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FEATURES

22 Star Power
BY BRADFORD S. COHEN AND KYLE R. NEAL
Celebrities can choose from among a variety of vehicles, including private foundations and donor-advised funds, to realize their philanthropic goals

29 More or Less
BY LEE S. BRENNER AND SARAH L. CRONIN
In copyright infringement analyses only an original work’s protectible elements should be included

Plus: Earn MCLE credit. MCLE Test No. 203 appears on page 31.

36 The Red and the Black
BY ROMAN M. SILBERFELD AND BERNICE CONN
Media consolidations since the repeal of the Fin-Syn rules have heated the controversy over profit participation agreements

DEPARTMENTS

8 Barristers Tips
If you have to ask if it’s insider trading, it probably is
BY PATRICK HUNNIUS

9 Practice Tips
The Comcast case and the fight for Net neutrality
BY PATRIC M. VERRONE

14 Practice Tips
Requirements for finding a joint work under the Copyright Act
BY CHRISTOPHER RITTER

17 Practice Tips
Defining liability for likeness of athlete avatars in video games
BY JAMES J. S. HOLMES AND KANIKA D. CORLEY

44 Closing Argument
Is a ZIP code really personal identification information?
BY SCOTT BARLOW

42 Classifieds

43 CLE Preview
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Mr. Gleitman has practiced sophisticated estate planning for 26 years, specializing for more than 14 years in offshore asset protection planning. He has had and continues to receive many referrals from major law firms and the Big Four. He has submitted 52 estate planning issues to the IRS for private letter ruling requests; the IRS has granted him favorable rulings on all 52 requests. Twenty-three of those rulings were on sophisticated asset protection planning strategies.

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runaway production is not a new issue in California. *Los Angeles Lawyer* has published articles on this topic in previous Entertainment Law special issues. For many years various groups urged the California Legislature to enact tax incentives in an effort to stem runaway production. In February 2009, the legislature adopted its first film and television tax incentive program. Administered by the California Film Commission, the program provides for up to $500 million in production tax incentives to be allocated from July 1, 2009, through June 30, 2014. In theory, the program provides $100 million in tax incentives each year for five years.

California’s tax incentive program differs from the programs in many other states. The program contains significant limitations on the types of expenditures that qualify for incentives. For example, almost all above-the-line expenditures for a film or television project do not qualify. Moreover, the production budget maximum for motion pictures is $75 million. As a result, a significant portion of the overall costs of a production does not qualify for any of the incentives—including costs for actors, directors, and producers. In addition, films with an extremely high budget do not qualify at all. Film and television projects produced in other U.S. jurisdictions qualify for far greater tax incentives than those produced in California.

The California program is based on a first-come-first-served application process, which often is referred to as a lottery. Starting at 9 A.M. each June 1, the California Film Commission accepts applications for its pool of tax incentives for the next fiscal year. The applications are numbered and prioritized based upon the date received. The commission allocates the tax incentives for the fiscal year by the numbers assigned to the applications until the full allocation for that year has been exhausted.

The effect of this process is that it encourages, or even requires, producers who have projects not ready for production to apply for the tax incentives on June 1 each year. Not surprisingly, many of the productions that have been allocated tax incentives were never produced, and the incentives were not reissued. (Although the commission may carry over the unused tax incentives into the following year, the likely result is that after five years a significant portion of the $500 million will not be used.)

Although California’s program is a step in the right direction, it should be modified and expanded. If the legislature believes that production tax incentives are a benefit to California taxpayers, which appears to be the case, it should enact a program that simplifies the application and approval process and expands the expenditures and productions that qualify for incentives. A good next move by the legislature would involve eliminating the lottery application process, including some portion of the above-the-line costs as qualifying expenditures, and eliminating or significantly increasing the budget maximums for projects seeking to qualify for the program.

The entertainment industry wants to produce more of its projects within California. Tax incentives play a major, if not primary, role in determining the location for productions. California cannot afford to continue with a tax incentive program that is not competitive with those offered in other jurisdictions.

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If You Have to Ask If It’s Insider Trading, It Probably Is

A FEW YEARS AGO, A COLLEAGUE who knew I used to be an enforcement attorney with the SEC asked for my opinion on whether he could legally trade on information he gained about Company A during his representation of Company B. I remember that the story about how he had come to learn what he knew about Company A was somewhat complicated and that my short answer was that were he to trade on the information, it would not clearly be a violation of the federal insider trading regulations. At the same time, I thought that it was also not clear that he would not be committing insider trading.

That lack of clarity can have consequences. If he were to trade on the information—and if his trade were to come to the attention of the SEC—he and his firm could be facing months of investigation, testimony, document requests, and other intrusions. Rather than list all the pros (minimal) and cons (severe), however, I simply told him that it is probably safer to assume that any scenario that leads a person to ask a lawyer if an act qualifies as insider trading is probably close enough to insider trading that the best course would simply be to not make the trade.

If that conversation with my colleague happened today, I would likely cut off his narrative a lot sooner, tell him unequivocally that what he was thinking about was a bad idea (and potential career suicide), and head back to my office to memorialize my advice to him (to present to the SEC or other relevant regulator should one come calling).

Recent enforcement actions by the SEC and the U.S. Department of Justice confirm that the U.S. government is reemphasizing prosecutions of insider trading and of individuals in gatekeeper positions, including attorneys and accountants. In the Galleon insider trading matter, for example, the SEC has charged at least 27 defendants.1 This new wave of insider trading prosecutions shows no signs of abating. According to Robert Khuzami, the SEC’s director of enforcement, “Prosecutors will continue using undercover techniques including informants and front businesses to attract wrongdoing and wiretaps to ‘ferret out’ misconduct.”2

In one case, at least four associates from major firms (including two prosecuted in connection with the Galleon case) have pleaded guilty to felonies stemming from insider trading. One of these associates was described by his criminal defense lawyer as “a star tax lawyer,” the ‘person other associates went to for help, and ‘a sure thing for partner.”3 Instead, he was disbarred upon being sentenced to nine months in a halfway house. In a second case, an associate allegedly bought 10,000 shares of her client’s stock 15 minutes after the client asked her to draft a letter of intent regarding a potential merger.4 She not only traded on information she received in confidence from a client but also lied to SEC attorneys about it. This conduct exposed her to a five-year prison sentence. When she sold her shares, she “realized a gain of approximately $5,800.”5

In addition, two partners of Big Four accounting firms have recently been charged with insider trading. One allegedly “committed insider trading on nine occasions between 2005 and 2008 by trading in the securities of multiple [firm] clients.” He settled the case without admitting or denying the SEC’s allegations and agreeing to pay more than $1.1 million. In addition, he consented to the entry of an order denying him “the privilege of appearing or practicing before the SEC as an accountant.” This was essentially a death knell for his professional career as an accountant.6 Another Big Four partner is alleged to have, with his wife’s assistance, tipped family members regarding at least seven acquisitions planned by clients of his firm and to have netted millions of dollars from the tips.7

The government’s pursuit of gatekeepers is not limited to insider trading. For example, the SEC recently brought an action against a Los Angeles-based partner of a major firm.8 The SEC alleges that this attorney altered documents requested by the SEC in conjunction with an examination. In 2009, the SEC obtained an order permanently barring a securities lawyer from practicing before it based on allegations that the attorney attempted to influence an SEC administrative proceeding. Specifically, the attorney—who represented a witness in the proceeding, which was brought by the SEC against the witness’s former employer—allegedly contacted counsel for the witness’s employer and “offered to have his client act in ways that would thwart the Commission’s prosecutorial activities in exchange for benefits for his client.” After a hearing, an administrative law judge concluded, “By seeking benefits for a client in exchange for behavior and/or testimony by the client that would adversely impact a Commission administrative proceeding, [the attorney] engaged in conduct that involved dishonesty, fraud, deceit, and misrepresentation.”9

The SEC “has long recognized that many securities law violations could not occur without the participation of lawyers.”10 The commission is acting on that recognition with renewed fervor.


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ROBB TOPOLSKI IS A FAN OF BARBERSHOP QUARTETS. In February 2007, the Oregon engineer, while on disability leave from Intel, tried to upload public domain, Tin Pan Alley-era barbershop harmonies using peer-to-peer file sharing. His anemia was surpassed by the anemic pace at which the files were being exchanged. After weeks of technical experimentation, he discovered that his Internet service provider, Comcast, was interfering with his transmissions. Topolski posted his findings on DSL Reports, a “bulletin board service shared by broadband enthusiasts.” His post incited indignant discussion among enthusiasts but no response from Comcast.

Over the next several months, the Associated Press did similar tests of Comcast’s broadband network, trying to perform peer-to-peer file sharing of the King James Bible. On October 19, 2007, correspondent Peter Svensson reported that Comcast was interfering with high-speed Internet traffic to provide preferential treatment to fee-based data or data that Comcast owned or controlled. In response, Comcast stated only that its network management practices required keeping “[n]et connections running smoothly.”

Two nonprofit advocacy organizations—Free Press and Public Knowledge—along with a consortium of public interest groups and law professors filed a complaint with the Federal Communications Commission. The complaint asked for a declaratory ruling that Comcast was in violation of the FCC’s 2005 Internet Policy Statement. That policy statement had adopted principles prohibiting practices that interfered with lawful consumer Internet access.

After a period of public comment, the FCC issued an order on August 1, 2008, finding that Comcast’s bandwidth management methods contravened federal policy by “significantly impeding consumers’ ability to access the content and use the applications of their choice.” By the time the order was issued, Comcast had adopted new management methods. As a result, the order effectively required only that Comcast disclose the details of those new methods and their implementation. Comcast agreed to comply with the order but also filed for review in the D.C. Circuit of the U.S. Court of Appeals, claiming (among other things) that the FCC did not have jurisdiction over its network management methods.

In an April 2010 opinion that sent shockwaves through the Internet broadband industry and policy communities (not to mention the blogosphere and the FCC), the court vacated the FCC’s order. The court held that the FCC had no authority over Comcast’s Internet service because “the Commission had failed to tie its assertion of ancillary authority over Comcast’s Internet service to any ‘statutorily mandated responsibility.”

Comcast Corporation v. Federal Communications Commission is an important case in the struggle between federal government regulators and policy communities (not to mention the blogosphere and the FCC), the court vacated the FCC’s order. The court held that the FCC had no authority over Comcast’s Internet service because “the Commission had failed to tie its assertion of ancillary authority over Comcast’s Internet service to any ‘statutorily mandated responsibility.’”

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ers have come to be known as the “ancillary authority” of the FCC.

Alternatively, the FCC’s “express authority” has been limited to “wire and radio communication services” specifically provided for under Title II (Common Carriers) and Title III (Provisions Relating to Radio). Over the years, these two titles were expanded to apply Title II “common carrier” jurisdiction to all telecommunications services delivered through landline wired telephony and Title III radio authority to broadcast television and cellular telephones.

Before cable television came under express FCC authority through the 1984 enactment of Title VI, which covers cable communications, three U.S. Supreme Court opinions considered the FCC’s Title I ancillary authority over what was then called community antenna television (CATV). In two of the three cases, the Court held that the FCC did have authority to control specific cable company practices when it was “reasonably ancillary to the effective performance of its various responsibilities for the regulation of television broadcasting.”

The CATV cases would have created a reasonable precedent for FCC ancillary authority over broadband Internet service but for an action taken by the FCC in 1980. In developing rules to regulate data-processing services offered through telephone lines, the FCC drew a distinction between “basic” and “enhanced” services. “Basic services” were those services that involved no computer processing and were to be regulated as Title II common carrier telephone services. Alternatively, “enhanced services” (which required “computer processing applications for transmission”) were exempted from Title II jurisdiction for the stated purpose of not inhibiting a “fast-moving, competitive marketplace.” This classification distinction was codified in the 1996 Telecommunications Act under two new names. Basic services became “telecommunication services.” These were designated “pure” or “transparent” transmissions between users, unaltered by computer applications. These basic services were subject to Title II common carrier regulations. “Information services” took the place of enhanced services and included transformed or processed transmissions, outside the Title II purview.

The FCC applied the information service classification to Internet service providers (thus exempting them from Title II authority) in 1998. In its so-called Stevens Report, the FCC evaluated typical dial-up ISPs of the day (America Online, Earthlink, Microsoft Network, etc.) for the purposes of deciding whether to require them to contribute to the Universal Service Fund and held that they were merely information services because the ISPs did not own telecom facilities. Four years later, the FCC applied the same classification to suppliers of broadband Internet access through cable transmission in its 2002 Cable modem Order. There, the FCC held that cable Internet providers (like the ISPs of the Stevens Report) did not offer “telecommunications services to the end user, but rather…merely use[ ] telecommunications to provide end users with cable modem service.” This ruling was substantially vacated by the Ninth Circuit when it held that the FCC could not exempt cable companies from Title II common carrier coverage. However, in National Cable & Telecommunications Associates v. Brand X Internet Services the U.S. Supreme Court reversed the lower court and reinstated the ruling.

The Brand X Court held that the FCC’s classification of cable broadband Internet providers as information services was a reasonable construction of the Communications Act under its test for evaluating agency actions. The test consists of interpreting the Administrative Procedures Act and Chevron U.S.A. Inc. v. Natural Resources Defense Council, Inc. The Court’s opinion relied on the act’s use of the phrase “offering of telecommunications” in its definition of “telecommunications service” to have been reasonably interpreted by the FCC to exclude broadband Internet service providers who “offer telecommunications” as a means to deliver Internet access, but not as a standalone service.

The Brand X Decision

Brand X includes a colorful dissent by Justice Antonin Scalia (joined by Justices David Souter and Ruth Bader Ginsburg) that opines that the only reasonable interpretation of the act requires the FCC to classify cable Internet providers under Title II as common carriers. The dissent drew analogies to pizza delivery, car dealerships, and pet shops; criticized the “Möbius-strip reasoning” by the FCC; and concluded by expressing “sadness that the Court should go so far out of its way to make bad law.”

While the Brand X Court held that the FCC’s classification decision “was a reasonable policy choice” under Chevron U.S.A., it also stated that “the Commission remains free to impose special regulatory duties on facilities-based ISPs under its Title I ancillary jurisdiction.” Citing that language, less than two months after Brand X was published, the FCC issued its September 2005 Internet Policy Statement, asserting that it held the “jurisdiction necessary to ensure that providers of telecommunications for Internet access…services are operated in a neutral manner.”

This was the FCC’s most provocative pronouncement on net neutrality and contained four principles that would guide its policy. The statement declared that “to encourage broadband deployment and preserve and promote the open and interconnected nature of the public Internet, consumers are entitled to access the lawful Internet content of their choice,….run applications and use services of their choice,….and connect their choice of legal devices that do not harm the network.” The policy statement goes on to assert that consumers are entitled to “competition among network providers, application and service providers, and content providers.”

Broadband cable Internet providers largely followed these principles, although there were still isolated examples of interference. Then, with the development of filtering technologies like deep packet inspection, concern built that ISPs could secretly and consistently review, speed up, slow down, and even block Internet communications. As a result, the FCC considered rules to enforce net neutrality principles under its Title I ancillary authority.

Before the rules were promulgated, however, Topoloski uncovered Comcast’s interference, and Free Press and Public Knowledge filed a complaint with the FCC, which ordered Comcast to disclose its amended methods. Comcast asked the D.C. Circuit Court of Appeals to review the order, which the court vacated, taking with it the FCC’s authority to enforce net neutrality under Title I.

In Comcast, the FCC admitted that it had no express authority over ISPs because of its previous classification of them outside of its Title II common carrier designation. Instead, the FCC argued that it could bar Comcast from interfering with its customers’ use of peer-to-peer networking applications through ancillary authority under Title I. Such authority, the FCC asserted, met the test created in 2005 by the D.C. Circuit Court in American Library Association v. FCC. That test was a “distillation” of the three Supreme Court opinions from the CATV era. It stated that the FCC “may exercise ancillary jurisdiction only when two conditions are satisfied: (1) the Commission’s general jurisdictional grant under Title I covers the regulated subject, and (2) the regulations are reasonably ancillary to the Commission’s effective performance of its statutorily mandated responsibilities.” Comcast stipulated that the FCC met the first condition of the test, so the court only had to decide if it met the second. The court found that it did not.

The Comcast court rejected the FCC’s reliance on the language in two sections of the Communications Act, holding that they were merely statements of Congressional policy (as distinguished from mandated responsibilities) and five other sections that, though
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arguably delegations of authority, were found by the court not to be delegations of the kind of authority the FCC was trying to exercise over Comcast’s network management practices. Not finding a legislative hook on which to hang its ancillary authority hat, the FCC also made a judicial estoppel argument (based on a Comcast admission in a prior California lawsuit that the FCC had subject matter jurisdiction over Comcast’s network management practices) and invoked Brand X dicta to assert that it had Title I ancillary authority over ISPs. The Comcast court discounted both arguments by stating that the FCC may indeed have some ancillary authority (and subject matter jurisdiction) over cable Internet providers, just not the kind the FCC attempted to enforce against Comcast.

**Comcast and Net Neutrality**

The Comcast decision was a crushing blow to the FCC, its enforcement of net neutrality rules, and its larger agenda to expand broadband access throughout America. Its Joint Statement on Broadband had been released only days before the opinion was issued. Most observers presumed that the FCC had two options to pursue while petitioning Congress to codify more direct authority. One was to continue to rely on ancillary authority to govern precise aspects of ISP behavior. The other was to reclassify cable Internet providers as Title II telecommunication services and claim jurisdiction over them as common carriers. Instead, less than a month after the Comcast decision was handed down, the FCC advocated for what it called the third way, which would only reclassify the “retransmission component” of broadband providers’ service under Title II and, even then, forbear from applying all but six of the sections of that title. The legal foundation for the approach relied heavily on Justice Scalia’s dissent (as well as the majority opinion) in Brand X to give the FCC its reclassification authority.

While the FCC again invited public comment, concerns about a court challenge to whatever authority the FCC might exercise led to calls for legislation. Such efforts had been in the works for years but the process always broke down along party lines, with Republicans favoring the cable industry’s desire for limited regulation in the interest of encouraging innovation, and Democrats siding with public interest organizations, unions, and consumer advocates pushing for codified FCC authority to regulate. Opponents of greater FCC powers characterized net neutrality rules as a “government takeover of the Internet,” which proponents consider tantamount to characterizing speed limits, traffic lights, and a highway patrol as a government takeover of Route 66. Longtime Los Angeles Congressman Henry Waxman came close to achieving bipartisan support for a bill in the weeks before the November 2010 midterm Congressional elections, but the process derailed when stakeholders on both sides of the issue withheld their support.

On December 21, 2010, the FCC voted 3-2 (along political party lines) to promulgate net neutrality rules. Two days later, it issued a report and order titled “In the Matter of Preserving the Open Internet Broadband Industry Practices.” According to the report and order, “To preserve the Internet’s openness and broadband providers’ ability to manage and expand their networks, we adopt high-level rules embodying four core principles: transparency, no blocking, no unreasonable discrimination, and reasonable network management.”

The FCC was especially mindful of the potential for litigation. Part IV of the report and order is devoted to the FCC’s authority to adopt open Internet rules. The report and order does not use the term “third way” and relies very little on Brand X dicta. Still, it declares to reclassify broadband as a Title II telecommunications service and, instead, bases FCC authority on specific sections of Titles II, III, and IV (forbearings others) as well as on Section 706 of the 1996 Telecommunications Act. This latter section, in which Congress authorized the FCC to “encourage the deployment…of advanced telecommunications capability,” receives the most attention. The report and order may be read as a direct response to the Comcast opinion, citing or referring to the case many times.

The report and order was met with immediate criticism from both sides of the net neutrality debate. The only thing about which the analysts agreed was that a court challenge seemed inevitable. That prediction proved accurate in 2011 when Verizon filed a lawsuit that sought to abolish the rules. Two facts about the case are noteworthy. First, the rules that Verizon sought to overturn were nearly identical to ones it had supported a few months earlier following negotiations with the FCC. Second, just two days before, the FCC had voted to approve a merger between Comcast and NBC-Universal, subject to a list of conditions that included adherence to the net neutrality rules it had just promulgated. Verizon’s suit (which was followed by a similar one by Metro PCS) relied heavily on Comcast not only for its legal theory but also its forum. Verizon filed the case in the D.C. Circuit and requested that it be heard by the same three-judge panel that issued the Comcast ruling. Although the court quickly rejected the latter request and may even reject the appeals outright on procedural grounds (as moved for by the FCC), it is clear that Comcast will continue to play a large role in litigation to come.

The FCC has a stated mandate to be the policing authority over communications in the United States. FCC chairs of both political parties have tried to enforce net neutrality over the evolving broadband Internet delivery system and will likely continue to do so as part of that mandate. The 2010 Open Internet rules are yet another step in that direction.

There is also a parallel history of evolving but powerful industries pushing back. No matter what the FCC does, there will be legal wrangling. It is hard to imagine that anything will be resolved other than through court opinions—even with industrial consent decrees, settlements, or even legislation. What does not always exist are vigilant public interest spokespersons and consumer advocates playing a proactive role. But with the stakes as high as Topolksi’s freedom to share barbershop harmonies, the Internet age may be different than the past, and the fight for net neutrality will continue.

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5 Id.
9 Id. at 13,059-60.
10 Comcast also claimed that the FCC’s adjudicatory procedure circumvented the rule-making process requirements of the Administrative Procedures Act and violated due process, and that the order was arbitrary and capricious. The court only ruled on the jurisdictional challenge. Comcast Corp. v. FCC, 600 F. 3d 642, 645 (2010).
11 Id. at 661.
12 Id. at 642.
13 In the Matter of Preserving the Open Internet Broadband Industry Practices, FCC 10-201 (Dec. 23, 2010).
14 47 U.S.C. §§151 et seq.
15 Id.
18 47 U.S.C. §§301-399B.
19 Comcast Corp. v. FCC, 600 F. 3d 642, 644 (2010).

22 Southwestern Cable Co., 392 U.S. at 178 (finding ancillary authority for the FCC to limit a cable company’s retransmission range). In Midwest Video I, the Court found ancillary authority to allow the FCC to require cable companies to create new programming. Midwest Video II, 406 U.S. at 670. But in Midwest II, the Court denied the FCC’s assertion of ancillary authority to require cable companies to make certain channels available for public use. Midwest Video II, 440 U.S. at 708-09.

23 In re Amendment of Section 64.702 of the Commission’s Rules and Regulations (Second Computer Inquiry), 77 F.C.C. 2d 384, 417-23 (1980). 24 “The term ‘telecommunications service’ means the offering of telecommunications for a fee directly to the public, or to such classes of users as to be effectively available directly to the public, regardless of the facilities used.” 47 U.S.C. §153(46).

25 “The term ‘information service’ means the offering of a capability for generating, acquiring, storing, transforming, processing, retrieving, utilizing, or making available information via telecommunications, and includes electronic publishing, but does not include any use of any such capability for the management, control, or operation of a telecommunications system or the management of a telecommunications service.” 47 U.S.C. §153(20).


27 In re Inquiry Concerning High-Speed Access to the Internet over Cable and Other Facilities, 17 F.C.C.R. 4798 (2002).

28 Id. at 4824.

29 Brand X Internet Servs. v. FCC, 345 F. 3d 1120 (9th Cir. 2003).


32 Brand X Internet Servs., 545 U.S. at 988-89.

33 Id. at 1020.

34 Id. at 996.

35 In the Matters of Appropriate Framework for Broadband Access to the Internet over Wireline Facilities et al., FCC 05-151 (Sept. 23, 2005).

36 Id. at 3.

37 Examples include alleged blocking of e-mails by AOL in 2006, AT&T’s censorship of lyrics critical of President George W. Bush made by Eddie Vedder during an August 2007 Pearl Jam concert, and Verizon Wireless’s denial of access to a text-messaging program by NARAL in late 2007. American Civil Liberties Union, Network Neutrality 101: Why the Government Must Act to Preserve the Free and Open Internet, at 9-11 (Oct. 19, 2010).

38 Two additional principles were presented in 2009 as part of a Notice of Proposed Rulemaking: 1) Broadband providers cannot discriminate against particular Internet content or applications, and 2) providers must be transparent about their network management practices. In re Preserving the Open Internet; Broadband Industry Practices, 24 F.C.C.R. 13064 (2009).


40 Id. at 691-92.

41 Comcast Corp. v. FCC, 600 F. 3d 642, 651-52 (1010). See also 47 U.S.C. §230(b), Protection for private blocking and screening of offensive material, and §1, mission statement.

42 Id. at 658-61. See also 47 U.S.C. §706 (deployment of advanced services), §256 (oversight of coordinated network planning), §257 (identifying and eliminating...market entry barriers), §201 (just and reasonable common carrier regulations), and §623 (cable rates).

43 Comcast Corp., 600 F. 3d at 647-51.


45 Christopher S. Yoo, Broadband for America, at 9, available at http://www.broadbandforamerica.com/sites/default/themes/broadband/reclass_broadband.pdf. This is the option generally favored by the cable broadband industry, as it gives the FCC the least explicit power and allows for greater influence on legislation through its political lobbying efforts.

46 A thorough discussion of the legality of this approach can be found in Lee L. Selwyn & Helen E. Golding, The Comcast Decision and the Case for Reclassification and Re-Regulation of Broadband Internet Access as a Title II Telecommunications Service, ICARUS (ABA, Fall 2010).


48 Genachowski, supra note 47, at 5.

49 Schlick, supra note 47, at 6-7.

50 The phrase was attributed to Speaker of the House John Boehner in Tony Romm, Boehner Slams FCC for “Takeover of Internet,” The Hill, May 6, 2010.


52 In the Matter of Preserving the Open Internet Broadband Industry Practices, FCC 10-201 (Dec. 23, 2010).

53 Id. at 27.

54 Id. at 62-82.

55 Id. at 68-76.

56 Id. at 62-68.

57 The FCC had raised 47 U.S.C. §706 in its argument before the Comcast court, and the court devoted a segment of its opinion to dismissing that portion of the argument. Comcast Corp. v. FCC, 600 F. 3d 642, 658-59 (2010).


60 Verizon v. FCC, No. 11-1014, D.C. Court of Appeals, filed Jan. 20, 2011.


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Los Angeles Lawyer May 2011
Requirements for Finding a Joint Work under the Copyright Act

COLLABORATORS OFTEN FIND THEMSELVES at odds over whether each of them has the right to exploit the work they have created together, or whether that right belongs only to one of them. Collaboration is common in many industries and is a driving force in the field of entertainment. The production of motion pictures, music videos, plays, musical recordings, and other artistic endeavors involves the creative contributions of many people. Before they begin their efforts, wise collaborators will take the precaution to state clearly in a signed written agreement whether they intend to be coauthors of the finished work and to account for who will own the copyright. In the absence of an agreement, a dispute over who owns the copyright is likely to follow.

Resolution of the dispute often depends on whether the work is considered a “joint work” under the Copyright Act. A determination that a work is a joint work often will be dispositive of a copyright infringement claim among collaborators, because the authors of a joint work are co-owners of the copyright in the work, and a co-owner cannot be sued for copyright infringement.

Coauthors are tenants in common. Each automatically acquires an undivided ownership interest in the entire work. Even if a person’s contribution is minor, once that person is accorded joint authorship status, he or she enjoys all benefits of joint authorship. These include an independent right to use or license the use of a work, subject only to a duty to account to the other co-owners for any profits earned on the work. As a consequence, establishing coauthorship can mean the difference between having the unfettered right to exploit the work without the consent of the other collaborators and being held liable for copyright infringement.

The Copyright Act of 1976 defines a “joint work” as “a work prepared by two or more authors with the intention that their contributions be merged into inseparable or interdependent parts of a unitary whole.” This language defining a “joint work” also defines “joint authorship” as well; courts and commentators have found the terms to be interchangeable. The statutory definition does not require collaborators to work in close physical proximity to each other during the creative process. Nor is there any requirement that they make their contributions at the same time or in an equal or qualitative manner. Each author, however, must intend that his or her contribution, at the time of its creation, will be part of an indivisible whole.

A classic example of coauthors of a joint work, according to the Ninth Circuit, is W.S. Gilbert and Arthur Sullivan, the lyricist and composer of many works, including the song “I Am the Very Model of a Modern Major General.” The Ninth Circuit deemed that song’s words and tune “inseparable.” Other examples include the innumerable works of Richard Rodgers and Oscar Hammerstein and John Lennon and Paul McCartney—but these joint works are easy to discern. As the Second Circuit noted in Childress v. Taylor, a finding of coauthorship intent requires “less exacting consideration in the context of traditional forms of collaboration, such as the creators of the words and music of a song.” Establishing coauthorship in other circumstances requires far more than demonstrating mere collaboration. Consequently, courts have imposed a number of requirements that are not readily apparent from the statutory language used to define a joint work.

For example, for a finding of a joint work, courts have held that each author must make an independently copyrightable contribution to the work. Indeed, the contribution must “stand on its own as the subject matter of copyright.” Courts have read this requirement into the statute to comport with the fundamental tenet of copyright law that ideas are not copyrightable.

Moreover, the requirement is supported by policy considerations, including 1) the ability of parties to predict whether their contributions to a work will entitle them to copyright protection as a joint author, 2) a goal of avoiding postcontribution disputes concerning coauthorship, and 3) allowing parties to protect themselves by contract if it appears they may not qualify as coauthors under the Copyright Act. Therefore, to be a coauthor of a joint work, one must supply more than the mere direction or ideas; an author must “translate an idea into a fixed, tangible expression entitled to copyright protection.”

Consequently, unless a coauthorship claimant can establish as a preliminary matter that his or her contribution would be entitled to copyright protection separate and apart from the work as a whole, the claimant will not be accorded coauthor status. While the contribution does not have to be substantial to satisfy this requirement, an author still must provide more than a de minimus addition to the work—and the addition must be independently created and involve some minimal degree of creativity.

Nevertheless, a person may make an independently copyrightable contribution to a work and still not be considered a coauthor of the entire work. For example, in Aalmuhammed v. Lee, the Ninth Circuit held that a consultant who had rewritten passages of dialogue and scenes for the movie Malcolm X had made an independently copyrightable contribution but was not a joint author of the film. Therefore, a person claiming coauthorship status also must establish that he or she is an author of the joint work as a whole.

This requirement is grounded, in part, in the statutory definition that requires a joint work to have “two or more authors.” Because the Copyright Act does not define “author,” courts have had to fashion tests for determining when someone is a coauthor of a joint work.

Second Circuit’s Mutual Intent Standard

In addressing this issue in Childress, the Second Circuit acknowledged that the Copyright Act states only that coauthors must intend

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that their contributions “be merged into inseparable or interdependent parts of a unitary whole.” The statutory definition makes no explicit reference to any other intention.

However, if the statute's threshold of coauthorship merely requires an intention for the contributions to be merged into a unitary whole, then, for example, a novelist’s editor, as well as any overreaching contributors, plus current and former spouses, lovers, and friends, “would endanger authors who talked with people about what they were doing.”

Anyone making even a minimal contribution to the writing of a work would be considered a coauthor as long as both parties intended their contributions to be merged into a unitary whole.

The Second Circuit held that in the absence of a more stringent requirement, the statute would accord coauthor status to individuals that Congress did not contemplate as joint owners. To avoid this result, the court held that in addition to making an independently copyrightable contribution to the work, a coauthorship claimant must establish that each putative coauthor fully intended to be coauthors. This requirement recognizes that coauthors are afforded equal rights in the coauthored work and ensures that an equal sharing of rights is reserved for collaborations in which all participants fully intend to be joint authors.

The Ninth Circuit incorporated the Second Circuit's requirement of mutual intent into its own test for determining when someone is a coauthor of a joint work. However, the Ninth Circuit made clear that the mutual intent to be coauthors must be established by “objective manifestations”—not the subjective intent of the parties. This requirement will prevent putative coauthors from perpetrating a fraud by hiding their true intent to take sole credit for the work.

In Aalmuhammed, the Ninth Circuit noted that the word “author” connotes a traditional concept of one person writing at a desk with pen and paper, composing a work for publication. It is relatively easy to apply the word, and the concept, to a novel, but the task becomes more difficult for works involving an increasing number of contributors.

For a music video, the authors may include the performers and the producer; for a movie, the authors could include the director, the star, and the cinematographer or an animator.

**Ninth Circuit’s Three-Part Test**

Against this backdrop, the Ninth Circuit devised a three-part test to determine whether, in the absence of a contract, a contributor is an author for the purpose of joint authorship. First, a putative coauthor must “superintend” the work by exercising control. A superintending author generally is “the inventive or mastermind who creates, or gives effect to the idea.” The issue of control is considered the most important factor and is often dispositive—and the essence of control is the ability to accept or reject the contributions of the other contributors. For example, in Aalmuhammed, the court noted that while a consultant could make “extremely helpful recommendations,” the director of Malcolm X, Spike Lee, was not bound to accept any of them.

Second, coauthors must make objective manifestations of a shared intent to be coauthors. A contract stating the parties intend to be coauthors is considered the best objective manifestation of a shared intent. In the absence of a written agreement, other relevant indicators of intent come into play. Key among these is how the parties credit themselves (for example, if they identify themselves as authors), because this presentation of their role in the creation of the work reflects how the parties regard their undertaking. A collaborator's self-styled manner of billing or credit has been called a “window on the mind.” Similarly, any agreements between the contributors—particularly those with any bearing on who would have ultimate decision-making authority regarding the final content of the work—and between a contributor and a third party also may provide objective manifestations of a shared intent to be coauthors.

Third, a coauthorship claimant must show that the audience appeal of the work turns on the contributions of the coauthors—and each individual's share in the work's success cannot be separately appraised. Courts of appeal have not yet explained how to determine each of these elements. This is most likely due to the fact that most coauthorship cases have been decided on preliminary issues, such as whether the parties intended to be coauthors.

However, in Morrill v. The Smashing Pumpkins, a district court addressed the issue of audience appeal. The case involved a music video, titled View Marked, of a band known as the Marked. The director of the video, who also produced and edited it, claimed he was the video's sole author. One of the original members of the Marked, Billy Corgan, later formed the Smashing Pumpkins and used excerpts of Video Marked in a new video, Viewphoria.

The court noted that music was “the central component” of the completed work, and when the video was first displayed where the Marked was playing, the video’s appeal presumably was based on the audience’s ability to hear more of the band’s performances. However, the court found that after the Smashing Pumpkins gained success, the appeal of the video was most likely based on the audience’s ability to view images of a younger Corgan. Therefore, the court found the video was a joint work because the audience appeal rested both on the video’s visual aspects and on the composition and performance of the music.

A contributor who is unable to establish coauthorship has only a glimmer of hope for relief. If he or she has made an independently copyrightable contribution to the work, the contributor may claim rights as sole author of the portion he or she contributed on the grounds that under the Copyright Act, copyright vests initially in the author or authors of the work. This type of claim emerged in Thomson v. Larson, a case that involved the musical Rent; however, the Second Circuit did not reach the issue because it was first raised on appeal. The court noted that the claimant, a dramaturge, had sought relief based solely on her alleged coauthorship of Rent and had not brought suit for infringement or an injunction in the district court based on use of her allegedly copyrighted material.

Whether a contributor not found to be a coauthor still has a copyright interest in the material he or she has contributed to the work—and whether by the act of collaborating the contributor has granted a license to use the contributed material—are open issues. However, Nimmer on Copyright states that the implied license doctrine may preclude a suit for infringement by one collaborator against the other. Moreover, according to Nimmer, since a collaborator’s contribution may be inextricably intertwined with portions of a work he or she does not own, a collaborator may be unable to exploit his or her work without the consent of the other collaborator—making the creation of no practical value during the copyright term of the work.

Practitioners should bear this in mind when advising clients who are planning to collaborate. A written agreement that states the parties’ intention to be coauthors is the easiest way to avoid a dispute. Without a written agreement, the parties will be left with uncertainty about their rights and with limited or no remedies.
1991; see also 1 MELVILLE B. NIMMER & DAVID NIMMER, NIMMER ON COPYRIGHT §6.01, at 3 (2003).

10 1 MELVILLE B. NIMMER & DAVID NIMMER, NIMMER ON COPYRIGHT §6.03, at 7 (2003).

11 Edward B. Marks Music Corp. v. Jerry Vogel Music Co., 140 F. 2d 266 (2d Cir.1944).

12 Aalmuhammed v. Lee, 202 F. 3d 1227, 1232 (9th Cir. 1999).

13 Edward B. Marks Music Corp. v. Jerry Vogel Music Co., 140 F. 2d 266 (2d Cir.1944).

14 Id. at 508.

15 Erickson v. Trinity Theatre, Inc., 13 F. 3d 1061, 1068-69 (7th Cir. 1994); Childress, 945 F. 2d at 507; Janky v. Lake County Convention & Visitors Bureau, 576 F. 3d 356, 363 (7th Cir. 2009) (“Ideas, refinements, and suggestions” are insufficient to establish joint authorship.).

16 Richlin v. MGM Pictures, Inc., 531 F. 3d 962, 968 (9th Cir. 2008); Ashton-Tate Corp. v. Ross, 916 F. 2d 516, 521 (9th Cir. 1990).

17 Erickson, 13 F. 3d at 1070.


19 S.O.S., Inc. v. Payday, Inc., 886 F. 2d 1081, 1087 (9th Cir. 1989); Erickson, 13 F. 3d at 1071.

20 S.O.S., 886 F. 2d at 1087 (citing Community for Creative Non-Violence v. Reid, 490 U.S. 730, 109 S. Ct. 2166, 2171 (1989)).


23 Aalmuhammed v. Lee, 202 F. 3d 1227, 1232 (9th Cir. 1999).

24 Id.

25 Id. at 1235-36; Thomson v. Larson, 147 F. 3d 195, 200 (2d Cir. 1998).

26 Aalmuhammed, 202 F. 3d at 1232.


28 Aalmuhammed, 202 F. 3d at 1235-36.

29 Childress, 945 F. 2d at 507.

30 Id.

31 Id. at 507-08.

32 Id. at 509.

33 Aalmuhammed, 202 F. 3d at 1234.

34 Id.

35 Id. at 1232.


37 Aalmuhammed, 202 F. 3d at 1232.

38 Id. (“The absence of control is strong evidence of the absence of co-authorship.”).

39 Id. at 1235; see also Thomson v. Larson, 147 F. 3d 195, 203 (2d Cir. 1998) (“An important indicator of authorship is a contributor’s decisionmaking authority over what changes are made and what is included in a work.”); Erickson v. Trinity Theatre, Inc., 13 F. 3d 1061, 1071-72 (7th Cir. 1994) (An actor’s suggestion of text does not support a claim of coauthorship if the sole author determined whether and where these contributions were included in the work.).

40 Aalmuhammed, 202 F. 3d at 1234.

41 Id.

42 Thomson, 147 F. 3d at 203.

43 Id.

44 Id. at 203-04.

45 Aalmuhammed, 202 F. 3d at 1234.


47 Id. at 1124-25.


49 Thomson, 147 F. 3d 195.

50 Id. at 206.

51 Id.

52 1 MELVILLE B. NIMMER & DAVID NIMMER, NIMMER ON COPYRIGHT §6.07, at 27 (2003).

53 Id. at n.32.
Defining Liability for Likeness of Athlete Avatars in Video Games

EA SPORTS, a video game developer, provides consumers with a level of realism that has led to legal challenges by former student athletes for misappropriation of likeness. One suit was initiated after Ed O’Bannon, star of UCLA’s 1995 championship basketball team, watched a friend’s child playing a video game featuring the team. O’Bannon soon recognized himself in the avatar that the child was playing in the game. O’Bannon observed of the avatar, “It didn’t have my name, but it had my number, left handed, it looked like me. It was everything but the name. My friend kind of looked at me and said, ‘You know what’s sad about this whole thing? You’re not getting paid for it.’ I was just like, ‘Wow, you’re right.”

The many similarities that exist between the former student athletes who have filed suit and EA’s digital avatars, however, are not necessarily sufficient to establish liability. The facts standing in the way of liability are that neither O’Bannon’s photographic image nor his name was used in the video games. Instead of the photographic images of college athletes, the video games have animated characters running plays in scenarios as created by EA. In addition, EA can argue that the games are constitutionally protected free speech.

In 2009, O’Bannon filed his suit against the National Collegiate Athletic Association (NCAA) and its licensing arm, the Collegiate Licensing Company (CLC), whose exclusive agreement with EA makes that studio the only one publishing NCAA sports games. The O’Bannon suit claims the use of student athlete images by EA violates the Sherman Antitrust Act. That same year, Sam Keller (a former starting quarterback for Arizona State University and the University of Nebraska) filed a class action suit against EA and the NCAA, accusing the organizations of using the likenesses of college student athletes in video games without player permission. Former Rutgers University quarterback Ryan Hart, joined by former University of California quarterback Troy Taylor, also filed suit against EA, the CLC, and the NCAA alleging similar violations. In 2010, the right of publicity claim in the Hart suit was dismissed without prejudice. In another action, former University of North Carolina football player Byron Bishop filed a class action suit against EA, the CLC, and the NCAA alleging similar violations. In 2010, the right of publicity claim in the Hart suit was dismissed without prejudice. In another action, former University of North Carolina football player Byron Bishop filed a class action suit against EA, the CLC, and the NCAA, alleging that the defendants conspired to violate the NCAA’s bylaws prohibiting the for-profit use of amateur athletes when they included likenesses—but not names—of current athletes in NCAA-branded games.

With the slight variation of the O’Bannon suit’s antitrust allegations, the fact patterns of the former student athlete lawsuits and legal arguments are very similar. The complaints allege that (with the exception of personal names and photographic images) the EA video games precisely replicate each NCAA team—including logos, uniforms, mascots, and stadiums. The lawsuits also allege that EA’s games depict distinctive equipment preferences of NCAA athletes, including wristbands, headbands, face masks, visors, back plates, arm sleeves, and armbands. The plaintiffs conclude that these facts are sufficient to establish liability for misappropriation of likeness because the student athletes did not consent and were not compensated for the use of their likenesses in the video games.

Before being allowed to perform each academic year, all Division I NCAA athletes must sign Form 08-3a—Student Athlete Statement. By signing, student athletes affirm that they understand that they are prohibited from profiting from the commercial use of their names, pictures, or likenesses. In Part IV of the form, student athletes expressly authorize the NCAA and the CLC to use their names or pictures in accordance with Bylaw 12.5, including to promote NCAA champi-

The right of publicity has proven particularly difficult to reconcile with free speech concerns.

Right of Publicity

The common law right of publicity derives from privacy law, which may be traced to the 1890 Harvard Law Review article by Samuel D. Warren and Louis D. Brandeis that argues that people should have some protection from media invasions into their private lives. In the 1928 U.S. Supreme Court case Olmstead v. United States, Justice Brandeis articulated a general constitutional right “to be let alone,” which he described as the most comprehensive and valued right of civilized people. Since then, the right to privacy has continued to develop, and every jurisdiction in the country recognizes some form of constitutional, common law, or statutory right to privacy.

The current formulation of privacy law has been influenced to a large degree by William L. Prosser, who further outlined the appropriation of a person’s name or likeness for commercial purposes. Prosser wrote that the law of privacy comprises four different interests that are tied together by the common name. Each interest represents a part of

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the right to be let alone, and violation of that right is a tort. According to Prosser, the four privacy torts are: 1) intrusion upon the plaintiff’s seclusion or solitude, or into the plaintiff’s private affairs, 2) public disclosure of embarrassing private facts about the plaintiff, 3) publicity that places the plaintiff in a false light in the public eye, and 4) appropriation, for the defendant’s advantage, of the plaintiff’s name or likeness. This characterization of the privacy torts was adopted by the Restatement (Second) of Torts as well as by a number of states.

In 1953, the U.S. Court of Appeals for the Second Circuit, in a case involving baseball trading cards, articulated the modern, assignable right of publicity, which descends from the right of privacy. The newly christened right of publicity did not immediately become the dominant model, but by the late 1970s it had gained footing in courts and legislatures around the country. The right of publicity has essentially expanded since then to apply when ever a monetary value exists. In California, the right of publicity is a statutory and a common law right. The statutory right originated in 1971 in Civil Code Section 3344, which authorizes recovery of damages by any living person whose name, photograph, or likeness has been used for commercial purposes without his or her consent.

Identifiable Likenesses

Courts and legislatures have struggled to define the likeness of a person. A likeness has been found to include one’s name and biographical information, persona, and voice. The essential aspect of any part of one’s likeness is that it makes the person identifiable. The identifiability of the image or other aspect of the plaintiff is an essential element of a claim for misappropriation. Few cases define “identifiability.” The Restatement and a few courts have offered some insight. The test that seems most appropriate is one that requires the plaintiff to demonstrate that his or her image is identifiable in the defendant’s use by more than a de minimis number of people. One court has held that a plaintiff did not establish identifiability when only 6 percent of 306 video game users could identify the plaintiff as the character in the video game. A person’s rights may be violated by the use of the person’s name or biographical information. However, there needs to be some similarity of details that creates the association to the plaintiff from the use by the defendant. The similarity may be as slight as referencing the subject matter under which the person is known. In many other situations, more will be required. The key is whether the plaintiff can be identified from the defendant’s use by more than a de minimis number of people.

In the sports game cases, the plaintiffs often can be identified from the game details. In one case, in opposition to a motion to dismiss, Hart produced a declaration stating: I was listed as standing six…feet and two…inches tall, the same height as the “virtual” Rutgers QB in the NCAA Football game versions in question; I weighed [197] pounds…the same weight as the “virtual” Rutgers QB in the NCAA Football game versions in question; [m]y jersey number was 13, the same as the “virtual” Rutgers QB in the NCAA Football game versions in question; I wore a left wrist band, the same as the “virtual” Rutgers QB in the NCAA Football game versions in question; and I wore a helmet visor, the same as the “virtual” Rutgers QB in the NCAA Football game versions in question.

In addition, Hart averred that the NCAA Football 2006 game’s virtual quarterback had the same speed and agility rating, passing accuracy, and arm strength as could be inferred from actual footage. Similarly, the game shows the virtual quarterback’s contribution to the team’s overall success as identical to that of Hart in the actual season. Finally, Hart averred that actual video footage of him is used in promotion material for EA’s NCAA game. Each of the former athlete claimants can recite similar experiences. If more than a de minimis number of people are able to attribute such characteristics to Hart, then the identifiability element of a misappropriation of likeness claim may be satisfied.

On the other hand, while details such as those listed in Hart’s declaration may serve to identify him, the digital images in the games do not match the claimants. The plaintiffs in each case concede that their names are not used and that the game images do not resemble them closely. Claims of use of image likeness pertain to allegations that, in nongame imagery, EA used stills and video of student athletes recorded while they played in NCAA championship games. But the driving force behind the suits is the avatar—for example, the one that O’Bannon saw in a game—no images that appear for a few seconds when the game is loaded. Hart’s idiosyncratic mannerisms and style do appear in the game, but his image does not. Since it is the digital image that is the basis for the complaints of Hart and the others, and digital images must be manufactured, the images are subject to a transformative use defense, despite the commercial nature of EA’s use. Since EA has not animated the actual photographic images of former student athletes, and since the characterizations (including those Hart described) are based on information made public while the former student athletes played their sports, EA may be successful in defending against liability.

Two other cases may also apply to EA’s possible liability. The Ninth Circuit has considered whether the use of robots depicting celebrities or the characters played by celebrities violates California Civil Code Section 3344 or the celebrities’ common law right of publicity.

In White v. Samsung Electronics America, Inc., the court held that because the defendants used a “robot with mechanical features” as opposed to a “manikin molded to (plaintiff) White’s precise features,” the robot at issue did not use plaintiff White’s likeness within the meaning of Section 3344. However, the court in Wendt based its holding on whether the identities of the plaintiff celebrities had been evoked, regardless of whether their names or likenesses were used. Applied to the student athlete cases, White would likely require that the plaintiffs show that EA’s digital images bear a sufficiently similar resemblance to their physical features to establish a Section 3344 claim. However, the student athletes stand a greater chance at maintaining a right of publicity claim by following Wendt, because the individual players’ background information contained in the video games can reasonably be said to implicate their identities.

Misappropriation

While the defendants in the video game lawsuits emphasize that actual images are not used, the plaintiffs emphasize that the games use identifiable likenesses. The characters in the games bear likenesses to former student athletes, so the video game makers must have assigned a value to the likenesses, which are protected by a right. Similar arguments have met with success. In 2007, EA paid the National Football League Players Association (NFLPA) more than $35 million for the use of the names and likenesses of the players. In 2008, a federal jury in San Francisco awarded $28 million to a group of 2,062 retired professional football players in a class action suit against the NFLPA. The jury returned a $7 million verdict against the NFLPA, plus $21 million in punitive damages. Although EA was not a party in that case, the NFLPA’s negotiations with EA over licensing the images of retired NFL players were central to the plaintiffs’ case in chief.

During discovery, lawyers for the retired players uncovered several e-mail messages indicating that the NFLPA sold rights to use the likenesses of retired players, although the plan was to shield the use. Those critical communications included a message from a former NFLPA executive to an EA game producer insisting that the identities of retired players be altered so that they were not recognizable. As a result, jersey numbers were...
scrambled for the video games. Lead plaintiff Herb Adderley said, “If you look at the 1967 Green Bay Packers, you’ll know that the only left cornerback that year had to be [me], but they scrambled my face and took the number off of my jersey. Yet, they had my correct height, weight, and years of experience.” Following an appeal, the retirees accepted a $26.25 million settlement.

The First Amendment and Transformative Use

Although misappropriation was found with respect to former football players, it may not be as clear in the case of former student athletes. As intellectual property rights have expanded, defendants are increasingly invoking the First Amendment as a defense against those who attempt to limit use by the exercise of a right of publicity claim. In the Keller case, EA argued in support of a motion to dismiss that the information contained in the video game about the digital avatars simply reflected statistics about the players that were already in the public record, which should shield EA from liability. The court rejected this argument, ruling that “EA’s game provides more than just the players’ names and statistics; it offers a depiction of the student athletes’ physical characteristics and enables consumers to control the virtual players on a simulated football field.”

In February 2011, the Ninth Circuit heard EA’s appeal to this ruling, which stressed the transformative character of the video games in which the likenesses of Keller and other college athletes appear. EA urged the court to look beyond its accurate portrayal of players and instead consider the player avatars in the overall context of the video game medium. In response, the student athletes cited Zacchini v. Scripps-Howard Broadcasting, arguing that the First Amendment does not provide a limitless defense against financial exploitation without consent.

The intersection of intellectual property law (including rights of publicity) and the First Amendment has become increasingly contested. As intellectual property rights have expanded, defining the zone of protected speech has become progressively more complex. The branch of intellectual property law known as the right of publicity has proven particularly difficult to reconcile with free speech concerns. Recently, some courts have begun importing a transformative use approach from copyright law to reconcile tensions between publicity rights and constitutionally protected free expression. This approach—focusing on transformative use as applied in copyright fair use—asks whether a putative fair user has simply used copyrighted expression in a more or less verbatim fashion or has added “new expression, meaning or message.” If the expression is new, the use is transformative and is more likely to be held protected.

In a 1990 Harvard Law Review article, Judge Pierre N. Leval renamed the concept of productive use as transformative use. Judge Leval argued that if the appropriated expression “is used as raw material, transformed in the creation of new information, new aesthetics, new insights and understandings—that is the type of activity that the fair use doctrine intends to protect for the enrichment of society.” The newly labeled transformative use doctrine was embraced by the Supreme Court in 1994 in Campbell v. Auff-Rose Music. That case involved the notorious rap group 2 Live Crew and its appropriation of portions of the Roy Orbison hit “Oh, Pretty Woman.” The Court, citing Judge Leval, defined transformative uses as those which take an earlier work and add “new expression, meaning, or message.” Although the Court did not definitively rule that the rap group’s appropriation was transformative, it stated in dicta that it might be. The Court deployed the transformative use doctrine primarily through the view of purpose and character of the use.

Justice Brandeis stated that the First Amendment has three purposes: 1) enlightenment—political, social, and scientific news and entertainment, 2) self-fulfillment—human self-expression in all forms, and 3) the safety valve—society’s need for free expression as an alternative to violence. The First Amendment has been held to protect certain types of speech, with “commercial speech” receiving less protection. The court further reasoned that video games generally are considered expressive works subject to First Amendment protections. However, Activision’s right of free expression is in tension with the rights of No Doubt to control the commercial exploitation of its members’ likenesses.

Liability in this instance can be deciphered by analyzing whether the student athlete likeness is one of the raw materials from which the video games’ digital avatars are synthesized, or whether the depiction or imitation of the student athlete likenesses is the sum and substance of the work in question. In other words, can it be affirmatively stated that the digital avatars created by EA are so transformative that the avatars have become primarily EA’s own expression rather than the likenesses of student athletes?

This has yet to be seen, but the California Supreme Court has held that in determining whether a work is transformative, courts are not to be concerned with the quality of the artistic contribution. Vulgar forms of expression fully qualify for First Amendment protection. On the other hand, a literal depiction of a celebrity, even if accomplished with great skill, may still be subject to a right of publicity challenge. The inquiry is in a sense more quantitative than qualitative, asking whether the literal and imitative or the creative elements predominate in the work. What is
clear is that transformative elements or creative contributions that require First Amendment protection are not confined to parody and can take many forms, including factual reporting, fictionalized portrayal, heavy-handed lampooning, and subtle social criticism.

The motto of EA once was, “If it’s in the game, it’s in the game.” This later changed to “It’s in the game!” It seems ludicrous to question whether video game consumers enjoy and, as a result, purchase more EA-produced video games as a result of the heightened realism associated with actual players. It is reasonable to claim that EA’s economic goal has been to adopt as many characteristics as possible from known commodities and to make its games imaginative. Whether, in effecting this goal, there has been a misappropriation of likeness or a transformative use will have to be decided in court.


6 Id. at Court Document 23.


12 Id. at 389.

13 See id.


16 Haelan Labs., Inc. v. Topps Chewing Gum, Inc., 202 F. 2d 866, 868 (2d Cir. 1953).

17 Waits v. Frito-Lay, Inc., 978 F. 2d 1093 (9th Cir. 1992); RESTATEMENT (THIRD) OF UNFAIR COMPETITION §46 cmt. d.


23 White v. Samsung Elec. Am., Inc., 971 F. 2d 1395, 1397 (9th Cir. 1992); Wendt v. Host Int’l, Inc., 125 F. 3d 806, 810 (9th Cir. 1997).
24 White, 971 F. 2d at 1397.
25 Wendt, 125 F. 3d at 810.
26 See the NFLPA’s 2007 FORM LM-2 LAB. ORG. ANN. REP.
27 A U.S. district judge dismissed a malpractice case brought by retired NFL players who claimed their attorneys did not do a good enough job representing them in a case against their union. Parish v. Manatt, Phelps & Phillips and McKool Smith, No. 10-03200 (N.D. Cal. Dec. 13, 2010).
31 See the NFLPA’s 2007 FORM LM-2 LAB. ORG. ANN. REP.
32 Campbell, 510 U.S. 569.
33 Id. at 579 (quoting Leval, supra note 30, at 1111).
34 Id. at 582-83.
35 Id. at 582-92.
38 McCarthy, The Rights of Publicity and Privacy §§7.3, 8.16, 8.18 (2d ed. 2008).
42 Id.
44 Id.
46 Id.
48 Kirby v. Sega of Am., Inc., 144 Cal. App. 4th 47, 58 (2006); see Video Software Dealers Ass’n v. Schwarzenegger, 556 F. 3d 950, 958 (9th Cir. 2009), cert. granted sub nom Schwarzenegger v. Entertainment Merchants Ass’n, 130 S. Ct. 2398 (2010); Romantics, 574 F. Supp. 2d at 765-66 (The Guitar Hero video game is “an expressive artistic work that is entitled to First Amendment protection.”).
THE PARTICIPATION OF CELEBRITIES in charitable causes is rooted in tradition and increasingly apparent in a variety of venues. When those who are famous for their achievements in the arts, entertainment, media, or sports decide to become involved in charities, they are undertaking a complex endeavor, with a wide variety of legal and business challenges involving many parties. They are becoming “charitable actors,” with many attendant rewards but also a number of responsibilities.

The close relationship between entertainment and sports celebrities and charities has a long lineage. In the entertainment world, Bob Hope’s decades-long support of the USO by performing for U.S. troops throughout the world led Congress to name him an honorary veteran. At last year’s Emmy Awards ceremony, George Clooney received the Bob Hope Humanitarian Award for his fundraising contributions. In the sports arena, Ted Williams, the legendary baseball player with the Boston Red Sox, worked behind the scenes for years on behalf of the Dana Farber Cancer Institute’s Jimmy Fund, making unannounced (and unreported) visits to children and paying their hospital bills.¹

Celebrities often respond when a natural disaster strikes or when they are asked to raise public awareness for a worthy cause. One example is Farm Aid, organized by Willie Nelson, John Mellencamp, and Neil Young in 1985. Sometimes a charitable event becomes

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an annual tradition, such as the Jerry Lewis MDA Telethon, which has taken place every Labor Day weekend since 1966. In response to a crisis, celebrities plan and present one-time fundraisers in a matter of days, such as the Hope for Haiti event organized by George Clooney and Wyclef Jean in 2010.

Whatever the circumstance, a legal team needs to oversee the formation of the charitable program. Attorneys provide direction in working with personal and business managers, public relations teams, agents, in-house counsel, corporate advisers, and nonprofit directors to ensure strict compliance with all applicable laws. They also monitor the proceedings so that all the participants’ objectives are met.

This process actually begins before any specific charitable need or involvement is even considered. Successful young entertainment or sports stars soon realize that the rap lyric distilling their lives to “mo money, mo problems” also includes “mo” people: lawyers, publicists, tax and wealth advisers, business managers, and CPAs. At some point, the young stars will usually have a conversation with one or more of these advisers about personal wealth planning. That conversation should include a discussion about charitable giving as a way to accomplish personal and financial goals.

A simple, direct gift to a charity results in a charitable income tax deduction in the year of the gift. The gift can be cash, or securities, or some other property. A gift that is not a readily valued asset (such as cash or publicly traded securities) requires an appraisal, and an attorney is needed to sort through the sometimes confusing rules on deductions for appreciated property. The deduction can depend on the type of property contributed, the holding period, who the donee charity is, what the donee does with the gift, if there were large gifts in prior years, and the number of elections that the donor and his or her CPA may choose to make.

If a celebrity wishes to make a gift of assets but still retain some ongoing benefit from the assets, he or she may consider a charitable remainder unitrust, which provides for a continuing income stream to the celebrity for a term of years, with the remainder to the charity’s family members after the charity’s term interest. If the asset to be donated is something other than publicly traded stock, the charity should carefully choose a trustee. Practitioners can help with this as well as advise the celebrity on managing expectations for investments. The celebrity donor also must be alerted to avoid the pitfall that occurs when the donor enters into a contract for sale of the asset prior to contributing the asset to the charitable remainder trust. If the trustee of the trust later sells the asset, what would have been a tax-free sale instead becomes a taxable sale followed by the donation of the after-tax proceeds.

**Private Foundations**

For some celebrities with a considerable record of charitable giving and adequate resources to continue doing so, the use of a private foundation may be the best means of sustaining the individual’s philanthropy in the future. A private foundation allows celebrities to channel their charitable giving through an organization under their control. This type of foundation can be formed fairly quickly by, for example, establishing a California or Delaware nonprofit public benefit corporation. A trust may be used instead of a corporation, but a trust is a less flexible structure than a corporation and tends to be used infrequently.

A California corporation may have as few as one director, is not required to have voting members, and is allowed to have honorary members if it so chooses. The corporation applies to the Internal Revenue Service (and to California’s Franchise Tax Board) for recognition as a tax-exempt organization. Once this status is granted, tax exemption is generally retroactive to the date of incorporation.

A celebrity or an authorized agent uses a private foundation to grant money to established charities. By law, a private foundation must make an annual minimum distribution of 5 percent of the average fair market value of its assets, as determined by periodic appraisals.

A private foundation allows a celebrity to put his or her name on a charitable organization and to directly manage how the funds will be distributed. However, there are drawbacks to this approach. The deductibility limitations are lower than they would be if the celebrity contributed directly to a charity or to a fund that the celebrity established at the charity. Moreover, private foundations have special excise taxes on net investment income. In addition, private foundations with gross revenues exceeding $2 million must prepare audited financial statements.

Celebrities also must guard against administrative expenses exceeding charitable spending. A private foundation’s good works could be overshadowed if its missteps are on display for all the world to see in publicly available filings.

Private foundations have special rules against self-dealing to prevent the founder, family members, related business interests, or otherwise disqualified persons from taking advantage of their position to engage in transactions with the private foundation, regardless of whether the transaction might benefit the foundation. Acts of self-dealing are subject to penalties in the form of additional taxes. A celebrity who establishes a private foundation needs to be well advised on what can and cannot be done with the funds he or she has contributed to the foundation. Even a seemingly insignificant act, such as distributing tickets purchased by the foundation for a gala dinner, must be carefully scrutinized with an eye toward the self-dealing rules.

Celebrities may appoint family members as salaried officers to the foundation. Reasonable salaries will not violate the self-dealing rules, but the board must demonstrate how it arrived at its determination of reasonableness. In addition, California rules provide that no more than 49 percent of the directors of a foundation may be “interested persons.” An “interested person” is defined as any person other than the director who is compensated for services rendered to the foundation during the previous 12 months, including brothers, sisters, spouses, parents, descendants, and in-laws of interested persons. The self-dealing rules prevent any sale, exchange, license, or lease of property between the foundation and the celebrity or his or her family members, unless the lease is without charge.

Celebrities who created private foundations include actor and director Matthew Modine, who formed Bicycle for a Day (BFAD), a nonprofit organization dedicated to educating individuals about environmental and health issues and encouraging students to ride their bicycles to school. BFAD’s first event attracted approximately 14,000 bicyclists to lower Manhattan. Modine himself has used a bicycle as his primary form of transportation since moving to New York City in 1980. Modine also serves on the board of New York City’s Transportation Alternatives, Madison Square Garden’s Garden of Dreams Foundation, the Lustgarten Pancreatic Cancer Foundation, and the Van Cortlandt Park Conservancy. To advise a strong charitable actor like Matthew Modine, practitioners must understand the complex rules applicable to founders and directors of charitable organizations.

Another example of a celebrity involved with a private foundation is musician Jack...
Johnson, who created the Kokua Hawai‘i Foundation to support environmental education in the schools and communities of Hawaii. The foundation raises money through an annual music and environmental festival and continues to grow and expand. As it does so, it takes on the characteristics of any other business and must address issues relating to employment, real estate, and intellectual property (including the protection of trademarks and logos). Moreover, it must ensure compliance with the relevant laws to maintain its tax-exempt status.

Artists for Peace and Justice, formed by film director Paul Haggis in 2009, has long-term plans to support a host of social projects, but its immediate goal is to serve children in the poorest areas of Haiti by building schools and providing meals, clean drinking water, and regular medical treatment. Practitioners advising charitable organizations with overseas operations must determine whether the U.S. charity will establish its own program in a foreign country or will operate by supporting an existing foreign charity. This decision may affect the deductibility of donations made by U.S. taxpayers.

**Donor-Advised Fund**

An alternative to a private foundation is a donor-advised fund (DAF), a kind of “mini foundation” that offers many benefits of a private foundation but without some of the pitfalls. A DAF is a giving vehicle that provides an individual with immediate tax benefits. At the same time, individuals forming a DAF may support the charities of their choice through grant recommendations—and may do so on timetables of their choosing.

DAFs are efficient, cost-effective alternatives to private foundations. Unlike a private foundation, there is no annual minimum gifting amount. The donor making a gift to the DAF is allowed the higher deduction limits that are provided to donors to a public charity. The donations may be made anonymously, unlike a private foundation that must make its records available to the public. The paperwork of the DAF, such as tax returns and informational reporting, is handled by the fund’s administrator, so the celebrity is only responsible for advising on the grant recipients.

A DAF can be formed swiftly and without difficulty, and many organizations are set up to facilitate their creation. These include the California Community Foundation, the Jewish Community Foundation, and many banks and trust companies. However, the donor does not have as much control as in a private foundation, because the celebrity donor acts only as the adviser to the DAF, and the fund’s administrator legally must have the final say on where to allocate the grant funds. Still, a celebrity donor working closely with a DAF customarily will find that his or her wishes will be fulfilled. According to Carol Bradford, senior counsel and charitable advisor of the California Community Foundation, “Donor-advised funds are a popular way for celebrities or anyone to make charitable contributions easily, quickly, and even anonymously. CCF can set up a fund within 36 hours, handle all sorts of contributions to the fund, and ensure that grants from the fund, whether large or small, are made efficiently and effectively.”

Some celebrities have a natural affinity for certain charities based on family circumstances or personal passions. For others, sorting through the many charities seeking support can be daunting. There is so much need and so many good causes that finding a way to make each dollar count requires time and due diligence. Organizations have emerged to help donors with these decisions. For example, Charity Navigator is an independent charity evaluator that assesses the financial health of more than 5,500 charitable organizations. Its Web site has a page that allows users to search charities based on which celebrities support the charity.18

Some organizations specialize in helping celebrities manage their philanthropy. For example, the Giving Back Fund, a 501(c)(3) organization, provides philanthropic consulting and foundation management to high-profile individuals committed to philanthropy. The Giving Back Fund can establish a DAF for the individual or provide consulting regarding a private foundation.19 Athletes for Hope, a 501(c)(3) charitable organization, was founded by a group of successful athletes20 to inspire and foster a commitment to charitable and community causes in the next generation of athletes and in the fans who support them.

Another advisory organization is Global Philanthropy Group, whose founder, Trevor Neilson, has been dubbed a “Charity Fixer to the Stars.”21 The company currently advises 20 clients, with some paying $150,000 to $200,000 a year for consulting services. These include research, education, and strategic design to ensure that a celebrity’s philanthropy will have the intended impact.

Celebrities must understand that donating their considerable and valuable time and energy to a cause they believe in does not pay off with an income tax deduction. The contribution of services cannot be deducted.22 Celebrities must contribute money or property to charity to receive an income tax deduction. However, a celebrity’s endorsement or link to a charitable cause can increase the celebrity’s value to a sponsor or marketer—and this, in turn, may increase the individual’s bottom line more than a charitable income tax deduction.

The 2010 Cone Cause Evolution Study, a 17-year benchmark study of cause marketing attitudes and behaviors, found that 83 percent of consumers want more of the products, services, and retailers that they use to benefit causes. According to the study, 88 percent of consumers say it is acceptable for companies to involve a cause or issue in their marketing, 85 percent have a more positive image of a product or a company when it supports a cause they care about, and 80 percent are likely to switch brands, similar in price and quality, to one that supports a cause.23

**Cause-Related Marketing Campaigns**

Celebrities who are publicly identified with a particular cause can align with a company as a partner in an effort to market a product that will benefit that cause. The celebrity, the developer of the product, and the charity all must make careful choices in taking this
Moreover, a celebrity presence does not guarantee that a charity will see an increase in donations. According to a 2006 Cone study, Americans rank celebrity involvement as one of the least effective methods for nonprofits to gain attention, placing it ninth on a list of 10 marketing methods to gain consumer support (just edging out telemarketing). The right combination, however, can be extremely effective—for example, Sheryl Crow’s 2008 concert for the Susan G. Komen Breast Cancer Foundation, with admission consisting of 10 specially designed lids from Yoplait products.

In creating a cause-related marketing campaign involving a concert and a product tie-in, numerous legal issues emerge. If the concert is filmed, a determination of who will own the film rights and any music recordings must be made. For liability purposes, the organizers must decide whether a separate entity from the charity should be used or established to produce the show. If the price of the ticket is an actual dollar amount (instead of the proof of purchase of a product), concertgoers need to be informed that they are not entitled to a charitable deduction for the portion of their ticket that represents the usual cost of attending the show. Normally, the concertgoer would be allowed to deduct any premium that was charged or intended to be a charitable gift. For example, when a $50 ticket is sold for $75 on the night of a gala, $25 of the ticket price is deductible. The legal team should consider how the event can be structured to best enhance the ability of donors and sponsors to receive income tax deductions. Attention to the charitable solicitation registration requirements for all applicable jurisdictions is key. A well-coordinated effort to comply with all state and local registration requirements will prevent penalties and fines.

The tax code provides a new, albeit underused, provision that could be a boon to cause-related marketing. Under Internal Revenue Code Section 170(m), a songwriter may donate a song to a charity, providing significant benefits to both the songwriter and the charity. The songwriter can donate all or a portion of the writer’s and/or publisher’s share of a copyright to a charity, avoid the income tax on the income from the exploitation of the copyright, and receive a significant income tax charitable deduction over a 10- to 12-year period, based upon the revenue received by the charity. The song can be either specifically written for the charity or an existing song from the songwriter’s catalogue. No appraisals are required; the deduction is instead based on the income received by the charity during the applicable period. Music publishers and record companies do not have to participate for the songwriter and charity to take advantage of this provision. However, music publishers and record companies generally are supportive of the songwriter’s donation, since it expands public awareness of the song and potentially increases the overall revenue from the song at no additional cost to them. Indeed, the charity steps in as a marketing and distribution partner for the song, so everyone wins.

**Qualified Sponsorship Payment**

Two main umbrella nonprofit organizations serve the charitable needs of the entertainment industry, but in very different ways: the Motion Picture and Television Fund (MPTF) and the Entertainment Industry Foundation (EIF). The MPTF was created in 1921 by Charlie Chaplin and Mary Pickford, among others. Its mission statement is “We Take Care of Our Own.” The MPTF recognizes that the vast majority of persons who work in entertainment are not the people whose familiar faces line the magazine racks at supermarket checkout counters. What started as coin boxes for Hollywood workers to donate change to help their fellow workers has evolved into a comprehensive organization offering health-related and financial services for needy members of the entertainment industry.

The mission of EIF is to harness the collective power of the entertainment industry—including artists and celebrities, film and television executives, guild members, talent agencies, and employees—to raise awareness and funds for critical health, educational, and social issues. EIF has created a series of initiatives to address specific issues and has developed a fundraising plan for each initiative. Often these plans involve one or more key celebrities who become the face of the cause.

EIF is a charitable organization with its own donors and sponsors. A tax-deductible payment by an EIF sponsor to a charity must be distinguished from a payment for a service, such as an advertisement for goods. Under the IRC, a “qualified sponsorship payment” is any payment made by any person engaged in a trade or business to which there is no expectation that the person will receive any substantial benefit other than the use or acknowledgment of the name, logo, or product lines of the person’s trade or business in connection with the activities of the recipient exempt organization. The tax code provides that the solicitation and receipt of qualified sponsorship payments does not constitute an “unrelated trade or business” that would cause the charity to receive unrelated business income and incur tax.

A sponsorship message crosses the line from mere acknowledgment to impermissible advertising if the message contains qualitative or comparative language; price information, or other indications of savings or value; endorsements; or inducements to purchase, sell, or use the payor’s products or services. There is a safe harbor for an arrangement that designates a corporate sponsor as the exclusive sponsor of an event, as long as the designation does not result in a substantial return benefit to the sponsor. If, however, the charity agrees with the sponsor that it can be the sole provider of a product or service at the event, then the transaction may be taxable, because the sponsor is receiving a significant benefit.

The Treasury Regulations provide an example of a qualified sponsorship payment: M, a local charity, organizes a marathon and walkathon at which it serves drinks and other refreshments provided free of charge by a national corporation. The corporation also gives M prizes to be awarded to winners. M recognizes the assistance of the corporation by listing the corporation’s name in promotional fliers, in newspaper advertisements of the event, and on T-shirts worn by participants. M changes the name of its event to include the name of the corporation. M’s activities constitute acknowledgment of the sponsorship. The drinks, refreshments, and prizes provided by the corporation qualify as a nontaxable sponsorship payment rather than as income from an unrelated trade or business. A charity such as EIF may provide a link on the charity’s Web site to the sponsor’s Web site—and this is a permissible acknowledgement, not advertising. However, the charity should not endorse the sponsor’s products in connection with this link on the charity’s Web site, because that can change the link from permissible acknowledgement to taxable advertising.

### Responding to Crises

A celebrity may have established a private foundation or a DAF, and may be working with an advisory organization, business manager, or lawyer to structure his or her appearances, sponsorships, and charitable gifts. At times, the celebrity seeks to join forces with others in response to an urgent natural or man-made crisis. Celebrities may decide to become involved in immediate action or set in motion a “spread the word” campaign.

An example of the acute response is the Hope for Haiti telethon. A telethon generally has celebrity hosts and performers, all donating their time and services, as well as celebrities operating the phone banks to receive pledges of support from viewers. In the case of the Hope for Haiti Now telethon, EIF processed the donations and distributed the funds to seven identified charitable recipients. Celebrities produced a top-selling album and video, with the proceeds benefiting the...
The preparations for the telethon involved determining whether intellectual property rights were donated or licensed as appropriate.

Examples of a “spread the word” response include Stand Up to Cancer (SU2C) and the RED Campaign. SU2C is an initiative formed by EIF to raise funds for ground-breaking research in the fight against cancer and bringing new treatments to patients as quickly as possible. The initiative involved a team of film, television, music, and sports stars appearing on all the major broadcast networks in a one-hour commercial-free program. It also included 30 online streaming partners as well.

The Red Campaign—with its tag line “Buy (Red), Save Lives”—focuses on stopping the spread of HIV/AIDS in Africa. A company pays a fee for permission to market a product under the Red logo. Then, when a consumer buys a Red product, the buyer donates a percentage of the sale to the Global Fund, which invests 100 percent from the sale to HIV/AIDS programs in Africa. The wide array of Red products allows celebrities a way to simultaneously associate with a brand and with the charitable campaign. Moreover, special edition products are being created for the campaign.

One of the next major collaborations between the charitable world and the entertainment industry will be a telethon this year on Veterans Day to provide support for the needs of U.S. veterans. The plan is to transform Veterans Day, November 11, into a participatory national holiday of major importance similar to July 4. EIF is developing an event that will be broadcast nationally with the Alliance for Veterans (AV), a tax-exempt organization. The broadcast will feature performances by acclaimed concert artists interspersed with testimonials from veterans and their families.

For a celebrity, living a life in the public eye may be measured by a list of credits and sometimes awards. But for many who have found fame, their resumes now include charitable work. Stepping into the role of charitable actor may begin as a way to save on taxes, but it can end as defining a celebrity’s true legacy.

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1 For years, Williams encouraged people who wanted his autograph to make out checks to “Ted Williams for the Jimmy Fund.” Williams would then endorse the check and send it to the charity. The Jimmy Fund would get the donation, and the check writers would get valuable Ted Williams autographs on the back of their canceled checks. See http://www.jimmyfund.org.

2 NOTORIOUS B.I.G., Mo Money Mo Problems, on LIFE AFTER DEATH (July 15, 1997).

3 I.R.C. §170.

4 I.R.C. §664(d)(2). Alternatively, a charitable lead trust provides for payment to a charity for a term of years, with the remainder passing typically to the donor’s children at the end of the term. I.R.C.
§170(f)(2)(B).
6 Because of the costs of formation and the annual costs of upkeep, a minimum of $1 million is usually recommended to fund a private foundation.
7 CORP. CODE §5151(a).
8 CORP. CODE §5132(c)(1).
9 IRS Form 1023 must be filed within 15 months of the close of the month the private foundation corporation is formed. An automatic 12-month extension of the time to file is available. Treas. Regs. §§1.508-1(a)(2)(i), (iii), 301.9100-2.
10 I.R.C. §4942.
11 A contribution to a public charity is deductible up to 50 percent of adjusted gross income (AGI), whereas the same contribution to a private foundation is deductible up to 30 percent of AGI. Each would have a five-year carryover for excess contribution.
12 I.R.C. §4940.
13 See GOV’T CODE §12586(e)(1).
14 A private foundation must file an annual information return, a 990-PF. It must be available for public inspection, and the public can search a foundation’s financial history online at http://www.guidestar.org.
15 In a private letter ruling, the IRS held that a private foundation could not split the cost of a charitable event ticket with a for-profit corporation that was a disqualified person under circumstances in which the for-profit corporation would pay the cost of the ticket attributable to the dinner and entertainment and its representatives would attend the event. I.R.S. Priv. Ltr. Rul. 9021066 (Mar. 1, 1990).
16 CORP. CODE §5227.
19 See http://www.givingback.org.
22 Treas. Regs. §1.170A-1(g) (as amended, Apr. 9, 2008).
26 EIF was created in 1942 as the Permanent Charities Committee. See http://www.eifoundation.org.
30 I.R.C. §513(i)(1).
33 Treas. Regs. §1.513-4(f) (Apr. 25, 2002).
34 Some Red partners donate a dollar amount per purchase, rather than a percentage. For example, Starbucks donates $1 to the Global Fund for each sale of one of its Red products. See http://www.joinred.com/aboutred.
COPYRIGHT INFRINGEMENT CLAIMS require courts and juries to compare the similarity of the works created by the plaintiff and the defendant to determine whether infringement occurred. One issue with which courts have grappled is whether the extent of the defendant’s access to the plaintiff’s work is relevant to the level of similarity required to establish infringement. Under the so-called inverse ratio rule, if the plaintiff establishes a high degree of access to its work by the defendant, a finding of infringement may be based upon a lesser degree of similarity. The inverse ratio rule is rooted in case law from the 1930s through the 1950s. It is long past time for the Ninth Circuit to abandon it.

In 1961, the Second Circuit considered the rule and rejected it. While some courts in the Ninth Circuit have embraced or at least acknowledged the rule, others have ignored it. Moreover, it is unclear what the precise role of the inverse ratio rule is, if any, in a copyright infringement case in the Ninth Circuit. A review of the leading cases in the Ninth Circuit and Second Circuit makes clear that the degree of access should be irrelevant to the degree of similarity required to establish infringement.

To establish copyright infringement in the Ninth Circuit, the plaintiff bears the burden of proving that he or she is the owner of a valid copyright, and the defendant copied elements of the plaintiff’s work that are subject to copyright protection. Copying is rarely established by direct evidence. Instead, plaintiffs typically attempt to establish copying through circumstantial evidence: The defendant who created the allegedly infringing work had access to the plaintiff’s material, and substantial similarity exists between the two works. Establishing access requires the plaintiff to prove that the defendant had a reasonable opportunity to view the plaintiff’s work. A “bare possibility” of viewing the plaintiff’s work is insufficient.

Substantial similarity is determined under an “extrinsic test” and an “intrinsic test.” The extrinsic test “focuses on ‘articulable similarities between the plot, themes, dialogue, mood, setting, pace, characters, and sequence of events’ in the two works” and is objective. When the extrinsic test is applied, unprotectible elements—such as basic, stock ideas and concepts, and situations and inci-

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The court also noted in dictum that the defendant’s admission of access affected the weight to be given to the similarities. In particular, the court explained that when there is an admission of access, there is a high probability—indeed a presumption—that the similarities are the result of copying. Nevertheless, the Shipman court concluded that its presumption of copying could not overcome the numerous differences between the two works and thus found no infringement.

In 1942, in O’Rourke v. R.K.O. Radio Pictures, Inc.20 a case before a U.S. district court in Massachusetts, the defendant admitted he had access to the plaintiff’s script but denied that he copied any part of it. The court ostensibly rejected the “presumption theory” set forth in Shipman but nevertheless stated, inexplicably, that “in the face of a showing of access strong proof from the defendant is required that its material is from an independent source.”21 Ultimately, the court held that even if some of the changes in the defendant’s work had been “suggested” by the plaintiff’s work, this only showed, at best, a use of such a small fraction of the plaintiff’s ideas that it did not rise to the level of copyright infringement.

In Golding v. R.K.O. Pictures, Inc.,22 the California Supreme Court in 1950 addressed state common law copyright infringement. The defendants in the case, who were producers of a motion picture, appealed a judgment against them, arguing that there was insufficient evidence to support a judgment that they plagiarized the plaintiffs’ play. The defendants admitted access,23 and the court noted that the defendants also demonstrated an inclination to pirate the plaintiffs’ work.24

In discussing whether the defendants had engaged in unauthorized copying, the supreme court looked to the decisions in both Shipman and O’Rourke. After reviewing these cases, the court concluded, “An inference of copying may arise when there is proof of access coupled with a showing of similarity.”25 Then, without citing any authority, the court stated:

Where there is strong evidence of access, less proof of similarity may suffice. Conversely, if the evidence of access is uncertain, strong proof of similarity should be shown before the inference of copying may be indulged.26

The Golding court addressed the issue of access in its determination of whether there had been actual copying, not whether the two works were substantially similar. Indeed, to find liability for damages, the court noted that the plaintiffs must also show “substantial evidence of similarity between plaintiffs’ literary property and the moving picture produced by defendants.”27 The court then compared the two works in order to determine whether there was substantial similarity between the plaintiffs’ play and the defendants’ motion picture regarding the protectible features of the plaintiffs’ play.28 In this part of the analysis, the court did not even discuss the issue of access.

Ultimately, the Golding court found the evidence sufficient for the jury to find that the two works were substantially similar and held the defendants liable for infringing on the plaintiffs’ protectible property rights.29 Still, it remained unclear whether federal courts would adopt any of the statements made by the Golding court.

Four years after the Golding decision, in 1954, a U.S. district court in the Southern District of New York issued a ruling in Morse v. Fields, a copyright infringement case.30 In the court’s determination of whether actual copying had taken place, the court distinguished between the similarity necessary to show actual copying and the similarity necessary to show actionable copying. The court analyzed the actual, in-fact copying element by looking to the evidence of access and similarity. Regarding access, the plaintiff showed that his article had appeared in a national publication. Nevertheless, the court found, “With the evidence so posited, the plaintiff is entitled to little benefit from the ‘inverse ratio’ rule to the effect that when access is established a lesser degree of similarity is required.”31 The Morse court never reached the issue of actionable copying.

In 1961, the Second Circuit expressly rejected the inverse ratio rule in Arc Music Corporation v. Lee.32 On appeal, the plaintiff argued that the lower court had committed an error by not accepting the rule. In response, the court held that nothing like the inverse ratio rule even existed with respect to federal copyright claims:

In the federal copyright law we find no such principle. The evidence for [the inverse ratio rule’s] existence is meager in any event; it is asserted to be contained in generalized statements in a state decision dealing with appropriation of literary property. The court [in Golding]...did not assume, however, to be erecting a new principle of law, but only to justify the sufficiency of the evidence to support a jury verdict...We fear that counsel with that semantic
1. In Sid and Marty Krofft Television Productions, Inc. v. McDonald’s Corporation, McDonald’s commercials were alleged to have infringed upon the characters appearing in which children’s television series?
   A. Dr. Shrinker.
   B. Sigmund and the Sea Monsters.
   C. H.R. Pufnstuf.
   D. Land of the Lost.

2. When a plaintiff has established that a defendant has actually copied his or her work, the plaintiff does not need to show that the defendant’s work is substantially similar to the plaintiff’s work with regard to protectible expression.
   True.
   False.

3. In Goldberg v. R.K.O. Pictures, Inc., the Ninth Circuit held that when the evidence of access is strong, less proof of similarity may suffice to uphold a judgment of copyright infringement.
   True.
   False.

4. In applying the extrinsic test, unprotectible elements are generally disregarded.
   True.
   False.

5. In 1961, the Second Circuit in Arc Music Corporation v. Lee stated that:
   A. The inverse ratio rule is helpful in the right context.
   B. The inverse ratio rule’s roots stem from the comments of Judge Learned Hand.
   C. The inverse ratio rule should be applied in all copyright cases in which access has been shown.
   D. None of the above.

6. Copying can be established by circumstantial evidence.
   True.
   False.

7. Proof of access alone may sometimes establish actual copying.
   True.
   False.

8. In 1968, Nimmer on Copyright noted that:
   A. The inverse ratio rule was completely rejected by one court.
   B. A very high degree of similarity is required to dispense with proof of access.
   C. Clear and convincing evidence of access will not avoid the necessity of also proving substantial similarity.
   D. All of the above.

9. In Rice v. Fox Broadcasting Company, the Ninth Circuit found that the plaintiff’s evidence of access was strong enough to trigger the inverse ratio rule.
   True.
   False.

10. A “bare possibility” of viewing the plaintiff’s work is insufficient to establish access.
    True.
    False.

11. In Benay v. Warner Bros. Entertainment, Inc., the Ninth Circuit held that the plaintiffs did not show sufficient similarity to maintain their claim, in spite of the lower standard that applied because of the inverse ratio rule.
    True.
    False.

12. If the inverse ratio rule is applied in a given copyright case, it follows that the plaintiff’s copyright claim will survive summary judgment.
    True.
    False.

13. What television show appeared in a Ninth Circuit copyright case because it allegedly infringed on the plaintiff’s screenplay, The Funk Parlor?
    A. The Sopranos.
    B. Six Feet Under.
    C. Sex and the City.
    D. Dexter.

    True.
    False.

15. In Funky Films, Inc. v. Time Warner Entertainment Company, L.P., the Ninth Circuit held that general plot similarities are protected under copyright law.
    True.
    False.

16. The court in Morse v. Fields held that the plaintiff was not entitled to the benefit of the inverse ratio rule, even though the plaintiff made a showing that his article appeared in a national publication.
    True.
    False.

17. No amount of proof of access will suffice to show copying if there are no similarities between the protected expressions in the two works.
    True.
    False.

18. In 1968, Nimmer on Copyright followed the Second Circuit’s lead by expressly rejecting the inverse ratio rule.
    True.
    False.

19. The Ninth Circuit questioned the viability of the inverse ratio rule in:
    A. Novak v. Warner Bros. Pictures, LLC.
    C. Arc Music Corporation v. Lee.
    D. Shaw v. Lindheim.

20. The inverse ratio rule may have some limited viability in the Second Circuit.
    True.
    False.
proclivity natural to our profession have allowed themselves to be seduced by a superficially attractive apothegm which upon examination confuses more than it clarifies.

According to Arc Music Corporation, access will not make up for a lack of similarity, “and an undue stress upon that one feature can only confuse and even conceal this basic requirement.” Thus, within the Second Circuit, the inverse ratio rule as a mechanism for finding infringement was dealt a seemingly fatal blow. Nevertheless, the life of the inverse ratio rule was not completely extinguished. For example, it appeared to be resuscitated in the 1968 edition of Nimmer on Copyright—one of the leading copyright law treatises since its initial publication in 1963. In “The Effect of Access upon the Determination of Substantial Similarity,” a section of the 1968 edition, author Melville B. Nimmer wrote:

It has been noted in a prior section that evidence of striking similarity will sometimes permit a finding of copying without proof of access. It is obvious that the converse proposition is not equally valid. That is, clear and convincing evidence of access will not avoid the necessity of also proving substantial similarity since access without similarity cannot create an inference of copying. However, this so-called “Inverse Ratio Rule” although completely rejected by one court, would seem to have some limited validity. That is, since a very high degree of similarity is required in order to dispense with proof of access, it must logically follow that where proof of access is offered, the required degree of similarity may be somewhat less than would be necessary in the absence of such proof. This is not to say that a showing of substantial similarity may ever be avoided.

Nimmer did not cite Golding, or any case, in support of the notion that the inverse ratio rule lowered the quantum of proof necessary to show substantial similarity.

Later Developments in the Ninth Circuit

Then the Ninth Circuit, in 1977, offered its version of the rule in Sid and Marty Krofft Television Productions, Inc. v. McDonald’s Corporation. In this case, plaintiffs Sid and Marty Krofft alleged that McDonald’s McDonaldland commercials infringed the copyright in the characters appearing in the H.R. Pufnstuf children’s television series. The defendants admitted that they copied the idea of the plaintiffs’ television series but argued that the expression of the idea was too dissimilar for a finding of infringement. After reviewing representative samples of the defendants’ and the plaintiffs’ work, the Krofft court held that the two works were substantially similar.

Surprisingly, only after finding that the two works were substantially similar did the court address the issue of access, which was undisputed as a matter of fact. Notably, the court stated, “No amount of proof of access will suffice to show copying if there are no similarities.”

The court then proceeded to set forth its version of the inverse ratio rule as a means for lowering the threshold of proof required to show substantial similarity. The court noted that, in doing so, “This is not to say, however, that where clear and convincing evidence of access is presented, the quantum of proof required to show substantial similarity may not be lower than when access is shown merely by a preponderance of the evidence.”

The Krofft court cited Nimmer in support of its formulation of the inverse ratio rule. Ultimately, the court concluded that the degree of access present in the case justified a lower standard of proof to show substantial similarity—but the court candidly admitted that the lowered standard was “impossible to quantify.”

The Ninth Circuit did not address the inverse ratio rule again for approximately 10 years. While the Ninth Circuit in 1987 questioned the viability of the inverse ratio rule in Aliotti v. R. Dakin & Company, three years later it held in Shaw v. Lindheim that the rule was still alive. Nevertheless, although the Shaw court stated that the inverse ratio rule was germane and cited to Krofft, the court never explained how the rule actually should be applied.

The Ninth Circuit appeared to apply a different version of the inverse ratio rule in Metcalf v. Bochco, a 2002 decision. The plaintiffs sued for copyright infringement, alleging that the defendants’ television show infringed their treatment for a motion picture. The court commented that the plaintiffs’ case was “strengthened considerably by [the defendants’] concession of access to their works”—a concession that had been made for purposes of the defendants’ summary judgment motion. In light of the evidence of access, the court held that a trier of fact “could easily infer that the many similarities between plaintiffs’ scripts and defendants’ work were the result of copying, not mere coincidence.” Notably, the Metcalf court never used the phrase “inverse ratio rule” or otherwise set forth the specifics of the rule—namely, that strong evidence of access can lower the quantity of proof required for substantial similarity.

Since Metcalf, the inverse ratio rule has enjoyed little success in the Ninth Circuit. Indeed, post-Metcalf, the Ninth Circuit has not relied upon the inverse ratio rule as a basis for finding that infringement occurred based upon some lower measure of similarity.

For example, in Rice v. Fox Broadcasting Company, the Ninth Circuit found that the plaintiff’s evidence of access was not strong enough to trigger application of the inverse ratio rule. The Rice court noted that in cases applying the inverse ratio rule, the fact that the defendants had conceded access to the plaintiff’s copyrighted work was a promi-
In 2006, the plaintiff in Funky Films, Inc. v. Time Warner Entertainment Company, L.P., alleged that the HBO television series Six Feet Under infringed her screenplay The Funk Parlour. The Ninth Circuit concluded that, while the two works shared certain plot similarities, these were not protected under copyright law. Notably, for purposes of the summary judgment motion, the district court assumed that the defendants had access to the plaintiff’s script.

The plaintiff argued that she should have been given an opportunity to satisfy a lower burden of proof under the inverse ratio rule. But the Ninth Circuit did not agree that the plaintiff’s invocation of the inverse ratio rule required the district court’s decision to be reversed. Borrowing a line from Krofft, the court reasoned that “[n]o amount of proof of access will suffice to show copying if there are no similarities.” The court must have been referring to the lack of protectible similarities, because the court’s opinion is littered with numerous examples of nonprotectible similarities between the two works at issue.

Later in 2010, the Ninth Circuit in Benay v. Warner Bros. Entertainment, Inc., assumed for the purpose of its analysis of a claim of copyright infringement that the inverse ratio rule applied to lower the burden on the plaintiffs to show similarity. In spite of the lower standard, the court held that the plaintiffs still did not show sufficient similarity to maintain their claim.

In Novak v. Warner Bros. Pictures, LLC, an unpublished opinion also issued last year, the Ninth Circuit once again held that the inverse ratio rule did not help the plaintiffs because there were no similarities of protected expression in the two works. Moreover, the court explained that even under a relaxed standard, the requisite similarities must be “concrete and or articulable” to satisfy the extrinsic test. Ultimately, the court rejected the plaintiffs’ copyright infringement claim, finding that the only articulable similarities between the two works consisted of unprotected elements.

The Second Circuit got it right. The Ninth Circuit appears to be struggling to get rid of the inverse ratio rule once and for all. Courts within the Second Circuit have made clear that the inverse ratio rule has no bearing upon the determination of whether or not two works are substantially similar in protectible expression. Indeed, the Second Circuit has maintained its rejection of the inverse ratio rule with respect to substantial similarity of protectible expression. Thus, when actual copying is either admitted or assumed, the inverse ratio rule “is irrelevant.”

As the Second Circuit has noted, the level of access a defendant may have had to the

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plaintiff's work can have no logical effect on whether two works—compared side by side—are substantially similar in their protectible elements. This is because no amount of access can make nonprotectible elements magically become protectible.

The Ninth Circuit recognized this principle in 2010, albeit in the unpublished Novak opinion. It also appears to have implicitly recognized this principle in Funky Films and Benay, in which the court assumed access yet found no substantial similarity between the works at issue—notwithstanding the numerous, nonprotectible elements shared by those works.

Even if the Ninth Circuit were to employ the inverse ratio rule, that decision would not necessarily make the rule any more meaningful than it is now. To date, it is not clear how much access is required to trigger the application of the rule in the first instance. Does the evidence have to be “strong,” or does it need to be “clear and convincing,” as the Krofft court suggested in 1977?

Moreover, as recently recognized by a district court in the Central District of California, even when a high degree of access is shown, “[i]t is not clear just how much less the showing of substantial similarity need be.” Assuming a high degree of access, how much similarity would the plaintiff need to show under the inverse ratio rule? Is it still substantial similarity, or something less?

At bottom, there is no logical role for the inverse ratio rule in the Ninth Circuit’s extrinsic test. Moreover, the Ninth Circuit already has recognized that the inverse ratio rule has no role in the intrinsic test. The Second Circuit was correct 50 years ago when it bluntly stated that the inverse ratio rule is irrelevant to the question of whether two works are substantially similar in their protectible elements. It is time for the Ninth Circuit to catch up.

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1 Feist Publ’s, Inc. v. Rural Tel. Serv. Co., 499 U.S. 340, 361 (1991); Kouf v. Walt Disney Pictures Television, 16 F. 3d 1042, 1044 n.2 (9th Cir. 1994).
2 Funky Films, Inc. v. Time Warner Entm’t Co., L.P., 462 F. 3d 1072, 1076 (9th Cir. 2006) (citations omitted).
3 Three Boys Music Corp. v. Bolton, 212 F. 3d 477, 482 (9th Cir. 2000).
5 Funky Films, 462 F. 3d at 1077.
6 Id. (citing Kouf, 16 F. 3d at 1045).
7 Id.
9 Cavalier, 297 F. 3d at 822 (quoting Williams v. Crichton, 84 F. 3d 581, 588 (2d Cir. 1996)).
10 Id. (quoting Kouf, 16 F. 3d at 1045).
See Narell v. Freeman, 872 F. 2d 907, 910-13 (9th Cir. 1989) (Despite the defendant’s admission of copying, “no reasonable reader could conclude that the works are substantially similar.”); Idema v. Dreamworks, Inc., 162 F. Supp. 2d 1129, 1143, 1171 n.44, 1174-87 (C.D. Cal. 2001) (Even assuming the defendants “made ‘use’ of Plaintiff’s works as source materials,” there was no substantial similarity as a matter of law.); Bensbargains.net, LLC v. XPBargains.com, No. 06-CV-1445, 2007 U.S. Dist. LEXIS 60544, at *9 (S.D. Cal. Aug. 16, 2007) (The plaintiff must still prove substantial similarity “regardless of how strong its evidence is that Defendants in fact copied from [the plaintiff’s work].”); See v. Durang, 711 F. 2d 141, 142-43 (9th Cir. 1983) (Even actual copying is irrelevant where no reasonable person could find any substantial similarity between the plaintiff’s and the defendant’s works.).


Id. at 537.

Id. at 538 (citations omitted).


Id. at 693.

Id. at 698.

Id. at 695 (citing Shipman v. R.K.O. Radio Pictures, Inc., 100 F. 2d 533, 538 (2d Cir. 1938), and O’Rourke, 44 F. Supp. at 482).

Id.

Id. at 698.

Id. at 699.

Id. at 701.


Id. at 66 (citing Golding, 35 Cal. 2d at 695).

Arc Music Corp. v. Lee, 296 F. 2d 186 (2d Cir. 1961).

Id. at 188 (citations omitted).

However, the inverse ratio rule may have some limited viability in the Second Circuit. It may apply to the separate inquiry of whether or not there has been actual copying, as opposed to the question of whether or not two works are substantially similar. See the Sheldon Abend Revocable Trust v. Spielberg, No. 08 Civ. 7810, 2010 U.S. Dist. LEXIS 99080, at *8 n.3 (S.D. N.Y. Sept. 21, 2010); see also Green v. Lindsey, 885 F. Supp. 469, 480 (S.D. N.Y. 1992).

2 Melville B. Nimmer, Nimmer on Copyright §143.4, at 634 (1968).

Sid & Marty Krofft Television Prods., Inc. v. McDonald’s Corp., 562 F. 2d 1157 (9th Cir. 1977).

Benay v. Warner Bros. Entm’t, Inc., 607 F. 3d 620, 625 (9th Cir. 2010).


Id. at *5-6.


A Slice of Pie Prods., LLC v. Wayans Bros. Entm’t, 487 F. Supp. 2d 41, 47 n.4 (D. Conn. 2007) (citing Arc Music Corp. v. Lee, 296 F. 2d 186 (2d Cir. 1961)).


Hollywood contracts are complicated and convoluted, especially when it comes to profit participation provisions. Thanks to a trio of recent cases that exposed the arcane world of Hollywood deal making and studio accounting, profit participation provisions are once again in the spotlight’s glare. The jury verdicts in *Celador International, Ltd. v. The Walt Disney Company*,1 *Don Johnson Productions, Inc. v. Rysher Entertainment, Inc.*,2 and *Alan Ladd, Jr. v. Warner Bros. Entertainment, Inc.*,3 dealt Hollywood’s media conglomerates unanticipated and unwelcome setbacks. In each case, the plaintiff successfully sued to enforce a contractual profit participation right and challenged some of Hollywood’s most controversial accounting and financial practices.

It often is the case that the contracts between studios or networks and the parties who provide intellectual property to them, such as producers, writers, directors and actors, include provisions under which the profits derived from distribution of the completed content are to be shared among the parties to the contract. However, as a result of the opaque accounting methods used in Hollywood—often referred to as Hollywood accounting4—profit participants typically do not receive any share of the promised profits, even for successful projects. In fact, the accountings generated by studios and networks typically reflect that popular, highly successful films and long-running television series produce financial returns for their owners that would be considered ruinous in any other industry. Challenges to these improbable accountings, however, have done little to effect any change in the way studios and networks do business.

Hollywood contracts generally are as incoherent as the tax code. Because of the immense inequality in bargaining power that exists between today’s media conglomerates (which own the major studios and networks) and talent and small production companies, studios and networks usually dictate contract

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terms. As a result, contracts typically are a mélange of vague terms, conflicting references, and provisions that have been copied from other contracts, resulting in documents that are needlessly long, disjointed, and unintelligible, and that require years of costly litigation to interpret. Only experienced lawyers whose clients have tremendous leverage in the entertainment community are able to negotiate provisions that better protect their clients’ profit participation rights.

The accounting that studios and networks provide to profit participants often are confusing, vague, and difficult to reconcile. Challenging studio accountants either through audits or litigation is time-consuming and expensive and may be beyond the financial means of the profit participant. On occasion, however, lawsuits are prosecuted by profit participants who have the means and clout to do so.

Typically, these lawsuits include allegations that, to some degree or another, media conglomerates are vertically integrated. Vertical integration allows affiliated entities to participate in self-dealing, which precludes profit participants from sharing in a project’s success. Vertical integration is a phenomenon resulting from the 1995 repeal of the Network Financial Interest and Syndication Rules, popularly known as the Fin-Syn rules. The Fin-Syn rules were an attempt to prevent studios and networks from consolidating their control over the ownership, production, broadcast, distribution, syndication, licensing, and merchandising of the properties they acquired.

After the repeal of the Fin-Syn rules, large media conglomerates were formed, through which networks and studios now control the creative process from development through distribution. Vertical integration also allows conglomerates to engage in accounting practices by which a property’s revenues may be manipulated to ensure that the property never generates profits that must be shared outside the conglomerate. For example, a studio or network that has contractual profit participation obligations may license a motion picture project or television show to its affiliated cable network at a below-market license fee so that the cable network receives most of the revenue (which it is not required to share with profit participants), thus reducing or eliminating entirely any distribution revenue to be shared by the studio or network with the profit participant.

Historically, Hollywood has chosen to settle profit participation disputes rather than divulge to the public (or, more importantly, to a jury) the inner workings of the conglomerates that control the media. But in *Celador, Johnson, and Ladd*, the studios and networks abandoned this strategy and instead attempted to justify to the courts and to juries the sweetheart deals and self-dealing that goes on behind the success of popular films and television shows. Their efforts failed.

**Recent Cases**

In 1998, a British company, Celador International, Ltd., developed a unique concept for prime time television: a game show in which the contestants, who played for ever-increasing amounts of money, could ask for help. The show premiered in the United Kingdom and was an overnight sensation. Soon, the show was being licensed worldwide, and ABC aggressively negotiated to obtain the North American rights to what became *Who Wants to Be a Millionaire?*

The contract that Celador signed with ABC and its affiliate Buena Vista Television provided that Celador was entitled to 50 percent of the “defined contingent compensation” derived by ABC and Buena Vista Television from the exploitation of any pilot and series produced under the contract. *Who Wants to Be a Millionaire?* debuted on ABC in August 1999 and, as in Europe, was a runaway success. The show was credited with taking ABC from fourth to first in network rankings and for reigniting the prime time game show and reality show genres. Yet, after three years on ABC and years in syndication, and after generating hundreds of millions of dollars in revenue for ABC and Buena Vista Television, the show—according to accountings given to Celador—was running at a loss. At the time of trial, 11 years after the show’s debut, Celador had not received any profit participation payments other than the initial, non-recoupable advances against contingent compensation that ABC and Buena Vista Television had agreed to pay when the contract was signed.

Celador sued the Walt Disney Company, ABC, Buena Vista Television, and Valleycrest Productions, Ltd. (collectively Disney) to collect 50 percent of the profits that would have been generated if a fair-market license fee had been paid for the network broadcast of the long-running television game show. Celador also challenged the expense deductions taken against the show’s merchandising revenue. On Celador’s claims for breach of contract and breach of the implied covenant of good faith and fair dealing, the jury awarded damages of over $269 million. In September 2010, an additional $50 million in prejudgment interest was assessed, for a total judgment of $319 million.

The television series *Nash Bridges* aired on CBS from 1996 through 2001. It was a highly rated series and entered syndication in 1999. Actor Don Johnson co-conceived, starred in, and produced the series pursuant to an agreement with Rysher Entertainment, Inc. Due to the success of his earlier series, *Miami Vice*, Johnson enjoyed tremendous leverage in the entertainment industry at the time he negotiated his contract with Rysher. As a result, he was able to negotiate a deal with Rysher by which his production company would acquire a 50 percent ownership of the series’ copyright if it was bought for 66 episodes and became eligible for syndication.

Notwithstanding the success of the series, and after delivering 122 completed episodes of *Nash Bridges* for distribution, Don Johnson Productions had been paid nothing as co-owner of the copyright. Although the network accountings for the series reflected that *Nash Bridges* had generated hundreds of millions in gross revenues, according to the network it allegedly still was running at a deficit of about $150 million in 2009.

Johnson sued to affirm his 50 percent co-ownership of the copyright in the *Nash Bridges* television series and his right to 50 percent of the show’s profits. The jury found in his favor and awarded him $23.2 million in damages owed to date. The show continues to run in syndication. In September 2010, the trial judge awarded Johnson an additional $28 million in prejudgment interest, bringing the total judgment to $51.2 million.

In a suit filed against Warner Bros., Alan Ladd Jr. and several production companies challenged the industry’s practice of “straight-lining,” by which studios license film packages to broadcasters or cable companies, valuing every feature film in the package the same, regardless of the value of the film to the broadcaster or channel. The suit followed an audit that Ladd initiated when he learned that a coinvestor in the film *Blade Runner* was receiving payments from Warner Bros., even though Warner Bros. had told Ladd the movie was unprofitable.

Ladd sued to collect his share of licensing fees that would have been generated if his films had been properly valued. Evidence at trial disclosed that, although Warner Bros. assigned each movie in a licensing package a grade of A, B, or C, the studio allocated the same proportion of the license fee to each title in the package, irrespective of the film’s letter grade. The jury found that during the four years preceding the filing of the suit, Warner Bros. had thereby undervalued Ladd’s films, which were all rated either A or B. Based on Ladd’s contracts, the jury concluded that Ladd should have received an additional $3,190,625 in profit participation payments.

On May 25, 2010, the California Court of Appeal affirmed the jury’s verdict. In doing so, the appellate court rejected as meritless the attempts of Warner Bros. to justify straight-lining, which it characterized as “the
buyer made me do it” defense.14 The court also rejected the argument of Warner Bros. that because straight-lining was a common industry practice, it could not constitute a breach of the implied covenant of good faith and fair dealing. The court held that “even if straight-lining were a common practice, it would not absolve Warner of its duty to Ladd, as a profit participant, to fairly allocate fees derived from licensing packages.”15

**Contract Language**

The outcome of these disputes was attributable, in part, to the cryptic and confusing language used in studio and network contracts. Indeed, these days, the word “profit” rarely appears in profit participation agreements. Instead, the contracts employ terms such as “contingent compensation,” “defined contingent compensation,” “adjusted defined receipts,” or some other similar phrase.16 The amounts owed pursuant to these vague terms are calculated by equally obscure accounting methods, with a typical result being that hugely successful shows inexplicably generate large deficits year after year, leaving profit participants with no profits whatsoever.22

For example, in the Celador trial, an incomplete, two-page exhibit describes “defined contingent compensation” in the contract among Celador, ABC, and Buena Vista Television. The description states, in part:

For purposes of Defined Contingent Compensation, Participant agrees that words and phrases used in connection with Participant’s contingent participation, if any, are not intended to correspond to any conventional understanding or dictionary definition of such words and terms, whether used in the entertainment industry or any other industry or business and are not intended to correspond in any way to generally accepted accounting principles (“GAAP”), or any other meanings thereof, which may be associated with the practices of accounting or auditing.17

So, according to the contract, the words used to describe Celador’s right to receive “defined contingent compensation” were not to be understood to mean what they generally do mean, either in the ordinary sense or in a financial context. What then was “defined contingent compensation” supposed to mean? According to Disney, it was not supposed to mean profit.

Disney filed a motion in limine to preclude Celador from using the term “profits” at trial and from contending that it was entitled to share in Disney’s “profits.” Disney argued that “profit” was a financial term that had a specific meaning and that because Disney did not calculate Celador’s share of “defined contingent contribution” according to generally accepted accounting principles, Celador’s right to share in “defined contingent compensation” could not be referred to as a right to share in profits. Disney also contended that the use of the word “profits” by Celador at trial would be inaccurate, prejudicial, confusing, and misleading to the jury.18 The motion was denied after Celador presented evidence that Disney’s current and former employees, as well as its own expert, commonly referred to “defined contingent compensation” as profits.19

Understandably, much of the evidence presented at trial was aimed at discerning the intentions of the parties at the time of contracting, understanding what “defined contingent compensation” encompassed, and determining how that compensation was supposed to be calculated. Ultimately, it was left up to the jury to interpret the contract, and the outcome did not favor Disney.20

Similarly, in Johnson, the contract provided that Don Johnson Productions was entitled to 50 percent of “all gross receipts,” which was defined as receipts to Rysker and its affiliates after deductions for distribution fees, distribution costs, direct production costs, and interest “on the net deficited portion of the direct production costs.” Johnson alleged that this contract provision was designed to make it impossible for a show ever to turn a net profit.

The confusion created by the use of uncertain terminology and vague definitions in profit participation contracts is compounded by the obscurity of the accounting methods used to calculate what is owed to a profit participant. As one industry insider has stated, Hollywood accounting can generate different results “depending on who’s asking,” and accounting methods differ depending on the result sought.21 For example, one method may be used to calculate profits when accounting to profit participants and another when accounting for tax purposes. Not surprisingly, when calculating a project’s profits for the purpose of paying profit participants, the goal often is to report reduced profits or no profits whatsoever.22

Profit participants also typically allege that in addition to improper accounting methods, the television distribution deals struck by the studios and networks are the result of self-dealing and sweetheart deals between affiliated entities. These deals often involve preferential and greatly diminished license fees being charged for the broadcast and syndication of the acquired properties—thus reducing, if not eliminating altogether, the profits to be shared with profit participants. The deals also may involve redistributing contract rights among affiliated entities,
thus diverting revenue from the profit participation calculations. The evidence presented at the Celador trial is illustrative of the type of intracompany dealings that can deprive a profit participant from sharing in a project's success.

In the 1999 contract with Celador, ABC and Buena Vista Television jointly acquired all rights to *Who Wants to Be a Millionaire?* The two acquired the rights to produce, broadcast, and syndicate the show throughout North America. Yet, shortly after the contract was signed, ABC, Buena Vista, and a wholly owned production company called Valleycrest Productions, Ltd., engaged in a series of partially documented, unsigned, or allegedly oral assignments among themselves that were not disclosed to Celador. Through these assignments, ABC and Buena Vista Television supposedly transferred all the contract rights they acquired from Celador to a third-party affiliate, either Valleycrest Productions or another affiliate, Buena Vista Productions.

After that initial transfer, further assignments allegedly occurred among these affiliates, resulting in a perpetual network license being issued back to ABC—even though ABC originally had acquired the right to broadcast the series on the network through its contract with Celador. The network license supposedly issued to ABC by one of these affiliates provided that the fee paid by ABC to Buena Vista Television for the broadcast rights to *Who Wants to Be a Millionaire?* always would be equal to Buena Vista Television's costs of producing the show. Disney also contended that “defined contingent compensation,” as used in the contract, only contended that “defined contingent compensation,” as used in the contract, only contended that “defined contingent compensation,” as used in the contract, only contended that “defined contingent compensation,” as used in the contract, only contended that “defined contingent compensation,” as used in the contract, only contended that “defined contingent compensation,” as used in the contract, only contended that "defined contingent compensation," as used in the contract, only referred to Buena Vista Television’s revenues and not ABC’s.

All this maneuvering deprived Celador of its share of the immense revenue that the show generated. According to Disney’s accountings, although the show has been on the air continuously in the United States since 1999 and has generated hundreds of millions of dollars of revenue for ABC and Buena Vista Television, *Who Wants to Be a Millionaire?* has produced $70 million in losses, continues to go deeper and deeper into the red with each episode and, so far, no “defined contingent compensation” is owed to Celador.

The *Celador and Johnson* verdicts make clear that juries find it difficult to believe that long-running, successful television shows generate nothing but losses for their owners. The studios’ traditional unwillingness to explain their accounting methods, and the costly, lengthy, difficult, and frustrating process of auditing participation statements, further escalates the general skepticism surrounding studio and network accountings. Frequently, audits create more questions than they answer.

There are exceptional cases in which lawyers negotiate language that anticipates and protects against these types of studio and network maneuvers. As an example, the contract between Alan Alda and Twentieth Century Fox contained the following provision: “If and to the extent Fox makes agreements in respect of exploitation of [M*A*S*H] with any affiliated entity which is a so-called ‘end user’ such as, by way of example only, [Fox Broadcasting Company] or the Fox television stations, the income of such end user shall not be deemed gross receipts hereunder, but Fox shall establish, fair, just and equitable market rates, arms-length prices in such dealings, which shall be created on a reasonable and empirically justifiable basis.”

In response to the vertical integration claims, some studios and networks include contract provisions that characterize transactions with affiliates as comparatively fair. For example, a Disney provision allows Disney affiliates to self-deal, requires the owner of the property being sold to prove that a specific deal is unfair, and, if the owner succeeds in doing so, limits the owner’s damages. The provision further reads:

In addition, Owner acknowledges and agrees that any agreement or other arrangement by ABC/BVT with an Affiliate or Related Party regarding the Exploitation Rights shall be conclusively presumed to be fair, reasonable and unobjectionable unless Owner shall establish that such agreement or other arrangement is on non-unique financial terms which, taken as a whole, are materially less favorable economica...
November 24, 2009

Jack Trimarco
Jack Trimarco & Assoc.
9454 Wilshire Blvd., 6th Floor
Beverly Hills, CA 90212

Dear Jack:

I am writing this letter to express my gratitude for your tremendous and outstanding expertise in assisting in a date rape by drug investigation which focused on my client (a former NBA player).

Your testing of my client and preparing him for the investigation and interview by the Huntington Beach Police Department led to the police department declining to even proceed to the District Attorney’s Office with the case. Your testing, procedures, and reputation led the Huntington Beach Police Department to conclude that the “victim” was lying and your conclusion that the “defendant” was telling the truth was correct. The cost of your test, literally saved my client thousands of dollars in attorney fees and months, if not, a year or so of aggravation.

On behalf of my client, and my office I want to thank you for your assistance in the matter.

Yours truly,

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Social Media and the Law

ON THURSDAY, MAY 19, the Los Angeles County Bar Association will host a panel of experienced technology law practitioners and regulators who will cut through the hype over social media risks. Moderated by Tanya L. Forsheit, speakers Alan L. Friel, Catherine C. Harrington-McBride, and Jennifer Mardosz will identify the laws affecting employee and consumer use of social media, analyze recent guidance from the FTC, discuss proposed legislation on online behavioral marketing, cover practical strategies for organizations to mitigate the risks associated with social media, outline key components of effective social media policies, and explore a hypothetical situation. The program will begin at noon at the Los Angeles County Bar Association, 1055 West 7th Street, 27th floor, Downtown. Parking is available at 1055 West 7th and nearby parking lots. This program is also available as a live Webcast. The registration code number is 011237. The prices below include the meal.

$20—CLE+Plus member
$55—Small and Solo Division member
$75—LACBA member
$105—all others
2 CLE hours

43rd Annual Family Law Symposium

ON SATURDAY, MAY 7, the Family Law Section and the Los Angeles Superior Court will host the 43rd Annual Family Law Symposium. Family law judicial officers and attorneys will offer a comprehensive update on topics relevant to the practice of family law. Areas under discussion will include due process, the testimony of children, social networking sites, Elkins and evolving procedures, how to streamline cases, and recent developments and opinions. Registration and continental breakfast will begin at 8 A.M., with the program beginning at 8:30. The registration code number is 010977. The prices below include the meals.

$105—CLE+Plus member
$160—Barristers
$210—Family Law Section member
$235—LACBA member
$270—at-the-door registrant
6.25 CLE hours, with family law legal specialization credit

Asset Protection in a Troubled Economy

ON WEDNESDAY, MAY 18, the Association and the Small and Solo Division will host a program covering the practical aspects of asset protection planning. Speaker Jacob Stein will teach those who attend everything they need to know about protecting assets from plaintiffs and creditors. Topics will include specific planning solutions, community property, business entities, and domestic and foreign trusts. Special emphasis will be placed on protecting assets in a troubled economy, including protection from lenders holding personal guarantees.

The seminar will cover common assets, including houses, bank and brokerage accounts, rental real estate, businesses, professional practices, and retirement plans. Course materials serve as a treatise on asset protection as well as an exhaustive reference source. The program will take place at the Los Angeles County Bar Association, 1055 West 7th Street, 27th floor, Downtown. Parking is available at 1055 West 7th and nearby parking lots. On-site registration will begin at 4 P.M., with the program continuing from 4:30 to 8:15. This seminar is also available as a live Webcast. The registration code number is 011245.

$65—CLE+Plus member
$80—Small and Solo Division member
$105—LACBA member
$135—all others
3.5 CLE hours

The Los Angeles County Bar Association is a State Bar of California MCLE approved provider. To register for the programs listed on this page, please call the Member Service Department at (213) 896-6560 or visit the Association Web site at http://calendar.lacba.org/where you will find a full listing of this month’s Association programs.
Is a ZIP Code Really Personal Identification Information?

THROUGH A CREATIVE BUT TORTURED ANALYSIS, the California Supreme Court recently ruled in *Pineda v. Williams-Sonoma Stores, Inc.*,1 that a ZIP code constitutes “personal identification information” (PII) under the state’s Song-Beverly Credit Card Act of 1971.2 The act defines PII as “information concerning the cardholder, other than information set forth on the credit card, and including, but not limited to, the card holder’s address and telephone number.” Based upon that definition, the court concluded that “requesting and recording a cardholder’s ZIP code” as part of a credit card transaction is generally prohibited. Although well intentioned, this flawed ruling could lead to unintended and odious consequences, including invasions of privacy and a loss of consumer protection that the act was originally intended to prevent.

In *Pineda*, a cashier at a Williams-Sonoma store in California asked for the plaintiff’s ZIP code during a credit card transaction. Pineda provided her ZIP code assuming it was necessary to complete the transaction. Unknown to Pineda, Williams-Sonoma used her name and zip code to conduct a reverse lookup in a third-party database and stored the resulting address for later use in direct marketing. Pineda learned what occurred and filed a class action lawsuit, alleging a violation of the Song-Beverly Act and California’s Unfair Competition law.3

Before *Pineda*, ZIP codes were not considered to be PII. In fact, the California Court of Appeal in *Party City Corporation v. Superior Court* held that a “five-digit ZIP code is not, as a matter of law, that kind of personalized or individual identification information” that the statute was intended to protect.4

But in *Pineda*, the supreme court rejected *Party City* and interpreted PII in an overly broad way to include any information concerning the cardholder. The court reasoned that since a cardholder’s ZIP code refers to the area where a cardholder lives or works, it would qualify as information that relates to the cardholder. The court further concluded—and this is where the court takes a leap in logic of Olympic proportions—that since a ZIP code is a part of the address, the statute “should be construed as encompassing not only a complete address but also its components.” Using this same logic, it could be argued that asking for and recording the cardholder’s state or country of residence should be considered PII as well.

That is just part of the slippery slope created by *Pineda*. Lost in all the legal gymnastics is the undeniable fact that knowing a person’s ZIP code, without more, does not in any significant way identify that person. Simply put, a ZIP code by itself is neither an address nor PII.

In reaching its conclusions, the court relied heavily on its review of the legislative history of the act. The court found that the California Legislature “intended to provide robust consumer protections by prohibiting retailers from soliciting and recording information about the cardholder that is unnecessary to the credit card transaction.” The court also concluded that the creation of the statute was motivated by retailers acquiring unnecessary PII to build in-house marketing lists or sell the information to third parties.

In fact, prohibiting the collection of ZIP codes may actually lessen consumer privacy and protection. The court failed to consider the less nefarious—and very beneficial—uses of a consumer’s ZIP code, such as security and fraud prevention. While there is a general reference to “positive identification” under the “exceptions” section of the act, the act does not clearly and directly delineate the parameters of permissible uses of PII (assuming *arguendo* that ZIP code information is PII) for security purposes. In *Saulic v. Symantec*,5 the Central District of California recently held that the act does not apply to online transactions because it is necessary to collect PII for security purposes. However, the federal district court opinion is not binding on the California courts.

As a result, numerous California retailers, including thousands of gas stations that request and record consumer ZIP code information for security purposes, are violating the act and are already being sued in class action lawsuits. Also troubling is the strict liability the act imposes and the lack of analysis of exactly how the collection of ZIP codes is of potential harm to the consumer. Moreover, the opinion fails to explain how marketing to a publicly available address is an egregious breach of privacy or even a cause for concern.

Businesses that collect and record ZIP codes are now subject to a fine of $250 for the first violation and up to $1,000 for each subsequent violation. Not surprisingly, within days of the court’s ruling, dozens of class action lawsuits were filed. This decision will cost businesses millions of dollars in litigation costs and may end up hurting consumers by weakening security and fraud prevention measures.

There is an ongoing debate concerning what constitutes PII in the online world. For example, should completely anonymous information such as a computer’s IP address be considered PII? The holding in *Pineda* is likely to skew that privacy debate as well.

Although well intentioned, this flawed ruling could lead to unintended and odious consequences.

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2 CIVIL CODE §§1747 et seq.
3 BUS. & PROF. CODE §§17200 et seq

Scott Barlow is the vice president and general counsel of ValueClick, Inc., and a former trial lawyer.
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