HERRICK

New York Office

2 Park Avenue

New York, New York 10016

Phone: (212) 592-1400

Fax: (212) 592-1500

Princeton Office

210 Carnegie Center

Princeton, New Jersey 08540

Phone: (609) 452-3800

Fax: (609) 520-9095

Newark Office

One Gateway Center

Newark, New Jersey 07102

Phone: (973) 274-2000

Fax: (973) 274-2500

Attorney Advertising

www.herrick.com

HERRICK QUARTERLY SPORTS UPDATE SUMMER 2010

THE HERRICK ADVANTAGE

Keeping the sports industry informed. Herrick will host a seminar entitled "The Business of Minor League Sports" to address issues involving acquisitions of teams, stadium strategies, business models, programming, media and sponsorships and franchise values. Panelists include Steve Horowitz of Inner Circle Sports, Brad Kwong of Northern Lights Hockey, LLC, Art Matin of Mandalay Baseball, Bobby Sharma of NBA Development League, and Irwin Kishner. Matthew Pace will moderate. Registration will be held from 8:00 am to 8:30 am and the seminar will run from 8:30 am to 10:00 am. For more information on this event, please click here.

1. Sponsors Beware: Collective Bargaining Agreement Negotiations May Affect You

The threat of a work stoppage in a professional sports league alarms—or at least should alarm—corporate sponsors. Many of America's leading corporate brands face this threat as the National Football League (NFL) continues to negotiate terms of its next collective bargaining agreement (CBA) with the players' union. A failure to agree to a new CBA may lead to a lockout or strike prior to the 2011 football season, severely impacting any previously negotiated rights between sponsors and the NFL and/or its member teams.

The down economy continues to impact revenues, as do increased costs for infrastructure projects such as new stadiums, the costs of international ventures, and decreasing sponsorship dollars. The decision as to who—the NFL or its players—should primarily shoulder this burden remains a major point of contention, and NFL Commissioner Roger Goodell has gone so far as to say that the league's owners "regret" the last CBA, signed in 2006. In actions that illustrate the league's acknowledgment of the economic climate, Commissioner Goodell took a 20 percent pay cut and laid off 169 NFL employees.

If negotiations fail, current NFL sponsors may be in trouble. The potential for a work stoppage impacts the sponsors' significant investments in assets, such as franchise venue naming rights or acting as a corporate partner in a particular sponsorship category. Sponsors involved in such arrangements—and those considering them—should be aware of the repercussions of a work stoppage, as their rights would be severely impacted.

A work stoppage caused by a strike or a lockout would likely constitute a "force majeure" event under many sponsorship agreements. Force majeure is an event or effect that can be neither anticipated nor controlled, including acts of nature (e.g., floods and hurricanes) and acts of people (e.g., riots, strikes and wars). If a strike or lockout does occur, it may suspend any obligations owed by a sponsor under the sponsorship agreement until resolution of the labor strife.

However, in a recent legal filing, the players' union brought to light the structure of the NFL's television contracts—a guaranteed $4 billion in television revenues, regardless of whether any football is played. The union argued that even in the event of a lockout, the guaranteed television revenues combined with the elimination of $4.4 billion in player

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salaries would create a profitable 2011 season for the owners. In its legal filing, the union asked that the league put all television money in escrow instead of distributing it during a lockout, allowing the union significant leverage, since the owners would be forced to find other funds to make interest payments, stadium payments and other bills that continue to accrue.

If you are involved in sponsorship arrangements with the NFL or any of its member teams, you should monitor this situation carefully. Sponsors need to review the terms of any NFL-related sponsorship agreements and be aware of any contingencies or remedies provided in their agreements in the event of a work stoppage.

2. Online Piracy: Why Buy the Cow If You Can Get the Milk for Free?

Why pay for the game when you can watch it online for free? Free online sharing crippled the music industry and threatens to wreak havoc on the sports world. The streaming of pirated live sports broadcasts causes companies to lose revenue—particularly companies with business models like boxing promoters or mixed martial arts leagues, which make their money by selling the event itself via pay-per-view. Pirating of pay-per-view events results in losses of tens of millions of dollars each year. Sports and entertainment companies need to be increasingly vigilant, especially in light of the rapidly developing and inexpensive technology, and aware of the tools available to protect their content. Content providers should also seek to offer their events via different means, where possible, as a way to deter pirates.

- **Offer alternatives to piracy**. Recently, CBS Sports and the NCAA attempted to combat piracy by allowing a set number of users to log on to a website and stream games on demand during the NCAA men's basketball tournament. But since the site operated on a "first come, first served" basis, it left many without a legally free option, creating an opportunity for the pirates.

  In an innovative step, Major League Baseball recently struck a deal with Sony, marking the first distribution of live sports through a videogame console. The deal makes the MLB.tv online game package available on PlayStation 3 consoles through the PlayStation Network. The console will function like a digital video recorder allowing viewers to pause, rewind and fast forward. However, viewers will still be unable to watch live games of teams in their local market due to local blackout rules imposed by MLB. While not preventing piracy, innovations like these provide consumers with legal alternatives to illegally streaming websites.

- **Fight piracy directly**. In addition to providing alternatives, content providers should be aware of steps they can take to combat piracy directly, both against illegal sites and the companies that host them. The Digital Millennium Copyright Act (DMCA) offers guidelines for content providers serving takedown notices to hosts of illegal websites. A takedown notice, which is a notice of infringement, identifies the infringing content and instructs the service provider to remove it. A service provider (e.g., GoDaddy) may be held liable for monetary relief, and may be subject to injunctive or other equitable remedies, if after notification the service provider fails to expeditiously remove or disable access to infringing material.

  When possible, content providers should also take direct action against the proprietors of websites that illegally distribute their content. A cease and desist letter pointing out the legal consequences of illegal streaming can be effective in

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> stopping pirates; provided that the infringer can be located, which is often difficult as many pirates are located in foreign countries. In crafting such letters, content providers can look to the United States Federal Communications Act, which prohibits the interception, receiving, or the assisting of such interception or receipt, of any communication service, including cable and satellite broadcasts, unless specifically authorized to do so, or as otherwise specifically authorized by law. Persons who willfully violate the law may be liable for criminal fines up to $50,000 and imprisonment up to two years per occurrence. In addition, an aggrieved party (i.e., the content provider) has a private right of action that can result in the award of actual damages plus statutory damages up to $60,000.

Content providers need to be aware of their rights and should develop procedures to stop pirates in advance of events when possible. When planning a significant sporting event, content providers can take the initiative by providing advance notice under the United States Federal Communications Act to known pirates, to the extent they can be located, and the companies that host them, rather than waiting until after the event when revenue has already been lost.

3. FTC Clarifies Rules on Blogging and Endorsements

The Federal Trade Commission (FTC) recently revised the guidance it gives to advertisers on how to ensure that endorsements and advertisements are in line with Section 5 FTC Act (15 U.S.C. 45). The "Guides Concerning the Use of Endorsements and Testimonials in Advertising," which address endorsements by consumers, experts, entities and celebrities, as well as the disclosure of important connections between advertisers and endorsers, were last updated in 1980. The revised Guides reflect FTC case law and make it clear that celebrities and bloggers have a duty to disclose their relationship with advertisers when making endorsements outside the traditional ads, such as talk shows or in social media outlets. The Guides also clearly state that both advertisers and endorsers may be liable for false or unsubstantiated claims made in an endorsement—or for failure to disclose material connections between advertisers and endorsers. These revisions are of particular concern to advertisers and sponsors who use athletes and other celebrities to pitch their products, as well as the individual athletes and celebrities who blog to endorse products.

The Guide states that "when there exists a connection between the endorser and the seller of the advertised product that might materially affect the weight or credibility of the endorsement (i.e., the connection is not reasonably expected by the audience), such connection must be fully disclosed." The Guide defines "endorsements" as receipt of cash or in-kind payment to review a product. The Guide also establishes penalties for violations of these rules, including monetary penalties that could bring bloggers, and potentially sponsors and advertisers, substantial fines for each violation. The Guides provide the following practical example of how the new guidelines will work:

> A college student video game expert blogs about his gaming experiences. Readers of his blog frequently seek the student's opinions about video game hardware and software. A manufacturer of a newly released video game system sends the student a free copy of the system and asks him to review it on his blog. The student tests the new gaming system and writes a favorable review. Because his review is disseminated via a form of consumer-generated media in which his relationship to the advertiser is not inherently obvious, the student should clearly and conspicuously disclose that he received the gaming system free of charge.

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Since the FTC also requires manufacturers to ask bloggers to comply with the Guides, the manufacturer in the example should advise the student to disclose the source of the gift and have procedures in place to monitor the student's postings for compliance or be subject to the possibility of fines.

Advertisers and sponsors of products should be aware of these new FTC guidelines and take steps to comply, including ensuring that the athletes and other celebrities they hire to pitch their products comply. Advertisers and sponsors must also notify athletes who seek to blog about their products of these changes, especially in light of the possibility that both sponsors and bloggers can face monetary fines for violating the Guides.

4. Managing "Off-the-Field" Liabilities for Individual Athletes

High visibility and significant wealth often make professional and ex-professional athletes the target of lawsuits. Athletes' involvement in "off-the-field" activities further heightens their exposure to liability. Athletes must ensure that the team they surround themselves with off-the-field—their managers, lawyers, accountants and other professionals—is prepared to confront the issues that can arise and address any vulnerabilities to liability. Here are a few examples:

- **Multi-state tax issues**. Athletes commonly play for a number of teams over a relatively short period of time, requiring frequent moves across state lines. An athlete who owns houses in several states will need to deal with the tax regimes in each of them. Incorrect reporting may result in significant financial penalties or, even worse, criminal sanctions (e.g., golfer Jim Thorpe).

- **Landlord liability**. To alleviate financial strain or set himself up for income when his playing days are over, an athlete may rent out one or more of his homes. However, rental properties are a major source of lawsuits from tenants and others. Compounding this problem, athletes and their advisors often overlook limitations in the insurance coverage for a residence that may void such coverage if the athlete rents it out. Plus, owning several houses may result in the athlete finding himself "house-rich" but "cash-poor."

- **Risky business.** Many athletes invest their money in businesses to generate revenue away from the field. A favorite pastime for professional athletes, from Mickey Mantle to Mariano Rivera, is owning a restaurant or bar. But restaurants carry a number of potential liability pitfalls, not to mention the fact that six out of every 10 restaurants go out of business within 10 years. Plus, owning a liquor license brings the risk of a drunk patron injuring himself or someone else and suing the restaurant. When this occurs, everyone—especially the high-profile athlete—gets sued.

- **On the hook.** Due to their name recognition and wealth, athletes are often looked to for significant funding, including guaranteeing loans, and may be responsible for the debts and liabilities of a failed restaurant or other business. The athlete's own personal assets may also be exposed to creditors. The mere fact of owning a business may itself have a negative impact on the player, since leagues, sponsors and fans may not approve of certain types of businesses, such as bars and nightclubs.

These off-the-field activities will, and should, continue, but athletes need to approach them with an informed and well-considered plan. For example, properly structuring an

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entity for owning business interests, such as restaurants and rental properties, can greatly reduce liability exposure. Ensuring proper and sufficient insurance coverage is in place and managing insurance coverage will also help protect the athlete from liability. Athletes and their managers should always seek out qualified professionals to assist at the outset of such ventures, rather than looking for help after a problem occurs when it may be too late to rectify a situation that could have been avoided with proper planning.

5. Texas Rangers in Bankruptcy

The Texas Rangers filed for bankruptcy relief in late May, 2010, to break an impasse between the club and its bank lenders, who are owed approximately $550 million and who oppose a planned sale to a group led by Nolan Ryan. The Rangers are owned by Hicks Sports Group, which acquired the club in 1998 and had guaranteed the debt.

Despite being located in the largest market in Major League Baseball (MLB) with only a single franchise, the Rangers have suffered in recent years from negative cash flow. Through 2009, Hicks Sports Group had helped stanch the negative cash flow, loaning the Rangers approximately $100 million. But with the economic downturn in 2009, Tom Hicks decided he was no longer prepared to provide support and the Rangers defaulted on the bank debt in April 2009.

The two separate deals to sell the Rangers baseball club and the related real estate were completed in late 2009, but the bank lenders refused to consent to the deal because they believe that there may be other buyers who are prepared to pay a higher price. The lenders have publicly stated that they do not believe the Rangers conducted a full and fair auction process before accepting the bid from the Ryan-led syndicate.

The negotiations dragged on during the first part of 2010 and when they were ultimately unsuccessful, the Rangers filed for bankruptcy in Texas. The Rangers filed what is called a "pre-packaged" bankruptcy and have argued that it should be approved on an accelerated timetable because it provides for payment in full to all creditors. The bank group, however, still wants to see a competitive auction run to see whether the club can be sold for a higher price.

A key issue in this case will be the position of MLB, which pre-approved the sale to the Ryan group. Under Major League rules, the sale of a franchise must be approved by MLB and it is unclear whether MLB would agree to a sale to another buyer.

Last year in the bankruptcy of the Phoenix Coyotes, the National Hockey League would not approve a sale to an investor group that proposed to relocate the club to Hamilton, Ontario. The difficulties of purchasing a franchise in bankruptcy also reportedly deterred other purchasers, including Jerry Reinsdorf. A similar dynamic could play out for the Rangers.

Overall, the troubled economic climate may spur the sale of sports franchises in the United States, creating opportunities for those eager to own franchises and those motivated by the diverse revenue streams that can accompany such ownership. However, as evidenced by the current situation involving the Texas Rangers, owning a sports franchise is not without its share of problems. Owners of sports franchises and entities interested in purchasing or investing in such franchises should monitor the Texas Rangers situation carefully and be aware of the potential pitfalls associated with owning a sports franchise.

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Herrick Highlights

Keeping the sports industry informed. As mentioned above, Herrick will host a seminar entitled "The Business of Minor League Sports" to address issues involving acquisitions of teams, stadium strategies, business models, programming, media and sponsorships and franchise values. Panelists include Steve Horowitz of Inner Circle Sports, Brad Kwong of Northern Lights Hockey, LLC, Art Matin of Mandalay Baseball, Bobby Sharma of NBA Development League, and Irwin Kishner. Matthew Pace will moderate. Registration will be held from 8:00 am to 8:30 am and the seminar will run from 8:30 am to 10:00 am.

Helping Top Rank fight the good fight. We represented Top Rank, Inc. In producing principal agreements for the WBO World Welterweight Championship boxing match between Manny Pacquiao vs. Joshua Clottey held on March 13 at the new Cowboys Stadium in Arlington, Texas, and distributed by HBO Pay-Per-View. This first boxing event held at the new $1.2 billion stadium drew a record crowd of over 51,000. We handled all agreements with the fighters, the site, HBO PPV, TV broadcasters around the world and sponsors.

Helping the Yankees stay at the top of their game. We represented an affiliate of the New York Yankees in connection with a new college football bowl game, the New Era Pinstripe Bowl, to be played at Yankee Stadium. The first New Era Pinstripe bowl will be played on December 30th of this year, featuring teams from the Big 12 and the Big East and will be televised by ESPN. We negotiated the telecast agreement, the title sponsorship agreement and the agreements with the Big 12 and Big East Conferences.

For more information on these and other sports law issues, please contact **Irwin A. Kishner, Esq**. at **(212) 592-1435** or **ikishner@herrick.com** or **Matthew D. Pace, Esq.** at **(212) 592-1481** or **mpace@herrick.com.**

To learn how we can help you succeed in the sports business, including information on our team, their experience, and our events and media appearances, visit **www.herrick.com/sports**.