

Filmmaking 101: Duties of the Film Company¹

Jon M. Garon²

This column is one of a series of book excerpts from INDEPENDENT FILMMAKING, THE LAW & BUSINESS GUIDE™ FOR FINANCING, SHOOTING & DISTRIBUTING INDEPENDENT & DIGITAL FILMS designed to introduce filmmakers and others interested in creating digital content for their websites, classrooms or other uses on the legal issues involved in the filmmaking process.

As mentioned in Chapter II, a typical film company of even modest size quickly undertakes all the attributes of a well-established business. The company, however legally structured, will need to engage employees, rent equipment, pay taxes, raise working capital, and sign contracts with landlords, insurance companies, lenders and many others. If at all possible, the duties of filmmaking should be separated from the duties of operating the film company. While many filmmakers serve as chief cook and bottle washer, team efforts are often more successful. In this way, the filmmaker working with an actor regarding character does not have to be discussing her payroll and tax forms at the same time. The separation of the business from the artistic functions improves both professionalism and focus.

While a film company has all the same legal and business obligations of any service company, certain obligations are most important for the successful completion of the film. The following introduces the most basic of these areas.

A. Financial Accounting & Responsibility.

The financial accounting of a motion picture is extremely detailed, complex and vital. It is not a coincidence that Michael Eisner became the CEO of Disney by learning the business in the accounting department. Many other studio heads were lawyers earlier in their careers. Good accounting increases the odds that the film company will have the funds necessary to pay salaries, rent equipment when needed, and still edit the film.

1. Planning.

Often, participants in independent filmmaking agree to be paid from the profits made by the film company on the film. This requires that the costs be carefully itemized and reported so that all participants are treated fairly and the profit participants develop confidence that there will be profit generated if the film becomes a success.

The most critical phase in filmmaking accounting is the first step – budgeting. Chapter V provides a detailed analysis of the film budget process and the items that go into that budget. The budget provides a blueprint for the structure of the film company and the film project. The production budget detailed in Chapter V focuses on the expenses of making the film, but the budgetary process is primarily a planning tool. The budget allows the filmmaker to identify the scope of the project, the magnitude of the financial resources needed, the scheduling of receipts and payments, and the long-term obligations that might exist if the film is not a financial success.

A well organized film company will create a business plan to serve as sounding board and map, anticipating each phase of the film project. That business plan will help communicate the corporate planning to potential investors and more cautious creative participants who demand a realistic chance of success before they commit to a project.

2. Record Keeping.

Equally important is the record keeping required for the film company. Record keeping serves two

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² Dean of Hamline University School of Law; of counsel Gallagher, Callahan & Gartrell.

distinct goals. First, it allows the film company to monitor the expenditure of its funds so that the filmmaker knows what has been spent on each budget category, how the actual expenditures compare to the projected expenditures, and project what future expenditures will be required.

For example, careful record keeping will allow the filmmaker to monitor the costs of set construction costs. If fourteen days into a twenty-one day shoot, the film company has already spent 90% of its set construction budget, the filmmaker will have to make some choices. Perhaps most of the money was spent on a single set that has been used throughout filming. Then the remaining 10% of the budget should be satisfactory. If, however, the set construction costs are generally the same for each day of filming, then the filmmaker can expect to run as much as 40% over budget on set construction. Knowing this, the filmmaker can choose to scale back on set construction, increase the set construction budget by reducing other costs, or plan to increase the production expense. Without the advance knowledge, the filmmaker could find himself without funds in a checking account, suddenly shut down in the middle of production. A good accountant may not improve the film but she certainly will improve the chances of completing the film.

3. Accountability.

The axiom, “a bird in the hand is worth two in the bush” applies to film budgeting. The best way to insure that funds raised will be available throughout the filming and editing process is to carefully account for all expenditures along the way. The budget is the roadmap for which the accountant must serve as vigilant navigator.

When money begins to flow, the danger always exists that it is misspent. The accounting process provides accountability. Independent films can range in budget from a few dollars to hundreds of millions of dollars on the scale of George Lucas' *Star Wars* films. For accounting purposes, misspent resources does not include failed creative choices, such as purchasing a wedding dress for a scene that is later redrafted to take place in a dance club. While that may be a regrettable expenditure, the money purchased the intended costume and the balance sheet reflects the value of the dress even if the film does not. Instead, misspent funds refers to personal purchases improperly attributed to the production company, money stolen, and expenses attributed to the wrong budget line.

Whenever there is more than a single person handling the film company's payments, a system of accountability must be established. The nature of the system depends on the size of the project and the number of individuals authorized to spend company money. The key is that for every expenditure there is a receipt, and every receipt is attributed to a particular budget line. A film company can authorize its scene designer to buy materials as necessary, so long as the expense remains within the agreed budget. As payments are made, the receipts are tabulated. This helps to guarantee that the designer has spent the money on set materials while allowing the business manager to compare the expenditures to the approved budget.

The need for careful accounting becomes most difficult near the end of principle photography. As the tension mounts to finish the filming on schedule, the frenetic pace often encourages frenzied choices. Late hours result in crumpled receipts piling up in ashtrays. After the frenzy, the receipts are flattened and submitted for reimbursement. The delay in submission allowed the expenses to balloon, nearly eliminating the funds left for post-production. Particularly on low budget films, money is tight. Even a few bad choices at the end of principle photography can derail the project.

A film company should plan to assign the accounting and internal auditing function to someone early in the development of the film company. While not glamorous, a good production accountant can help assure the film is made.

4. Reporting.

The final aspect of accounting relates to the obligations to report income and pay taxes. Unless the filmmaker operates a sole proprietorship, the film company must report income or losses. That information is used to pay taxes – either directly by the corporation or indirectly by the participants in limited partnerships and limited liability companies. Movies are unique assets subject to illogical and

highly manipulable generally accepted accounting practices. These accounting rules allow the film company to either speed up the depreciation of the film to generate business losses and reduce tax liability or to slow the depreciation down by predicting long-lasting revenue from the movie that increases the film as an asset on the books of the company.ⁱ

Although the guerilla filmmaker may pay little heed to the accounting consequences of the film, investors and financiers will. The successful film company should engage the services of a qualified accountant who can help the company establish a strategy to deal with the tax and reporting obligations for the project.

One additional note of caution – the tax reporting for a marginally successful film may continue for years – in some cases, the tax forms outlast the prints of the film itself. The filmmaker must be prepared to accept this obligation to continue to collect fees and provide tax reports when creating the film company.

ⁱ FSA 53. See also, *The Biz ...* for a brief introduction to the application of the GAAP principles.