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THE ROLE OF COMPLETION BONDING COMPANIES IN INDEPENDENT PRODUCTIONS

Mark C. Phillips†

INTRODUCTION

Independent movie producers ("independents") breathe new life into Hollywood by offering a creative alternative to traditional major studios. That creativity, however, is being threatened from an unexpected direction — the bonding companies that guarantee a movie's timely completion. Everyone involved in movie production should become familiar with how these "film guarantors" work, because guarantors wield enormous power and influence on the set. This understanding is especially significant for the independent because the arrangement whereby a guarantor supervises the creation of a movie often wrests production control away from the independent. Such an arrangement is required by the independent's backers — banks¹ and major studios/distributors ("majors")² that invest in production — who want their losses covered if the independent fails to complete a movie on time and under budget.

If a film guarantor's role ended when it paid out claims, it would be like that of other guarantors, such as those in the construction industry. However, a film guarantor has more pervasive powers than do other guarantors, including the right to intervene if a project falls apart or goes over budget. While the more common recourse in the event of production breakdown is renegotiation with the independent's backers, the guarantor has a contractual right to eject the independent and take over...
production if the guarantor — not the independent — thinks it is necessary to save the film. This scenario typifies the perennial tension between independents and guarantors: one seeks artistic freedom, while the other attempts to keep that freedom within the bounds of fiscal propriety.

Many independents are uncertain as to how to deal with guarantors. Independents typically demand unfettered "creative vision and control" over the whole production. Even independents who take their independence literally, like Randy Turrow, are not immune to the authority of guarantors. In February, 1991, Mr. Turrow was caught in a quandary: Should he listen to his guarantor, who ordered him to stop shooting, or to his director, who wanted to continue shooting? He was overheard arguing with his director in a restaurant parking lot: "You knew what the situation was. You said you could shoot it in 30 days. You're four days over schedule and over budget. The bonding company wanted me to stop shooting yesterday. I had to beg for one more day [emphasis added]."

Another independent concerned about guarantors is superstar Sylvester Stallone. He had a multi-project deal with Carolco Pictures to star in five films and produce five others. That deal has been renegotiated, in part because of Stallone's perception of guarantors as an impediment to his creativity. He explains why he will now appear only in four films and not produce at all: "I'm not enamored of the business behind the camera, the catering, the bonding companies. It kills the aesthetic."

There is a very real danger that an independent will lose production control to a guarantor. One industry observer commented in August, 1990, that four pictures then in production were over budget and rumored to be "blowing up." Three particularly large claims in the 1980s were Yentl (which went $1 million over budget); Porky's (the guarantor, Film Finances, recouped its payments when the film became a box

3. Jack Matthews, Good Show for Independent Film Makers, L.A. TIMES, May 21, 1989, (Calendar), at 23. Mr. Joe Roth, a former independent and now studio chief at Twentieth Century Fox, describes the "independent's mentality" as "the belief that he can and should be on top of all aspects of the craft." L.A. TIMES, Feb. 21, 1991, (Calendar), at 80.


7. YENTL (United Artists 1983).

8. Ray Loynd, Risky Business: Film Bond Companies Will Guarantee That Your Film Gets Finished Even If You Can't Do Same, DAILY VARIETY, June 17, 1985, at 115.

9. PORKY'S (Fox 1981).
office hit\(^{10}\)); and *The Adventures of Baron Munchausen* \(^{11}\) (Film Finances was forced to spend $14 million to save the film, and the picture eventually cost twice its projected $23 million budget\(^{12}\)).

Just as the number of independent films has increased since the early 1980s, so the number of guarantors has multiplied.\(^{13}\) Several guarantors are spin-offs from larger companies and have been operating only since 1989 or 1990.\(^{14}\) Many guarantors, both large and small, are now major players in the entertainment financing industry. At a time when independents are earning more professional respect in Hollywood and in Cannes alike,\(^{15}\) their agents and attorneys are well-advised to decide how much creative control they want to negotiate with these guarantors/co-producers.

This article analyzes the rights and obligations assumed by film guarantors vis-a-vis independents and backers. Part One discusses the independent’s need for creative license and the limits imposed upon that license by third-party financing. Part Two discusses how guarantors work beside independents in producing movies, and explains the sequence of events triggered when an independent defaults on production. Part Three outlines important considerations for agents and attorneys who help independents negotiate guarantees. The Conclusion offers a working solution to resolve this tension between finances and freedom.

I. THE INDEPENDENT PRODUCER’S GAME

A. Life Outside the Majors

The drive to create a motion picture is a heady experience, which some independents have compared to compulsive gambling\(^{16}\) or drug addiction.\(^{17}\) Indeed, their battle cry could be, “Give me liberty!” Independents usually work outside of the majors because they perceive them as a death knell to the creative process. The independent gives up

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13. *Id.* Film guarantors have worked in Europe for more than 40 years, and have become dominant players in the United States only since the mid-1970s. Stephen Chrystie, *How Arbitration Clauses ‘Ensure’ Film Delivery*, 4 ENT. L. & FIN. 1 (Feb. 1989).
14. Complete Film Corporation was established in November, 1989; International Film Guarantors was established in February, 1990; and Galaxy Group was established in March, 1990. Noglows, *supra* note 6.
17. GREFÉ, *supra* note 2, at 53.
the majors' vast financial resources to avoid the corporate constraints that accompany those resources.

This reluctance to work for the majors reflects in part constraints that date back to Hollywood's "studio system" of the 1920s. Each studio required stars, directors and producers to sign long-term employment contracts that prevented them from accepting employment elsewhere while their contracts were in force. This system enabled a handful of majors to monopolize Hollywood's best and brightest talent for decades. Only a select few broke away, most notably Olivia DeHaviland and Gene Autry.

Independents shy away from the studio system because they have the utmost respect for their own creativity. Irwin Winkler, a well-respected independent in Hollywood, believes the movie industry needs people like him to rejuvenate itself: "One of the best reasons to do a film is when everybody tells you you shouldn't do it. Because if you stick to formulas, you're usually doomed to failure. . . . When everybody tells you there's not a chance in the world, that's the one you should go after."

For other independents, the production urge is more playful and represents a chance to turn fantasy into reality. The thrill of taking an idea to the big screen without having to satisfy someone else's "bottom line mentality" is enough of a motive to break away from the majors. David Puttnam expresses his excitement at being an independent: "I can't believe my luck, that I'm in a business that allows me to pursue my hobby. And it does frighten me how many of you are obsessed by how much money is spent. . . . I'll never see a penny on the picture, but I'm enormously proud of it."

B. The Need to Finance Production

1. An Independent's Many Jobs

In order to turn fantasies into reality, independents need help from

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20. 2 FILMMAKERS ON FILMMAKING 207 (Joseph McBride ed., 1983). Oliver Stone, Oscar-winning director, commented, "Yeah, I have much more freedom to make the subjects that I want, but I don't see myself as Darryl Zanuck. I would feel bad if I got indulgent. All good films come from people with an independent spirit, those who push." De Vries, supra note 2, at 10.
21. McBRIDE, supra note 20, at 206-07. The film to which Puttnam alluded was The Duellists starring Albert Finney.
two types of backers — lenders who will front start-up capital, and a major that will buy or "pick up" their films and distribute them to the public. These deals are often more interesting to watch than the films themselves.\(^2\) A guarantor's priority concerns are financing and selling a film, and must be satisfied before production begins, since independents may be creatively brilliant but often cannot pay salaries or negotiate deals with theater chains.

Independents face the same responsibilities as the majors when making a motion picture. The tasks involved are diverse: creative direction (e.g., working with stars and reviewing dailies), line administration (e.g., finding equipment and solving logistics), and fund raising.\(^3\) The practical difference between independents and majors is that producers at the majors can delegate tasks to assistants, whereas independents generally have smaller staffs and therefore must handle many of these tasks personally.\(^4\) In effect, independents must be creators and administrators, as well as fundraisers that woo prospective investors and distributors.

2. Calculating a Budget

Independents and majors also share horrific production expenses, or "negative costs." Film productions have become so expensive that Mr. Jack Valenti, President of the Motion Picture Association of America ("MPAA"), has called for an industry-wide reduction in negative costs.\(^5\) Accordingly, backers require independents to submit ever more detailed budgets which anticipate possible contingencies that might increase overall costs. This is an onerous task because, unlike other commercial budgets, film budgets are inherently detailed and already account for most

\(^2\) BIEDERMAN, supra note 18, at 281.
\(^3\) Bruce Mallen, Bruce Mallen Discusses Interim Financing, 1 ENT. L. J., July 1982, at 22.
surprises that can disrupt production.  

An example of a surprise is when a star commits to production, and later walks off the set due to "creative differences." Production might stop altogether until a suitable replacement is hired. Production insurance will cover part of the cost of finding and paying a replacement, but the balance must be absorbed into the overall budget. Despite such potential difficulties, independents expect an early commitment from stars. Talent commitments are important because they are used to calculate the film's future revenues and can be used as collateral for a bank loan.

C. Working with Backers

After making a budget and obtaining star commitments, independents turn to prospective backers. Established independents have an advantage because they can point to earlier box office hits to induce backers to join in on another "sure thing." Nevertheless, even established independents must compete for the small number of backers in Hollywood.

Backers come in two types — equity and non-equity. Equity backers share financially in a project's ups and downs, enjoying the profits and paying out to creditors on losses. Non-equity backers, by contrast, do not share in a film's profits and losses; they only want a return on their investment.

Although some entrepreneurs welcome equity backers ("general partners") because they cover business losses during hard times, independents usually do not want equity backers because they will likely

26. WILLIAM B. ADAMS, HANDBOOK FOR MOTION PICTURE PRODUCTION 48 (1977); JOHN QUICK & TOM LABAU, HANDBOOK OF FILM PRODUCTION 45 (1972).

27. Most professional liability and all-risk insurance policies issued to independents provide coverage for "all risks of direct physical loss or damage" that create extra expenses, such as replacing stars, broken equipment, or lost film. SYLVIA ALLEN COSTA, HOW TO PREPARE A PRODUCTION BUDGET FOR FILM AND VIDEO TAPE 139 (2d ed. 1975); QUICK & LABAU, supra note 26, at 38. Independents should advise their insurance brokers or agents about all production risks they reasonably anticipate will occur, in order to clarify the independents' reasonable expectations of coverage.


29. For a discussion of the differences between equity and non-equity investors and their respective roles in film financing, see Dekom, supra note 25, at 232-33.

30. Equity investors are general partners. The law of partnerships is codified under the Uniform Partnership Act (e.g., DEL. CODE ANN. tit. 6, §§ 1501-1543 (1991); CAL. CORP. CODE §§ 15001-15045 (West 1991)). "A partnership is an association of two or more persons to carry on as co-owners a business for profit." CAL. CORP. CODE § 15006(1) (West 1991). "All partners have equal rights in the management and conduct of the partnership business." CAL. CORP. CODE § 15018(e) (West 1991). Partners are also liable for the wrongs of other partners. CAL. CORP. CODE §§ 15013, 15018(b) (West 1991); Alioto v. United States, 593 F. Supp. 1402, 1413 (N.D. Cal. 1984).
desire a voice in production. Independents generally prefer non-equity backers ("limited partners"), because they only contribute capital and have no input in the production process. Most movie backers do not want an equity stake either. As non-equity backers, they are not responsible for paying all the losses if a picture bombs at the box office.\(^{31}\)

The principle categories of backers in film financing today are private investors, banks, and majors/distributors. Each one offers unique attractions and problems from an independent's viewpoint.

1. Private Investors

Limited partnerships were hot topics for discussion at Hollywood parties until the mid-1980s, as independents and private investors tried to search each other out.\(^{32}\) However, movies became less profitable investments as the decade ended.\(^{33}\) A heavy blow to investors was the Tax Reform Act of 1986.\(^{34}\) It repealed an investment tax credit for motion

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For the role of limited partnerships in funding motion picture productions, see James L. Thompson, Comment, Independent Motion Picture Financing: Unregistered Limited Partnership Offerings, 1989 B.Y.U. L. Rev. 1287 passim.


34. Biederman, supra note 18, at 282; Kenoff & Rosenberg, supra note 32, Form 16-1, at 17; Thompson, supra note 31, at 1311-12. It is certainly ironic that not even the Internal Revenue Service can scientifically predict a motion picture's gross profits. Greffe, supra note 2, at 29. Part of the difficulty is the rapidly changing area of tax law related to entertainment investments generally and film production companies particularly. Schuyler M. Moore, ENTERTAINMENT INDUSTRY AFFECTED BY SEVERAL TAX DEVELOPMENTS, 73 J. Tax'n 176, 176-80 (Sept. 1990).
picture losses that had been available before December 31, 1985.  

Independents can no longer rely on private investors seeking tax breaks. Even with foreigners buying film companies in record numbers, most private investors are cautious about fronting capital without a guaranteed return. Independents cannot promise such returns, given the inherently unpredictable value of any film before it hits the box office. Nevertheless, funding must be gained quickly once stars commit to a project, or else they may commit somewhere else. Independents have little choice but to use other sources of funding.

2. Banks

Banks are more practical financing sources than private investors for a number of reasons. Banks have the monetary reserves to fund multi-million dollar pictures. They are staffed with loan officers who understand the technical problems that independents face. Most importantly, several banks have created an “interim production loan” package, which offers production financing to many independents. An interim loan gives independents fairly quick access to funds from a backer with little or no interest in controlling the production's creative flavor.

Interim loans were first provided in the mid-1970s by Chemical Bank, City National Bank, and Crocker Bank. They differ significantly from ordinary commercial loans in four ways: (1) the bank lends both the principal and the interest needed to repay the principal; (2) the loan collateral (i.e., the motion picture) is also the vehicle through which the

35. I.R.C. § 48(k) (West Supp. 1989) allows a business credit for “qualified films” (i.e., “motion picture film . . . created primarily for use as public entertainment”) but only to the extent the investor has an “ownership interest” in the film (i.e., “determined on the basis of his proportionate share of any loss which may be incurred with respect to the production costs of such film”).

36. See Lilliston, supra note 33, at 252-53; Bodovitz, supra note 33, at 22.

37. Banks almost uniformly are not interested in becoming equity investors in the movie project. Their interest lies primarily in recovering the loan proceeds. Nigel Sinclair, Bank Lending in Independent Film Making, 4 ENT. L. & FIN. 3 (Apr. 1988).

independent expects to repay the loan; (3) the loan continues to fund throughout production until the independent delivers the picture to a distributor; and (4) the distributor (not the independent) is ultimately responsible for repaying the loan.39

However, some independents do not qualify for interim financing. They may have poor credit references or have difficulty finding a distributor who wants to agree to the financing terms. In that case, independents may decide to negotiate a financing/distribution package directly with a major.

3. Majors/Distributors

The fact that independents sometimes agree to have majors finance and distribute their films raises a troublesome question: Who ultimately decides creative issues of production — the independent or the major? Most independents respond without hesitation: "Being an independent film maker means you have the ability to make the film you want to make without having somebody tell you how it should be made."40 As seen below, majors think differently.41

Independents sometimes choose a major over a bank because they want to rent the major's extensive financial and technical network. A major has economic assets such as casualty insurance, bank credit lines,42 and letters of credit43 to finance foreign shoots.44 It also can rent set crews, props, cameras, electrical equipment, and post-production facilities.45 A package deal from the major, including financing, costs considerably less than obtaining, financing, and renting items piecemeal.

The majors, however, are usually interested in doing more than just

40. Matthews, supra note 3, at 23.
41. See infra notes 47-49 and accompanying text.
42. MOLLIE GREGORY, MAKING FILMS YOUR BUSINESS 151-52 (1979).
43. Long-distance buyers and sellers use local banks to negotiate letters of credit when handling the payment of a business transaction. Letters of credit are commonly used both for transactions within the United States and for international transactions. Letters of credit are legally controlled in the United States by Division 5 of the Uniform Commercial Code ("UCC"). The UCC and California's version of the UCC (CAL. COM. CODE §§ 5101-5117 (West 1991)) do not state rigid rules, only fundamental guidelines that recognize customs and practices of the business community. Crocker Nat'l Bank v. Super. Ct., 136 Cal. Rptr. 481, 486 n.3 (Cal. Ct. App.) cert. denied, 434 U.S. 984 (1977).
44. Letters of credit are standard tools in the entertainment industry for financing foreign location shoots. Mallen, supra note 23, at 26.
renting equipment. They prefer to negotiate equipment rentals within a larger package, which includes funding and distributing the independent's picture, especially when the major's in-house inventory of releases is low. The two most frequent package deals made are "straight distributions" and "negative pickups."

A straight distribution deal is a comprehensive agreement between the independent and major. It requires the major to distribute the independent's picture in exchange for the independent paying the major a percentage of the picture's gross profits. Both sides benefit from straight distribution: independents acquire a major's name-recognition value on their picture's release, and the major gets a larger payment than from merely renting equipment. Straight distribution might not provide sufficient funds to complete production, however, particularly if the independent cannot secure collateral funding from private investors or banks.

In contrast to the straight distribution deal, a negative pickup deal involves more than enough funding to complete production, because the deal advances production costs along with distribution costs. It requires the major to front the independent a percentage of the film's estimated gross profits to pay for the costs of production. In exchange for the advance, the independent agrees to deliver a "reasonable facsimile" of the script before production starts. Negative pickups are very popular among independents who use them as collateral for bank loans, and thereby sidestep the possibility of the major's controlling creative decisions because it is funding production.

A negative pickup, however, poses problems of its own. The agreement's terms usually provide that the independent finish the picture in complete conformity with the script. If a picture materially deviates from its script, the major is entitled to reject it and sue for contractual damages under the agreement. Hence, no funding package is entirely

46. The industry standard for calculating a film's profit is 3 to 7 times the film's total negative costs, which in turn equals \( \frac{1}{4} \) to \( \frac{1}{2} \) the film's gross revenues. As an illustration, a film costing $10 million to produce and distribute must gross a minimum of $70 million to avoid creating a loss. *Id.* at 46, 48.

47. *Id.* at 49. Majors can also cover their negative costs by selling pre-distribution rights ("pre-sales") to television, cable, video, and foreign markets. Pre-sales only represent anticipated revenues in particular markets. If enough films are actually distributed over a predetermined time period, pre-sales are deemed irrelevant because distribution revenues theoretically will generate sufficient amounts to equal or outweigh the pre-sales. *See* Dekom, *supra* note 25.


49. GREFÉ, *supra* note 2, at 8-10.

50. GREGORY, *supra* note 42, at 152.
satisfactory from the independent's viewpoint.

D. The Bonding Requirement

1. The Financing Triad

The typical financing arrangement for a motion picture consists of three parties: the independent and two backers—a lender and a distributor. Sometimes a major may act as both the lender and the distributor. The guarantor works with all three parties to ensure that the film is completed on time and under budget. In other words, the guarantor's job is to assure backers that an independent will comply with all the terms of their agreements:

"Completion Guarantor" means a third party guarantor who may agree to advance funds necessary above the final approved budget of the Picture to complete the Picture in conformity with its final approved shooting script, notwithstanding the fact that the "final negative cost" of the Picture may exceed the final approved budget.51

The guarantor is not a member of the triad, but works for the benefit of the backers through the independent. The guarantor's rights and obligations arise from a separate guarantee agreement with the independent.52

2. Why Independents Like Guarantors

Independents want to have guarantors approve their films for various reasons. Less experienced independents may consider a guarantee the equivalent of "money in the bank" for paying backers, in case production fails and backers come looking for their money. Older independents want to preserve the profession's good reputation, and have commented that they like guarantors because younger independents can benefit from the guarantor's "good discipline" on the set.53

Banks welcome the professional services a guarantor offers them. A guarantor meets with a loan officer before the bank ever issues a loan, and examines on the bank's behalf all the production documents needed

51. Kenoff & Rosenberg, supra note 32, at Form 13-4, cl. 1.15. See also Lazarus, supra note 45, at 52; Chrystie et al., supra note 25, at 296.

52. Nigel Sinclair, Key Forms for a Film-Production Loan, 4 Ent. L. & Fin. 4 (May 1989). Cal. Civ. Code § 2792 (West 1991) provides: "Where a suretyship obligation is entered into at the same time with the original obligation, or with the acceptance of the latter by the creditor, and forms with that obligation a part of the consideration to him, no other consideration need exist. In all other cases there must be a consideration distinct from that of the original obligation."

53. Loynd, supra note 8, at 116.
to secure the loan. The guarantor analyzes every contingency that could stop production, and recommends ways to prevent problems before they occur. Banks also appreciate a guarantor's willingness to mediate loan disputes that arise between themselves and independents. Ms. Bette Smith of the Completion Bond Company, a prominent guarantor, comments, "We view ourselves as a support organization. Our job is to help producers and directors overcome problems and overcome them quickly."

Majors generally have no need to work with guarantors on in-house projects, due to their relatively extensive financial resources. Most of their contact with guarantors arises when they purchase an independent's film for their inventory and require the independent to buy a guarantee during production. However, majors that co-produce a picture with other majors and anticipate inter-studio disputes, will make an exception and purchase a guarantee themselves.

3. Additional Benefits

Backers want to see a film guaranteed for another reason. Guarantors are not insurers, but they negotiate with major insurance companies such as Lloyd's of London, Fireman's Fund, and Transamerica, for additional coverage if a guarantor cannot pay its obligations to backers. Therefore, backers write into their financing agreements with independ-

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54. The guarantor reviews the full range of documents needed to secure interim financing, including loan applications, lease agreements, distribution agreements, certificates of insurance, shooting schedules, laboratory pledgeholders' agreements, contingency budgets, lists of beneficiaries and other lenders, "above the line" agreements (e.g., literary property agreements, screenwriter agreements, inducement letters to key personnel, and salary schedules), other financing agreements, union agreements, and letters from distributors on recoupment of completion sums. See PAUL A. BAUMGARTEN & MORTON L. LEAVY, LEGAL AND BUSINESS PROBLEMS OF FINANCING MOTION PICTURES at 350, 388 (1979).

55. Richard Soames of Film Finances, a prominent guarantor, revealed that his company will not write a letter of intent to bond a film "unless all production monies are in place." Loynd, supra note 8, at 114.

56. Id. at 115.

57. Noglows, supra note 6, at 29.

58. Loynd, supra note 8, at 115; Noglows, supra note 6, at 29. Productions involving two or more majors are more frequent than ever. Lilliston, supra note 33, at 253-54. Many contract disputes between majors, or disputes between a major and a director are resolved through the relevant guild, collective bargaining agreement, or arbitration tribunal. BIEDERMAN, supra note 18, at 283-84.

59. Lancer, supra note 38, at 74. For example, Film Finances is covered by Lloyd's of London, and the Completion Bond Company is covered by its owner, Transamerica. Noglows, supra note 6, at 29. Similarly, Fireman's Fund established International Film Guarantors (in February, 1990). Id. The guarantor and insurance company divide the guarantee premium between themselves. BAUMGARTEN & LEAVY, supra note 54, at 342.
ents a provision that they "cut through" as direct beneficiaries of these proceeds.\textsuperscript{60}

These funds, however, are seldom tapped. The guarantor must first exhaust a contingency fund — usually ten percent of a movie's production costs set aside by the independent before shooting begins — and then its own assets before it can give the insurance company notice of a claim.\textsuperscript{61}

II. ANATOMY OF A COMPLETION GUARANTEE

A. Identifying the Players

The concept of finance companies guaranteeing the completion of a motion picture is not novel. Film guarantors have worked in Europe for decades. They gained attention in Hollywood in the 1980s with the sudden proliferation of independent production companies and the desire of backers to avoid repeating such notable flops as \textit{Heaven's Gate}, which went grossly over budget.\textsuperscript{62} Despite their success, the working styles of guarantors are still unfamiliar to many in Hollywood.\textsuperscript{63} Even when they are listed in reference books, the identities and function of guarantors are not discussed.\textsuperscript{64}

1. Names of Well-Known Guarantors

A relatively small number of guarantors handle today's high volume business of bonding independent films. More than half of all films bonded worldwide are handled by only two companies — Film Finances and the Completion Bond Company.\textsuperscript{65} Other notable guarantors include: Cine Guarantors, Complete Film Corporation, Entertainment Completions, Inc., Galaxy Group, International Film Guarantors, Motion Picture Bond Company, Motion Picture Guarantors (a Toronto-based company), Percent Enterprises Completion Services, Performance

\textsuperscript{60} SINCLAIR, supra note 52, at 4. For an exemplar financing agreement that obliges the guarantor to give lenders "cut-through" endorsements, see KENOFF & ROSENBERG, supra note 32, Form 16-1, at 16-11 (para. 4(a)(ii)).

\textsuperscript{61} Loynd, supra note 8, at 114, 116.

\textsuperscript{62} \textit{Heaven's Gate} (United Artists 1980). It earned $1.5 million against $44 million spent in negative costs (or $57 million, if one adds the distribution costs and studio overhead). PATRICK ROBERTSON, GUINNESS MOVIE FACTS AND FEATS 30 (1988).

\textsuperscript{63} SINCLAIR, supra note 52, at 4.

\textsuperscript{64} See, e.g., IRA KONIGSBerg, THE COMPLETE FILM DICTIONARY 60 (1987); RALPH S. SINGLETON, FILMMAKER'S DICTIONARY 35, 78 (1986).

\textsuperscript{65} Loynd, supra note 8, at 114. A recent study states that together these two companies bond more than 100 pictures annually. Noglows, supra note 6, at 29.
Guarantees, Inc., and Rampart Services. 66

2. Distinguishing a Guarantee from Insurance

Independents should not confuse a film guarantee with production insurance. The law defines guarantors as sureties and not as insurers. In fact, "guarantor" and "surety" are interchangeable legal terms. 67 The difference between a guarantee and insurance is one of function, in that guarantors do not operate like insurers. 68

An insurer covers the independent for surprise losses that disrupt production and damage the independent. In contrast, a guarantor pays backers — not the independent — for investments that are lost when the independent does not shoot a picture according to the backers' terms. A guarantor or surety is "one who undertakes to pay money or to do any other act in event that his principal [the independent] fails therein." 69

In addition to providing coverage if production collapses, a film guarantor also lends an independent its name value and expertise in marketing pictures for use in negotiating with prospective backers. However, at the risk of being blackballed in the industry, the independent bears the ultimate responsibility of paying back the losses it generates, even when the guarantor initially pays out claims. The guarantor is entitled to recover its payments, with interest, from the independent. 70

66. Lancer, supra note 38, at 74; Noglows, supra note 6, at 29.

67. See, e.g., CAL. CIV. CODE § 2787 (West 1991), which provides in pertinent part: "The distinction between sureties and guarantors is hereby abolished. The terms and their derivatives . . . shall have the same meaning." California courts construe guarantee agreements as they would construe surety agreements. See, e.g., Southern Cal. First Nat'l Bank v. Olsen, 116 Cal. Rptr. 4, 8 (Cal. Ct. App. 1974).


70. "If a surety satisfies the principal obligation, or any part thereof, whether with or without legal proceedings, the principal is bound to reimburse what he has disbursed, includ-
In performing these functions, film guarantors meet the traditional definition of a surety. If their roles ended there, guarantors would represent the singular blessing that many independents and backers consider them to be. This description, however, does not constitute all that a film guarantor must do if an independent goes over budget or beyond schedule. Unlike other types of guarantors, the film guarantor has a broad contractual right to intervene, take over production and exercise all of its legal rights against backers and other third parties.\textsuperscript{71}

\textbf{B. Components of the Guarantee}

1. Formal Documents

When an independent first applies for an interim loan, the bank officer refers the producer to a list of preferred guarantors. The independent selects a guarantor and pays it a commitment fee to review the production documents attached to the loan application.\textsuperscript{72} If the guarantor approves the paperwork, it issues the independent a letter of intent to bond the film. The letter does not commit the guarantor. Nonetheless, it is an important record of the initial negotiations.\textsuperscript{73} Additionally, the parties can agree therein to identify which party will be responsible for specific tasks if one of the parties later disputes the guarantee's terms.\textsuperscript{74}

Once an independent and guarantor have agreed on the guarantee's terms, they execute a guarantee agreement. This agreement, preferably in writing, confers a number of production-related rights and duties on

\begin{itemize}
  \item \textsuperscript{71} Baumgarten \& Leavy, supra note 54, at 377; Sinclair, supra note 37, at 3.
  \item \textsuperscript{72} Noglows, supra note 6, at 29. See also Baumgarten \& Leavy, supra note 54, at 343, 350, 388.
  \item \textsuperscript{73} For an exemplar letter of intent, see Kenoff \& Rosenberg, supra note 32, Form 13-1. This exemplar is between an independent and the bank. It includes a "completion bond clause," which provides: "The Investment shall be delivered by cashier's check made payable to (name of production company) upon delivery to [bank] of a duly-executed completion guarantee and a fully-executed distribution agreement."
  \item Agents and attorneys are advised to consider every party's expectations when drafting every letter of intent. In this way, one can avoid the circular process, which can be very frustrating, whereby a guarantor wants to see the independent's financing before agreeing to issue a letter to bond production, and a bank wants to see the guarantee before issuing a letter to fund production. See, e.g., 14TH ANNUAL PROGRAM ON LEGAL ASPECTS OF THE ENTERTAINMENT INDUSTRY: PRODUCTION FINANCING 6 (1968).
\end{itemize}
the guarantor. After backers have funded the start of production, the guarantor assigns a representative to supervise production and assure backers that the independent will comply with the script and financing agreements. The representative must approve every phase of production until the distributor accepts the finished product. Hence, the independent’s lament: “[Y]ou are only as independent as the deal you can cut. In that sense, it’s no different from working within the studio system. The more money you need, the more help you’re going to get.”

The guarantee agreement is paid with a premium. Until two or three years ago, guarantee agreements routinely provided that independents pay five or six percent of their total production budget as a premium. This has changed. The current flurry of new guarantors has forced some competitors to adjust their premiums downward. Currently, some premiums are as low as 1.5% of the budget. Other guarantors lower their premiums if an independent has an extremely high budget or buys a multi-picture guarantee, also known as a “continuing” guarantee. The guarantor places the premium in a reserve fund, which is used to pay claims if the independent defaults on any of its obligations.

75. Sinclair, supra note 37, at 3. An exemplar guarantee agreement is reprinted in BAUMGARTEN & LEAVY, supra note 54, at 349-87. The writing requirement is codified in CAL. CIV. CODE § 2793 (West 1991): “[A] suretyship obligation must be in writing, and signed by the surety; but the writing need not express a consideration.” However, an oral guaranty is not void, merely voidable. Salomon v. Ellis, 94 P.2d 393, 396 (Cal. Ct. App. 1939).

76. Sinclair, supra note 37, at 5; Sinclair, supra note 52, at 5. If the independent does not sign a distribution deal before the film is guaranteed, the guarantor usually reserves for itself (in the guarantee agreement) the right to approve all pending and future distribution deals. BAUMGARTEN & LEAVY, supra note 54, at 346.

77. Matthews, supra note 3, at 23.


Mr. Lawrence Vanger, president of Performance Guarantees, Inc. (established in 1986), questions whether the move to lower premiums is smart for business: “The market has been driven down competitively to the point where, for most, if not all of the bonding people, it’s a question of non-profitmaking productivity.” Noglows, supra note 6, at 29.

The premium is authorized by CAL. CIV. CODE § 2811 (West 1991), which provides in pertinent part: “Any party required to give a bond undertaking or other obligation may agree with his surety for the deposit of any money and assets for which the surety is responsible with a bank ... for the safekeeping of such money and assets . . . .”

79. See, e.g., CAL. CIV. CODE § 2814 (West 1991); Loynd, supra note 8, at 114. A continuing guaranty may be revoked absent ongoing payments of cash into the reserve. CAL. CIV. CODE § 2815 (West 1991).

80. GREGORY, supra note 42, at 154. The guarantor may also negotiate to acquire a percentage of the film’s gross or net revenues if the guarantor is compiled to pay out claims. See, e.g., CAL. CIV. CODE § 2849 (West 1991). This “percentage clause” is similar to penalty provisions in the major/distributor’s deals with the independent. The guarantor’s clause often requires the guarantor get 1% of the film’s net revenues for every 1% of the budget that it must pay out. BAUMGARTEN & LEAVY, supra note 54, at 346-47.
Legally, this is not a trust account held for the independent's benefit; it remains the independent's property until production is finished.

Many guarantors build an incentive around the premium to encourage independents to work under budget. If an independent completes production satisfactorily and no claims must be paid, the independent is entitled to negotiate a rebate, also known as a "no claims bonus," of up to half of the original premium amount. This is an important incentive for new independents who have only secured minimal financing initially.

Lastly, the parties are advised to draft a reciprocal inter-party agreement that addresses the needs of the guarantor, the independent, and all the backers. The guarantor probably will advocate the need for a single, inclusive document that defines all potential conflicts of interest. Examples of potential conflicts are priorities in security interests, set-off rights, and respective rights to insurance proceeds. The guarantor wants to protect itself in case, for example, the shooting schedule stops abruptly.

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81. BIEDERMAN, supra note 18, at 367-68. However, the independent is treated as a trustee of all investors' funds and royalties during production. See, e.g., KENOFF & ROSENBERG, supra note 32, at Form 16-1, cl. 11:

FUNDS HELD IN TRUST: All monies received by Production Company which are payable to Investor in accordance with the provisions of this Agreement shall be held by Production Company, in trust, for the sole use and benefit of Investor and shall be immediately deposited upon receipt in a separate interest-bearing bank account naming Investor as the beneficiary thereof. Production Company shall not commingle the monies payable to Investor hereunder with other monies of Production Company.

Even though third parties cannot sue the guarantor as trustee to force payment of claims, they can still sue the guarantor based on its obligations under the guarantee agreement. Strangely enough, the reverse is not true as well. The otherwise astute guarantor is not entitled ordinarily under the independent's financing agreements to sue backers if they do not fund production as promised. The following exemplar financing agreement, id. at Form 16-1, cl. 17(b) provides: "This [financing] agreement shall in no event be construed as a third party beneficiary contract and is not intended for the benefit of any person or company whomsoever except the parties hereto."

82. RESTATEMENT (SECOND) OF CONTRACTS § 114 cmt. b (1981). The guarantee agreement gives the guarantor a security interest in the reserve. Sinclair, supra note 52, at 4. That security interest is perfected over all other creditors' liens and security interests, except for liens imposed by law or by subordination agreements. BAUMGARTEN & LEAVY, supra note 54, at 372-73.


83. Lancer, supra note 38, at 74.

84. "Several contracts relating to the same matters, between the same parties, and made as
because a lender does not fund production as promised. The guarantor invariably intervenes before that point and negotiates a new inter-party agreement.

2. Supervising Production

The guarantor is not legally obligated to cover production losses or take over production until backers actually start paying for production to begin. The independent deposits these funds into a "production account" at a bank approved by the guarantor.

The guarantor's designated representative then begins to act as a super-producer on the set, supervising the independent. The representative exercises its knowledge and expertise by estimating the budget requirements for each scene and imposing restraints if the independent exceeds those demands. Equally important is the representative's ultimate power to replace key personnel if it reasonably decides that production has become too expensive.

The representative is never a passive observer on the set. The guarantee agreement requires the representative to intervene and order production stopped when it reasonably believes an independent will go over budget or miss the deadline for delivering a picture to the distributor. This situation occurs frequently on location shoots in unstable foreign countries. This does not mean the representative wants to disrupt the independent's creative vision. Nonetheless, the representative is respon-
sible for overseeing all disbursements and reviewing all dailies, and must approve all periodic progress reports. This constant scrutiny is necessary to protect the guarantor should backers start to make claims against it.

3. Limits on a Guarantor's Obligation

A guarantor's obligation toward backers is not unlimited, but is defined by the terms of the guarantee agreement reached with the independent. This includes the maximum amount a guarantor is obliged to pay out, regardless of the actual amounts that backers lose. Thus, a backer can lose thousands or millions of dollars and not be able to recoup from the guarantor any money in excess of the guarantee limit.

To protect their interests, guarantors are advised to negotiate with specificity all their obligations to backers in the guarantee agreement. This prevents backers from contending after a loss occurs that a guarantor has somehow agreed to assume a responsibility that is not spelled out therein. In short, the guarantor's production responsibilities are identical to those of the independent.

Sometimes a guarantor does not need to pay the backers' losses at all. The guarantor is let off entirely if the independent — without the guarantor's consent — alters the guarantee agreement or other contracts so as to increase the guarantor's obligations to backers or other parties. Often this happens when the independent negotiates a new repayment deal with different interest rates, agrees to pay crew salaries before they...

by guarantors until the mid-1980s because guarantors considered local conditions too unpredictable for bonding purposes. Loynd, supra note 8, at 116.

92. BAUMGARTEN & LEAVY, supra note 54, at 368-69; LAZARUS, supra note 45, at 52. A spokesperson for Entertainment Completions once said that his company looks to the production's end results and not at "piecemeal things." Loynd, supra note 8, at 116.

93. LAZARUS, supra note 45, at 52; Sinclair, supra note 52, at 4. See, e.g., Kane v. Mendenhall, 56 P.2d 498, 500 (Cal. 1936); Petrovich v. City of Arcadia, 222 P.2d 231, 236 (Cal. 1950). However, accrued interest on the guarantee may be recovered in addition to the guarantee amount, and the total amount can thus exceed the guarantee amount. See, e.g., Burns v. Mass. Bonding & Ins. Co., 146 P.2d 29, 30 (Cal. Ct. App. 1944).


95. "The obligation of a surety must be neither larger in amount nor in other respects more burdensome than that of the principal; and if in its terms it exceeds it, it is reducible in proportion to the principal obligation." CAL. CIV. CODE § 2809 (West 1991). See also, e.g., Pacific Employers Ins. Co. v. City of Berkeley, 204 Cal. Rptr. 387, 394 (Cal. Ct. App. 1984); County of Los Angeles v. Wilshire Ins. Co., 119 Cal. Rptr. 101, 103 (Cal. Ct. App. 1975).

96. "A surety is exonerated, except so far as he may be indemnified by the principal, if by any act of the creditor, without the consent of the surety the original obligation of the principal..."
are due, or does not pay production insurance premiums.

The guarantor is also not liable to pay backers if it becomes economically impractical for the guarantor to take over production and complete the picture as originally planned. This occurs, for example, when backers invest in a movie based on the independent's track record, and that independent suddenly dies. Another scenario occurs when production hinges on backers making timely deposits to the production account, and payments stop without warning. In these circumstances, however, the guarantor is not relieved of liability automatically, but must prove to all parties (and to the court if litigation ensues) that such surprises have irrevocably prejudiced its interests. If the guarantor then does not act quickly to revoke the guarantee, backers are entitled to demand that the guarantor cover their losses.

C. Taking Over Production and Paying Claims

A number of incidents can trigger a guarantor's obligation to intervene and take a more active role in production. In one scenario, an independent completes a picture and delivers it to the major/distributor pursuant to a negative pickup agreement. The distributor then rejects

is altered in any respect, or the remedies or rights of the creditor against the principal, in respect thereto, is in any way impaired or suspended.” Cal. Civ. Code § 2819 (West 1991).

Cal. Civ. Code § 2821 (West 1991) provides: “The rescission of an agreement altering the original obligation of a debtor, or impairing the remedy of a creditor, does not restore the liability of a surety who has been exonerated by such agreement.”


98. See, e.g., 13 George J. Couch, Cyclopedia of Insurance Law, § 47:315 (2d ed. rev. 1982). Nor is the guarantor required to pay legal fees or any judgment that arises from the independent's tortious conduct during production, notwithstanding standard language in many guarantee agreements that purportedly cover “production liabilities.” Id. at § 47:320; see also National Sur. Corp. v. Charles Carter & Co., 539 F.2d 450, 457 (5th Cir. 1976). On the other hand, the guarantor must pay premiums for workers' compensation insurance if the independent neglects to pay them. Couch, supra, § 47:319.

99. See, e.g., Gaffigan v. Lawton, 37 P.2d 79, 80 (Cal. 1934); Restatement of Security § 112 (1941). The guarantor's obligations are exonerated if the independent cancels production before spending the entire budget. Baumgarten & Leavy, supra note 54, at 370.

100. The guarantor is still obligated to cover the independent's deals, even if those deals are modified to include fraud. Cal. Civ. Code § 1640 (West 1991) provides: “When, through fraud, mistake, or accident, a written contract fails to express the real intention of the parties, such intention is to be regarded, and the erroneous parts of the writing disregarded.” See also Cal. Civ. Code §§ 1667-1668 (West 1991) for California's public policy on fraudulent contracts.

the picture, claiming it does not comply with the script.\textsuperscript{102} Even if the independent has remained in control of production, the guarantor is required to aid in correcting the problem.\textsuperscript{103} In another scenario, the guarantor steps in because a backer establishes that it cannot recover its investment, or stops funding production due to the independent's breach of a material term of their agreement.\textsuperscript{104}

Claims are not paid out, however, simply because backers lose money. Before a guarantor pays out claims, the backer must prove its losses are covered under the guarantee agreement.\textsuperscript{105} This becomes complicated if the independent purchased a multi-picture guarantee, since the backer must specify the losses pertaining to each film covered by the guarantee.\textsuperscript{106}

A guarantor generally has two choices when production "blows up."\textsuperscript{107} The more draconian choice entails taking over production. Under this option, the guarantor may fire and replace the production crew, change locations and shooting schedules, and terminate agreements made by the independent that the guarantor considers superfluous to finishing the picture.\textsuperscript{108} The independent agrees, as part of the guarantee agreement, to waive any liability against the guarantor for taking over

\textsuperscript{102} See supra notes 47-49 and accompanying text.

\textsuperscript{103} This requirement was discussed recently in the bonding of \textit{Mermaids} (Orion 1990). See Bodovitz, supra note 25, at 14. "A surety who has assumed liability for payment or performance is liable to the creditor immediately upon the default of the principal, and without demand or notice." \textsc{Cal. Civ. Code} § 2807 (West 1991). See, e.g., Baralat Dev. Co. v. Lichtner, 236 Cal. Rptr. 701, 702 (Cal. Ct. App. 1987).


\textsuperscript{104} The guarantee agreement usually provides an objective standard for determining when the guarantor must pay out to backers, e.g., when the negative costs exceed a pre-agreed percentage over budget or when production exceeds a specified number of days behind schedule. Thompson, \textit{supra} note 31, at 1298.

\textsuperscript{105} See, \textit{e.g.}, Weisz Trucking Co. \textit{v.} Emil R. Wohl Constr., 91 Cal. Rptr. 489, 493 (Cal. Ct. App. 1970); \textsc{Couch, supra} note 98, § 47:267.

\textsuperscript{106} Some costs are disallowed by guarantors. Production materials that are delivered to a location shoot or post-production site typically are not covered because they are not used just on one picture. The guarantor likewise does not cover the costs of materials that the independent is expected to furnish at one site and then transfer to another site for a future production. \textsc{Cal. Civ. Code} § 2822 (West 1991) provides that if the lender accepts any payment in partial satisfaction of the loss, the guarantor's obligation is reduced proportionally but not extinguished completely.

\textsuperscript{107} Noglows, \textit{supra} note 6, at 29.

\textsuperscript{108} \textsc{Baumgarten & Leavy, supra} note 54, at 378. This procedure is relatively easy to implement because the guarantor requires the independent to grant the guarantor an irrevoca-
production.\textsuperscript{109}

The more common choice is to step between the warring parties and help negotiate new deals that will salvage both the picture and investments.\textsuperscript{110} Before taking this step, some guarantors have used the prospect of a takeover to prevent the war from ever starting by persuading independents to stick to their script and budget.\textsuperscript{111}

An independent cannot rely on the guarantor's obligations in order to avoid paying for its mistakes. To the contrary, the independent must reimburse the guarantor, with interest, for any funds the guarantor expends from its own coffers after the production account is exhausted.\textsuperscript{112} The guarantor is repaid from the movie's gross profits after the distributor deducts fees and costs, and before other creditors are paid.\textsuperscript{113} As a further sign of its powerful status, the guarantor, after taking over production, puts backers on notice that they must pay the guarantor, not the independent, to continue production.\textsuperscript{114}

III. CONSIDERATIONS WHEN PURCHASING A BOND

A. Draft an Unambiguous Agreement

Independents and backers are advised to draft carefully the guaran-

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\textsuperscript{109} Id. at 377-78.

\textsuperscript{110} Id. at 380-81.

\textsuperscript{111} Id. at 375-77; GREGORY, supra note 42, at 154.

\textsuperscript{112} Id. at 381. CAL. CIV. CODE § 2847 (West 1991) provides in pertinent part: "If a surety satisfies the principal obligation, or any part thereof, whether with or without legal proceedings, the principal is bound to reimburse what he has disbursed, including necessary costs and expenses . . . ."

When a guarantor pays out to cover for the independent, the guarantor is subrogated to the lender's claims against the independent. Leatherby Ins. v. City of Tustin, 143 Cal. Rptr. 153, 157 (Cal. Ct. App. 1977). CAL. CIV. CODE § 2848 (West 1991) provides in pertinent part: "A surety, upon satisfying the obligation of the principal, is entitled to enforce every remedy which the creditor then has against the principal to the extent of reimbursing what he has expended . . . ." Section 2848 was not intended to preclude implied indemnity. Commercial Standard Ins. v. Bank of Am., 129 Cal. Rptr. 91, 94 (Cal. Ct. App. 1976).


\textsuperscript{114} COUCH, supra note 98, § 47:55.
tee agreement and other production documents, such as financing agreements and inter-party agreements. Documents should be drafted to reflect the parties’ intent at the time they agreed to the deal.\textsuperscript{115} Although every guarantee agreement ideally is the product of arms-length negotiation, people in the entertainment industry frequently do not get involved in the drafting process and rely instead on the guarantor’s expertise for drafting an air-tight, all-encompassing document that covers every contingency. The decision to rely on a guarantor may be ill-fated, as the resulting document will only be as good as the guarantor’s drafting abilities.

Independents are encouraged to take an active part in negotiating the conditions on which they expect the guarantor either to intervene or pay backers’ claims, because the guarantor surely will try to limit those conditions.\textsuperscript{116} Mutual involvement in drafting the agreement is essential to future good will, lest the parties later argue that the document is ambiguous, and their original contractual intent must then be analyzed. Like other contracts, a guarantee agreement is interpreted according to traditional rules of contract formation.\textsuperscript{117} It is read according to the plain meaning of its terms,\textsuperscript{118} except where it uses terms of art readily familiar to people in the industry.\textsuperscript{119} If a guarantor alone drafts the guarantee agreement and the resulting document is ambiguous, the ambiguity will be construed according to how the guarantor believed the independent understood the provision.\textsuperscript{120} The ambiguous term will be interpreted in favor of the independent and against the guarantor-drafter.\textsuperscript{121}

\begin{itemize}
  \item \textsuperscript{115} "When a contract is reduced to writing, the intention of the parties is to be ascertained from the writing alone, if possible . . . ." \textit{CAL. CIV. CODE} § 1639 (West 1991).
  \item \textsuperscript{116} "However broad may be the terms of a contract, it extends only to those things concerning which it appears that the parties intended to contract." \textit{CAL. CIV. CODE} § 1648 (West 1991).
  \item \textsuperscript{117} "In interpreting the terms of a contract of suretyship, the same rules are to be observed as in the case of other contracts . . . ." \textit{CAL. CIV. CODE} § 2837 (West 1991). Those rules are codified under \textit{CAL. CIV. CODE} §§ 1549-1701 (West 1991). Specific statutes regarding contract interpretation are found at \textit{CAL. CIV. CODE} §§ 1635-1662 (West 1991).
  \item \textsuperscript{118} "The language of a contract is to govern its interpretation, if the language is clear and explicit, and does not involve an absurdity." \textit{CAL. CIV. CODE} § 1638 (West 1991).
  \item \textsuperscript{119} "The words of a contract are to be understood in their ordinary and popular sense, rather than according to their strict legal meaning; unless used by the parties in a technical sense, or unless a special meaning is given to them by usage, in which case the latter must be followed." \textit{CAL. CIV. CODE} § 1644 (West 1991).
  \item \textsuperscript{120} "If the terms of a promise are in any respect ambiguous or uncertain, it must be interpreted in the sense in which the promisor believed, at the time of making it, that the promisee understood it." \textit{CAL. CIV. CODE} § 1649 (West 1991).
  \item \textsuperscript{121} "In cases of uncertainty . . . the language of a contract should be interpreted most strongly against the party who caused the uncertainty to exist." \textit{CAL. CIV. CODE} § 1654 (West 1991).
\end{itemize}
B. Perform in Good Faith

In addition to abiding by the express terms, every party to a contract has an implied good faith obligation to cooperate in completing the film.\textsuperscript{122} The independent is obliged to finish production on schedule, under budget, and according to the script. Backers are obliged to fund production. The distributor is obliged to accept the film and distribute it. The guarantor is obliged to cover the backers’ losses if production “blows up.” The precise nature and extent of each party’s good faith obligation is based on the agreements between the parties and their reasonable expectations of how the parties will perform their respective obligations.\textsuperscript{123}

Independents and backers should know that guarantors face unique penalties if they breach their implied good faith obligation. The State Insurance Commissioner regulates guarantors.\textsuperscript{124} Therefore, guarantors are liable for bad faith practices\textsuperscript{125} if they unreasonably fail to pay out claims when the independent’s fault is reasonably clear.\textsuperscript{126} When the court finds that a guarantor acted in bad faith, the prevailing party is entitled to recover the bond amount, consequential damages, and in an appropriate case, punitive damages and attorney’s fees.\textsuperscript{127}


\textsuperscript{124} A guarantor is “in the business of insurance.” CAL. INS. CODE § 105.

\textsuperscript{125} “[O]bligees under surety contracts are as susceptible to deceptive and unfair claims settlement practices as insurers [sic] and claimants under liability insurance contracts.” General Ins. of Am. v. Mammoth Vista Owners Ass’n, 220 Cal. Rptr. 291, 298 (Cal. Ct. App. 1985).

However, independents and lenders can sue guarantors only for common law bad faith, not for statutory bad faith. First-party and third-party private causes of action are no longer permitted under CAL. INS. CODE § 790 (West 1991) (“insurance bad faith”), ever since Moradi-Shalal v. Fireman’s Fund Ins., 758 P.2d 58 (Cal. 1988). Nonetheless, independents and lenders may still submit § 790 complaints to the Insurance Commissioner, who is empowered to impose civil penalties under CAL. INS. CODE §§ 790.05-.035(a) (West 1991).

\textsuperscript{126} See, e.g., Pacific-S. Mortgage Trust v. Insurance Co. of N. Am., 212 Cal. Rptr. 754, 761 (Cal. 1985).

\textsuperscript{127} See, e.g., General Ins. Co. of Am. v. Mammoth Vista Owners Ass’n, 220 Cal. Rptr. 291, 298 (Cal. Ct. App. 1985); Brandt v. Super. Ct., 693 P.2d 796, 800 (Cal. 1985). The prevailing plaintiff may also recover prejudgment interest that accrues from the date when the plaintiff first made a claim on the guarantee. CAL. CIV. CODE § 3287(b) (West 1991).

The right to recover attorney’s fees may also be drafted into one of the agreements, as in this financing agreement example, reprinted in KENOFF & ROSENBERG, supra note 32, Form 16-1, cl. 18: “In any action or proceeding between or among the parties hereto to interpret or
C. Arbitrate Any Guarantee Disputes

The parties should incorporate an "alternate dispute resolution" clause into every agreement. Arbitration and mediation can often re-establish strained business relationships without the cost, time and bitter feelings that accompany ordinary litigation. Many contractual disputes in Hollywood are resolved in this way by relevant trade guilds, collective bargaining agreements, and arbitral tribunals.\textsuperscript{128}

A standard arbitration clause appears in many entertainment contracts\textsuperscript{129} and can be incorporated into guarantee agreements:

Should there be any dispute between the parties concerning the interpretation of this Agreement or concerning an alleged breach of this Agreement, which the parties are unable to resolve after consultation with each other, such dispute shall be decided by arbitration pursuant to the regulations and procedures of the American Arbitration Association. The parties agree that any award rendered by the American Arbitration Association may be entered in either the (name of state court) or (name of federal court).\textsuperscript{130}

In some circumstances, it is appropriate to request the guarantor arbitrate disputes between independents and backers over the same productions it guarantees. Most guarantors are well-informed about industry politics and production techniques, and their existing ties to the project will encourage them to reach a fair resolution so that production can move forward quickly and economically.

D. Pick the Right Guarantor

Not all guarantors are created equal, and an independent has many from which to choose when seeking a backer for production funding. Some guarantors are well-established, high-volume businesses that offer extensive services. Other guarantors are newly-formed spin-offs that offer a more personal touch because of a smaller client base. The broad range of services and premiums now available in the marketplace allows an independent to choose a guarantor that fits its needs.

Many "older" guarantors do not like the competition. They cannot rely solely on their connections and are forced to implement intensive

\textsuperscript{128} Biederman, supra note 18, at 283-84.
\textsuperscript{129} Chrystie, supra note 13, at 1.
\textsuperscript{130} Kenoff \& Rosenberg, supra note 32, Form 16-1, cl. 17(f).
marketing and deal-making efforts just to maintain their existing market share. Many guarantors are accepting projects they would have dismissed five years ago, just to keep their name listed in the trade papers. Ms. Bette Smith of the Completion Bond Company is afraid that this headlong rush may lead some of her colleagues toward disaster: "I don't know if a lot of the completion guarantors who are entering the marketplace have the background that is necessary to properly analyze these projects and to monitor them through completion. It's just a very risky time in this market right now."\textsuperscript{131}

1. "One-Stop Financing"

Some guarantors have decided to garner business by offering an independent all the financial and technical needs, short of distribution, to produce a film. An independent may have the guarantor broker all the project's insurance, funding, crew, and equipment needs, in addition to the guarantee. The boldness of this step cannot be over-emphasized; these services were practically the majors' exclusive domain until now. By using the guarantor-broker, an independent can circumvent the independent-major dilemma over who dictates creative control. On the other hand, the guarantor has added incentive to supervise production closely and evaluate how the independent uses its services. Has the independent really preserved creative license, or does the problem continue, with the majors having been replaced by the guarantor?

One of the first guarantors to sell package deals was the Completion Bond Company, which created a "cut-rate production network" in 1986. A typical package provides vans, generators, grip and electrical equipment, laboratory processing, opticals, and titles.\textsuperscript{132} Another one-stop financier is Mr. Lawrence Vanger of Performance Guarantees, who explains:

We are maintaining a level of profitability by offering additional financial services which make it more attractive for the filmmaker to use us, rather than just looking simply at the price of the completion guarantee. That includes banking advice, production financing, distribution financing and expertise and some overall elements which help the producer get his package together; [we're] not simply interested in getting the cheapest possible deal on one element.\textsuperscript{133}

\textsuperscript{131} Noglows, \textit{supra} note 6, at 29.

\textsuperscript{132} Completion Prod'n Package To Feature Ryder Services, \textbf{DAILY VARIETY}, May 14, 1986, at 4.

\textsuperscript{133} Noglows, \textit{supra} note 6, at 29.
Apart from issues of who dictates creative control, a comparative analysis of the costs and relative degree of supervision involved with one-step financing may chill an independent's interest. Independents should weigh the benefits and disadvantages of every package. Mr. Robert Vince of the Motion Picture Bond Company, which guaranteed approximately eighty films worldwide in 1990, encourages independents to shop the competition. Like other guarantors, he simply dismisses the idea of one-stop financing as "wishful thinking."

To paraphrase Mr. Lionel Ephraim of Percenterprises, the question of picking a guarantor is simply: Does the independent want a large bonding company with considerable assets that supervises two or three different productions each week, or a smaller company with fewer assets and a more personal touch? Because individual claims are usually in the $1 million range rather than the $100,000 range, some independents look more to a guarantor's assets while others seek hands-on supervision.

2. "One-Stop Insurance"

Some independents are attracted by a guarantor who joins forces with an insurance company to sell a guarantee along with production insurance. This activity now occurs both in the United States and internationally, and is a variation of one-stop financing which targets an independent's insurance needs. An independent should ask the same questions about one-stop insurance as it would ask about one-stop financing.

In the United States, independents can purchase production insurance and a guarantee through International Film Guarantors. In 1990, this company began a joint venture with Fireman's Fund and the Near North Insurance Agency in Chicago, which provide the insurance.

Overseas, international ventures between Hollywood's guarantors and foreign insurers make good business sense because many independents want to cultivate the twenty percent or more of their financing that comes from foreign sources. In 1986, the Completion Bond Company and Australia's Cine Bond Company (which is aligned with Cinesure, Australia's leading film underwriter) struck a landmark international

134. Id.
135. Id.
136. Id.
137. Id.
138. Noglow, supra note 6, at 29.
139. Id.
deal. They began to sell a mandatory combination guarantee/insurance policy for Australian films budgeted over $700,000 Australian (about $560,000 U.S., based on the average Australian-U.S. exchange rate in 1991).

E. Closing Credits

It is appropriate to end this article by discussing the last thing most moviegoers see — the closing credits. Even guarantors appreciate their fifteen minutes of fame; increasingly, more guarantors want their name listed in the closing credits. This area has become subject to intense negotiations between producers and guarantors.

Some recent hits featuring credited guarantors are Kevin Costner's Oscar-winning Field of Dreams and Dances with Wolves (Completion Bond Company for both), and Honey, I Shrunk the Kids (Film Finances). Other films listing guarantors are The Adventures of Baron Munchausen (Film Finances), Winter People (Entertainment Completions), and L.A. Story (Complete Film Corporation).

CONCLUSION

Some independents treat guarantors as a necessary evil intrinsic in the motion picture production process. On one hand, they are "necessary" insofar as they are knowledgeable about the industry, expert in negotiating deals and resolving problems, and financially indispensible if production falters. They save pictures that might otherwise end up on the cutting room floor. On the other hand, they can take ultimate creative control over independents, which cuts at the heart of the reason why many producers make films.

An independent is justified in fearing a loss of creative identity to this supervising guarantor. Nevertheless, blockbusters are still being made. Films still gross millions of dollars. The independent market is expanding, and more guarantors are entering into it. The success of guarantors has not killed the independent market.

The key to resolving creative tensions lies in having the independent incorporate the guarantor into the production game and learn how the

141. FIELD OF DREAMS (Universal 1989).
142. DANCES WITH WOLVES (Orion 1990).
143. HONEY, I SHRUNK THE KIDS (Disney 1989).
144. THE ADVENTURES OF BARON MUNCHAUSEN (Columbia 1989).
145. WINTER PEOPLE (Columbia 1989).
guarantor can help achieve the mutually desired result — an efficiently produced motion picture. Independents must continue to adjust their visions according to financial restraints. Guarantors must continue to anticipate and preempt problems. Until now, the prospect of an independent being fired has created tension and fear on many sets. In the future, guarantors and independents should move beyond this tension and create joint production companies that offer both creative and technical services for projects the majors choose not to make.

In the meantime, independents must work within the restraints imposed by guarantors. One bright light is that, by having guarantors supervise the business aspect of production, the independent is left free to be creative. The guarantor, however, still has the final word, as expressed by Mr. Richard Soames of Film Finances:

We do impose a discipline. We make contributions. We rely on a relationship with the producer and director and department heads. We keep in touch with the production on a daily basis. We are advised of what was shot the day before, anything that happened that was untoward. We are a shoulder to cry on. And we go through all the legal documentation. And if, in our opinion, the film is going over budget, we have the right to step in.147

147. Loynd, supra note 8, at 116.