

W E L C O M E

A message from Andrew N. Krinsky



Andrew N. Krinsky

Welcome to the summer 2011 edition of The TKD Advisor. I am pleased to report that in recent months TKD has added practice areas, welcomed exceptional new legal talent to our team, and has been recognized by Chambers and Partners. Our expansion, as always, has been driven by our goal of deepening our resources and enhancing our ability to best serve our clients, who face an increasingly complex business environment. Some of those complexities, including cyber liability issues related to social media, risks inherent to corporate transactions in China in the wake of recent enforcement actions by regulatory authorities, and best practices and remedies for non-copyrightable work, are highlighted in the articles in this edition of The TKD Advisor.

During the past quarter we expanded our Trusts & Estates Practice Group, welcoming Executive Compensation and Benefits Attorney and new partner, Stephen L. Ferszt, as its chair. And, as I write, we are welcoming another new partner, Douglas Gilbert, a veteran in intellectual property matters, to the firm's newly established IP Litigation Practice Group. You can read more about all of our recently hired attorneys and practice group expansions in the Firm News section of this Advisor.

Best wishes for an enjoyable summer, and, please do not hesitate to contact me at 212.216.8080 or by email at akrinsky@tarterkrinsky.com if I may be of any assistance to you.

THE OTHER GREAT WALL OF CHINA: CURRENT ISSUES IN CHINESE TRANSACTIONS

By Peter Campitiello



Peter Campitiello

In recent months, a number of publicly traded Chinese companies have faced a wave of regulatory actions and sanctions coupled with a precipitous erosion of their stock prices and market capitalization. There seems to be no shortage of news coverage, even in non-financial publications such as The New Yorker, covering the issues plaguing Chinese companies, especially those that have gone public via reverse merger. It seems The Wall Street Journal or investors' websites report a different Chinese reverse merger casualty each week. These events have led many experts in the China region to question the continued viability of transactions in China, particularly those involving capital raising. A representative from one prominent investment bank, heavily involved in financing reverse mergers of Chinese companies, declared that the market for Chinese Companies "is now closed".

But what went wrong? Certainly, bubbles have burst before, such as the tech bust of the late 1990's. However, that was a market conceived in speculation, where companies fully disclosed their lack of revenues and assets, but fortunes were knowingly made or lost on the hope of a concept or an idea. China, however, is different. Built on the understanding that "everything is made in China", investors had no overt reason to

Continued on page 2



THE OTHER GREAT WALL OF CHINA: CURRENT ISSUES IN CHINESE TRANSACTIONS

Continued from cover page



doubt financial statements which reported several hundred million dollars of revenues and assets. Unfortunately, what few expected was a subculture of deceit from Chinese companies borne from decades of Communist rule and an undue reliance by U.S. auditing firms on their Chinese counterparts.

The Securities and Exchange Commission (“S.E.C.”) estimates that as many as 600 reverse mergers have been consummated since 2007, and more than 150 of them were with companies from China and the China region.

In large part, the issues that have arisen in many of these transactions have squarely been centered on deficiencies in the accounting capabilities of the Chinese companies, often combined with a culture of non-transparency or outright fraud. These accounting failures have led to entire boards of directors resigning, audit firms and independent advisors to publicly-held companies demanding internal investigations and several, material restatements of financials. Several formerly-perceived darlings of the Chinese reverse merger market have been subjected to S.E.C. investigations, trading suspensions and exchange delisting. Two such companies had been listed numbers 1 and 2 on the Investor’s Business Daily 100 index; one was found to have fabricated the existence of certain contracts and the other was delisted after having to materially restate its financials.

In examining the companies that have faced enforcement actions, trading halts and delisting, a recurring fact pattern emerges. Typical is the presence of a local or regional U.S. auditor with no or nominal connections to mainland China (relative to physical offices and personnel), engaging in audits of larger or mid-market companies with (purportedly) significant assets and operations. These audits may have been performed against the Public Company Accounting Oversight Board (“PCAOB”) procedures by failing to even send personnel to the China

region to perform the fieldwork, relying on Chinese accountants and maintaining substantially all of the audit documentation with the Chinese accounting firm. These deficiencies are even more problematic in the context of a reverse merger because, in most cases, the audit performed for the transaction is the first audit these companies have ever had.

Partly in response, in a recent speech, S.E.C. Commissioner Luis A. Aguilar noted the S.E.C. has established an internal task force to investigate fraud, particularly among foreign companies that have participated in reverse mergers. Commissioner Aguilar stated an additional concern was the lack of audit work being performed by U.S. firms auditing financial statements. Adding that a number of audit firms may simply be “selling” their names to Chinese auditing firms without ever performing audit work or sending auditors to China for fieldwork. This exacerbates the problems since the PCAOB, the regulatory authority charged with reviewing accountants who practice before the S.E.C., is prevented from inspecting Chinese audit firms.

In an executive report, the PCAOB identified two issues involving Chinese companies: systemic concerns with the quality of the auditing and financial reporting; and limitations on the ability to enforce securities laws. The PCAOB further indicated additional challenges firms face in auditing mainland companies include the need to understand the local language; the use of local audit firms to complete a portion of the audit work; travel time and expense; and the need to understand the local business environment.

S.E.C. Chairman Mary Schapiro stated the S.E.C. was concerned with the number of small private companies seeking reverse mergers, particularly from China, and that the S.E.C. was probing investment banks and accountants that brought the companies to U.S. stock exchanges, as well as lawyers and stock promoters. Additionally, the S.E.C. recently issued a

bulletin advising investors on potential risks related to reverse mergers (<http://sec.gov/investor/alerts/reversemergers.pdf>). The bulletin is curious since even in the midst of the tech bust, the Enron and Adelphia accounting scandals or the Madoff and other Ponzi debacles, the S.E.C. never offered similar “protection” or guidance to investors.

Certainly, while there is considerable basis to approach transactions in the China region with skepticism and heightened due diligence, it is hardly likely that the world’s second largest economy, with more than 1.3 billion potential consumers, is “closed”. Rather, as practitioners working with Chinese companies and U.S. securities markets have learned, your partners in China are essential, particularly a company’s independent auditors. While the recent shift has seen a flurry of enforcement actions, the regulations will settle and the climate will likely change as well. Even now, the PCAOB has announced that it expects to reach an agreement with Chinese authorities to gain some measure of oversight over Chinese auditing firms. China’s role in the world economy is not likely to change in the near future, nor is the appetite of U.S. consumers for Chinese products. While the number of transactions and reverse mergers may not return to their previous levels, the importance in selecting the deal team will be greater than ever.

About Peter Campitiello

Peter Campitiello is a Partner in the Corporate and Securities Practice Group at Tarter Krinsky & Drogin LLP. His practice focuses on the representation of public companies and those in the process of going public in the high technology and life sciences industries, as well as the venture capital and private equity firms that support them. Peter can be reached at pcampitiello@tarterkrinsky.com.

THE RISE OF ELECTRONIC MEDIA AND SOCIAL NETWORKING: UNRECOGNIZED RISKS FOR EMPLOYERS AND RECRUITERS

By Richard L. Steer



Richard L. Steer

As the use of electronic media and social networking increases in daily life, employers and staffing companies are becoming exposed more frequently to risks for which they may be unexpectedly uninsured. It is not all uncommon for employers, staffing firms and their employees to turn to social media sites such as Facebook, LinkedIn, MySpace, Twitter, various blogs and the like in an effort to locate information and network with potential candidates and clients. Such use of social networking sites and electronic media, however, raises a variety of legal issues and risks that companies may not yet recognize and that may not be covered by traditional Commercial General Liability (CGL) or Employment Practices Liability Insurance (EPLI) or other types of insurance coverage. The more significant risks that employers should watch for are discussed below.

Employment Discrimination

One problem with the use of social media in recruiting is that there is the potential for the recruiter to learn and use information that could open the door to employment discrimination claims. Ordinarily when

a candidate sends a resume to an employer or staffing company, it is impossible to identify the individual's race; the normal resume does not include a photo. In addition, it is generally impossible to tell from a resume whether a candidate has a disability or, perhaps, figure out his religion; a recruiter viewing a LinkedIn or Facebook account is likely to obtain such information. An applicant who is denied employment is generally covered under federal, state and local laws prohibiting employment discrimination. Thus, when protected information about an applicant is readily available online, there is the potential for an applicant to bring claims against recruiters and their companies, if he alleges that his rejection came about because the recruiter utilized information gleaned from the Internet that was protected by the employment discrimination laws. It is not hard to imagine, for example, a scenario where a woman who is highly qualified for future assignment might be denied employment because of her pregnancy. Depending on the insurance policy in question, a recruiter may not be covered once there is an assertion that a discriminatory act involved the use of social media and electronic media.

Defamation

The circulation of an untrue statement that damages an individual company's reputation is subject to claims of defamation. There are reported legal cases where

individuals have bad-mouthed competitors or their clients in an effort to gain a competitive advantage. In the event that an individual who holds himself out to be an employee or officer of a company makes an untrue defamatory statement, the company as well as the individual, may be held liable for defamation. When such defamation is circulated through social networking sites and over the Internet, there are questions of whether traditional CGL or EPLI policies would cover the claim.

Misappropriation of Trade Secrets

To date it is not at all uncommon for employers and staffing companies to include their client and candidate lists in the databases on their computers. However, where a recruiter has been working with potential candidates or clients using social networking, questions might arise as to who actually owns the client list when the recruiter leaves a particular company to go to another staffing firm or to start another firm. In addition, the unauthorized access and misappropriation of confidential information through the use of computers is covered by the federal statute known as the Computer Fraud and Abuse Act. Our firm has direct experience litigating a case where recruiters started their own firm and, upon leaving their former firm, allegedly misappropriated or deleted confidential candidate information so that they would have exclusive use of it when they left.

Unauthorized access to or deletion of computer information that causes damage in excess of \$5,000 is subject to the Computer Fraud and Abuse Act, which may be enforced by means of a temporary restraining order and injunction or by the granting of monetary damages.

Unfair Labor Practice Charges and Wage Claims

Social networking also raises possible exposure to claims under the traditional labor laws and wage and hour laws. Under the National Labor Relations Act, employees have a right to engage in "concerted activity" where they discuss and attempt to remedy issues concerning terms and conditions of employment affecting the workplace. Employers who attempt to limit employee discussions concerning workplace conditions on blogs and social networking sites, may run afoul of the National Labor Relations Act and find themselves subject to unfair labor practice charges, even where the employees are not unionized.

In addition, alleged violations of the Federal Fair Labor Standards Act and state labor laws that require the

Continued on page 4



THE RISE OF ELECTRONIC MEDIA AND SOCIAL NETWORKING: UNRECOGNIZED RISKS FOR EMPLOYERS AND RECRUITERS

Continued from page 3

payment of minimum wages and overtime generally require non-exempt employees to be paid for all hours worked. Depending on the EPLI policy at issue, it is possible that the cost of defending a litigation for failure to pay wages may not be covered by insurance. For example, employees may claim that while they were talking to their “friends on Facebook” or networking on LinkedIn and the like, they were actually performing company duties, and therefore they were entitled to be paid for their working time.

One way for companies to protect themselves with regard to these new electronic risks is by obtaining a “Cyber Liability Insurance Policy.” Such policies may

offer coverage when other policies may not address situations where state or federal laws require public notification when confidential personal information is inadvertently disclosed. (Such personal information could include specifics regarding social security, bank accounts, driver’s license numbers or, in the case of medical records, patient information.) Notifications to the public regarding such disclosures of information maintained on company computer systems can be extremely expensive and potentially not covered in the absence of cyber liability policies.

All in all, a prudent company will review its insurance policies with its broker and seek assistance to make sure

that it is sufficiently covered for risks presented by the use of electronic and social media.

About Richard L. Steer

Richard L. Steer is a Partner in Tarter Krinsky & Drogin LLP’s Labor and Employment Practice Group and heads the firm’s Employment Practices Liability Insurance practice. He has defended and counseled a wide range of employers, insurance companies and their policyholders in employment discrimination, labor and housing discrimination litigation. Richard can be reached at rsteer@tarterkrinsky.com.

PROTECTING YOUR BUSINESS IDEAS: BEST PRACTICES

By Giuliano Iannaccone and Kimberly Carson

In an all too common scenario, an “Idea Purveyor” presents an idea to an interested party across the boardroom table in a pitch meeting, is informed the idea will not be pursued further, and soon thereafter discovers that the recipient has developed a product or plan which closely resembles the Idea Purveyor’s idea without permission or compensation. Whether the idea is literary, business, or scientific in nature, the rights that an Idea Purveyor has in such a scenario are determined by a contested and evolving body of jurisprudence termed “idea submission law.”

Ideas are not protectable by copyright or patent law, although the expression or tangible extension of an idea may be. This article focuses on protection of ideas themselves. By way of illustration, for example, in 2003, a federal jury awarded over thirty million dollars to marketers who claimed that Taco Bell “stole” their idea to use a talking Chihuahua in advertisement campaigns. This case demonstrates the potential value of an idea.

Mere disclosure of an idea, of course, will not entitle an Idea Purveyor to compensation. Under New York law, if an Idea Purveyor pitches an idea that is both novel and concrete, and the idea is used by the recipient without the Idea Purveyor’s permission in violation of a contractual promise (express or implied), confidential relationship, or property interest, the Idea Purveyor may be able to state a claim for relief.

Despite New York courts’ willingness to consider claims arising under idea submission law, however, in practice it is often difficult for an Idea Purveyor to prevail on a claim for damages or injunctive relief for unauthorized use or disclosure of an idea. Where a court does not find a claim to be preempted by copyright law, it will often find that the idea is not sufficiently novel or concrete, or hold that the claim cannot withstand a defendant’s defense of independent creation. Accordingly, the following five



best practice recommendations may be followed to proactively safeguard an Idea Purveyor’s interests in an idea when marketing it to potential investors, vendors, or business partners.

First, prior to making a pitch, an Idea Purveyor should strive to execute an express agreement to pay for the business idea upon its use. An express agreement should establish the parties’ obligations and specify the types of ideas involved. However, this may not be a practical option for many Idea Purveyors, especially those working independently or relatively unknown in their fields, because recipients are often not willing to sign such an agreement prior to assessing the value of an idea.

Second, an Idea Purveyor should request an express non-disclosure agreement that clearly establishes the

receiving party’s acceptance of a duty not to use or disclose the idea without permission.

Third, where reaching an express agreement is not feasible, an Idea Purveyor nevertheless should clearly condition the disclosure of the business idea on payment upon use or maintenance of confidentiality. In this regard, an Idea Purveyor should take steps to create documentation to support an implied agreement or understanding, both through communications prior to making the pitch and through follow-up correspondence reiterating the parties’ mutual understandings. This may also involve marking all documents submitted with appropriate legends to indicate their confidential and proprietary nature.

Continued on page 5

PROTECTING YOUR BUSINESS IDEAS: BEST PRACTICES

Continued from page 4

Fourth, because courts are most likely to find an implied agreement or understanding to pay or maintain an idea in confidentiality in situations where an idea was solicited and disclosed in a formal business meeting, Idea Purveyors would be well advised to limit disclosure to such contexts if feasible.

Fifth, while an Idea Purveyor may feel naturally inclined to limit a pitch to a skeletal outline in order to shield valuable details, because ideas must be sufficiently novel and concrete to merit protection, Idea Purveyors should submit an idea in its entirety in a tangible form if possible.

Idea Purveyors should feel confident sharing their business ideas having taken the appropriate

precautionary approach. By following the aforementioned best practices, Idea Purveyors should be able to weed out unscrupulous potential partners who are unwilling to recognize the value of their ideas and ensure their pitches land before those best positioned to receive them.

On the other side of the table, businesses that frequently receive ideas, such as those in the entertainment, advertising and technology industries, are subject to risk of claims arising under idea submission law. For such businesses, it is important to have a clear policy statement that clarifies the rights of the parties to such ideas. A policy statement may also require Idea Purveyors to waive rights by virtue of submission.

About Giuliano Iannaccone

Giuliano Iannaccone is a Partner in the International and Corporate and Securities Practice Groups at Tarter Krinsky & Drogin LLP. Mr. Iannaccone represents U.S. and non-U.S. companies in a broad spectrum of international and domestic transactions and acts as general counsel for many of his clients. Giuliano can be reached at giannaccone@tarterkrinsky.com.

About Kimberly E. Carson

Kimberly is a Summer Law Clerk at Tarter Krinsky & Drogin LLP. She is an incoming third-year student at Fordham University School of Law.

SECURITIES TICKER

By James G. Smith

SEC RAISES THRESHOLDS FOR INVESTMENT ADVISERS TO CHARGE PERFORMANCE FEES

On July 12, 2011, the Securities and Exchange Commission raised the thresholds that determine whether an investment adviser can charge its clients performance fees. Rule 205-3 under the Investment Advisers Act allows an investment adviser to charge a client performance fees if the client meets certain criteria, including two tests that have dollar amount thresholds. Effective September 19, 2011, an investment adviser will be able to charge performance fees if, at the time of entering into the advisory contract, the client has at least \$1 million under the management of the adviser, or if the client has a net worth of more than \$2 million. Previously, these threshold amounts were \$750,000 and \$1,500,000, respectively.

About James G. Smith, Partner

Jim is a Partner in the Corporate and Securities Practice Group at Tarter Krinsky & Drogin LLP, where he focuses on complex securities and corporate transactions, investment management and corporate law. He can be reached at jsmith@tarterkrinsky.com.

GETTING TO KNOW... ANDREW S. KOERNER

What do you find most satisfying about practicing law?

I enjoy knowing that I have had a direct positive impact on my client's life. Immigration Law is a unique area of the profession, one where the lasting impact of an attorney's work is so immediately profound and changes the lives of the client and his or her family. Even today, when I call a client to say that their petition has been approved — whether it someone just out of college or the top executive of a large multinational company — the joy and happiness is overwhelming. In those moments I think, this is why I became a lawyer, to help change people's lives for the better.

What was your most memorable legal assignment?

It was the first time I called a client to tell him he was approved. He was a Senior Vice President of a Bank,

yet he screamed in excitement. He told me that he would never forget me and that I had changed his family's life for the better.

When did you first become interested in your area of practice?

In law school I had the opportunity to take part in the Immigration Law Clinic. After that semester I was pretty sure this was the area in which I wanted to practice.

Which historical figure do you most admire, and why?

I admire people who have a vision of how to better the world, to better the lives of everyone in it, and who decide to play their part in helping to achieve that vision, regardless of the size of the part they play and with no intention of receiving acknowledgement for their contribution.

What is your favorite city in the world, and why?

New York, because no matter where I go, I always look forward to coming back.



About Andrew S. Koerner, Counsel

Andrew is Counsel in the Business Immigration Practice Group at Tarter Krinsky & Drogin LLP. He counsels clients in all areas of immigration law and represents numerous national and international companies in their efforts to recruit and retain top multinational staff. Andrew can be reached at akoerner@tarterkrinsky.com.

F I R M N E W S

RECOGNITION

Tarter Krinsky & Drogin's Construction Practice Group has been recognized for the first time by Chambers and Partners as one of the top construction practices in New York City. This year Chambers highlighted the firm's representation of Tishman Speyer in connection with the \$500 million development of the WaveRock Building, a matter that is being led by Partner Eric Zipkowitz.

PRACTICE AREA GROWTH

Earlier this summer we expanded our Trusts & Estates Practice Group with the hiring of Stephen L. Ferszt and Frank H. Klein, both of whom have significant experience representing and advising clients in their estate planning needs. And, as this edition of The TKD Advisor goes to press, TKD is about to announce the formation of our Intellectual Property Practice Group, being joined by Douglas J. Gilbert.

NEW PARTNERS

- Stephen L. Ferszt, who is a Fellow of the American College of Trust and Estate Counsel, where he is a member of the Employee Benefits Committee, and is listed in The Best Lawyers in America and New York magazine's "Top Lawyers" for both Employee Benefits and Trusts and Estates Law, joined TKD as chair of the Employee Benefits and Executive Compensation, and the Trusts and Estates Practice Groups.
- Douglas J. Gilbert, who has over 25 years experience litigating intellectual property matters for leading chemical, pharmaceutical,

consumer product, medical device, Internet and computer industry clients, and has been recognized as a leading patent lawyer by New York Super Lawyers and Expert's Guide to the World's Leading Patent Law Practitioners, joined TKD as a partner in the Intellectual Property Practice Group.

- Giuliano Iannaccone, who represents U.S. and non-U.S. companies in a broad spectrum of international and domestic transactions, and leads the firm's practice with Italian clients, as well as U.S. companies interested in doing business in Italy, joined TKD's International and Corporate and Securities Practice Group.

NEW COUNSEL

- Frank H. Klein, who has advised high net worth clients on estate planning and asset protection matters for more than four decades, joined TKD's Trusts and Estates Practice Group.
- Marilyn Simon, who has four decades of experience representing and advising corporate and individual clients in all aspects of insolvency law, debtor / creditor law, bankruptcy law, and secured transactions, joined TKD's Bankruptcy and Corporate Restructuring Practice Group.
- Eric Su, who represents management in all aspects of labor and employment law, joined TKD's Labor and Employment Practice Group.

NEW ASSOCIATE

- Mark Cermele, who, in addition to a Juris Doctor from the Benjamin Cardozo School of Law, holds a Bachelor of Science degree in Mechanical Engineering, joined TKD's Construction Practice Group.

PRACTICE AREAS

BANKING AND FINANCE

BANKRUPTCY AND CORPORATE RESTRUCTURING

BUSINESS IMMIGRATION

CONSTRUCTION

COOPERATIVE AND CONDOMINIUM

CORPORATE AND SECURITIES

EMPLOYEE BENEFITS AND

EXECUTIVE COMPENSATION

INTELLECTUAL PROPERTY

INTERNATIONAL

LABOR AND EMPLOYMENT

LITIGATION

NOT-FOR-PROFIT AND EDUCATION

REAL ESTATE

TAX

TRUSTS AND ESTATES

The information contained in The TKD Advisor is of a general nature and does not constitute legal advice. Consultation with our personnel is recommended before taking action based upon any of this information. Under the rules of certain jurisdictions, this material may be considered attorney advertising. Prior results do not guarantee a similar outcome.

Circular 230 Disclosure Notice: To ensure compliance with Treasury Department rules governing tax practice, we inform you that any advice contained herein (including in any attachment) (1) was not written and is not intended to be used, and cannot be used, for the purpose of avoiding any federal tax penalty that may be imposed on the taxpayer, and (2) may not be used in connection with promoting, marketing or recommending to another person any transaction or matter addressed herein.