FINANCING MOVIES AND COMPLETION BONDS

By Mark Litwak

There are different ways to finance a film. One path is to present a package of script, principal actors, director, and budget to a major studio like Warner Brothers with a request that they finance the project.

If the studio says yes, keeping in mind that only a small percentage of the projects pitched are approved, the studio will provide the entire budget. The film is fully financed, and the budget will include a production services fee of up to 10% to compensate the producers for their services. Producers may also be able to negotiate bonus, deferment, and/or profit participation. The studio will own the movie and usually will have the right to make changes and control the final cut of the film. Nowadays major streamers also enter into similar deals.

In this scenario, there is very little financial risk to the producer, because the studio is providing all the funds needed. Moreover, there is often a completion bond and a contingency line of about 10% of the budget to cover any unanticipated expenses or overages. If you are a producer with a track record, this is likely the quickest way to fund your project. But many aspiring producers cannot even get in the door to pitch their projects to a major studio or streamer.

An alternative way to pay for a film could involve private equity and/or debt financing. This is where the producer raises funding from private investors and/or pre-sells distribution rights to various territory buyers. For example, a German distributor wanting to distribute the film in its country might enter into a license agreement which could be collateral for a production loan. This is a more difficult path to take because there are a lot of hurdles that have to be overcome before funding is secured.

These deals require a foreign distributor to sign a contract to license a movie for distribution in their country even though the movie does not yet exist. By pre-buying the movie, the buyer knows that when the movie is completed they will not have to compete with other buyers for the rights to distribute the film in their territory. Pre-sale buyers will usually require a completion bond before committing to license a movie. To read more about pre-sales go to: https://www.marklitwak.com/financing-motion-pictures.html

Whether relying on private investors or bank loans based on pre-sales, a producer cannot commence production until they have assembled a package including the script, stars, director, and budget. Writing a great script can take years of effort. Once the script is ready, the producer then assembles the other elements, namely the lead actors, director, and budget. However, investors, pre-sale buyers, and directors often want to approve the script, budget, and stars before making a commitment.

The script is the blueprint for making the movie. By analogy, when a builder wants to erect a skyscraper, they hire an architect, draft blueprints, obtain whatever permits are needed, and if everything is approved and ready to go, they order materials and start construction.

The time for assembling these elements is called development. When these elements are secured, you begin pre-production by renting equipment, hiring crew, and securing locations. On the first date of principal photography the cameras roll, you commence production.

Investors who are willing to invest early in development take a lot of risk because if the script does not turn out well, or the producer cannot attract the other elements needed, their investment can be a complete loss. If the project never goes into production, there is no potential source of revenue to pay back investors. Therefore, development investors are often compensated generously because they are taking more risk.

Those who invest in production after completion of development also take considerable risk. Their funds are often held in escrow and only if certain conditions are met are they released to be used to produce the film.

Investors are often concerned about what happens if the producer runs out of money before production has been completed and the film delivered. In order to provide comfort, the producer will often secure a completion bond. This is a special type of insurance that provides completion funds if a movie goes over budget such as when the production encounters unforeseen circumstances such as bad weather or a star gets sick. Or, perhaps the worst-case scenario, the star dies without completing his or her role. In such a scenario, the completion bond company steps in to supply enough funds to finish the film. Or if the project cannot be completed, it will reimburse the investors their contributions. Completion bonds are expensive usually costing 2-3% or more of the budget. Some companies may rebate part of this fee if no claims are made.

Completion bond companies are selective in which projects they are willing to insure. They want their premium dollars but don't want to take unnecessary risk. Therefore, they impose many conditions before they will issue a completion bond. The bond company have staff experts in budgeting and production, and they will make sure the budget is a realistic estimate of what it will cost to make the movie. The "strike price," or "production price" is the amount that the guarantor believes will be needed in order to complete and deliver the film. This includes above and below the line costs, fringes, insurance and financing costs, and the completion bond guarantor's fee and the contingency allowance.

The contingency line in the budget is usually ten percent of direct costs to cover unanticipated costs. So, a $20 million film might allocate up to $2 million dollars for these unforeseen overages. The bond is usually issued right before production commences because a lot of documents and approvals need to be secured. The bond company wants to see signed contracts with the director and the stars firmly committing them to perform in the movie. An actor expressing interest in the film is not the same as one signing a binding contract. If the production is funded in part by a bank loan, the bank will not disburse the funds until the completion bond company issues the bond.

The bond company will also insist that the producer buy other insurance to cover equipment breakdowns, liability insurance for accidents, cast insurance, workers comp insurance, negative insurance to ensure the film negative or hard drive is not defective and so forth.

The bond company will review the credentials and background of all the key people making the movie, such as the department heads, director, producer, and principal cast. If your star has a history of drug use, or being unreliable, that person may not be bondable, and the bond company might refuse to insure the production. Stars may also have to submit to a medical exam.

In the event the bond company agrees to bond the film, it is given extraordinary powers. The bond company can fire the director if he or she goes over budget. The bond company is liable for overages, so if a director is taking more time than expected, he can be replaced.

This process can be stressful for the producer because so many deals need to be finalized quickly. What happens if the producer signs a deal with a star and guarantees a one million-dollar fee with a start date of July 1, and then is unable to secure a co-star, director, or other essential element of the package? The producer could lose the star, have to pay her fee, then start the process over.

Movie stars usually will not agree to perform in a film without the producer committing to pay them. That is because if you are a star like George Clooney, you are offered hundreds of projects every year. Even an actor who is a workaholic only has time to perform in a few movies each year because each one takes several months to shoot, plus rehearsal time and post-production for looping after the shoot.

So, if you offer Barbara Streisand a role in your movie, and she wants to do it, she will not firmly commit to it until you give her a start date and guarantee that she will be paid her fee, regardless of whether or not you actually commence production. Because Barbara Streisand knows once she signs a contract with you, if the next day she is offered the role of a lifetime, in a movie about something she cares deeply about, she will have to turn that job down. So, she is not going to firmly commit to be in your movie until you have secured the entire production budget or at least commit to pay her regardless of whether you can assemble all other elements needed to go into production. Moreover, if you are an independent producer, you will have to make a substantial deposit in an escrow account for her to sign a contract. If she is contracting with a major studio, she might not require this, but for an independent producer, her agents will insist on a deposit. And stars may also require approval over the selection of the director, co-star, and any script changes.

Arranging financing for film projects is often difficult even for experienced producers. Unlike some products, no one can really predict the potential success of a film so there is always a lot of financial risk that has be taken when producing a film.