LEGAL AFFAIRS

International Tax Planning for Artists in the Entertainment Industry (Part 3)

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II. International and Domestic Estate Tax Planning

A. Overview

Federal estate taxes in the United States are presently imposed at a rate of 55% on large estates (except that property passing to a spouse is, in most instances n17 exempt from current tax). There is also a generation skipping tax under IRC Secs. 2601 et seq., so that there

will be two estate taxes before money passes from an artist to his grandchildren. Therefore, a grandchild may only receive about 20% of the artist's estate after two 55% death taxes are imposed (and the artist has already paid income tax on most of the money during his lifetime before the above two death taxes totalling 80% are imposed!).

Now that federal income taxes have been reduced to 28%, these high estate tax rates make estate tax planning a very important part of the overall tax plan for a wealthy artist or athlete who cares about passing wealth to his heirs.

B. Domestic Estate Tax Planning for United States Artists and Athletes

Whenever possible, a writer who creates a work that could have value remaining at the time of the artist's

death should own and license the right to use his works so that the literary property will obtain a "step-up" in basis upon the death of the author (or on the death of either the author or his spouse if the work is community property). See Rev. Rul. 57-544, 1957-2 CB 361; Rev. Rul. 60-227, 1960-1 CB 262; and Rev. Rul. 54-409, 1954-2 CB 174. The license of the literary property should be so designed that it will be upheld as a license, and not treated as a sale, because a sale will create Income in Respect of a Decedent ("IRD") which is subjected to continued federal income and death taxes at a maximum rate of about 70-3/4% (instead of just the estate tax of 55%). This higher tax results from the fact that IRD is not calculated with the benefit of a step-up in tax basis at death. IRC Sec. 1014(c). See Rollert Residuary Trust, 80 T.C. 619 (1983).

If a license is exclusive in any medium (e.g., publication or free television) in at least an entire country, and

if the license is for the full useful life of the work, n18 the license will probably be treated as a sale for purposes of determining whether the proceeds of the license will be treated as IRD. It is unclear exactly what constitutes the "full useful life" of a copyright or film. Probably, it is more than seven years and less than twenty years, but the law is unclear and it might depend in part on the facts of the particular case. See, IRM, Audit Para 45(11)(B), Para 5(3)(A)(2), and PLR 8020001 (Dec. 18, 1979).

The estate of a producer, who has an ownership interest in a film that will obtain a step-up in basis on death, will pay lower total taxes than will the estate of a producer who has only a profit participation, since a profit participation will constitute IRD and be subjected to both income and death taxes.n19 The position of a producer who has an ownership interest in a film is similar

to the position of a writer who owns his work and licenses, rather than sells it, as described above.

It may be feasible for a writer or producer to work in conjunction with an adult child so that copyrights or films will be owned partially by the child. This is only feasible in cases where there is a talented child who actually works with the parent in creating the work. Tax counsel should consider what other business opportunities can be given to a talented child.

Tax counsel should consider the problems, as well as the advantages, of having a writer work in corporate form (possibly through an S corporation) rather than individually. For example, as an alternative to sharing ownership with a child, a corporation could pay a reasonable salary (including pension benefits) to an artist's children or parents who do research or writing. Where the artist lives abroad and has a nonresident alien spouse and/or nonresident alien children who work with him,

reasonable compensation or joint venture arrangements for such foreign family members can totally avoid all tax on the reasonable compensation of such foreign persons (if they are not taxed by the foreign country).

There are also estate tax deferral possibilities if the author's works comprise a large part of his estate. See, IRC Sec. 6166 for deferral possibilities if the works constitute a closely held business (with, at present rates, an approximate twelve percent per annum interest charge, but the interest is deductible in computing the estate tax so the net cost may be less than six percent). See Rev. Rul. 61-55, 1961-2 CB 713, for some indication as to whether an author will be considered to have used the works in a "closely held business." See, also, IRC Sec. 6161 and Treas. Reg. Sec. 20.6161-1(a)(1), Ex.(2), regarding a "reasonable cause" deferral of estate tax when the estate does not have sufficient liquid assets to pay the estate tax immediately.

A married artist might consider giving $20,000 per year to a trust with a "Crummey" power for each child and grandchild. Only $10,000 is permitted if the artist is either unmarried or married to a nonresident alien spouse. IRC Sec. 2513(a). The artist's trusted advisors can retain control over the use and investment of the trust funds. If the artist should need funds at a later time, the trust can pay the child's expenses (including college costs and weddings) that the artist would otherwise have used his own funds to pay. If the artist has substantial excess assets that he will not need, he should give the $600,000 equal to his unified federal estate and gift tax exclusion ($1,200,000 if he is married) to a trust for the children as soon as possible so that the growth of these assets will be out of his estate. Tax counsel should consider when it is appropriate to elect to use the client's generation-skipping tax exemption with respect to a

particular gift in trust (e.g., it should not be elected if the trust is likely to distribute before the child dies).

It may be possible for an artist to make transfers in a manner such that the artist will continue to be liable to pay the income tax on the trust income by reserving certain powers over the trust. See, IRC Sec. 677(9)(3); Treas. Reg. Sec. 1.671-3; and Rev. Rul. 85-13, 1985-1 CB 184.

If the artist has a spouse who is a nonresident alien, he might loan her about $1,100,000 free of interest. There would be no gift tax if the value of the imputed interest foregone on the loan each year (which is treated as a gift under the Code) doesn't exceed $100,000 per year (i.e., approximately 9% on $1,100,000). IRC Sec. 2523(i). Further, there is no imputed interest for income tax purposes on the loan to a spouse. IRC Sec. 7872(f). The nonresident alien spouse can then invest the $1,100,000 and earn about $100,000 per annum of tax free interest,

unless tax is imposed in the spouse's country of residence.

It is often advisable to give away assets that are likely to rapidly appreciate in the future. However, there is a disadvantage in giving away assets that have already appreciated, because there is no step-up in tax basis at death for property that is given away during decedent's lifetime. In each case where an appreciated asset is being considered as the possible subject of a gift, counsel must weigh the benefits of avoiding death tax on the future appreciation as against the loss of a basis step- up on the past appreciation. The decision will depend on the age of the donor, whether the asset is likely to be sold in a taxable transaction in the near future, whether the asset is depreciable and other factors. In some situations, a GRIT (Grantor Retained Income Trust) for less than ten years, a life estate/remainder purchase of a primary residence (and also a second residence if it is not

rented out) and life insurance, qualified loans, and similar planning devices can be used to the extent that they do not fall within the scope of the "estate freeze" rules in IRC Sec. 2036(c). See Notice 89-99, 1989-38 IRB 4 (9/1/89).

Note: There can be a problem when a child sells a residence held in a trust because the trust cannot replace it tax free pursuant to IRC Sec. 1034 (except certain grantor trusts). If the trust is not a grantor trust, it might be possible under IRC 1031 to rent the property and exchange it for another house that would also be rented for a while.

A private charitable foundation should be considered as a possible recipient for pension benefits and other IRD items in large estates. The private foundation can meet the charitable obligations of the artist's children with money that avoids both income tax and death tax, and the foundation can be designed so that each child

can control his proportionate share of the foundation's charitable contributions. If the children want to make substantial charitable donations in any case, this is the best way to provide for these charitable gifts at the lowest after-tax cost, because only 29 1/4% of the pension and other IRD items would be left for the children to invest after taxes if these items were given to the children, with the children later using the income from this 29 1/4% for charitable contributions (instead of having the income from 100% of the money available in a charitable foundation). Before the money reaches the grandchild, there would be another 55% death tax, leaving only 45% of 29 1/4% or 13.16% for the grandchild to invest!

Counsel should consider name and likeness protection for a major star from a non-tax viewpoint. (For example, consider using a company owned in whole or in part by the artist's children to hold the rights to his or her name

and likeness so as to reduce death taxes.) As a minimum, counsel should be sure to have the appropriate heirs file the California form entitled "Registration of Claim as Successor-in-Interest" under Civil Code Section 990 to at least protect such rights in California.

C. International Estate Tax Planning for Artists and Athletes

1. Estate Planning for Aliens not Domiciled in United States

Alien artists who are domiciled abroad are generally subject to estate and gift taxes on only United States situs assets. Thus, they can minimize United States death taxes either by not holding United States situs assets, or by mortgaging such assets in a manner that they won't

have a large net equity that will be subjected to United States death taxes.

The new estate freezing rules of IRC Sec. 2036(c) should also be considered in connection with estate planning for a foreign artist who owns United States property. Notice 89-99, 1989- 38 IRB 4 (9/1/89), allows a taxpayer to purchase a life estate in a primary residence (and often in a secondary residence), using trusts for children and grandchildren to buy the remainder interest so as to avoid estate taxes. But see new IRC Sec. 167 (q), added by the Revenue Reconciliation Act of 1989, P.L. 101- 239, changing the depreciation/amortization rules for such term interests.

a. United States Real Estate

United States real estate is a United States situs asset which will be subject to federal estate tax when held by a foreign domiciliary.

It is often advisable to mortgage appreciated real property, because it will obtain a basis step-up and estate tax will be imposed only on the net equity value in excess of the mortgage. The mortgage should be nonrecourse and from an unrelated party, especially if the property is to be held by the non-domiciled alien individually (rather than through a partnership and trust). See Harcourt Johnstone, 19 T.C. 44 (1952). Recourse loans are allocated among the decedent's worldwide assets, instead of reducing the equity of the particular asset securing the debt. It is preferable to place the real property in a partnership, mortgage it, and then place the partnership interest in a trust, since this arrangement is more likely to result in the debt reducing the taxable value of that

particular asset and hence in a death tax only being imposed on the net equity of the property.

Having real estate owned by a foreign corporation will completely avoid estate tax and also provide some degree of secrecy about ownership, but it will cause higher rate of income tax on sale of the real estate by the corporation, and the real estate will obtain no step-up in tax basis at the time of the artist's death (or the death of his spouse if it is community property).

Note: Whenever one is planning to transfer the title to California real property to a related entity, consider the effect on real property taxes under Proposition 13. Recently enacted Proposition 58 may allow some of this property tax increase to be avoided on transfers from a parent to his children.

b. Planning for United States Situs Intangibles

Aliens who are not domiciled in the United States should avoid owning intangibles with a United States situs.n20 For example, they should usually acquire stock or securities in United States corporations through a foreign corporation. If the artist already owns such assets, he can sell such assets to a controlled foreign corporation if the sale can be planned so there will be no income tax or IRC Sec. 1491 excise tax on the transfer. In many cases, the United States tax treaties, together with Prop. Treas. Reg. Sec. 301.7701(b)-7, will avoid income tax on a sale to a foreign corporation, whereas the tax treaty and the above regulations may not preclude an excise tax on a contribution to a foreign corporation.

It is not entirely clear whether benefits under a qualified pension plan will always constitute a United States situs asset for estate tax purposes. There is no code section or regulation on point. See, however, the report of the Committee on Foreign Relations, CCH Para. 1318Q,

with regard to Article 11(o) of the United States/Canadian tax treaty. The Committee viewed the rule applicable under the Internal Revenue Code as being similar to the "debt rule" where the benefits would be situated at the place where the debtor company is organized. This approach would cause most pension benefits to be United States situs assets. Possibly, if the foreign beneficiary were trustee of his own pension plan, the benefits might be a foreign situs asset. However, it may be wise to pay the income tax and take pension distributions before death (and United States income tax on the distribution may be avoided under certain income tax treaties). If distribution is taken, the proceeds should be held in a manner such that the distributed assets will not constitute United States situs property.

2. Planning Before Moving to the United States

Counsel should consider possible estate tax planning opportunities for a foreign artist intending to move to the United States.

Gifts can be made in trust for children and grandchildren before the artist comes to the United States. This can avoid United States estate tax on the artist's death and possibly also avoid United States generation skipping tax but the effect of the generation skipping tax on such transfers is unclear. Of course, the taxes in the artist's home country must also be considered.

Foreign parents can create " grantor" trusts for the artist so that the income will not be taxed to the artist after he moves to the United States, but only for so long as the artist's parents remain alive. Rev. Rul. 69-70,1969-1 CB 192. See generally, Chopin "Use of Foreign Grantor Trusts in Income and Estate Planning," note 20, above.

3. Example

The following hypothetical example will illustrate the types of problems that will often arise in international estate planning. The solution to these problems will vary, depending upon the laws of the particular countries involved, but the general nature of the problems will frequently be similar to those contained in this example.

a. Factual Situation

A motion picture producer (herein "Producer") was born in Lebanon where he still has some family ties and some assets. He carries a Lebanese passport and he intends to return to Lebanon some day when the political situation there stabilizes. His will provides that he is to

be buried in Lebanon and he considers himself to be domiciled there.

Producer makes films in the United States, in England and in France. He is considered to be a resident of the United States under the internal law of the United States, and he is considered to be a resident of England under internal English law (i.e., he has dual residence), but he is not treated as a French resident under the laws of France where he spends only a little time. There is some risk that either the United States and/or the United Kingdom might also consider him to be domiciled there, although tax counsel believes that Producer has sound arguments that he is domiciled in neither country and that he has retained his "domicile of origin" i.e., Lebanon.

At the present time, Producer's closest contacts are to England where he maintains his home worth 750,000 pounds and bank accounts containing a total of

1,200,000 pounds. However, Producer has appreciated United States stocks worth $1,000,000, a United States pension worth $500,000 and an appreciated apartment building in California that is now worth $1,500,000. Producer is prepared to take some risk that the United States or England might treat him as domiciled there and hence subject to gift or death tax on worldwide transfers.

b. Problems Presented

Since Producer takes the position that he is not domiciled in either England or the United States, and since he is not a citizen of the United States, he will hopefully not be subject to gift taxes or death taxes in either England or in the United States, except on property having a situs in those countries. His five major assets (his home and large bank account in England, and his stock

portfolio, his pension benefits and his apartment building in the United States) have a situs in the United Kingdom and the United States, respectively.

If Producer were to undertake no advance tax planning and merely prepared a typical will providing that he is domiciled in Lebanon, his will might be probated under Lebanese law if he did not have wills for his United States and United Kingdom assets that specify that Californian and English law govern the assets in those countries. Also, there could be probates in Lebanon, England and the United States. With probate proceedings in England and the United States, there could be some increased risk that each of those countries would assert that Producer is domiciled there. Further, England would tax the English house and bank account, and the United States would tax the stock portfolio, the apartment building and the pension plan, even if the Lebanese domicile is upheld.

c. Use of Trusts

In domestic estate planning, there is a question as to whether a will or a revocable trust is the preferred vehicle. The answer will depend upon the facts of the particular case. However, in the international estate planning arena, the trust is almost always the preferred vehicle, even as compared to a properly drafted international will. The trusts should be set up in the Cayman Islands, the Channel Islands, Bermuda, the Bahamas or another tax haven jurisdiction which recognizes the law of trusts. There can be problems if the trust is to own real property or certain other types of assets situated in a country that doesn't recognize the law of trusts - it may be necessary in some cases to use an "off-shore" corporation to hold the asset and give the stock of that corporation to the trust.

The trust instrument should provide for an automatic change of situs and governing law in the event of political instability or the imposition of burdensome tax or regulatory controls. Consideration should be given to holding the bulk of the trust assets in the United States, the United Kingdom or other politically and economically stable, democratic countries. In some countries (e.g., England), it may be best if the trust can only be revoked by the grantor with the consent of one of a number of people located outside of that country, and there is no reason not to use this approach as long as Producer is comfortable that at least one of the named people will grant the consent if he wishes to revoke or amend the trust.

In some cases (depending on applicable tax, creditor rights and other laws), instead of using a revocable trust, it may be better to use an irrevocable "spray trust" where the trustee can spray the income between

Producer and other members of his family. The Producer or a trusted person would usually retain the power to replace the trustee with another bank in a tax haven jurisdiction, so that Producer can be assured of obtaining the funds he needs for his reasonable support.

It is, of course, imperative that title to the assets be placed into the trust during Producer's lifetime, or otherwise Producer's will would have to be probated in order to move the assets into the trust, and his family then would have many of the same administrative problems present in instances where a trust is not used, as described above. If all assets are placed into the trust at the present time, there may be no need to probate Producer's will in any country, because there would be no assets to pour-over under the will.

Note: If Producer (or his revocable trust) has over $60,000 of United States situs assets, an estate tax return will be required. IRC Sec. 6018(a)(2). (The

$13,000 credit allowed under IRC Sec. 2107(c)(1) will eliminate the tax on a taxable estate of $60,000.) In the absence of an applicable tax treaty provision, a non-citizen who is not domiciled in the United States will obtain a marital deduction only if his spouse is a U.S. citizen. See footnote 17, above. Therefore, if Producer chooses to place his United States apartment building into a partnership (rather than a corporation) so as to minimize income taxes when the property is sold and obtain an increase in tax basis at death, an estate tax return will probably be required, since it may not be feasible to reduce the net equity value to less than $60,000 and still have a non- recourse mortgage note (that would represent almost the entire value of the property and that would probably require outside guarantees and/or security) recognized as a true debt obligation secured by the property.

d. Planning for Pension Assets n21

Producer should consider taking a lump sum distribution of his pension plan while his closer ties are to the United Kingdom so that he will not be subject to United States income tax as a United States resident. See Article 2 of the United States/United Kingdom income tax treaty. See, also, Prop. Treas. Reg. Sec. 301.7701(b)-7(a). However, note that Producer would not avoid the 15% excise tax under IRC Sec. 4980A on excess distributions, if any.

However, he might avoid the "excise" tax on early distribution under IRC Sec. 72(t) because it is phrased as an "increased" tax of 10% of the amount "includible in gross income," because the treaty excludes the pension benefits from gross income. See the analysis used in PLR 8904036 which holds that the 15% excise tax imposed by IRC Sec. 4980A on excess distributions is not

an "income tax under Chapter l." The negative inference about the tax in IRC Sec. 72(t), which is in Chapter 1, is that it is such an income tax.

Interestingly, the United Kingdom does not tax a lump sum distribution from a pension plan under its internal law, so neither country will tax this distribution. Counsel may want to distribute a commercial annuity to increase the likelihood that the lump sum distribution will constitute a "pension" under the United States/United Kingdom treaty, but this precaution might not be necessary. See PLR 8901053 (October 13, 1988) and PLR 8934025 (May 25, 1 989). Once the pension distribution is received, it should be invested in assets that do not have a United States situs for death taxes.

e. Planning for U.S. Stock Portfolio

With respect to Producer's stock portfolio which has a situs in the United States under IRC Secs. 2104 and 2105, there will be no United States income tax imposed as a result of transferring these assets into a grantor trust. See Rev. Rul. 85-13, 1985-1 CB 184. But merely placing the assets in an offshore grantor trust will not avoid United States death tax. See, generally, William Newton 111, International Estate Planning, Ch. 4; and Robert C. Lawrence III, International Tax and Estate Planning, a Practical Guide for Multinational Investors (PLI 1989). However, if the transferee of the assets is not a grantor trust (e.g., if it is a corporation owned by the trust so the situs of the asset will no longer be in the United States), then any appreciated assets should be sold to the corporation, because if they are merely transferred, an excise tax would be imposed under IRC Sec. 1491. See generally, Prentice-Hall Federal Taxes, 14,468 as to when a related-party sale will be

recognized as a sale. See INTL-55-86, 1987-2 C.B. 946, setting forth Prop. Treas. Reg. Sec. 301-7701(b)- 7(a), which only protects Producer against United States income taxes - not excise taxes. See the Technical Explanation to Article 2, par. 2 of the United States/United Kingdom income tax treaty which discusses the fact that the treaty will not preclude excise taxes imposed under IRC Sec. 149 1.

England will not tax the gain on the sale of Producer's stock portfolio to a related foreign corporation because non-domiciled person's are only taxed on such gains on the remittance basis (i.e., when the proceeds are brought into England). Article 4, par. 5 of the United States/United Kingdom income tax treaty, that denies protection to income not taxed in the United Kingdom because of non-remittance, will not cause the United States to tax the gain because, as a non-resident under Prop. Treas. Reg. Sec. 7701(b)-7, Producer should not

need to use the treaty to avoid tax on the gain from the sale of his stock portfolio - the gain from this type of sale is not taxable to a nonresident alien under the Code.

f. Planning for U.S. Real Estate

Producer's United States apartment building presents a special problem. If it is owned by a corporation, there would be no estate tax problem, but the income tax rate at the corporate level, including federal and state taxes, would be about 40%. Further, there would be an immediate tax if the property is placed in a foreign corporation, since this building has already appreciated and FIRPTA would cause a tax on the gain from real estate (unlike the stock portfolio that could be sold without paying United States income tax). On the other hand, if the real property is held in partnership form, there is only a 28% tax when the property is sold (state income

tax might be avoided if partnership interests are sold), and, if an IRC Sec. 754 election is made, the property will receive a step-up in basis at the time of the Producer's death.

While there are Commerce Department reporting requirements when an apartment building is held in a foreign corporation (See, 22 USC Sec. 3101-3108), still there is more secrecy as to ownership if the asset is held in a corporation than if it is held in a partnership (e.g., a United States estate tax return would probably be required if the apartment building is not held in a corporation).

If the property is heavily mortgaged with non-recourse debt, there will not be a large estate tax since only the net value of the partnership interest (considered after subtracting the mortgage from the property) should be subject to death tax. However, there is an expense involved in maintaining a mortgage from an unrelated

party, and there is always a question as to whether a mortgage from a related party, or a mortgage additionally secured by a certificate of deposit, will be recognized by the IRS. A large non-recourse loan from an unrelated party would probably be recognized, but it may not be obtainable at a reasonable cost. Further, where there is a related party mortgage, there can be problems of using the interest deduction, and there can be taxable income created if the related party is an offshore entity that makes the loan is owned by Producer (i.e., probably a foreign personal holding company if Producer becomes a U.S. resident), and if there should not be treaty protection in a future year when Producer's closer connections may be to the United States so that he becomes a U.S. resident.

In each situation, Producer will have to consider whether it is preferable to hold his United States real property in partnership form with a mortgage, or in

corporate form. The answer will vary, depending on the age and health of the owner, his tax basis for the property as compared to its value, his intent regarding the future sale of the property, his desire for secrecy, the tax and other costs of transferring the property to a foreign corporation, and other factors. Note that, in England, there is a tax by statute on imputed rental value if a taxpayer holds a house where he resides in corporate form. (It is possible that the United States could assert a similar tax on imputed rental value, although we are not aware of any situation where the IRS has done so and many foreign persons live in rent-free houses held in corporate form.)

g. U.K. Estate Planning Considerations

The following discussion describes some of the most important United Kingdom estate planning

considerations for Producer. The discussion is based on the most current information which we have obtained from United Kingdom estate planners. However, in any international estate planning problem, foreign advisers must be contacted to confirm the local tax consequences for each jurisdiction in which the taxpayer holds substantial assets or conducts substantial activities.

Producer would like to avoid both probate procedures and also death tax on his home and bank account in England. The English bank account should be placed in the tax haven corporation, along with his United States stock portfolio.

Producer should sell his English home to an off-shore "spray trust" of which he and other members of his family are beneficiaries. Producer would give the spray trust the money to buy the house and this gift of cash would be made outside the United Kingdom so there would be no United Kingdom capital transfer tax on the gift.

There would be a 6% tax in England every ten years on the net value of the English situs real property given to a spray trust, after subtracting mortgage, but only if this net amount exceeds Producer's unused gift tax exclusion (presently 118,000 pounds). This house would not, at today's values, be subject to any tax if the property is mortgaged for at least 85% of its value since 15% of 750,000 pounds is less than the 118,000 pound exemption. Also, the mortgage need not be placed on the property for nearly nine years since it is only necessary that the mortgage be in place when the ten year tax is imposed (but Producer should not wait to draw down the mortgage until immediately before the expiration of the ten year period).

h. Interplay of U.S. and U.K. Planning

The problem in selling the property to the spray trust is that the United States would tax the gain (i.e., the excess of 750,000 pounds over the basis for the property), unless either: (1) Producer qualifies as a nonresident under Prop. Treas. Reg. Sec. 301.7701(b)-(7), supra; or (2) the purchasing spray trust is a "grantor trust." This income tax problem only arises in the United States, since England will not tax the gain on a person's principal residence. So long as Producer actually uses the United States/United Kingdom tax treaty to avoid United States income tax on any item of income during the year in which the sale is made, he will be treated as a nonresident under Prop. Treas. Reg. Sec. 301.7701(b)-7. Further, the purchasing trust would be a grantor trust. Therefore, either of the above two defenses would preclude the United States from taxing the gain from the sale of Producer's UK home.

Ordinarily, for English tax planning purposes, it would be desirable to have the mortgage (i.e., when it is put in place in about nine years) made by a controlled tax haven corporation. However, there would be imputed interest on the mortgage in the United States, and therefore if the United States/United Kingdom tax treaty does not at that time preclude the taxation of this interest, Producer would have a United States income tax problem (i.e., because the income of the tax haven company would be taxed to Producer under the foreign personal holding company provisions of the Code. See IRC Sec. 551 et seq). This imputed interest problem can be avoided by the use of three grantor trusts which would be respected in England but ignored for purposes of United States tax law, as described below. (Note that the difference in the way that two countries characterize and tax a transaction is the basis for much international tax planning.)

Example. Producer gives enough money to fund the mortgages (i.e., 85% of 750,000 pounds) to Grantor Trust No. 1. This trust could, in turn, lend the money to another grantor trust (Grantor Trust No. 2). Then Grantor Trust No. 2 could make the mortgage loan to another grantor trust (Grantor Trust No. 3) which would use the money to buy the house from Producer. (Producer could borrow part of the money from a bank in the tax haven to enable him to make the gift to Grantor Trust No. 1. The money would soon be returned to Producer when he sells the house to Grantor Trust No. 3 and he could then use this money to repay the bank loan.)

Producer should succeed in (1) having the mortgage reduce the value of the house for English gift taxes at the end of each ten year period, (2) still not have the mortgage note subject to gift or death tax in England,n22 and (3) avoid imputed interest on the mortgage in the United States because the interest accrual or payment to a

grantor trust should be ignored for United States income tax purposes. See Rev. Rul. 85-13, 1985-1 CB 184.

i. Results of Planning

On the above facts, Producer will have succeeded in avoiding probate in all countries which recognize trusts. (Assets in certain civil law countries might best be held by a corporation that, in turn, is owned by the trust.) The assets will be administered by a bank in a tax haven jurisdiction, with the family having significant influence over the actions of the bank by their power to replace the trustee. (There may be a problem in obtaining the power to replace the executor since this might require the approval of the court, where the will is probated, and it is therefore an important decision as to who will be executor of Producer's will if the will must be probated.)

There would be no United States death tax on the trust assets as long as the trust does not hold United States situs property (e.g., the United States stock portfolio will be held by a foreign corporation owned by the foreign revocable trust, and the United States apartment will be either sold to a foreign corporation or placed in a partnership and heavily mortgaged as described above). Producer would avoid United States death and income tax on his United States pension if he takes a lump sum distribution of the plan benefits, free of United States income tax because of the US/UK tax treaty, and places the pension assets in a foreign corporation owned by the spray trust. Accordingly, so long as Producer does not become domiciled in the United States, there would be no United States estate tax.

The spray trust would be successful in avoiding English death taxes because the English house was sold to the trust, and the 1,200,000 pounds in United Kingdom

bank accounts were moved out of England and then placed in his tax haven corporation owned by this foreign trust.

In summary, the assets in the trusts should totally avoid any U.S. or U.K. tax (except U.S. estate tax on the net equity in United States real estate). These trusts should also avoid any exchange control or other regulatory jurisdiction by Lebanon, the country in which Producer is domiciled and any country where the beneficiaries may reside, and these trusts should greatly simplify the administration of Producer's assets at the time of his death, and reduce the attendant expense. The three grantor trusts can be "merged" after Producer's death so as to simplify the long-run administration.

The above example shows the need for international gift and estate tax planning, as well as international income tax planning. Producer's United States estate planner should coordinate closely with tax counsel and

probate counsel in the other important countries that might assert jurisdiction to tax or regulate Producer's estate, and then work out a creative plan that will be effective in each of the countries involved so that Producer's assets will be administered with a minimum of cost, tax, red-tape" and regulatory control.

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NOTES

17. Prior to the Technical and Miscellaneous Revenue Act of 1988 ("TAMRA"), P.L. 100-647, there was no marital deduction if the decedent was not either a, United States citizen or domiciliary who was subject to United States federal estate tax on worldwide assets. However, this was changed by TAMRA which added IRC Sec.2106(a)(3). A marital deduction is now allowed under IRC Sec.2106(a)(3) to a non-citizen decedent (even if the decedent is not domiciled in the United States) if his spouse is a United States citizen; but if the recipient spouse is not a United States citizen, then the deceased spouse must be a citizen or domiciliary of the United States and the marital deduction is only allowed if a Qualified Domestic Trust is used. See IRC Sec.2056(d).

18. See the discussion in PLR 8501006 (Sept. 24, 1984) regarding the sale vs. license issue. See, also,

Rev. Rul. 75- 202, 1975-1 C.B. 170; and Rev. Rul. 85-353, 1985-2 C.B. 408. See, generally, Schaaf, Estate Planning for Authors and Artists, BNA Tax Management Portfolio 423 (1981).

19. See, generally, Banoff, "Conversions of Services into Property Interests: Choice of Form of Business", Taxes (Dec. 1983), p. 844. Note that many provisions of the law have changed since this article was written in 1983.

20. See IRC Sec.2105 and 2106. There are very specific situs rules which should be reviewed by counsel preparing estate plans for non-domiciled persons. For example,in order to enable United States banks to attract deposits of foreign individuals, United States bank deposits are considered to be foreign situs assets unless they are " effectively connected with a U.S. trade or

business". IRC Sec.2104(c), 2105(b) and 871(i). However, cash held with a stock broker does have a situs in the United States. Rev. Rul. 56-421, 1956-2 C.B. 602. Although stock and obligations of United States companies are generally United States situs property, see IRC Sec.2105(b)(3) and 871(h) for certain exceptions, such as certain "portfolio" debt obligations. Life insurance policies, even if issued by, a United States company, are usually deemed to be foreign situs property unless effectively connected with a United States trade or business. IRC Sec.2105(a). Tangible personal property (including currency and checks), is ordinarily United States situs property if physically located here. See Treas. Reg. Sec.20.2104-1(a)(2) and Rev. Rul. 55-143, 1955-1 C.B. 465. The situs rules contained in applicable tax treaties will, of course, override the above statutory rules. See generally, Chopin, "Use of Foreign Grantor Trusts in

Income and Estate Planning", World Trade Institute at New York City 5/8-9/1989 pp. 31 et seq.

21. See, Labor Regulation Sec.2550.404(b)-1 regarding the possibility of having the pension fund invest in foreign securities. See generally v, E.L. Wyckoff, Jr., U.S. Taxation of Foreign Trusts, U.S. and Non-U.S. Grantors and Trust Beneficiaries (PLI 1984). Note that the "indicia of ownership" of the foreign securities must be kept in the United States. ERISA Sec.404(b). Note also that, for income tax purposes, the IRS takes the position that employer contributions with respect to domestic services and all investment income is domestic source income. Only employer contributions with respect to foreign services are foreign sourced. Rev. Rul 79-389, 1979- 2 C.B. 281. Query as to whether there is an argument that foreign sourced earnings of the pension trust, if any, should retain its character as foreign source

income, especially if there is a foreign trustee. See the discussion in Rev. Rul. 79- 388, 1979-2 C.B. 270.

22. United Kingdom death tax would be avoided on the following reasoning: (1) Trust 1 is given 85% of 750,000 pounds or 637,500 pounds by Producer. The gift is made outside of the United Kingdom and hence is free of United Kingdom gift tax. (2) This $637,500 pounds would be loaned by Trust 1 to Trust 2. (3) Trust 2 would loan this 637,500 pounds to Trust 3 that would use this 637,500 pounds (together with the 1 12,500 pounds that would be given outside of England to Trust 3 by Producer) to buy the house from Producer for 750,000 pounds, leaving Trust 3 with a net equity of 112,500 pounds. After the above transactions, Trust 1 would have no United Kingdom situs asset -- just a note from a nonresident trust for 637,500 pounds. (Only an obligation of a resident of the UK or an obligation

secured by UK property is a UK situs asset.) Trust 2 would have a United Kingdom situs asset -- a 637,500 pound mortgage secured by United Kingdom real estate; however, that trust would have no net assets subject to death tax because it would owe 637,500 pounds to Trust 1. Trust 3 would have less than 118,000 pounds of United Kingdom situs real estate because its 750,000 pound house would be mortgaged for 637,500 pounds, leaving a net equity of only 112,500 pounds. The interest accruing on the mortgage would help to offset any inflationary increases in the value of the house.
[ELR 11:8:3]

RECENT CASES

French appellate court allows television broadcast of colorized version of "Asphalt Jungle," but French exhibitors of the colorized film must include statement that heirs of director John Huston opposed colorization

The Court of Appeal of Paris has reversed a lower court order that had barred French television stations from broadcasting colorized versions of the film "Asphalt Jungle" (see ELR 11:2:17; 10:10:3).

The Court of Appeal found that Turner Entertainment held the copyright in the film, and was free to modify the work. The contracts between MGM/Loew's, Turner's assignor, and the screenwriters of the film, John Huston and Ben Maddow, provided that the company had the right to modify and/or revise the literary material

produced by the writers. Huston and Maddow did not assign any copyright interest to MGM/Loew's, noted the court, emphasizing that the company "would judge when the work was in their opinion complete and would also decide whether or not to publish or carry out, after publication, any modifications which seemed to them appropriate..."

The court declared that the Huston parties were not entitled to attempt to escape from the MGM/Loew's contract by seeking to exercise a moral right, and that the Berne Convention did not permit the use of one state's legislation to undermine contractual obligations entered into in another state.

The lower court erred in relying on "false premises" which may have reflected the traditional views in France of the relationship between producers and directors, but which could not be applied "without damage to the truth of what actually happened, to the epoch in which

'Asphalt Jungle' was created according to the practice of large Californian studios..." MGM/Loew's was "totally involved in the conception and creation of the film," and, again, "had the final word in all matters from the choice of the subject matter ... right up to the definitive editing, and in particular with regard to the script on which the director operated..."

In all, the court refused to set aside the relevant contracts, and rejected the Huston parties' claims concerning the late director's moral right, stating that such a rejection would not violate the public order in France. It was observed that Turner carried out the colorization of "Asphalt Jungle" in a legal manner in the United States. Furthermore, the court recognized not only Turner's right to exploit the colorized version of "Asphalt Jungle," but the public's right to "access to developments carried out in audiovisual communication" - the French broadcaster pointed out that colorization would

encourage many television viewers to become familiar with older films made in black and white.

The colorization of "Asphalt Jungle" constituted an adaptation of the black and white film, noted the court, and the Huston parties did not allege a defect in the quality of the adaptation. Indeed, stated the court, Turner neither destroyed nor altered the work in black and white "which it could commercialize again in cinemas if there was a public demand."

The court concluded by ordering the French broadcaster, in accordance with the broadcaster's request, to display a notice reminding the television audience of the possibility of watching the colorized film in black and white. And the court acknowledged the right of Huston's heirs, even if they are not included in the copyright succession, to prevent any false attribution concerning the work. Thus, in addition to announcing to television viewers that the broadcast of "Asphalt Jungle" consists

of an adaptation in color of a film made in black and white, the colorized version of the film, for all use in France, must state: "In respect for the memory of John Huston, screenplay writer and director of this film made in 1950 in black and white, his heirs oppose the projection in France of this [colorized] version created in 1986. Ben Maddow, co-screenplay writer, joins in this declaration. By a decision of 6 July 1989, the Court of Appeal of Paris ... rejected the above opposition but stated that the spectators or television audience would be informed of the opposition of the Huston estate."

In summary, the court found as follows: the author of the film "Asphalt Jungle" was Turner; the heirs to John Huston as well as Ben Maddow, had no moral right in the work filmed in black and white; the colorized version of the film was an adaptation for which Turner had obtained a certificate of copyright registration; and the Huston and Maddow parties could not criticize the

colorization, in itself, even if they could invoke a moral right in the black and white film.

Turner Entertainment Co. v. Huston, Court of Appeal of Paris, 4th Chamber, section B (July 6, 1989) [ELR 11:8:13]

Paramount Pictures is denied preliminary injunction barring placement of local advertisements on video-cassettes of studio's films

Video Broadcasting Systems, Inc. may continue to place advertisements on the lead-in tape of videocassettes rented or sold by video retail stores to the public, a Federal District Court in Kansas has ruled.

Paramount Pictures claimed that Video Broadcasting's activities constituted trademark and copyright

infringement and unfair competition. According to Paramount, some of the advertisements overlapped the FBI warning and the Pepsi commercials on videocassettes sold by Paramount. Paramount alleged that the public was likely to believe that the advertisements placed by Video Broadcasting were a part of or connected with Paramount, and sought to enjoin Video Broadcasting from, among other conduct, adding the unauthorized advertisements.

In reviewing the factors relevant to a determination of likelihood of confusion, Judge Sam Crow noted that Paramount's trademark was a strong mark suggesting the production source of motion pictures and videocassettes. However, Paramount did not present evidence of actual confusion, noted the court.

Furthermore, Paramount's primary argument on confusion was that a reasonable consumer renting or purchasing a videocassette bearing a Paramount trademark

could rightfully assume that what was contained in the package was produced, licensed, or sponsored by Paramount. But the court called Paramount's argument " overly simplistic," and raised several factual issues requiring further evidence, such as the extent to which consumers know that videocassettes are owned by video retailers, whether consumers believe that it is technologically possible for local video retailers to place advertisements on the videocassettes, and whether consumers would believe that Paramount actually licensed the sale or directly sold advertising space on its videocassettes to local businesses. In the absence of evidence on these issues, and in view of its skepticism that viewers "actually care" whether Paramount was the source or sponsor of the advertisements, the court found that Paramount did not meet its burden under section 32(1) of the Lanham Act of showing a likelihood of product confusion or sponsorship confusion.

Given the court's conclusion concerning the likelihood of confusion, injunctive relief also was unavailable to Paramount on the company's claim for false designation of origin in violation of section 43(a) of the Lanham Act. The court also rejected a section 43(a) claim based on the alleged alteration or mutilation of videocassettes bearing Paramount's trademark since Video Broadcasting's advertisements purportedly overlapped and obliterated prerecorded material. Any overlapping in this case did not amount to a "substantial and material" alteration of Paramount's work.

With respect to Paramount's copyright infringement claims, Judge Crow first denied any claim based on the company's moral rights as a copyright owner to prevent the unauthorized editing of a copyrighted work. It was noted that Paramount did not allege that Video Broadcasting was granted certain rights in any motion pictures which the company exceeded or abused, or that the

substance of a protected work "was significantly altered and its quality and integrity compromised by a licensee or grantee who oversteps his authority." It did not appear to Judge Crow that the placement of advertisements resulted in the distortion of Paramount's motion pictures.

Judge Crow also rejected Paramount's argument that the addition of the advertisements amounted to an unauthorized derivative work, stating that no support was presented for the conclusion that "the mere addition of a commercial to the front of a videocassette recasts, transforms, or adapts the motion picture into what could represent an 'original work of authorship.'"

A claim based on the unlawful distribution of mutilated versions or derivative works was rejected in view of the disposition of the prior two claims.

Paramount's state law claim of unfair competition was denied, as was a claim for tortious interference with

prospective business advantage. Paramount argued that Video Broadcasting's advertisements jeopardized the studio's expectations that Pepsi and other national companies would enter contracts to place advertisements on future videocassettes. Judge Crow stated that "critical gaps" in the evidence, such as whether Video Broadcasting engaged in malicious conduct, prevented the court from finding that Paramount was likely to succeed on this claim.

Judge Crow concluded by observing that on the basis of letters exchanged by the parties Paramount should have investigated Video Broadcasting's activities and commenced its action by September 1988, rather than in August 1989 - the delay in suing was "inordinate," stated the court. Furthermore, a preliminary injunction would cause a substantial hardship to Video Broadcasting, found the court, outweighing Paramount's claim of irreparable harm to the studio's reputation and goodwill.

Any presumption of harm to Paramount also was diluted, according to Judge Crow, by the studio's failure to name almost twenty video retailers in the Wichita area, in addition to the one store named as a party, carrying videocassettes containing Video Broadcasting's advertisements.

Paramount Pictures Corporation v. Video Broadcasting Systems, Inc., Case No. 89-1412 (D.Kans., Oct. 11, 1989) [ELR 11:8:14]

DIC studio's freelance animation writers are independent contractors, not employees, rules National Labor Relations Board

The National Labor Relations Board has ruled that the freelance animation writers working for DIC Animation

City are not employees within the meaning of section 2(3) of the National Labor Relations Act. The Board reversed a Regional Director's decision (ELR 10:9:20) finding that DIC's writers were employees. In its ruling, the Board described DIC's production procedures. The company prepares "developmental bibles" for each animated series; each "bible" contains detailed drawings, character descriptions and other information about a series. Story editors also may attach a writer's guide, containing additional story and technical guidelines, to the "bible." Producing an episode of a series first requires the hiring of a writer, and the negotiation of the number of scripts to be written, residuals, royalties, and any guaranteed work on future series. However, noted the Board, usually there is no negotiation over fees because the fees are set per series.

After an informational meeting between the story editor and writer, the writer generally prepares several

premises - brief descriptions of the writer's story ideas. The Board noted that the writer "works at home, sets his or her own hours, and uses his or her own equipment and supplies." The editor then determines which premises to accept; the writer is not paid for the premises, whether accepted or rejected. Once certain premises are approved, DIC enters a contract with the writer providing, in part, that the premises and all further writing produced on the basis of the premises are DIC's sole property.

The writer next submits an outline, a second outline draft, and a script. At each stage of the writing process, the editor or a client, such as a television network, a toy company, or the series producers may request changes, ranging from a different ending to more action scenes. The writer usually will incorporate such changes, noted the Board, but may argue for his or her approach. DIC pays a flat fee for the writer's outline and script, and can

require only one rewrite of the outline and one rewrite of the script. Again, the script is DIC's sole property.

Writers receive no benefits, overtime pay, or expense reimbursements, observed the Board, and writers may turn in late work, or turn down assignments without losing future work on other series. DIC does not require exclusivity of its writers, and many writers work on projects for other producers.

In turning to the relevant statute, the Board noted that section 2(3) of the Act excludes "any individual having the status of an independent contractor" from the definition of employee. The Regional Director had found that DIC controlled the manner and means of the writing process from premise to final script draft because, as described by the Board, "the editors supervise and dictate the story direction, the bible and samples control creativity, and the editor and client control how the results are achieved." The Regional Director also pointed out

that the writers have regular contact with DIC at the company's office, and that there was "practical exclusivity" in the company's relationship with the writers because nine out of ten writers work for DIC exclusively until a project is completed. Furthermore, 95 percent of the writers undertook every assignment from DIC; thus, according to the Regional Director, there was no actual right to refuse work.

The Board concluded that DIC did not substantially control the manner and means of the writing process, based on the following factors: the writer creates the story idea, the premise, the outline, and the script' the writer determines where and when to work,and owns the equipment used; the writer determines whether to write stories as part of a team, and whether to form and work through a "loan out" company; and the writer negotiates the number of scripts, residuals, royalties, and work on future series.

DIC controlled the end product of the writer's work to the extent that the company, in order to conform to the 30 minute time limit for each episode, specified the lengths of scripts, outlines and premises. And in editing a writer's work for content, changes were made, according to the Board, "to ensure that the script fits within the time limitations, is consistent with the series tone, and is appropriate for the audience."

The Board further found that there was no practical exclusivity in the relationship between DIC and the writers, and commented that the writers "bear some of the risks and enjoy some of the opportunities for gain associated with an entrepreneurial enterprise." In all, the writers were independent contractors because they controlled the manner and means by which the result of the project was to be accomplished, and were subject to certain risks involved in an entrepreneurial enterprise. DIC's "limited control" was insufficient to warrant a

finding that the writers were employees, for the end product remained "primarily the independent work of the writers."

DIC Animation City, Inc. and Animation Writers of America, Case 31-RC-6444; 295 NLRB No. 107 (National Labor Relations Board, July 14, 1989) [ELR 11:8:15]

Damage award of $3.5 million to Record Club of America in breach of contract action against United Artists Records is vacated, and matter is remanded for further proceedings

A Federal District Court judgment awarding over $3.5 million to the Record Club of America in the company's

breach of contract action against United Artists Records has been vacated and remanded for further proceedings.

The lengthy litigation between the parties evolved from a 1970 licensing contract entered into as part of the settlement of an antitrust action brought by Record Club against United Artists and other parties. Under the contract, United Artists granted Record Club a nonexclusive license to advertise, manufacture, and distribute "albums," i.e, phonograph records, tape cassettes, and eight-track cartridges, by mail. The contract, among other provisions, stated that the record club could distribute a quantity of albums as bonuses or on any other free basis without paying United Artists a royalty on those albums.

In May 1972, United Artists asserted that Record Club breached the contract by failing to maintain accurate records as to its inventory and distribution of albums and

by failing to pay royalties on a quarterly basis for the excess free albums distributed by the record club.

In December 1972, Record Club sued United Artists, seeking injunctive relief preventing the record company from refusing to provide the record club with the materials necessary to manufacture albums, and a declaratory judgment that the contract remained in effect and the record club was not required to pay royalties on excess free albums prior to the expiration of the initial term of the contract.

At about the same time, United Artists, in a state court action in California, sought a declaration that the record club had breached the contract by failing to keep accurate accounts, and by not paying the royalties in issue on a quarterly basis; the California action was transferred to the Federal District Court in New York and the two actions were consolidated.

In August 1973, United Artists notified Record Club of its failure to give notice of the exercise of its option, under the 1970 contract, to renew the contract.

The Federal District Court issued a ruling in 1974, in which the court found that Record Club's failure to pay for excess free albums on a quarterly basis did not breach the contract, and that the record club's notice of renewal, although late, was effective. The action subsequently was placed on the District Court's suspense docket due to Record Club's filing of a petition in bankruptcy court.

Proceedings resumed in 1982, and, after bench trials on the issues of liability and damages, the District Court found that Record Club had established by a preponderance of the evidence that United Artists had anticipatorily repudiated the contract with Record Club. With respect to damages, the court awarded the record club damages for profits lost because of the record club's

inability to continue distributing United Artists' albums. After deducting certain setoffs and adding prejudgment interest, the court awarded Record Club about $3.5 million.

Federal Court of Appeals Judge Kearse first found inappropriate the 1974 ruling granting summary judgment to Record Club on the issue of the timing of payment for excess free albums. The contract did not state when the royalties for such albums were to be paid, and the question of which of two plausible interpretations as to the required timing of payment should be applied was a question of fact, stated Judge Kearse.

The District Court had ruled that in view of its decision that the failure by Record Club to pay royalties for excess free albums on a quarterly basis did not constitute breach of contract, and in view of other factors related to the negotiations of the parties, the record club's late notice of renewal was effective to extend the term of the

contract. However, by vacating the summary judgment ruling on the issue of the timing of royalty payments, the decision to excuse the record club's late notice also had to be set aside, ruled Judge Kearse, since the record club's failure to pay royalties on a quarterly basis may have constituted a breach of the contract.

Judge Kearse further noted that even if Record Club had not breached the contract, the District Court's decision to excuse the late notice "was not authorized by New York law on the record before it, if at all." Nothing in the contract or in United Artists' conduct obscured the date by which notice was required, and the record precluded any inference that United Artists led the record club to believe that an extension would be granted without the contractually required notice of renewal. And although Judge Kearse was "skeptical" that Record Club would be able to make a showing of the circumstances in which New York law would recognize a forfeiture

warranting the modification of the contract, further proceedings were ordered on the issue of whether the enforcement of the renewal option provision would work a forfeiture within the meaning of New York law.

On remand, concluded Judge Kearse, Record Club, in order to recover damages, will have the burden of showing by a preponderance of the evidence that the contract did not require it to pay for excess free albums on a quarterly basis, and that the enforcement of the contract's deadline for giving notice of the exercise of the renewal option would work a forfeiture on it. Record Club also must show, before being awarded damages for any period after September 30, 1973, that it would have been willing and able, absent United Artists' repudiation, to perform its own obligations under the contract during that period.

Record Club of America, Inc. v. United Artists Records, Inc., Case No. 89-7039 (2nd Cir. 1989) [ELR 11:8:16]

Record producer may proceed with claims against distributor alleging breach of contract and tortious interference with contract, but fraud claim is dismissed

In March 1987, certain parties identified only as "Ahee" by a New York trial court entered a contract with Select Records. Ahee agreed to produce records for a rap group known as "Kid In Play." Select agreed to market and distribute the recordings. Ahee also granted ownership and partial merchandising rights of the artists to Select in exchange for the right to an eleven percent royalty interest of net sales, and the right to an executive

producer credit on all of the artists' recordings under the contract.

Several months later, Ahee entered into a new contract with Select; Ahee sought to assign the rights under the Select contract to a company known as Noise, in return for which Noise was to pay Ahee two percent of royalties for all records sold under the Select contract, up until that contract expired in February 1991, and to credit Ahee as executive producer on records recorded through that date.

Subsequently, in March 1988, "Kid 'n Play" agreed to terminate Noise's production responsibilities upon the completion of an album called "2 Hype."

A lawsuit brought by Ahee claimed that the first two singles recorded by the artists did not contain the agreed-upon executive producer credit and that Ahee did not receive any royalties.

It appeared to Judge Davis that the failure to provide Ahee with the required credit, "a very important consideration, and for which [Ahee] specifically bargained," breached a material element of Ahee's contract with Select. The court rejected Select's argument characterizing Ahee's claim as merely seeking "reputational damages," or as being too speculative to provide a basis for recovery in a breach of contract action. Judge Davis pointed out that dismissing Ahee's claim for damages because such damages might be for an uncertain amount "would in effect allow [Select] to escape liability for the probable breaching of an element of the contract."

In turning to Ahee's claim of fraud, the court found that the requisite elements of the cause of action were not established . The misrepresentations alleged by Ahee appeared to the court to be breaches of Select's contractual obligations.

Ahee proposed to add a third cause of action alleging that Select intentionally interfered with Ahee's contractual relationship under the Noise contract by inducing Noise to revise, i.e., terminate, its contract with the artists.

Judge Davis observed that there was no clause in the March 1988 termination contract between Noise and the artists stating who would be responsible for paying, or causing to pay, royalties due Ahee. Ahee's right to receive two percent of the royalties of "Kid 'n Play" records was effectively ended after the one record produced by Noise; the termination contract thus may have damaged Ahee's rights, stated the court, and Ahee was entitled to add a cause of action alleging tortious interference with contract.

Ahee v. Select Records, New York Law Journal, p.21, col. 5 (N.Y.Cnty., Sept. 29, 1989) [ELR 11:8:17]

Briefly Noted:

Tax.

The Internal Revenue Service has announced that non-resident alien entertainers and athletes who are subject to income tax withholding due to performances in the United States can request central withholding agreements and qualify for a reduced withholding rate. Individuals must submit requests in advance for the central withholding agreements, and must comply with specified procedures including providing an itinerary and proposed budget for the performances, and identifying a central withholding agent.

Internal Revenue Service, Rev. Proc. 89-47, 1989-33 IRB 29 [ELR 11:8:18]

Auto Speedway Injury.

During an auto racing event at Brewerton Speedway, a jagged, baseball-sized stone was propelled by a race car's tire over a chain link fence; the stone struck spectator Richard Cortwright in the knee. Cortwright had chosen to sit in the top row of the bleachers, just above the top of a fence that separated the grandstand from the racetrack. Judgment was entered on a jury verdict finding that the speedway owner was not negligent, but a New York appellate court has reversed the judgment and granted a new trial to Cortwright. The court stated that the duty owed to a patron by an owner of an auto speedway is not the same as that owed by an owner to a

patron of a baseball game. Flying debris from a race-track is "not an expected occurrence," and there is no one location around a track that is safer than another, stated the court, observing that it was for this reason that a wall and fence were erected along the entire length of the grandstand. The court also noted that the danger of a stone flying from the track is a constant threat during a race, and the proximity of the seating to the track in the instant case provided little time to react to avoid being struck. The duty of the speedway owner was "to provide adequate protection to all the customers seated in the grandstand, rather than only those seated in areas of greatest danger. It will remain for a jury to decide under general common law negligence principles the question of whether the owner provided a "reasonably safe condition" under all circumstances "without strict delineation between areas of lesser and greater danger."

Cortwright v. Brewerton International Speedway, Inc., 539 N.Y.S.2d 599 (N.Y.App. 1989) [ELR 11:8:18]

Auto Speedway Injury.

A Federal Court of Appeals in Missouri has affirmed a District Court decision granting summary judgment to the owner of the St. Charles Speedway and to a racing event promoter in an action brought by race car owner Norman Haines. Haines was injured when struck in the infield of the racetrack by his own race car while attempting to have it started before an event. The court upheld the validity of the release form signed by Haines, stating that the release was not overbroad and that Haines, who had been involved in racing since 1952, "doubtlessly knew that the sport placed risks on both participants and spectators."

Haines v. St. Charles Speedway, Inc., 874 F.2d 572 (8th Cir. 1989) [ELR 11:8:18]

Billy Joel/Elizabeth Weber Case.

In the ongoing property dispute between performer Billy Joel and his former wife and former manager Elizabeth Weber (see ELR 10:12:11), a New York trial court has permitted Weber to amend her $7 million counterclaim. Weber sought to pierce the corporate veil of Frank Management, Inc., Joel's manager, and hold her brother Frank Weber personally liable for the actions of the corporation on the ground that the corporation lacked a separate existence. Weber alleged that Frank Weber, the president of Frank Management, not only controlled the corporation, but disregarded

corporate formalities, commingled funds of the corporation with his own, and employed the corporation "as a vehicle for his own personal purposes." The court noted that there was some evidence supporting these charges in Frank Weber's deposition, and that Elizabeth Weber, in all, sufficiently stated a claim for piercing the corporate veil. It will remain for a trier of fact to determine, among other issues, whether Elizabeth Weber failed to pay for management and consulting services, and whether Frank Management and Frank Weber met their contractual obligations.

Frank Management, Inc. v. Weber, New York Law Journal, p. 22, col. 1 (N.Y. Cnty., Oct. 3, 1989) [ELR 11:8:18]

Trademark Infringement/"Watchimal."

A Federal District Court in Texas has granted summary judgment to Hasbro, Inc. in an action brought by Patricia Hagaman alleging that Hasbro's plush animal wrist watch known as "Watchimal" infringed Hagaman's trademark rights in "Wristimal," a small stuffed animal with a timepiece attached, which is worn around the wrist like a watch. The court first found that the Lanham Act was not applicable because Hagaman never registered her trademark. And Hagaman, who produced only two prototypes of the "Wristimal," would not be able to establish priority of use under Texas trademark law, concluded the court for the trademark was not used in a way "sufficiently public to identify or distinguish the marked goods."

Hagaman v. Hasbro, Inc., 710 F.Supp. 1119 (S.D.Tex. 1989) [ELR 11:8:18]

IN THE NEWS

Warner Bros. and Sony Corp. resolve dispute over Sony's hiring of producers Peter Guber and Jon Peters

Sony Corp. and Warner Bros. have settled a dispute involving the services of producers Peter Guber and Jon Peters.

Warner, in return for receiving several hundred million dollars worth of assets from Sony, will release Guber and Peters from an exclusive production contract; Sony plans to hire the producers to be the chief executive officers of Columbia Pictures Entertainment Inc. According

to news reports, Warner will become a joint owner of Sony's mail order record club, a subsidiary of CBS Records; Sony also will provide Warner with basic cable television distribution rights to Columbia's feature and television films.

The settlement of Warner's $1 billion lawsuit also provides Warner with Columbia's thirty-five percent share of the Burbank Studios in exchange for the Warner-owned former MGM lot in Culver City. And Warner will retain the rights to about fifty film projects developed by Guber and Peters, including "Bonfire of the Vanities" and the sequels to "Batman." [Jan. 1990] [ELR 11:8:19]

Beatles settle lawsuits against record companies

George Harrison, Paul McCartney, Ringo Starr, Yoko Ono Lennon and Apple Records have settled their outstanding lawsuits against EMI Records and Capitol Records. The parties agreed not to comment on the settlement of the Beatle parties' claims concerning royalty payments, the use of the recording "Revolution" in an athletic shoe commercial, and other issues. [Jan. 1990] [ELR 11:8:19]

Copyright Royalty Tribunal increases mechanical royalty rate

The Copyright Royalty Tribunal has announced that the mechanical royalty rate will increase to 5.7 cents, or 1.1 cents per minute of playing time, whichever is larger. The 8.7 percent increase, effective as of January 1, 1990, reflects a rise in the cost of living, as

determined by changes in the consumer price index between September 1987 and September 1989. Mechanical royalties are paid for performances of a work on record or tape. [Jan. 1990] [ELR 11:8:19]

Federal Communications Commission imposes fines on four radio stations accused of broadcasting indecent material

Los Angeles radio station KFI-AM has paid a $6,000 fine imposed by the Federal Communications Commission, although, according to news reports, the station still denies the Commission's charges of broadcasting indecent material.

The Commission found that KFI aired the allegedly indecent material during three programs presented by afternoon talk show host Tom Leykis; the remarks in

issue, according to Leykis, were made by callers to the shows.

Three other radio stations also were fined for various alleged instances of broadcasting indecent programming in the daytime - a $10,000 fine was imposed on WIOD, Miami, and fines of $2,000 each were imposed on WZTA-AM, Miami and on KLUC-FM, Las Vegas.

Four other stations, including WXRK-FM, New York; KCCL-AM/FM, Paris, Arkansas; WWWE-AM, Cleveland; and KSD-FM, St. Louis, were given thirty days to respond to complaints that they had broadcast indecent material. The Commission then will decide whether violations occurred and whether to impose sanctions. [Jan. 1990] [ELR 11:8:19]

Screen Actors Guild approves contract with producers covering programming for basic cable

The Screen Actors Guild and three production companies have entered a contract covering television movies and other longform works made directly for basic cable.

In approving the first contract covering such works, the Guild's national board of directors offered Paramount Pictures, Turner Network Television and Universal Studios the terms and conditions, with certain exceptions, contained in the Guild's 1989 television agreement, insofar as those terms and conditions apply to dramatic programs produced for first run syndication. One of the exceptions is a new residuals formula, based on the actors' total applicable minimum salaries, with percentages ranging from twelve percent for the second run, down to one percent for the thirteenth and each subsequent run.

According to news reports, the contract also provides that no residuals will be due actors from the "first sale" of programming to Canada; that actors who earn double scale may agree to an advance payment for reruns, subject to individual negotiations; and, under a favored- nations clause, that any increases in residuals compensation gained by the Directors Guild of America in its negotiations next year for a basic cable contract will apply to the Screen Actors Guild as well. [Jan. 1990] [ELR 11:8:19]

Actors' Equity Association and League of American Theaters and Producers agree to salary increase and disability leave in new three year contract

Actors Equity Association and the League of American Theaters and Producers have agreed to the major provisions of a new three year contract.

The contract, which is subject to ratification by Actors' Equity's Council, includes a fifteen percent pay increase over the term of the contract, which will bring the minimum salary for an actor up to $900 per week by 1991. Producer contributions to a health insurance plan will increase, but only by a minimal amount. However, for the first time, actors will be entitled to disability leave under a provision allowing an actor to return to a show within a year of leaving for disability, which also includes pregnancy.

The contract, covering actors and stage managers on Broadway, national tours, and bus and truck tours, will be in effect through June 1992. [Jan. 1990] [ELR 11:8:20]

Federal District Court jury in Florida upholds Twentieth Century Fox's exclusive agreement with exhibitor

An exclusive exhibition agreement between Twentieth Century Fox Film Corp. and Wometco Theaters did not constitute an illegal clearance, a Federal District Court jury in Miami has concluded. The jury, according to news reports, rejected a claim by Royal Park Cinema in deciding that Fox was entitled to enter the exclusive exhibition agreement with Wometco, Royal Park's competitor in the Gainsville market. [Jan. 1990] [ELR 11:8:20]

Postproduction company is a "joint employer" along with two union signatories, rules arbitrator

An arbitrator has ruled that Catalina Post, a nonunion postproduction company, was a "joint employer," along with two postproduction companies signatory to Sound Local 695 and its parent union, the International Alliance of Theatrical Stage Employees. Catalina will be required to terminate its nonunion workers, and replace those workers with union members.

The arbitrator, Louis Zigman, found, according to news reports, that one individual, Bill Oliver, was the chief operating officer of each company; that the three companies had many officers in common; that several of the officers were related to one another; and that the companies shared some physical facilities, as well as payroll and administrative functions.

The arbitrator also ordered the Sound Department, one of the signatory companies, to pay almost $80,000 in wages and benefits to a union employee who allegedly was underpaid during a two year period.

Oliver has questioned the accuracy of most of the arbitrator's findings, acknowledging only that Oliver was the chief operating officer of all three companies and that the Sound Department had helped secure loans for Catalina Post. [Jan. 1990] [ELR 11:8:20]

DEPARTMENTS

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