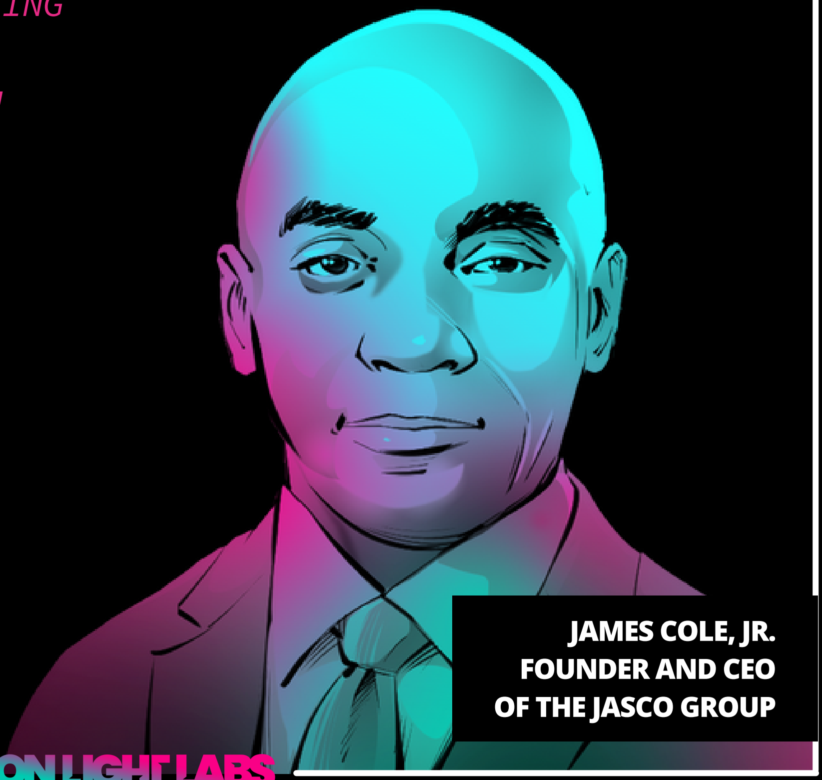
LAB REPORT

AN IRON LIGHT LABS PRODUCT

Nontraditional Film Financing

BY JAMES COLE, JR.

IRON LIGHT LABS



JAMES COLE, JR.
FOUNDER AND CEO
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Executive Summary

"Movies can and do have tremendous influence in shaping young lives in the realm of entertainment towards the ideals and objectives of normal adulthood."

-Walt Disney

The art of storytelling is one of the oldest and most profound methods of disseminating information, and it has significantly evolved over the years. From oral stories to written books and now films, we have created increasingly influential ways to shape the hearts and minds of our audiences.

Today, we have filmmakers of all sorts spreading their truth, introducing people across the globe to a reality otherwise unbeknownst to them. We have the opportunity to hear stories of inspirational triumph, tragic loss, and everything in between. However, creating films can be costly and many storytellers do not have the luxury of being backed by large corporations. Even for the most basic short films, budgets have to include costs for actors, set, equipment, and insurance—just to name a few. The starting price for all this is thousands of dollars, but it can be tens, if not hundreds of thousands of dollars, depending on the movie. It is simply unrealistic to believe that a person or an organization without a dedicated filmmaking budget has access to the funding required to produce a film. This is why expertise around film financing is so important, especially for independent filmmakers.

This Lab Report provides a detailed description of how to finance an independent film, including how to create a financing plan, an overview of financing sources, and post-financing steps.

James Cole, Jr.

James Cole, Jr.
The Jasco Group, Founder and CEO

4 Step Process

NON TRADITIONAL FILM FINANCING

1. DUE DILIGENCE
2. TYPES OF FINANCING
3. GAP FINANCING
4. POST-FINANCING

1 DUE DILIGENCE

Before seeking financing, there are a few tasks that should be undertaken to ameliorate potential issues and maximize the amount of money raised. We refer to this step in the financing process as due diligence. To answer any questions from potential investors or contributors, you as the creator should have all the information about the film in what we call a pitch deck. This includes the name, team (cast, producers, and directors), a description of the film, social impact goal, target audience, budget, financing plan, and distribution strategy. The budget sets forth the cost of making the film, while the financing plan sets forth the sources, and related amounts, of financing. A lot of this is general information about the film, but the more nuanced topics such as impact goal and distribution strategy help investors gauge not only if the project is for them but if they have confidence in the team to execute.

2 TYPES OF FINANCING

EQUITY

There are multiple sources of funding to finance a film. The foundation is equity financing. This is when you sell a percentage ownership (equity) of the film. First, you should form a limited liability company (LLC) and then transfer the rights to the film to the LLC. This way you can split up ownership of the company rather than dealing with the complications of splitting the film up directly. Additionally, working under an LLC protects your investors from potential lawsuits, making them feel more secure and more willing to invest. An operating agreement should also be created to set forth the organizational structure of the company and how the company will be managed.

Next you should create agreements with investors that detail their ownership, contribution, credit (production role or not), and limits on liability, among other things, specific to the film. The agreement should also include a recoupment schedule, called “the waterfall,” which sets forth how revenue from the film will be allocated among investors, debt financiers, talent, sales agents, other service providers, and the production team.

Finding equity investors is not an easy task. But if you understand what motivates different types of investors, and cater to those motivations, you will increase your likelihood of attracting investors. There are several types of equity investors, including those who (i) seek financial return, (ii) appreciate art, (iii) want to discover new ideas or experiences, (iv) seek social impact, or to make the world a better place, (v) are excited about filmmaking generally, or (vi) are excited about "walking the red carpet" and rubbing elbows with actors, directors, writers, producers and other creatives. Think about how your film addresses those types of investors and modify your pitch accordingly.

Due to the difficulty in finding investors, you should maintain a relationship with them such that they will want to invest in your future projects. You will want to under-promise and over-deliver. Do not set investors' expectations so high that you cannot achieve them. Be realistic about what you can accomplish, then work hard to exceed expectations. Other best practices include transparency and periodic updates on the status of the project.

SPONSORSHIPS AND GRANTS

Sponsorships and grants are similar to equity investments in the sense that individuals or organizations are devoting resources to the creation of the project. In this case, the resources may not just be money. Sponsors could give you equipment, space to shoot, a place to hold screenings, and many other things, including money. The primary difference is what you give to them. Although they do not have equity in the film and will not receive money back from revenue, they will expect name recognition and, in certain cases, for the film to have a social impact. This could be in the form of credits in the movie or in advertisements, or updates on the social impact of the project, which might include the number of individuals reached or other milestones. If they give you a venue to set up screenings they could require you to set up banners recognizing them as sponsors for the project or event.

CROWDFUNDING

Crowdfunding is another type of financing used to raise money for films. Unlike receiving money from sponsors and equity investors, there are no complex contracts or agreements that need to be created. With crowdfunding, you publicize the production of your project and ask people to contribute to its creation. In its most basic form, you are trying to persuade people to give you money based on how intrigued they are with the project. In some instances, you can offer perks for contributions. This could be in the form of a credit on the film, tickets, or anything you can give to encourage contributions. This could vary depending on the amount of money contributed or there could be standard perks. A few of the most popular sites for crowdfunding are Kickstarter, Indiegogo, Gofundme, and Patreon. Using any or all of these sites is completely acceptable and will make it significantly easier to reach your fundraising goals. Although it is not complicated to create a crowdfunding account, you will need a strategy. One key component of your strategy should be a marketing campaign, including, most importantly, social media.

A lesser-known strategy for crowdfunding involves momentum. People are less likely to donate to a campaign that has yet to receive contributions. They feel that others have not donated for a reason so they should shy away too. A good way to ameliorate this concern is by obtaining soft commitments for the project before going live with the crowdfunding campaign. Twenty-five percent of your total goal is a good reference number for a soft commitment. Once the crowdfunding campaign goes live, contributors who made soft commitments should immediately contribute. That way your project will have momentum and others are more likely to contribute as well.

Finally, just tell your story. You can come up with plenty of incentives to give out, but if people do not understand or are not intrigued by the film, they probably will not contribute. Be your genuine, unadulterated self, or clearly explain the mission of your organization, and let the public know why you are so passionate about creating the project.

STATE FILM REBATES & TAX CREDIT

Now that you've received money from investors, sponsors, and the general public, it is time to go to state and local government. You may think the state gains no benefit from your indie film—however, states benefit through movies being filmed in their area because it drives the economy through employment opportunities, revenue, and related infrastructure development. Importantly, the rebates or tax credits the state provides are contingent on fulfilling promises to shoot in the state, hiring people from the area, or other criteria. So there are plenty of incentives for states to offer credits and rebates. As you research state and local incentives, pay close attention to the details. Some incentives may be tax-free, while others may be taxable. The state can also offer bonuses or discounts on local goods and services. This ranges from equipment to shooting sites, or even food for the cast and crew.

After you have selected a state or locality and understand the criteria, all you have to do is finish the movie and comply with any other requirements, and the state will uphold its end of the bargain. The only problem with all this is that you need the money to shoot the film. Although it seems like a real challenge, it really just adds an extra step to the process. To get the money to actually finish the movie, you can take the agreement with the state to lenders and request a loan with the rebate as collateral. Certain financiers will loan you the money and once you deliver the film to the state you repay the financier with the funds you receive from the state or local government. One caveat to this is that it will cost you money to receive a loan. Lenders typically charge 10–15% of the money loaned, but this can change depending on experience, budget size, timeline, and overall risk. So you will want to increase your budget accordingly. One more positive thing about receiving incentives is that you reduce the amount of equity investors in your film. This means you keep a higher percentage ownership of the company and accordingly, keep more profits.

PRE-SALES

Pre-sales are commitments from international or US distributors to purchase the rights to sell your film in a particular territory for a given period of time. Just like state and local incentives, you will not receive the money until after the project is complete. But the agreements can also be used as collateral to obtain additional financing to complete the project. So, like tax rebates and credits, you can approach a lender and borrow the amount of the pre-sale.

You can solicit distributors directly or use a sales agent who can solicit distributors on your behalf. Most films use pre-sales in some capacity. The packages received from distributors are based on a number of factors, similar to state incentives. However, these packages are based less on the credibility of the company owner and more on the actual project. Key criteria include the director, cast, producers' resume, and genre of the film. Another advantage of working with a distributor is marketing. Distributors' profit on the project is determined by how many people pay to see the movie so it is in their best interest to help with or take the lead on marketing. But be mindful of the contractual details; some distributors may not cover marketing expenses

UNION BONDS

If your film is feature-length and has actors who are members of unions such as SAG-AFTRA, you may be required to make a bond (or security deposit) with the union. If applicable, unions typically charge a percentage of your total payroll. The bond is required to be paid prior to commencement of principal photography and is returned when principal photography has wrapped and all required paperwork has been submitted to the union, which could be weeks or months following the conclusion of principal photography. The bond cannot be used to pay your actors, so the deposit is basically an add-on to your budget. One way to alleviate the need to raise the amount of the bond as part of the financing is to seek a loan collateralized by the bond. Lenders typically charge 10%–13% of the total bond amount. So the amount of that fee must be included in the budget for the film.

3 GAP FINANCING

Let's assume that your film has a budget of $100,000, and that you have raised $40,000 in equity, received $15,000 from sponsors, successfully crowdfunded $10,000, and through collateralizing state rebates and pre-sales contracts, you secured $25,000, for a total of $90,000. Where can you obtain the final $10,000?

Gap financing is the difference between all the money you raised from financing sources and the budget for the film. Most often gap financing comes in the form of a loan that is paid back from revenue before equity. Generally gap financing is only available if you have already raised a substantial portion of the budget. Depending on your reputation and that of your sales agent, some banks may require that you have raised anywhere between 60-80% of your total budget. Furthermore, they may ask for sales estimates, in addition to pre-sales, from a reputable sales agent that total 1.5 to 2 times the amount they are lending. The criteria providers of gap financing evaluate is similar to that used for pre-sales financing. Due to the risk, gap financing tends to have relatively high interest rates, ranging from 7-15% and in some cases up to 25%.

4 POST-FINANCING

You finally have all of the financing; now you can stop worrying about funds and devote all your attention to making your film. Not quite. There are a few things that you should pay attention to once you have obtained financing. One of the most important things is to update your financing sources about the progress of the project. This applies more to equity investors than other financing sources because they have the most risky interest in the film. It is good to stay in everyone's good graces because you never know if you will need more money in the future for your current project or future projects. You should also focus on fulfilling all the contractual requirements such that you receive all your conditional funds, including state and local tax credits and rebates and pre-sales amounts. In addition to delivering the film, you should finalize the recoupment schedule and add anything you may have missed along the way. Once you have done all this, all your financing bases should be covered and you will be good to go.

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ABOUT IRON LIGHT LABS

Iron Light Labs is an award-winning nonprofit focused on R&D for social impact. The nonprofit is called "Labs" because it experiments, innovates and tests to discover the best way to drive change. Iron Light Labs is building a future where storytellers leap out of their echo chambers, creators partner with effective messengers, changemakers experiment with emerging media, and everyone measures what matters.

ABOUT James Cole, Jr.

James Cole, Jr. is the Founder and CEO of The Jasco Group, a multidimensional investment management firm based in New York City. He also produces and invests in independent films and broadway productions.

James is also a member of the Board of Directors of American International Group, a leading global insurance organization. He also serves as the Chairman of the Board of Entrepreneurs of Tomorrow and serves on the Board of Directors of Jumpstart.

James served as the U.S. Delegated Deputy Secretary of Education under President Barack Obama where he was the Chief Operating Officer and oversaw a broad range of operational, management, policy, legal and program functions, including the Department's work on President Obama's My Brother's Keeper Task Force.