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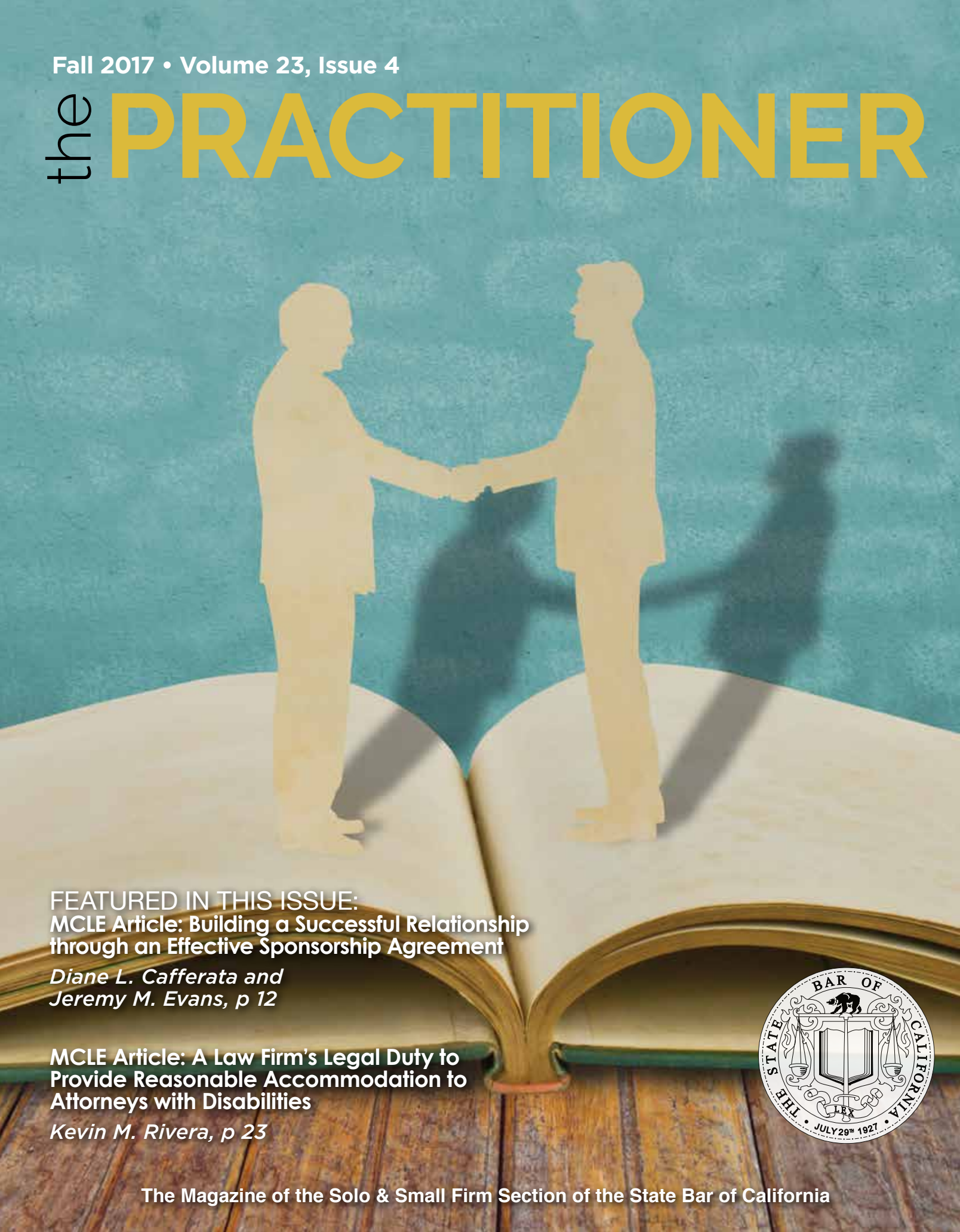

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MCLE Article: Building a Successful Relationship through an Effective Sponsorship Agreement

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In this article, Jeremy Evans with California Sports Lawyer® and Diane Cafferata with Quinn Emanuel Urquhart & Sullivan, LLP provide insights into the drafting and negotiation of sponsorship and endorsement agreements. Both attorneys are based in the heart of the entertainment and sports industries, Los Angeles, California.

The sports industry's rapid evolution and growth continues to generate increasing opportunities for sponsorship exposure. In North America, the world's largest sponsorship market, sponsorship spending is projected at $23.2 billion, up from $22.3 billion last year, with sports accounting for 70% of that market.[1] Per *Forbes*:

> "[W]hat separates the Dallas Cowboys ($2.3 billion value) and Oakland Raiders ($825 million) is their stadiums and the revenue derived from each venue. **Sponsorship revenue plays a huge part in this. The Cowboys earned $100 million from sponsorships and advertising signage last season, and this was before owner Jerry Jones inked his 25-year, $500 million naming rights deal with AT&T. Teams like the Raiders and Buffalo Bills generate less than $20 million in sponsor revenue."**[2]

Per *CNBC*:

> In [Major League Baseball], the league reached $695 million[3] and $778 million[4] in sponsorship revenue for 2014 and 2015, respectively. Since 2011, sponsorship revenue has gone up every year.[5]

Sponsorship agreements, the legal vehicle creating such relationships, are becoming increasingly common as a result. Whether you represent a sponsored party, a sports league, a charity, a company, or the government, it is wise to be familiar with these agreements and their key provisions before they cross your desk. The purpose of sponsorship agreements—to clearly describe the contours of the

parties' successful relationship into the future—compels candid discussion and clear and unambiguous drafting of the parties' rights and obligations under the agreement.

There are many articles that explore the basics of sponsorship agreements, and the typical provisions that should be included,[6] but here we examined some provisions that have generated significant litigation over sports sponsorships in the last several years to illustrate and develop some conclusions about how these agreements may be drafted to avoid or at least minimize such disputes in the future.

PROPER REPRESENTATIONS OF PARTIES' CAPACITY AND AUTHORITY

In addition to ensuring that the agreement properly identifies the parties to the agreement, there should also be clarity around each party's authority to enter into the agreement and its ability to grant the rights it will provide under that agreement.

In *VICI Racing, LLC v. T-Mobile USA, Inc.,* 763 F.3d 273 (3rd Cir. 2014), for example, section 5.8 of the parties' agreement provided that "VICI grants to [T-Mobile] the right to be the exclusive wireless carrier supplying wireless connectivity for the Porsche, Audi and VW telematics programs beginning in model year 2011 with such exclusivity continuing throughout the term of this Agreement."[7] In that case, T-Mobile terminated the agreement and alleged that VICI, a former operator of a racing team that competed in the American Le Mans Series, had breached this provision of the agreement because "VICI does not have and has never had the authority to grant such rights."[8]

The district court found section 5.8 was "too convoluted to have any one clear meaning."[9] For example, it could mean the sponsor had bargained for the right to seek the telematics business from those companies, or it could mean the sponsored party was supposed to facilitate the sponsor's efforts to get that business, or it could have some other meaning entirely. Further, it included undefined key terms that were open to conflicting interpretations, and the balance of the contract contained no other provisions that would clarify section 5.8.[10] The court held section 5.8 severed from the contract and unenforceable based on the parties' clear intention in section 14.7 of the agreement that unenforceable provisions would be severable.[11] This result was upheld on appeal.[12]

A sponsored party's capacity came into play in a different way in *Oakley Inc. v. Nike, Inc. et al,* 988 F.Supp.2d 1130 (C.D. Cal. 2013). In that case, Oakley and professional golfer Rory McIlroy had signed a two-year endorsement contract for the period January 1, 2011 through December 31, 2012, which contained a provision requiring McIlroy to provide Oakley a right of first refusal for the next endorsement period after 2012.[13] In September 2012, an Oakley executive backed out of the running for that next endorsement deal with a late-night email: "Understood. We are out of the mix. No contract for 2013."[14]

Nevertheless, when McIlroy entered into a new agreement with Nike, Oakley sued him for breach of contract and Nike for intentional interference with contractual relations.[15] The Court entered summary judgment in favor of Nike, because McIlroy's representatives had repeatedly stated to Nike that they had the ability to contract with Nike and that Oakley was not submitting a competing proposal and in fact had chosen not to do so.[16] On these facts, the Court found that Nike was entitled to rely on the representations of the only party in the know, McIlroy.[17]

Practically speaking, when drafting a sponsorship contract, it is important to include representations in the agreement that each party has the legal authority to sign the agreement and the capacity to deliver the items negotiated in the contract. Each party should speak candidly during the negotiations about what it expects the other party to do, and about its own true capabilities and willingness to perform its obligations, in order to avoid problems later. In *VICI Racing,* neither party had a clear sense of what the "telematics" provision required, creating a great deal of misunderstanding that poisoned the relationship and sent it into litigation. In contrast, Nike benefited from its many statements to McIlroy's representatives during negotiations that it would not sign a contract with McIlroy until he was contractually able to do so, and from insisting on representations by McIlroy that he in fact was contractually able to do so. Take

the time to ensure the person/entity has the authority and approvals necessary before agreeing to any contract and put that authority and approval in writing inside the agreement.

CLEAR PROVISIONS ON THE TERM FOR THE AGREEMENT, THE PARTIES' ABILITY TO TERMINATE, AND WHAT HAPPENS UPON TERMINATION

The parties to a sponsorship agreement will benefit from clarity as to when their rights under the agreement, for example, a license to use the other party's trademarks, have ended. In *All Star Championship Racing, Inc., v. O'Reilly Automotive Stores, Inc.,* 940 F.Supp.2d 850 (C.D. Ill. 2013), the plaintiff, an organizer and advertiser of automobile races, continued to use O'Reilly's marks after the parties had failed to renew their contract in 2010 and 2011. A factual dispute as to whether an implied license to use the marks continued to be in effect between the end of the 2009 contract and July 16, 2011 prevented summary judgment from being granted in favor of O'Reilly for that time period.[18]

In *United States ex rel. Landis v. Tailwind Sports Corporation,* 155 F.Supp.3d 12, 14 (D.D.C. 2016), a former member of Lance Armstrong's professional cycling team brought a *qui tam* action against Armstrong and several affiliated defendants for violations of the False Claims Act, and in particular, for reverse false claims.[19] Reverse false claims accrue where someone has improperly withheld money or property to which the United States is legally entitled.[20] Therefore, the question before the Court was whether the Sponsorship Agreement created a legal obligation to repay the United States Postal Service any sponsorship fees that were obtained and retained because of Armstrong's materially false statements that he was not using performance-enhancing drugs.[21] The clause at issue permitted the U.S. Postal Service, in the event of defendants' breach of the moral turpitude and drug clause, to immediately terminate the agreement and pursue whatever remedies it had available to it under law or equity.[22]

The court initially denied defendants' motion to dismiss this claim, finding that the agreement created a legal obligation "sufficiently certain to give rise to an action of debt at common law."[23] The Court reasoned that the doping activity alleged would constitute a "total breach" so serious that this conduct generated a sufficient obligation for purposes of reverse false claim liability.[24]

However, Judge Cooper, who presided over this case later in the proceeding, thoroughly reconsidered this reasoning, and granted defendants' motion for summary judgment on the same claim. Judge Cooper concluded that the clause in question only created a *contingent* obligation, because it did not require Tailwind, the manager of the cycling team, to return any funds during periods in which team members were in violation of the moral turpitude and drug clause.[25] An obligation to the U.S. Postal Service for purposes of reverse false claims liability would only arise after it sued to enforce the obligation and obtained a favorable judgment.[26]

When drafting these types of provisions, we suggest seeking clarity and balance. Clarity is helpful to avoiding misunderstanding later about what was agreed to. Balance is required because a sponsorship agreement is about creating an ongoing and positive relationship between the two parties and an environment where the parties seek to go beyond what is contractually required to provide value to the other and increase the value of the contract in the next negotiation period. In negotiating term ending dates, renewal provisions, and rights of first refusal, each side should carefully consider the terms and their true effect on the parties and try to negotiate fair terms that engender enthusiasm for the partnership. If the term is set up to lock up the talent for a very lengthy period of time, for example, the sponsor may find that it has a half-hearted partner looking for exit opportunities halfway through the term.

In thinking about creating a partnership feeling in drafting sponsorship agreements, morals clauses are some of the most difficult in negotiations because sponsors want to ensure they are not purchasing a public relations crisis, or liability, with their sponsorship money. In the last few years, we have seen many instances in which sponsors have pulled their sponsorships when the talent/athlete has engaged in problematic conduct (*see, e.g.,* Lance Armstrong, Tiger Woods, Ryan Lochte, the list goes

on). Both parties should do thorough due diligence before entering an agreement and ask for consent to a background check where there is any doubt. Asking the right questions and being clear about one's expectations can go a long way to avoiding problems later. Of course, some misconduct cannot be foreseen, and so the best way to protect against damage during and after contract is to have termination, liquidated damages, and similar provisions that delineate the remedies available when the relationship ends or goes sour.

CLEAR DESCRIPTION OF SPONSOR RIGHTS AND ANY EXCEPTIONS

In every sponsorship agreement, the sponsor bargains for a unique bundle of rights it is to receive from its sponsored party as consideration for its sponsorship. Some examples of common sponsor rights include:

- ***Exclusivity*** (rights to be the exclusive sponsor or one among sponsors in a given business sector);
- ***Trademark and logo use*** (rights to use the sponsored party's marks or logos);
- ***Advertising and promotional rights*** (rights to promote or advertise oneself as the sponsor);
- ***Presentation rights*** (rights to present awards or play a certain role in presentational events);
- ***Merchandising rights*** (rights to develop and sell related merchandise);
- ***Filming/recording/broadcast rights*** (rights to go beyond the event and merchandise to record and broadcast coverage);
- ***Hospitality rights*** (rights to entertain clients, for example, box seats);
- ***Management rights*** (rights to control aspects of event planning and management);
- ***Naming rights*** (rights to name venues, facilities or events); and
- ***Exposure on social media*** (views and impressions from social media posting).

Being clear in describing the rights being granted and candidly discussing what the sponsored party expects to do to fulfill its obligations to the sponsor while negotiating those descriptions in the agreement, are good ideas because they set and match the parties' perceptions of what is expected throughout the relationship. As we saw with *VICI Racing, LLC v. T-Mobile USA, Inc.*, an ambiguously worded pseudo-representation like the "telematics" statement can generate a great deal of expensive litigation that could easily have been avoided.

Similarly, it is wise to be clear about the circumstances under which the sponsored party's performance is to be excused. In the *VICI Racing* case, T-Mobile also accused VICI of breaching the agreement by failing to run its racecar at Le Mans for the rest of the 2009 season after an accident at the Lime Rock race on July 18, 2009, that resulted in engine and body damage.[27] The court found, however, that this failure did not constitute a breach under the parties' force majeure clause, which required fulfillment of three conditions: that "(1) the prevented obligation is a nonmonetary obligation that is prevented by a condition beyond a party's control, (2) the affected party provides prompt notice of the interference, its nature and expected duration; and (3) performance of the prevented obligation resumes as soon as the interference is removed."[28] VICI properly adhered to these procedures and was excused from its failure to race the car for the remainder of the year.[29] T-Mobile unsuccessfully argued that the interference preventing VICI from racing was actually a monetary interference because it lacked the money to repair the damage in time to finish the 2009 season, but as the court put it, "[t]he fact that money can solve a problem does not mean that a lack of money caused the problem."[30]

On the transactional front, sponsor rights and sponsored party's obligations are really the core of the agreement. Each party should have a clear vision of what this sponsorship will look like going forward, for example, how and when their intellectual property is to be used or not used; how they can protect themselves from confusion with other brands and products; how they each can maintain sufficient

control over joint activities to ensure their own interests are protected; and how they will protect each other from attacks by third parties. In the *VICI Racing* case, the owner of the racecar benefited from negotiating a sensible procedure to follow in the somewhat likely event that its racecar would sustain damage, making it unable to fulfill its obligations for some period of time, and then following that procedure when that event occurred.

In negotiating sponsor rights, special attention should be given to the protection of the intellectual property of the product or brand because inadvertent misuse or infringement can be destructive, harming the relationship and diminishing the value of the deal. Further, knowing what other products a talent or company has been, is currently, or will be in a sponsorship/endorsement relationship with may be helpful to developing a clear picture of what the sponsorship being negotiated will look like with that talent or company. Both parties will benefit from a clear vision of the relationship going forward, and from taking the time to express what each side wants and papering it appropriately.

***In closing*,** we have developed a few broader themes for the successful negotiation of a sponsorship agreement. First, it is important to recognize, and deal effectively with, the very different interests represented by each side of a sponsorship agreement, to better understand the likely nature of the future relationship. For example, a large retailer recently selected an attorney with experience representing talent to help it negotiate and draft a sponsorship agreement that it would use with its talent, because the attorney would be better able to explain proposed terms to talent likely unfamiliar with those terms. It was a smart move by the retailer and ended in a positive negotiation and fair contract.

Second, a sponsorship agreement should read less like legalese and more like a story that accurately portrays the relationship going forward. It should be easy to understand and both parties can benefit from taking the time to accurately describe what they expect out of their respective rights and obligations. Remember, sponsorship agreements are first and foremost based on relationships. If one party does not feel comfortable with the contract, its terms, or the relationship in general, its performance under the contract will be lackluster, diminishing the value of the contract and making renewal unlikely. Also, spelling out the terms and the conditions in an easy-to-understand way makes it easier for parties to work out difficulties by renegotiating specific aspects of the agreement based on a clear understanding of what the agreement would otherwise provide, rather than resorting to litigation because there is confusion over ambiguous terms.

Third, a mandatory arbitration clause should be considered. Most people and entities, specifically talent and large companies, would rather keep things private and out of the public eye. Arbitration is typically more streamlined than litigation, saving money and time. The parties can select the decision maker, who may bring relevant experience to the table and help the parties resolve their differences and move forward positively through a settlement.

Fourth, with regard to terms and conditions, it is wise to lay out the deliverables clearly and concisely, preferably in an addendum to the contract. For example, in most sponsorship contracts there are terms like "Amount of Social Media Posts" (regarding the product or brand), "Public Appearances or Promotions," "Product Placement or Signage," and the like. These terms are the lifeblood of the agreement between the parties because it is the underlying service or act in promoting the brand or product that creates the reason why the parties are contracting in the first place and it is helpful for the delivering party to know precisely what it is responsible for doing under these terms and fulfilling those responsibilities. Understanding the deliverables make for happy contractual relationships and minimize the likelihood of costly litigation.

Last, in any sponsorship agreement, it is unwise and unethical to guarantee the results of the sponsorship relationship. A contract directs the parties, and creates opportunities, but it does not control the markets or consumer decisions. A sponsorship agreement should on its surface only attempt to influence consumer spending based on what the parties promote, and the emphasis should be on good communications between the sponsor and sponsored party about how to maximize both the

promotional opportunities coming out of the relationship and the value of the sponsorship deal.

ENDNOTES

1 http://www.sponsorship.com/IEGSR/2017/01/04/Sponsorship-Spending-Forecast--Continued-Growth-Ar.aspx

2 http://www.forbes.com/sites/kurtbadenhausen/2013/08/14/nfl-stadiums-by-the-numbers/#4e1642cc6e19 (emphasis added)

3 http://www.sponsorship.com/iegsr/2014/10/20/MLB-Sponsorship-Revenue-Totals-$695-Million-In-201.aspx

4 http://www.sponsorship.com/iegsr/2015/11/09/Sponsorship-Spending-On-MLB-Totals-$778-Million-In.aspx

5 Id.

6 *See, e.g., David J. Ervin and James Hennigan, Sponsorship Arrangements in the U.S.*, Practical Law Practice Note 0-503-9158 (2017).

7 *VICI Racing, LLC v. T-Mobile USA, Inc.*, 763 F.3d 273, 279 (3rd Cir. 2014).

8 *Id.* at 280.

9 *VICI Racing, LLC v. T-Mobile USA, Inc.*, 921 F.Supp.2d 317, 328 (D. Del. 2013).

10 *Id.* at 328, 329.

11 *Id.* at 330.

12 763 F.3d at 286.

13 *Oakley Inc. v. Nike, Inc. et al*, 988 F.Supp.2d 1130, 1132 (C.D. Cal. 2013).

14 First Amended Complaint, 8:12-CV-02138 JVS-MLG at ¶ 45.

15 998 F.Supp.2d at 1133.

16 *Id.* at 1137, 1138.

17 *Id.* McIlroy was dismissed per stipulation of the parties.

18 *All Star Championship Racing, Inc., v. O'Reilly Automotive Stores, Inc.*, 940 F.Supp.2d 850, 864-865 (C.D. Ill. 2013)

19 *United States ex rel. Landis v. Tailwind Sports Corporation*, 155 F.Supp.3d 12, 14 (D.D.C. 2016).

20 *Id.*

21 *Id.* at 26.

22 *Id.* at 15.

23 *Id.* at 18.

24 *Id.* at 18-19.

25 *Id.* at 28.

26 *Id.*

27 921 F.Supp.2d, at 331.

28 *Id.* at 332.

29 *Id.*

30 *Id.*