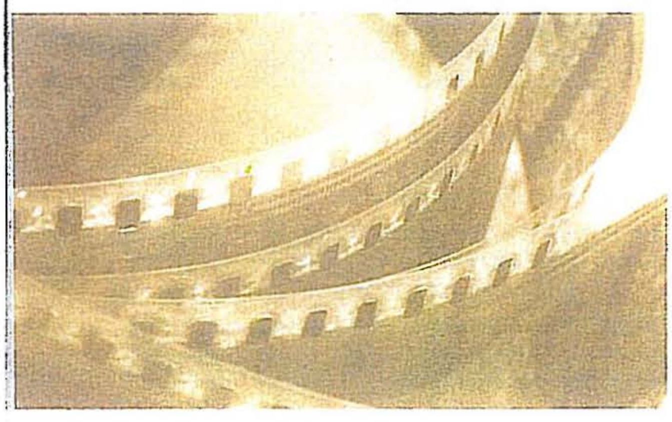
To Guarantee or Not to Guarantee

A COMPLETION BOND IS THE QUESTION

Q: Is there any reason to use a completion bond if I'm not using a bank loan for my film? —Tony F., SYLMAR, CA

A: A completion bond provides a guarantee to film financiers that the film in which they are investing will be completed. For all practical purposes, a completion bond acts as insurance—although, technically, the bond is a "guarantee" and not an insurance policy. However, the mechanics of a guarantee are very similar to those of an insurance policy. The producer pays a premium to the bond company in exchange for a guarantee that the film will ultimately be finished and suitable for delivery to a distributor in the event that the producer goes over budget and would not otherwise be able to complete the film.

The predominant attitude among producers is that completion bonds are only necessary at the insistence of equity financiers, lenders, distributors or some other interested party. This attitude prevails because producers fear that the bond company will unnecessarily interfere with their creative vision. Producers would rather spend the substantial sum necessary for purchasing a completion bond on actual film elements. Statements such as "let's put the money into the picture instead of into the hands of an unnecessary administrative cost" pop up quickly when talk of a non-mandatory completion bond is broached. A bond costs about five percent of the total budget of a film—and generally only films with a minimum budget of $1 million or more qualify.



"What guarantees can I give you? I am the hunted one. I've missed my chance. You think too highly of me, my friend... I am not so clever."

—Virgil Sollozzo to Michael Corleone in response to Michael's request for a guarantee that there will be no further attempts on his father's life in *The Godfather*

REPAYMENT Lending institutions uniformly insist on having a completion bond in place before lending money for a film. The lending institutions understand that collateral for the loan will only exist if the film is actually made and ready for exhibition. Before the advent of completion bonds, banks were wary of lending to producers who were usually unable to show how potential budget overages would be addressed. Without proof that a film would be completed, the loans were seen as too speculative or risky. No finished film means no possibility of repayment on the loan. Completion bond companies provide lenders and other financiers with a service that gives them the assurance that the film will be completed on schedule and that the budget overages will not be the financier's problem.

Like lending institutions, sophisticated equity financiers with a background in film finance understand the importance of a completion bond. The vast majority of films that do not employ lender financing or sophisticated investors with the power to demand a bond rarely take advantage of the completion bond guarantee. I believe it is the ethical duty of every producer seeking financing—even if only from friends and family—to inform potential investors of the existence of completion bonds and explain how they function. They should also explain what can happen if the film does not have a completion bond and eventually goes over budget. Information about what will happen in the event the film's budget exceeds the amount of money raised by a producer is a material disclosure that, legally, must be communicated when seeking equity financing via a private placement offering.

LOSS OF CONTROL Many producers believe that completion bonds only act as a detriment to the creative process. To paraphrase the banditos in *The Treasure of the Sierra Madre*, when posed with the option of voluntarily obtaining a completion bond, most indie film producers reply, "Bonds? We don't need no stinkin' bonds!"

Contrary to this prevailing attitude, completion bonds are a benefit to producers, because the bond ensures that their labored efforts will not be for naught in the event that money troubles or unforeseen disasters strike the film. Completion bond companies are not the enemy.

It is true that, as a condition of the bond, the bond company has the right to take control of the film if the production goes over budget and falls behind its shooting schedule. But contrary to popular belief, the bond company does not *want* to take over your film. The bond company makes more money if it simply takes the production company's premium and never has to do another thing.

Wise producers can take full advantage of the bond company's vast knowledge and experience in completing a film on time and on budget. In order to obtain a completion bond, the application process will require a careful scrutiny of a film's projected budget, a process that sometimes reveals unforeseen contingencies that may have been overlooked by the producer.

THE APPLICATION PROCESS The application process for a completion bond is also known as the "Production Evaluation." During this process, the completion bond company will seek to gain a comprehensive understanding of a film by requiring the producer to disclose information relevant to the making of the picture. The bond company will review the script, shooting schedule and budget. Most bond companies prefer that these three documents have prior approval from the financiers and distributors of the picture (if they exist) prior to its evaluation. These three documents will be thoroughly examined by the bond company, so the producer should pay careful attention to details when drafting the budget and the shooting schedule for the particular script at issue.

The completion bond company is not interested in altering the creative or artistic vision of the screenplay; the bond company does not care what your film is about or how the characters develop and grow from Act I to Act III. Rather, their interest in the screenplay is only to dissect it and determine whether your budget and shooting schedule are realistic for what the screenplay requires. Sometimes the completion bond company will reject the bond application outright after reviewing these documents. But if they have a concern about the budget, it is more likely that they will ask questions and request revisions to the budget, shooting schedule or certain expensive scenes. Producers often see this as the bond company "stifling" their vision. But if they lack the sufficient funding to complete the project, no one but the creator will be capable of seeing that vision anyway.

The completion bond company forces the producer to take a hard look at these elements and the crew that has been assembled to maximize the likelihood that the film will be produced on time and on budget. Even if a bond is not obtained, the application process itself is a worthy exercise for all producers, as it provides a wake-up call about items a producer may never have contemplated. It is better to realize, in pre-production, that an effects-heavy explosion scene could be easily—and affordably—replaced with stock footage.

If the completion bond company approves the screenplay, shooting schedule and budget, an application will move to the next stage of the production evaluation. In the next stage, the completion bond company will evaluate the key members of the production team to determine whether these individuals are "bondable" for the particular project. The bond company will look at the past track record of these individuals.

Once the completion bond company performs the production evaluation and is satisfied with the requisite documents and personnel, the bond company's legal department will confirm that the proper rights have been obtained by the producer for the story, screenplay, intended music and other essential elements requiring releases. If the completion bond is granted, the bond company's legal department will also draft what is known as a "Letter of Intent." The letter of intent is issued to the producer in order to confirm the "Guarantee of Completion." The letter of intent may also identify other costs and concerns not contemplated by the producer in the original budget, such as legal, music and hidden post-production costs. It will also specify the bond company's fee, which is usually due upon completion of the legal documentation—or no later than the first day of principal photography.

CLOSING THOUGHTS While many indie producers are all about the big picture and do not sweat the small details, it is these little details that must be considered to maximize the likelihood that your film will be completed. Producers should view the completion bond company as a fiscally-wise and encouraging parent, permitting its child to make its movie its own way—but only after first laying down the ground rules. Nobody wants their parents constantly looking over their shoulder. But when you get in a jam, it's nice to know that they're there. MM

Want David Pierce to answer your legal question? E-mail counselor@moviemaker.com.