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Checklist

# Investor Advice For Choosing Indie Films

**By Mark Litwak**

*This article is the first of a two-part series.*

FILM investments have a bad reputation, and deservedly so. Motion pictures are as much an art form as a business, and, consequently, creating a marketable product will always be risky. The major studios regularly release big-budget flops made by top writers, filmmakers and stars. The batting average of independent producers is no better.

Movie investments are also avoided because of the many stories of financiers who complain they have been cheated by producers or distributors. The industry appears to attract more than its fair share of disreputable characters. The glamour of the business ensures a steady stream of star-struck investors motivated by non-financial concerns. Consequently, experienced investors often refuse to even consider film-related investments. This is unfortunate because an intelligent investment in a motion picture can earn substantial returns. Not only can the film earn revenue from box office receipts, but there are many ancillary sources of income that include revenues from television, home video, merchandising, music publishing, soundtrack albums,

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Talent Agencies Act

# California Court Finds Violation By Manager, Despite Lack of Fees

**By Edwin F. McPherson**

A PERSONAL manager who charges no commission for soliciting employment for an artist nevertheless violates the California Talent Agencies Act, Cal. Labor Code Sec. 1700 et seq., the California Court of Appeal, Second Appellate District, Division Two, has decided. The ruling renders void such artist agreements with managers who lack a state talent agent license. *Park v. Deftones*, B124598 (May 11). But the Court of Appeal's reading of the language of the statute has problems.

The case arises out of a series of written management agreements between Dave Park and the members of the music group The Deftones for the years 1992, 1993 and 1994. Park acted as the band's personal manager from its inception in 1991 through February 1995. In September 1994, The Deftones entered into a recording agreement that was apparently secured by Park with Maverick Records. Five months after the recording agreement was executed, The Deftones terminated Park's services.

In October 1996, Park filed a breach-of-contract action against The Deftones in Los Angeles Superior Court, seeking to recover recording agreement commissions. In the same complaint, Park sued Maverick Records and Guy Oseary, one of Maverick's partners, for intentional interference with contractual relations, claiming that Oseary strongly and continuously urged the band to replace Park with a "stronger" manager.

Four months after the suit was filed, The Deftones filed a petition with the California labor commissioner, seeking to void the management agreements on the ground that Park had violated the Talent Agencies Act. The superior court action was stayed pending the outcome of the labor commission proceeding.

The labor commissioner found that Park had violated the act by soliciting and securing 84 performance engagements for The Deftones and that Park's 1992, 1993 and 1994

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management agreements were "null, void and unenforceable." The Los Angeles Superior Court affirmed; in June 1998, the court granted judgment in favor of The Deftones, Maverick and Oseary. (Maverick and Oseary argued that, if the underlying agreements were unenforceable, there was no contract with which to interfere.)

## Statute of Limitations

Park argued in the trial court and on appeal that The Deftones' labor commission petition was time-barred. Labor Code § 1700.44 (c) provides that:

> [n]o action or proceeding shall be brought pursuant to this chapter with respect to any violation which is alleged to have occurred more than one year prior to commencement of the action or proceeding.

The evidence indicated that the last occasion on which Park booked a concert for The Deftones was in August 1994, more than two full years prior to Park's commencement of the superior court action, and almost three years prior to The Deftones' commencement of the labor commission proceeding. The labor commissioner ruled that the supposedly strict one-year statute of limitations in § 1700.44 (c) did not bar The Deftones' claims. The labor commissioner also said that Park's attempt to collect commissions under the void agreements was, in and of itself, a violation of the act.

The superior court noted that the "Labor Commissioner's interpretation . . . assures that the party who has engaged in illegal activity may not avoid its consequences through the timing of his own collection action" (i.e., Park's filing suit more than two years after he last booked a Deftones concert).

This portion of the ruling might make more sense if Park were attempting to recover commissions for services that he performed in violation of the act. Park only sought to recover commissions for his participation in securing a recording agreement, which is completely proper activity not prohibited by the act. It is difficult to understand how seeking commissions for sanctioned behavior could possibly constitute a violation of the act.

Essentially, what the commissioner has ruled and what the California courts have endorsed, is that a manager who has ever violated *any* provision of the act, even once, whether within the past year or the past 30 years, can never recover any commissions from an artist. There appears to be no support whatsoever in the act itself for such a concept.

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## Incidental Procurement of Employment

The court next addressed Park's claim that, because his goal in procuring engagements for The Deftones was ultimately to obtain a recording agreement, his actions were exempt from regulation. The court rejected this argument, citing *Waisbren v. Peppercorn Productions Inc.*, 41 Cal. App. 4th 246 (1995).

In *Waisbren*, the defendant argued that his primary function was to counsel the artist with respect to his career and that the vast majority of his activities were directed to counseling duties, as opposed to "procurement." He further argued that the procurement activities in which he engaged were incidental to his counseling activities. The *Waisbren* court concluded that even incidental activity in procuring employment for an artist is subject to Talent Agencies Act regulation.

At the time, the law in California appeared to be *Wachs v. Curry*, 13 Cal. App. 4th 616 (1993), in which the personal manager plaintiffs brought a declaratory action challenging the constitutionality of the act. The plaintiffs argued that the act's exemption from licensing for procurement activities involving recording agreements violated equal protection and that the definition of "procurement" was unconstitutionally vague.

The *Wachs* court rejected both the plaintiffs' claims. The court noted that the act only applies to "persons engaged in the occupation of procuring employment for artists" and that "occupation" in that context refers to procurement activities that constitute a significant part of the individual's business. The *Wachs* court therefore stated that, consistent with New York law for many years, procurement activities that are incidental to one's primary counseling activities are exempt from the prohibitions of the act.

However, 2-1/2 years after the *Wachs* decision was published, the *Waisbren* court rejected the *Wachs* court's interpretation — and a dictionary definition — of the word "occupation." The *Waisbren* court claimed that the discussion in *Wachs* of the definition of "occupation," and that court's ruling that incidental procurement was acceptable, were dictum and wrong.

In this author's opinion, the *Waisbren* rule is devoid of

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any practical application in today's entertainment arena; the *Wachs* rule is much more entrenched in reality. But the *Park* court agreed with *Waisbren* that, not only was the *Wachs* court's interpretation dictum, any form of procurement by an unlicensed individual or entity, no matter how incidental to that individual's or entity's duties, violates the Talent Agencies Act.

## No Commission Charged

Park further argued that his procurement activities were not regulated by the act, because he never charged a commission for that work. The court acknowledged that the act "only regulates those who engage in the occupation of procuring engagements for artists." Park also pointed to language in the Waisbren case that clearly supported his position. The *Waisbren* court indicated, at footnote 6 of its opinion, that "[b]y using [the term 'occupation'], the Legislature intended to cover those who are compensated for their procurement efforts."

Nevertheless, the *Park* court held that, because the issue of compensation was not before the court in *Waisbren*, *Waisbren*'s use of the word "compensation" was dictum. The *Park* court also concluded that the *Waisbren* definition was "not supported by the purpose and legislative history of the Act," noting that "[o]ne may engage in an occupation which includes procuring engagements without receiving direct compensation for that activity."

The appellate court noted that the purpose of the act is to do more than regulate the amount that can be charged for procurement activities and that, because "the Act is remedial, it should be liberally construed to promote its general object." The court went on to say that "[t]he abuses at which these requirements are aimed apply equally where the personal manager procures work for the artist without a commission, but rather for the deferred benefits from obtaining a recording contract." The appellate court affirmed the lower court's grant of summary judgment for the defendants, stating a general rule that "the Act requires a license to engage in procurement activities even if no commission is received for the service." (Park expected his compensation to come from his commission for obtaining a recording contract.)

## The Purpose of the Act

Although the court speaks in lofty terms about the "purpose" and "remedial" nature of the act, and the "abuses" to be remedied by the act, it is difficult to ascertain the purpose of the act to which the court is referring, or the precise nature of the abuses that the court is addressing, when a manager charges nothing for his procurement activities.

Even if the manager receives "deferred benefits" from such activities by receiving a commission in connection with a recording agreement, how could this adversely affect the artist when the procurement of recording agreements is exempted by the act, and any and all commissions received by a manager in connection with the procurement of such a recording agreement are perfectly proper and legal?

The act does not preclude a manager who has not engaged in any prohibited procurement activities from charging an 80 percent commission for securing a recording agreement. The record in the Park case indicated that the manager was to receive only a 20 percent commission for the recording agreement, and this is well within industry standard. Does it really make sense that it is lawful for a manager to charge 80 percent solely for securing a recording agreement, but it is unlawful for a manager to charge 20 percent for both securing a recording agreement and booking 84 performances?

Once again, it appears that, notwithstanding the court's — as well as the labor commissioner's and other courts' — statements that the act is "remedial" and that the purpose of the act is supposedly to protect the artist, it is not the artists who are being protected, but the agents. In fact, the act in this case is protecting the very same agents that refused to represent The Deftones when Park was booking their performances, because the band was not getting paid enough money to generate enough commissions for those agents.

It seems that, with even minimal common sense, one can understand that an artist who pays someone 20 percent of his or her gross earnings to secure (and negotiate) a recording agreement and to book 84 performances is better off than an artist who has to pay one person 15 percent or 20 percent for the record deal, and someone else another 10 percent for the bookings (on which the manager also

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# A Checklist for Film Investors Considering Indie Projects

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sequels and remakes.

As an attorney who represents investors as well as filmmakers, I have learned ways to reduce the risk of film investments. Following is my checklist:

- **Due Diligence.** Thoroughly investigate the reputation and track record of any producer or distributor your client contemplates doing business with. Speak to filmmakers and investors who have done business with a candidate. Check court records to see if the company has been sued. To research distributors, visit the Filmmaker's Clearinghouse, which I sponsor along with Film Arts Foundation, the Association of Independent Video and Filmmakers, and MovieMaker Magazine. The survey form, and the responses, can be found at the Entertainment Law Resources web site (*http://www.marklitwak.com*).
- **Full Disclosure.** Federal and state security laws are designed to protect investors. Offerings to the public generally require prior registration with the Securities Exchange Commission or a state agency. Usually, private placements are limited to persons with whom the offeror has a pre-existing relationship. Even if registration is not required, the antifraud provisions of the security laws require that the offeror make full disclosure of all facts that a reasonably prudent investor would need to know in deciding whether to invest. The information disclosed should include a detailed recitation of all the risks involved in developing, producing and marketing a movie. Avoid offerings that appear to violate this requirement by making less than full and truthful disclosure. Carefully review the prospectus.
- **Track Record.** Do not back a filmmaker or production team that does not possess the proven skill needed to make a professional-looking movie. Avoid first-time filmmakers. Investors are safer backing filmmakers who have completed at least one short or a feature-length work.
- **Identify the Potential Market for the Film.** There is a very limited market, and modest potential revenue, to be earned from short films, documentaries, black-and-white films and foreign-language pictures. Distributors and exhibitors are prejudiced against motion pictures shot on videotape. They prefer films shot on 35mm stock, although quality films shot on 16mm or Super 16mm stock can obtain distribution. The top festivals do not exhibit motion pictures on videotape.

Certain themes, topics and genres can be difficult to sell. Religiously themed pictures can easily offend audiences. Cerebral comedies can be difficult to export, because their humor may not translate well. Films with a great deal of violence may be shunned by European television stations, which are prime markets for independents. Films with explicit sex may not pass censorship boards in certain countries.

Independent films without name actors are difficult to sell. Of course, name recognition varies around the world. The star of an American television series may be a big name in the United States, but unknown abroad. On the other hand, some actors have large followings abroad, yet are relatively unknown in the United States. There are several publications that can be consulted to determine the commercial appeal of actors. The Ulmer Guide (*julmer@primenet.com*) surveys financiers, sales agents and other industry insiders. Also, the Hollywood Reporter [(213) 525-2087] publishes its "Star Power" guide.

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receives a commission).

It appears to require even less common sense to understand that an artist is much better off having someone secure 84 performances for him or her free than to have someone else secure the same 84 performances for 10 percent of his or her gross earnings.

What is quite clear, however, is that a starving artist who has a manager that will invest his or her time, effort and money into that artist, with only the hope of recouping that investment, and who may secure performances for that artist (with or without charging a commission), is better off than the artist who cannot obtain agency representation, has nobody willing to invest in his or her career and therefore does not get to perform at all (and presumably does not secure a recording agreement, either). However, it appears that neither the labor commissioner nor the California courts will be rendering any assistance in remedying this abuse. In light of the vast changes that have occurred in the entertainment industry during the past 15 years, as well as labor commission and court decisions that have expanded the act beyond anyone's expectation, it appears clear that a new commission should be created by the California Legislature, to examine many aspects of the act, the most fundamental of which is the issue of whether or not it really protects the class of people that it was designed to protect. ■