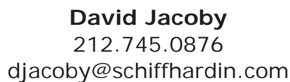
SCHIFF HARDIN LLP

In Fashion

Spring 2009



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ACCESSORIES COUNCIL

SINGING IN THE RAIN

We return to a topic we explored in the Winter issue of ***In Fashion*** and which unfortunately remains timely: how to deal with a challenging economy. Last time, we focused on five potential problems more likely to occur in a down market. Now we give equal time to some potential opportunities presented by this economy. Grab your galoshes as we look to make lemonade from lemons. Fair warning: this isn't so much about legal issues — though legal issues have a bearing — as it is about business issues.

1. New Rules. To borrow a phrase from Bill Maher, the downturn in the economy is declaring "New Rules" practically daily. Some of those new rules also have changed business relationships, perhaps to your advantage. For example, the downturn may have given buyers more leverage with suppliers, who are much hungrier for customers — especially reliable customers who pay promptly — than they were a year ago. A study by the Midwest-based Small Business Research Board of 1,000 small business owners and managers found about 15% had renegotiated long-term fixed-cost supply contracts — and that was in September, before the worst of the downturn hit. It may not only be price that is more negotiable; businesses may be willing to accept contract terms they would not have considered in flush times — for example, broader protections against potential knock-off or materials problems. Or take a page from the books of Blockbuster and Quiznos, among many others, who are renegotiating leases. Blockbuster said in December it is hoping to renegotiate leases on a third of its 7,000 stores nationally, while Quiznos set up teams to help its franchisees try to

renegotiate leases to reduce a major cost for operators. Firms that are leasing space, even if there are years to go under a current lease, may find it a good time to talk to their landlords about perhaps extending the term of the lease and securing funds for improvements to the leasehold or rent reductions.

Buy It When It's Cheap.

2. Buy It When It's Cheap. You may have read recently that a home developer, which sold huge tracts of land to a California public employees' retirement fund in 2007, is about to buy back choice bits at a steeply discounted price. Why would a home builder want land when it probably can't sell the houses it has built already? Presumably, the builder figures the market will rebound, and it will have acquired a key asset for less than it usually would cost.

If it works for real estate, why not brands and market share? If you are in a field where there will be ongoing demand, even if at a temporarily reduced level, the downturn may be a moment to take territory away from competitors or to assert a foothold in an emerging area. Procter & Gamble took this approach during the Great Depression: they reasoned that people still needed to buy soap, and saw the opportunity to strengthen P&G brands. To accomplish this goal, they increased advertising and funneled some of it toward a new medium — commercial radio — in the process inventing what we now know as the soap opera. That was bucking the trend, because most companies axed their ad budgets. But by becoming less visible, those companies unwittingly may have contributed to an impression that they were less durable brands — think about General Motors worrying now that no one would buy a car from a company in bankruptcy. During the Depression, heavy advertising by Chevrolet helped it surpass Ford as the nation's largest-selling car. Companies that maintain a high profile and provide better value can make inroads by winning customer loyalty that lasts past the downturn.

3. Help from Uncle Sam. The American Recovery and Reinvestment Act of 2009 — a.k.a the $787 billion stimulus bill — has a host of provisions and programs intended to help businesses. We can't fit a comprehensive list into this newsletter, but here are some examples.

SBA loans: With credit markets still largely frozen, the Recovery Act seeks to make SBA loans more affordable and available. The new law increases the percentage of SBA loans the government can guarantee and eliminates fees on loans during 2009. The SBA can now guarantee up to 90% of qualifying loans. Fees on loans are eliminated through the end of 2009 with a start date retroactive to the Recovery Act's enactment. The Recovery Act also establishes the small business stabilization financing program, which allows the SBA to make no-interest loans to back existing loans up to $35,000. Businesses can then use the money to make up to six months of payments on previous loans. Interest on stabilization loans will be fully subsidized but

borrowers must repay the loans within five years. The Recovery Act also is intended to pump more dollars toward purchase of SBA paper in the secondary market to promote lending.

Business tax changes: The Recovery Act makes a number of changes in business tax provisions. These include:

- Qualifying small businesses can reach back five years to offset net operating losses against past income; that means a company might be able to get a refund now based on prior payments;

- Qualifying small businesses can reduce estimated tax payments to 90% of the previous year's level;

- Businesses can claim accelerated first-year depreciation (50% of cost for capital equipment); qualifying small businesses enjoy a special rule, allowing them to take a first year write-off of all depreciation on capital equipment up to $250,000.

Industrial bonds for creating designs: Of special interest to firms in creative fields is an important change Congress made in the uses to which industrial development bonds, issued by states and localities, can be put. Previously, they were available only for manufacturing of tangible goods. The Recovery Act expands this to take in creation of intangibles, including copyrights, patents and designs, among other things.

Tax incentives to consumers: The Recovery Act also seeks to spur spending on consumer items by virtue of a refundable tax credit. The credit ranges in amount from $400 to $800 for working families with incomes up to $150,000. Also expanded is eligibility for the refundable child tax credit and the earned income tax credit. The Act also provides a one-time $250 payment to various government retirees, SSI recipients and disabled individuals.

Tax credit for hiring underemployed youths and veterans: The Recovery Act provides for a per worker tax credit of $2,400 for companies that hire unemployed youths and veterans who have not been regularly employed or in school for the past six months.

Recharging credit cards: The Federal Reserve's Term Asset-Backed Securities Loan Facility (TALF) may help loosen purse strings for credit cards. The idea is for the Fed to leverage its own funds and credit to encourage purchases of securitized portfolios of loans for auto, credit card and other consumer borrowing. The first three TALF-backed deals took place in mid-March, including one for securitization of Citicorp credit card obligations.

4. State and local incentives. Many states and localities also have funds and programs available. For example, in New York, assistance may be available in a variety of ways, including through cheaper energy, tax credits, and other benefits, depending on employment, location and other variables. One example: the Garment Center is an Industrial Business Zone, meaning that a job at an industrial or manufacturing firm moved there from a non-industrial business zone area qualifies for a one-time $1,000 per job tax credit against New York City taxes.

FROM THE SHIRE TO THE COURTS FOR THE RING OF COVERAGE

Must a General Liability Insurer Defend and Indemnify Claims Associated With Alleged Infringement of the "Hobbit" Trademark?

The Minnesota Supreme Court just answered this question "yes", as it held that the standard form general liability insurance policy required an insurer to defend and indemnify its policyholder for claims of trademark infringement. The claims were made by Tolkien Enterprises, the holder of the trademark rights relating to J.R.R. Tolkien's famous works "The Hobbit" and "Lord of the Rings." General Casualty Co. of Wisconsin v. Wozniak Travel, Inc., _____ N.W.2d ____, 2009 WL 702437 (Minn. March 19, 2009). At issue was the language of the general liability insurance policy, which also provided coverage for something known as advertising injury and whether the claims of trademark infringement fell within the advertising injury coverage for "misappropriation of advertising ideas."

Wozniak Travel Inc., doing business as Hobbit Travel, had been sued by Tolkien for its alleged wrongful use of the "Hobbit" trademark for its travel business. The claim was made that Wozniak was confusing the general public about its association with the Tolkien-licensed users of the "Hobbit" name and mark, such as a licensee that had an agreement with Air New Zealand for the airline to market itself as the "Airline to Middle-earth." Noting the conflict among courts on this issue, the Minnesota Supreme Court determined that the absence of the word "trademark" in the policy's advertising injury section was not conclusive and that coverage for "infringement of title" claims encompassed trademark infringement claims. The court further ruled that use of trademarks is "advertising" within the meaning of the policy, giving advertising a broad definition to take in any oral, written or graphic statement made by a seller in any manner to solicit business. The opinion noted that the majority of courts considering the issue now have held that claims of trademark infringement can be covered by advertising injury coverage in general liability insurance policies.

If you don't know an ent from an exclusion or an orc from advertising injury, here's the point to take away: a kind of insurance coverage most businesses already have may provide coverage for lawsuits claiming trademark infringement.

YET MORE ON CONSUMER PRODUCT SAFETY LAW

At a program sponsored by the Accessories Council, the Fashion Jewelry Trade Association and Schiff Hardin in September, 2008, we discussed the Consumer Product Safety Improvement Act (CPSIA) adopted last summer. We updated with new developments in the Winter issue of this newsletter. Now there has been conflict between the CPSC and the courts over the ban on phthalates. The courts won. Additionally, the Commission backed off for a year on enforcing most testing and certification requirements.

A federal court recently held that the CPSC got the law wrong and ordered it to bar sales of previously manufactured children's products containing banned phthalates after February 10, 2009. The CPSC had issued an advisory letter in November 2008 saying that the February 10, 2009 deadline to end sales of children's products with lead levels prohibited by the Act did not apply to phthalate levels. Put differently, the CPSC letter grandfathered phthalate-containing products made prior to February 10, 2009, meaning they could continue to be sold. That was just wrong, concludes U.S. District Judge Paul G. Gardephe in an opinion in National Resource Defense Council v. U.S. Consumer Product Safety Commission, __ F. Supp.2d ___, 2009 WL 297708 (S.D.N.Y. February 5, 2009). The court ruled the CPSC had violated the law and its advisory letter should be set aside. Moreover, the court said the Commission's opinion letter was "not thorough, well-reasoned or substantiated."

Roughly two weeks earlier, the CPSC effectively kicked back for one year (to February, 2010) the start date of new testing and related certification requirements for both lead and phthalates in children's products by adopting a stay of enforcement. However, the delay does not apply to lead testing in paint and jewelry.

New advertising rules for Web sites offering children's toys for sale took effect on December 12, 2008. Catalogues in print offering children's toys that don't meet the new CPSIA requirements, and which were printed before February 10, 2009, may continue to be distributed, but only until August 8, 2009.

For further information on CPSIA developments, go to www. schiffhardin.com.

NEW YORK CAN TAX ONLINE SALES REFERRED BY AMAZON "ASSOCIATES"

The collection of sales tax on Internet purchases continues to be an issue of obvious importance to Internet vendors, competing brick and mortar vendors, and revenue-hungry governments. New York State's attempt to impose taxes on Amazon.com sales to New Yorkers generated by "associates" survived the first round of a challenge to its legality in January. New York Tax Law § 1101(b)(8) (i), the so-called Commission-Agreement Provision, was adopted last April, adding to the sales tax provisions a rebuttable presumption that an entity like Amazon, which had New Yorkers who referred potential customers to it, including by Internet links, was soliciting sales in New York if its total referred sales exceeded $10,000 annually. Amazon.com challenged the statute on several constitutional grounds, including that Amazon.com lacked a sufficient nexus to New York to be subject to its sales tax, that the statute denied Amazon.com due process of law by creating an effectively irrebutable presumption, and that it violated the Equal Protection Clause by singling out Amazon.com. Amazon.com has been collecting the taxes, under protest.

All of Amazon.com's arguments were rejected by Justice Eileen Gransten of Supreme Court, New York County, in her January 12, 2009 opinion in Amazon.com LLC v. New York State Department of Taxation and Finance, ____ N.Y.S.2d ____, 2009 WL 69336. The court found that the Commission-Agreement Provision test for liability to pay New York taxes has a constitutionally sufficient nexus to New York, so Amazon.com's facial challenge to the statute fails. So does its as-applied challenge, despite Amazon.com's contention that associates were responsible for less than 1.5 percent of its total New York State sales. The court also dismissed the due process claim, finding the statutory presumption rational because there was a high degree of probability to support it and because it was rebuttable. Finally, the court found no basis to sustain Amazon.com's claim of unequal treatment.

Quick on the heels of the decision, a California legislator introduced Assembly Bill 178, which would impose a similar tax.

LILLY LEDBETTER FAIR PAY RESTORATION ACT EXTENDS DEADLINES TO BRING DISCRIMINATION CLAIMS

President Obama signed the Lilly Ledbetter Fair Pay Restoration Act (P.L. 111-002) into law just nine days after taking office, reversing a 2007 U.S. Supreme Court decision, which had given a narrow construction to when the

time to sue begins to run under Title VII of the Civil Rights Act. The 5-4 decision in Ledbetter v. Goodyear Tire & Rubber, 550 U.S. 618, had said the clock started with the decision — a hiring choice or an annual review, for example — that created an unlawful pay disparity. The new law says the time to sue revives each time the plaintiff is paid wages, benefits or other compensation arising from the allegedly discriminatory action. Moreover, the statute is retroactive to May 28, 2007 and covers all claims pending on or after that date. In addition to changing Title VII, which addresses discrimination including that based on gender, race, color, religion and national origin, the law makes parallel changes to the limitations rules for equal pay claims under the Age Discrimination in Employment Act, the Americans with Disabilities Act and the Rehabilitation Act of 1973.

Our colleagues in the labor and employment area warn that the new legislation is expected to generate many new wage discrimination claims. They recommend that employers review their policies and procedures to make sure they are based on legitimate factors, such as prevailing labor market conditions and job performance, and that they review their procedures for documenting compensation decisions to make sure they can back up the legitimate basis for decisions made.

Changes also are being made to requirements for employee compensation and benefit plans. Our Employee Benefits and Executive Compensation Group has created a checklist of those changes, which can be found at www.schiffhardin.com.

SCHIFF HARDIN NEWS
HARDLY NEWCOMERS

Schiff Hardin is pleased to announce that Jeffrey Laytin and Richard Verner have joined its Intellectual Property Group in the New York office. While new to Schiff Hardin, they are hardly newcomers to a broad range of intellectual property work, here and abroad.

Mr. Laytin practices domestic and global intellectual property law, focusing on trademarks, copyrights, licensing issues and rights of publicity as well as international trade. He advises clients on the extent of their intellectual property rights, negotiates agreements for the exercise of those rights, such as licenses, and protects rights through customized enforcement programs and litigation. He works with clients on manufacturing and distribution agreements; helps implement solutions to protect the integrity of their supply chain and distribution networks; and enforces their contractual rights against distributors of grey-market and diverted goods. He also has an active China practice.

Mr. Verner focuses his practice on trademark prosecution and enforcement and has managed worldwide trademark portfolios for a broad range of companies in the apparel and entertainment fields. He consults with clients regarding the full spectrum of brand management and revenue enhancement issues, including negotiation and drafting of license and other business-development agreements. Mr. Verner has developed and implemented worldwide anti-counterfeiting programs for numerous businesses in order to protect their valuable intellectual property rights.

Catwalks, Courthouses and Copyrights: Cutting Edge Issues in Fashion Design Protection

Practising Law Institute, Advanced Seminar on Copyright Law 2009

April 30, 2009
9:00 AM - 5:00 PM EDT

Judith S. Roth

Judith S. Roth, Of Counsel in Schiff Hardin's Intellectual Property Group, will speak on the state of the law in the U.S. and elsewhere with respect to protections available to designers against copying and counterfeiting of fashion designs. Her talk will discuss key case law, existing and proposed U.S. intellectual property legislation affecting fashion, non-U.S. design protection programs, technological developments, academic research and her own experience representing designer clients in fashion and related fields.

For more information or to register, visit www.pli.edu.

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Schiff Hardin LLP is a general practice law firm with nearly 400 attorneys, founded in 1864.

The Accessories Council is a not-for-profit, national trade association that was established in 1995 with the mission of increasing consumer use and awareness of accessories.