comedian's average gross earnings over a three year period, arriving at a value of about \$160,000. The trial judge, however, relied on Piscopo's earnings over a five year period, and because his

earnings had been lower during two of those years, goodwill was valued at about \$99,000.

The appellate court observed that Piscopo was engaged in a business based on, personal competence, the earnings of which were undisputed"; that "whatever [Piscopo] had achieved as a celebrity had taken place during the marriage;" and that the goodwill value of Piscopo's business was a distributable marital asset.

According to news reports, Nancy Piscopo will receive about \$47,000. The New Jersey Supreme Court has denied certification for review.

Piscopo v. Piscopo, 557 A.2d 1040 (N.J.App. 1989)
[ELR 11:7:18]

Houston Astros shareholder obtains hearing on contract and fraud claims against majority shareholder, but ruling invalidating voting agreement is upheld

In 1984, when minority shareholders of the Houston Sports Association, the corporation that owns and operates the Astrodome and the Houston Astros Baseball Club, tried to remove John J. McMullen as the association's Chairman of the Board, Don A. Sanders withdrew from the voting agreement. The shareholders were left with only forty-nine percent of the shares when Sanders withdrew his two percent interest, and McMullen was able to retain control of the association.

Sanders claimed that he withdrew from the voting agreement and eventually purchased additional stock in reliance on certain promises made by McMullen. According to Sanders, McMullen agreed, among other items, to grant Sanders participation in management

decisions involving the baseball team; participation in league meetings, World Series and All Star game activities; and access to all baseball facilities and to all operational information.

In 1986, Sanders was not re-elected to the Board of Directors of the association and was advised that he was not entitled to any special privileges as a shareholder.

Sanders sued McMullen, alleging breach of contract and fraudulent misrepresentation. A Federal District Court granted McMullen's motion for summary judgment on the ground that the agreement between Sanders and McMullen was a "voting agreement," and that the statutory requirements for such an agreement, including a writing, were not met.

A Federal Court of Appeals first found that of the seven promises allegedly made by McMullen, only the one that required McMullen to vote his shares so as to keep Sanders on the board was controlled by the

applicable statute. The District Court's decision granting summary judgment to McMullen with respect to the alleged promises not relating to the voting of shares there-fore was reversed and remanded.

However, McMullen's alleged promise to vote so as to keep Sanders on the board was clearly a voting agree-ment not in compliance with statutory requirements," and the District Court properly awarded summary judg-ment on that issue.

In turning to the fraud complaint, a cause of action not considered by the District Court, Judge Gee found that Sanders stated a cause of action on the tort claim, and remanded this issue as well for further consideration.

Sanders v. McMullen, 868 F.2d 1465 (5th Cir. 1989)
[ELR 11:7:18]

Topps Company must pay \$200,000 due to National Football League Players Association under licensing agreement because 1987 player's strike did not excuse performance

Following the 24 day strike of the National Football League Players Association during the 1987-1988 football season, Topps Company refused to make a payment due under the company's license agreement with the association. The agreement stated, in part: "Anything herein to the contrary notwithstanding, if performance by either party is prevented or substantially impaired by war, strikes, lock-outs, acts of God ... or any other cause beyond Licensee's control, then such party ... shall be excused from performance hereunder, except Licensee shall pay the percentage of Net Sales (as defined herein) that were made before and up to the event causing the disruption" (emphasis added by the court).

Topps claimed that the sale of football trading cards bearing the names and pictures of NFL players was substantially impaired by the players' strike.

The association claimed that the reference in the agreement to "strikes" meant strikes which would inhibit production.

A New York trial court noted that Topps presented no evidence of its inability to perform under the agreement, or that the strike prevented the company from either producing or distributing its products. New York State Supreme Court Acting Justice Diane A. Lebedeff observed that although Topps claimed that its performance was substantially impaired because fewer football cards were purchased during the strike, year-end figures showed that Topps' net sales for the year increased.

The court found that the football players association was entitled to the \$200,000 quarterly payment due, plus interest from April 5, 1988.

National Football League Players Association v. Topps Company, Inc., New York Law Journal, p.22, col.2 (N.Y.Cnty., Aug. 30, 1989) [ELR 11:7:19]

Purchaser of Missouri television station may not recover damages from ABC for termination of affiliation agreement

Television station KMTC in Springfield, Missouri, became an affiliate of American Broadcasting Company in 1966. The affiliation agreement was renewed without interruption through January 1985.

In January 1985, Charles Woods Television Corporation agreed to purchase KMTC from Midland Television Corporation for \$13 million. However, in February 1985, ABC informed Woods TV and KMTC that

Telepictures Corporation was seeking the network's Springfield affiliation for station KSPR. ABC invited KMTC and Woods TV to make a presentation for retaining the affiliation.

After KMTC and KSPR delivered presentations to the ABC Affiliation Review Committee, the network, in May 1985, approved the assignment of the affiliation from KMTC to Woods TV. ABC stated, however, that it still was evaluating the competing presentations and reserved the right to terminate the affiliation upon six months' notice. In June 1985, ABC notified the various parties that the network had decided to defer a decision concerning its affiliation for at least the rest of 1985.

Woods nevertheless proceeded to close the purchase of KMTC (which received the new call letters KDEB) in July 1985, after obtaining an agreement that the sales price would be reduced by \$5 million in the event that

ABC terminated the affiliation before July 1986. ABC terminated KDEB's affiliation on April 3, 1986.

Woods then sued ABC (which became a wholly owned subsidiary of Capital Cities/ABC, Inc. in January 1986) for fraud; ABC removed the action to federal court on diversity grounds. A Federal District Court jury awarded Woods TV a total of \$3.5 million in damages, but the District Court granted ABC's motion for judgment notwithstanding the verdict.

Senior Federal Court of Appeals Judge Bright, in affirming the District Court's decision, noted that Woods' claimed false misrepresentation based on ABC's statement, in June 1985, that it had not yet decided whether to switch its affiliation. Woods argued that the jury could have determined from the evidence that ABC already had decided to change its affiliation before sending the letter. But Judge Bright noted that the network reviewed the November 1985 and February 1986

ratings, and reports from its research and engineering departments submitted in the spring of 1986 before reaching its decision, and that the June 1985 letter did not constitute a false representation.

Judge Bright also pointed out that no jury could reasonably find that ABC intended the June 1985 letter to induce Woods to purchase KMTC and improve the facility, and that Woods did not establish that it relied on ABC's alleged misrepresentation in buying the station and making improvements.

Charles Woods Television v. Capital Cities/ABC, Inc.,
869 F.2d 1155 (8th Cir. 1989) [ELR 11:7:19]

Cable television company in Maryland obtains access to private residential community, but Pennsylvania courts find that Cable Act does not provide right of access to apartment buildings

Several cases brought by cable television companies seeking access to residential communities have been decided recently.

In *Cable Investments, Inc. v. Woolley*, the owner of two apartment complexes in Pennsylvania notified Cable Investments in July 1985 that the company no longer would be permitted to provide cable television service to apartment tenants. When Cable Investments refused to remove its equipment, Waterford Associates (whose general partner was Mark Woolley), disconnected the system.

Cable Investments sought damages and injunctive relief which would allow the company to continue to offer

cable television service to Waterford's tenants. A Federal District Court granted Waterford's motion to dismiss Cable Investments' claims.

Federal Court of Appeals Judge Sloviter first found no support in the express language of the Cable Communications Policy Act of 1984 for Cable Investments' position that Congress authorized franchised cable companies "to force their way onto private property, over the protests of the property owner, in order to offer cable television service to the tenants of the property owners." And the legislative history of section 621(a)(2) of the Cable Act also did not warrant a finding that the easements available to a franchisee "run up to as well as into an apartment building for purposes of mandatory access."

The Pennsylvania Landlord and Tenant Act did not give Cable Investments any rights to the interior of Waterford's buildings, and the company did not allege the

requisite state action to support its First Amendment claim.

Judge Sloviter therefore found that Cable Investments did not state a cause of action under the Cable Act, and concluded by emphasizing that the court did not reach the issue of whether a private right of action to enforce the right asserted by Cable Investments can be implied from the Act.

In *Cable TV Fun 14-A, Ltd. v. Property Owners Association Chesapeake Ranch Estates*,

Cable TV Fund, a Colorado limited partnership providing cable television service to consumers in Maryland as Jones Intercable, sought access to a residential community known as the Chesapeake Ranch Estates. Federal District Court Chief Judge Alexander Harvey, II, found that Cable TV Fund had an implied right of action under section 621(a)(2) of the Cable Communications Policy

Act to enforce its rights as a cable provider under a non-exclusive municipal franchise.

Judge Harvey pointed out that although the decision in Woolley (above) concluded that a cable company's complaint based on the Cable Act did not state a cause of action, the Court of Appeals did not find it necessary to reach the issue of whether a private right of action can be implied under the Cable Act to enforce the rights asserted. Woolley thus was "of little assistance" to Property Owners Association, stated Judge Harvey, for the case held only that the Cable Act provides no substantive right whereby a cable company would be entitled to run cable wires along utility casements within the interior (emphasis by Judge Harvey) of a multi-unit dwelling in order to provide cable service.

In the instant case, telephone and electric utility easements were situated along the roadways of the residential community. The court concluded that the Cable Act

provides franchised cable companies a substantive right of access to properly through such easements, and granted Cable TV Fund, after a thorough analysis of the relevant factors, a preliminary injunction barring the Property Owners Association from taking any action to prevent Cable TV Fund from constructing and operating a cable system within the Chesapeake Ranch Estates.

In *Cable Associates, Inc. v. Town & Country Management Corporation*, a Federal District Court in Pennsylvania, stating that it was bound by the decision in *Woolley*, denied a cable television company's motion seeking injunctive relief to permit the company to continue to supply cable television service to two apartment complexes. Cable Associates, doing business as Suburban Cable of Lancaster County, argued that the fact that telephone company easement ran into the individual apartments in the complexes distinguished the instant case from *Woolley*. But Judge Cahn stated that even if

Suburban was correct that Woolley should be read to allow Suburban to "piggyback" on the telephone company easement, the court would deny the company's request for access.

Judge Cahn stated that Congress did not intend the Cable Act to confer eminent domain rights on franchised cable operators; the telephone company easement was not "dedicated" to the public in the sense that a franchised cable operator, as a member of the public, was entitled to use the easement provided that the easement was compatible for cable television purposes. The court also pointed out that there was no evidence in the record that Suburban's drop lines were within the telephone company easement and, if not, whether there was room left in the easement for additional drop lines.

Cable Investments, Inc. v. Woolley, 867 F.2d 151 (3d Cir. 1989); Cable TV Fund 14-A. Ltd. v. Property

Owners Association, 706 F.Supp. 422 (D.Md. 1989); Cable Associates, Inc. v. Town & Country Management Corporation, 709 F.Supp. 582 (E.D.Pa. 1989) [ELR 11:7:20]

Federal District Courts in Massachusetts differ on whether local regulation of cable television basic service rates is preempted by Cable Communications Policy Act

Soon after Cablevision of Boston raised the rates for its basic service, the company sought a declaration in a Federal District Court that the Cable Communications Policy Act of 1984 preempted the municipal regulation of cable television rates. The court found that Congress, in enacting the Cable Act, did not intend to "totally occupy" the field of cable television services. Cablevision

was entitled to raise the preemption argument on remand to the state trial court as a possible defense to the city of Boston's common law claims against the company, but preemption did not provide a basis for subject matter jurisdiction in the District Court, concluded Judge Young.

In a separate case, Nashoba Communications, the operator of a cable television system in the town of Danvers, also filed a complaint in the Federal District Court in Massachusetts seeking declaratory relief with respect to a proposed rate increase. Senior District Judge Caffrey found that the action arose under federal law, rejecting Danvers' argument that the action was a common law contract dispute governed by state law. Judge Caffrey stated that the Cable Communications Policy Act of 1984 preempted the field of cable television regulation. The court, pointing out that Nashoba was subject to effective competition, barred any action by the town to

enforce the rate freeze contained in its franchise agreement.

A subsequent opinion by Judge Caffrey noted that Nashoba had implemented its proposed rate increase on August 1, 1988; this information was not previously presented to the court. The court's initial memorandum and order therefore was amended by striking all references to prospective relief concerning the rate increase.

It should be noted that Judge Young expressed respectful disagreement with Judge Caffrey.

Cablevision of Boston Limited Partnership v. Flynn, 710 F. Supp. 23 (D. Mass. 1989); Nashoba Communications Limited Partnership No. 7 v. Town of Danvers, 703 F.Supp. 161 (D.Mass. 1988); 709 F.Supp. 263 (D.Mass. 1989) [ELR 11:7:21]

DEPARTMENTS

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[ELR 11:7:23]