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# Hot~Points

## Might as well face it... You're addicted to ~~LOVE!~~ <sup>the 'Net</sup>

*Remember that cool Robert Palmer hit from the '80s, Addicted to Love? With a quick lyric edit, the song might reflect today's obsession with the Internet. But is this computer craving really and truly an addiction? And just as important, how should employers treat compulsive Internet use at work?*

In a recent case, *Pacenza v IBM Corp.*, the plaintiff claimed, in part, that his firing over compulsive Internet abuse was in violation of the Americans with Disabilities Act (ADA). While the court hasn't yet ruled on the employer's motion to dismiss, its decision could have broad implications for on-line misuse in the workplace.

Is it possible that excessive Internet use—like alcoholism—is a genuine disability?

There's little doubt many individuals do spend significant time using the Internet. A recent study showed 69% of adults are regular users; more than 8% use the 'Net to escape problems; and nearly 6% feel their relationships suffer because of excessive use. But mental health professionals disagree whether overuse constitutes a legitimate psychological "addiction." For Internet abuse to qualify for protection under the ADA, it would have to be recognized as a disability—that is, a physical or mental impairment—that substantially limits one or more major life activity.

While Internet use may impact social interaction, it just doesn't seem to render an individual substantially limited in performing major life activities.

Yet, even if it were to be acknowledged as a disability under the ADA, employers could still discipline or discharge employees for violating electronic communication policies. The ADA does not immunize disabled employees for incidents of misconduct in the workplace—even if that misconduct is "caused" by the disability.

So, as long as employers create and implement uniform electronic communication policies regulating email and Internet usage—and impose penalties equitably and consistently—they are well within the law, provided the policies are job-related to the position and consistent with business necessity.

What's more, employers are required to accommodate a disabled employee's condition only if that accommodation is reasonable and presents no undue hardship.

It's arguably not reasonable for an employee with an alleged Internet addiction to fritter away hours of work time. Nor, since those who abuse the Internet often do so by frequenting adult or sexually explicit Web sites, should they be permitted to expose their employer to liability for a sexually hostile work environment. An employee who violates the company's Internet usage

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# Get Ready for Michigan's New Business Tax



**O**n July 5, 2007, Governor Granholm signed a five-bill package into law, replacing the State's Single Business Tax with a unique double levy of a net-income tax and a modified gross-receipts tax. The new structure also provides some personal property tax relief and enhances the number of available tax credits.

Although revenue-neutral after application of the credits, Michigan's new law significantly changes the distribution of tax liability. Manufacturing enterprises likely will see their tax liability decrease, while non-manufacturing businesses are apt to experience a tax increase. In addition, the tax burden will fall more heavily on non-Michigan, multi-state businesses.

The new tax act is complex and highly detailed. But here are a few of the key changes you can expect.

## General Highlights

- The new tax is levied on all forms of business enterprise having business activity in Michigan
- The tax uses a more encompassing nexus standard than the previous Single Business Tax
- Unitary business groups that are related based on ownership of more than 50% and have a flow of value between entities will file as a single taxpayer
- There are no filing or payment requirements for businesses with receipts less than \$350,000, and there's phase-in liability—via a credit—for those having receipts between \$350,000 and \$700,000

## Net Income Tax

- The base begins with federal taxable income
- A rate of 4.95% is imposed
- Inter-company transactions between members of the same unitary group are not taxed
- "Substantial nexus" is now defined as companies doing business in Michigan for a period of more than one day

## Gross Receipts Tax

- A rate of .8% is imposed on a modified gross receipts base (less purchases of inventory and assets subject to depreciation or amortization)
- Inter-company transactions in the same unitary group are not taxed
- The tax is levied on businesses with "active solicitation" (to be defined by the State Treasury in future guidance) and receipts from sales sourced to Michigan greater than \$350,000

## Personal Property Tax Relief

- Industrial personal property is exempted from the 18-mill local school property tax and the six-mill State education tax
- Commercial personal property is exempted from 12 of the 18-mill of local school property tax
- Property taxed under the industrial facilities tax exemption is also exempt from the local school property and State education taxes
- Industrial personal property is also permitted a 35% credit, which is refundable

## New Tax Credits

- Many existing credit programs are retained and several new credits added: Compensation Credit; Investment Credit; Research & Development Credit; Michigan Entrepreneurial Credit; and a Culture Credit

A number of unresolved issues remain. We will continue to monitor interpretation, guidance, and amendments as the new tax law is implemented—and provide our clients with the necessary assistance.

*Taking a Closer Look at the New Business Tax*

## Spotlight on 2 New Structural Changes

### 1. Use of the Unitary Business Group

In a significant change from the Single Business Tax, the new Tax Act applies the unitary business enterprise concept to define a taxpayer. A unitary taxpayer is any group of U.S. businesses with greater than 50% common control, having a flow of value between the members of the group. The definition is broad and encompasses concepts of integration of activities, inter-dependency, and a flow of value. The new Tax Act requires a unitary business group to file a combined return. While insurance companies and financial institutions pay an in-lieu-of-tax, they can be members of a unitary group.

### 2. The Nexus Standard

For tax purposes, Michigan now requires only a physical presence of more than one day in the state to establish nexus. In addition, for purposes of the gross receipts tax, businesses that actively solicit sales in the state and have gross receipts of \$350,000 or more sourced to Michigan will be deemed to have nexus as well. This broader nexus test applies to individual business entities as well as entire unitary business groups. Out-of-state businesses with minimal contacts here may find their new Michigan tax liability increased in comparison to the former rules.

Help is  
just a  
click away

For up-to-the-minute information on the new Michigan Business Tax, visit [www.michiganbusinesstax.com](http://www.michiganbusinesstax.com)

## E or Paper Hot Points?

It's hard to believe it's been 14 years since we began publishing *Hot Points* to help clients and friends stay up to date on emerging legal issues. A few years ago, we started posting the newsletter on our Web site too. (Just click on Newsroom, and scroll to *Hot Points* for past and current editions.) Now, we're offering our readers an opportunity to rely exclusively on our electronic version of *Hot Points* for news and views.

(Since the e-edition is immediate, you might say it's **HOT, HOT, HOT** *Hot Points*!)

If you'd like to discontinue receiving your hard copy of the newsletter, just email us, [silkworth@millercanfield.com](mailto:silkworth@millercanfield.com), and give us your preferred online address. We'll email you each time a new issue of *Hot Points* is posted to our Web site. **E-asy!**

Join us for our Annual Fall Seminar

### Issues in Labor & Employment Law

October 18, 2007

MSU Management Education Center  
Troy, Michigan

All human resource professionals, managers, in-house counsel, CEOs, and business owners will want to attend this informative update

Details and Registration online  
[www.millercanfield.com/newsroom/seminars.asp](http://www.millercanfield.com/newsroom/seminars.asp)

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# Aircraft Financing Changes Take Effect

*The Cape Town Convention requires electronic registration of security interests. Are you in compliance?*

*The Cape Town Convention has changed the way we buy, sell, and finance many aircraft and engines. While there are a few wrinkles to be ironed out, the overall impact will make aircraft financing less costly. With increased certainty about the security of transactions, a more diverse group of financial institutions may now get involved in lending.*

## **WHAT**

Called the Cape Town Convention on International Interests in Mobile Equipment (after the city that hosted the global diplomatic conference), this legal agreement establishes a process for the registration, priority, and enforcement of security interests in various types of aircraft. The Cape Town protocols came into effect in the United States on March 1, 2006. To date, 38 countries have signed on. Canada has signed the treaty and—although it hasn't yet been ratified—it's expected to be soon.

## **WHY**

The treaty and protocols are designed to encourage and facilitate the acquisition and financing of aircraft equipment by establishing safeguards for creditors. For example, the protocols create an electronic international registry to record all financial interests, and provides creditors with a range of remedies for dealing with default and insolvency.

## **WHO**

All parties to a transaction involving aircraft (bank, borrower, buyer, and seller) need to record details of their transaction on an electronic, international registry. Aircraft owners, financiers, and companies that lease aircraft meeting various size criteria are affected.

## **HOW**

To register a financial interest, you may access the electronic registry 24/7 at

[www.internationalregistry.aero](http://www.internationalregistry.aero). Your registration should be completed well in advance of the financial transaction date, as the vetting process may take anywhere from 48 hours to more than a week.

Under the Cape Town Convention, various types of interest can be registered, including international and prospective international interests, national interests, and non-consensual rights of interests arising under national law.

## **...AND MORE**

Registration of Cape Town-eligible equipment is mandatory, and the failure to properly record an interest may result in a loss of priority should default or loss occur.

FAA filing for airframes and propellers is still required, and the FAA Web site is continuously updating its list of aircraft and engines that qualify for the Cape Town international registry. UCC filings are also still necessary since the Cape Town convention only addresses proceeds from loss, confiscation, condemnation, or requisition.

*Whether you are a lending institution or buyer of affected aircraft, we can walk you through the electronic registration step by step. Call if you would like some help.*

# Investment opportunities continue in biotech and medical devices

The stock market may be on a roller coaster of late, but for investors looking for quality venture capital opportunities in life sciences or medical device development, the ride still looks good.

According to the National Venture Capital Association, 68 venture capital firms raised \$7.2 billion in the second quarter of 2007. While that figure represents a decline in the number of funds, the dollar amount is up—a sign that the venture capital industry is healthy.

Here are a few trends we've observed, along with highlights of the 22 venture capital transactions our firm was engaged in during the last quarter of 2006, and the first half of this year.

## • SERIES A FINANCINGS

Of the 22 transactions, more than half were Series A Preferred financings and five were convertible debt financings. The median pre-money valuation was \$2.5 million; and the average size was \$1 million.

## • MILESTONE FUNDING

Increasingly, venture capital investors are funding portfolio companies in increments, based on reaching operational or developmental milestones. The approach enables investors to confirm a portfolio company's predictions for future success.

## • LIQUIDATION PREFERENCES

The vast majority of transactions contained a 1x liquidation preference. Over half the transactions our firm was involved in provided investors with participating preferred stock that was not subject to a cap. So, in addition to the liquidation preference, investors are able to participate in any remaining proceeds on an "as-if converted to common" basis above the amounts designated as the liquidation preference.

## • MANDATORY CUMULATIVE DIVIDENDS

In nearly half of our financings, portfolio companies agreed to annual dividend rates of 6-8%. Dividends typically were to be paid in cash or stock, and would accumulate if not declared and paid.

## • ANTI-DILUTION

Almost 90% of the transactions provided for broad-based, anti-dilution protection.

## • CONVERTIBLE DEBT FINANCING

This type of financing typically converts to preferred stock, or common stock if the portfolio company is sold prior to the next financing round. It's a very good

vehicle for early-stage investments, and can serve as a bridge between financing rounds. We've seen warrant coverage for the next issued series of preferred stock in the range of 15-30% of the principal amount of the convertible notes purchased in the convertible debt financing. In nearly three-quarters of the convertible debt financings we handled, convertible promissory notes were secured by a lien on the portfolio company's assets.

## • CRAM-DOWN ROUNDS & PREFERRED STOCK OPTION GRANTS

These two innovative tools can help overcome the challenge of retaining management whose stock may be behind numerous rounds of liquidation preferences. In the cram-down, new investors may require all previous investors to participate in a new financing round or convert into common stock. If carried out successfully, this will benefit management and new investors by reducing the amount of liquidation preferences outstanding, and giving the remaining preferred stockholders greater control over the company. Likewise, the preferred stock option grant gives stock options to executives, allowing them to receive the same economic benefits available to the venture capital investors.

## • INCREASING OPTION POOLS BEFORE VALUATION

Venture capital investors are now requiring that the option pool be increased to handle up to three years of option grants. This approach shifts all dilution associated with the option pool to the founders and original investors, reducing the per-share price of the preferred stock for new investors.

## • MANDATORY REDEMPTION

The long path to liquidity—particularly in pharmaceutical companies—has led some venture capital investors to guarantee a liquidity event by requiring a portfolio company to repurchase a venture capital investor's stock after a stated period of time (usually three to seven years). That mandatory redemption may raise financing issues, since banks view the obligation as a company debt. Furthermore, the ability of a portfolio company to redeem can be limited by state law, or the practical reality of generating sufficient funds to repurchase shares.

*Our Life Sciences & Biotechnology Practice Group is prepared to help clients take advantage of all the opportunities within this burgeoning field. Call us if you'd like to know more.*



# SAFETY FIRST

## *Explosive growth in imports ups concerns*

**R**emember that recall of the popular imported toys whose paint contained traces of lead? Yet another timely reminder. While imports provide needed work and trade opportunities for developing countries—and an abundance of affordable goods here—those benefits are not without risk.

Imported products may contain hidden problems that could adversely affect consumers. That's why manufacturers, importers, distributors, and retailers should know the U.S. Consumer Product Safety Commission (CPSC) rules and procedures.

Established by Congress in the Consumer Product Safety Act, the CPSC is responsible for protecting all of us from unreasonable risk of injury or death caused by a faulty item. With jurisdiction over some 15,000 different types of products used around the home, in schools, and for recreation, that's a lot of responsibility.

So, how do the CPSC's rules and procedures work?

When manufacturers, importers, distributors, and retailers learn that their product could fail to meet safety standards or may contain a defect that may pose a danger to consumers, they're required to notify the CPSC within 24 hours.

That notification sets in motion an investigation into the matter to determine whether in fact there's a product hazard and, if so, what corrective action is necessary. The reporting process includes protection for trade secrets and other commercially sensitive information. Failure to comply with reporting provisions of the Safety Act can lead to civil and criminal penalties. After investigation, the CPSC may conclude that no problem exists and corrective action isn't necessary. But when a risk is confirmed, the product must be recalled.

Alternatively, a company may choose to take advantage of the "Fast Track Product Recall Program." Under that program, the CPSC will forego a preliminary determination if the company voluntarily implements a satisfactory recall within 20 working days.

Millions of products have been recalled over the years and today consumers are less likely to view a recall in a negative light. In fact, a timely, responsibly conducted recall can positively influence consumer attitude and reward a company with continuing customer loyalty.

For those reasons and more, it's important that companies develop a comprehensive plan that reaches throughout the entire distribution chain and motivates consumers to respond to a recall. That plan should include a system for collecting and analyzing information concerning product performance, and methods for identifying any product defects or issues that present unreasonable risk of injury.

If you'd like more information about the Safety Act and the CPSC's reporting requirements, or help developing your company's consumer safety plan, please give us a call.





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standards by checking out x-rated Web sites on work time can't plead for his job as an accommodation of his condition.

Regardless of the outcome of *Pacenza*, companies should take note.

If a medical consensus is one day reached, Internet addiction could be categorized as a mental impairment. And, while it's unlikely to be considered as a disability under the ADA for the same reasons Congress excluded compulsive gambling and other similar mental conditions, stranger things have happened.

For now, it's up to employers to create electronic communications policies, and workplace conduct standards that are job-related to the position and consistent with business necessity. Then, it's absolutely necessary to enforce them uniformly every time.

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## Cheers!

This year marks the 15th anniversary of Miller Canfield in Poland. Starting as a small practice in Gdansk in 1992, we've since added offices in Warsaw and Wrocław. Opportunities abound in this dynamic part of Eastern Europe, and we're pleased to be part of the growth. Congratulations to our colleagues in Poland—and thanks for helping to make our international venture a success.

## Gratulujemy!

W roku 2007 mija 15-lecie działalności Miller Canfield w Polsce. Zaczynaliśmy w 1992 roku jako niewielka kancelaria w Gdańsku i od tego czasu wciąż się rozwijamy – otworzyliśmy biura w Warszawie i Wrocławiu. Dynamiczny rozwój Europy Wschodniej stwarza wiele nowych możliwości działań – cieszymy się, że możemy uczestniczyć w tym procesie. Gratulacje dla naszych współpracowników w Polsce! To dzięki Waszemu wsparciu międzynarodowe przedsięwzięcie Miller Canfield odniosło sukces.

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