

# Entertainment and Media Law Signal Podcast Series | Production Financing

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## SPEAKERS

David Steinberg, Jim Russell

### Jim Russell 00:04

Hi, everybody. Welcome back to the Entertainment and Media Law Signal podcast brought to you by Dentons. Today we're here to talk about production financing in Canada. Typically, this involves various sources of financial support in film, television and digital media projects. And we'll offer some tips on how to actually close these deals. Listen in to learn more. My name is Jim Russell, I am a partner in the Media, Entertainment & Sports group in the Toronto office at Dentons.

### David Steinberg 00:33

And I'm David Steinberg. I'm a partner in the Media, Entertainment & Sports as well. You can find me in the Toronto office of Dentons as well. So, Jim, why don't we jump right in. One of the one of the questions that comes up a lot is - What do we mean, when we're talking about production financing? In your in your view, what does that encompass?

### Jim Russell 01:02

Yeah, it's a great question, because I think sometimes people think we're talking about sort of how to go out and get people to invest in their shows. And we do a lot of that for our clients, obviously. But what we're really here to talk about today is sort of the the nuts and bolts of the bank loan or interim financing of the various financing sources in a project. So the producers and their-- their teams have already done all the hard work, they've already gone out and found people to pay money to help them produce the show. And now they need to get the money to actually get into production. And production financing is a key component of that. Because obviously, you may get milestone payments during production, but most of your money, including your tax credits, comes at the end. So production financing is really a type of bridge loan, that allows the producer to borrow the money they need during production and then it all gets repaid at the end of production.

### David Steinberg 02:01

Okay, so over the years we have received many, many calls from producers, you know, that really come in all shapes and sizes and levels of experience. Sometimes they will tell us that they have their financing, or that they need help looking for financing. And in many cases, we find ourselves asking whether they're fully financed. So when a producer makes that call to one of us, and we put that question to them, and they say, 'Oh, don't worry, I'm fully financed, or we are fully financed'. What do we see as a production being fully financed? What does that mean?

**Jim Russell 02:51**

It's a really great question and I think it will vary. So let's start with a more kind of traditional or basic structure, which is probably a good starting point, we can talk about some of the more exotic variants if you want. But the basic one is, the producer has said, or hopefully has said unlock their budget. So once their budget is known, this idea of being fully financed means that you have enough financing sources to cover all the costs that are in your budget. Now, because a portion of the budget is set aside for payments to the producer for producer fees, or for what we call corporate overhead recoveries, you don't always need to have 100% of the budget covered by external sources. But it would be best if you did. So when the producer says I'm fully financed, what we expect to see are financing sources that will add up to the entire budget.

**David Steinberg 03:51**

And if we don't have financing sources that add up to the entire budget, let's say from distribution advances, license fees, tax credits, and other-- other incentives, where does that shortfall come from? Like if a producer is basically explaining that they're covered, I'm just going to pick a number - 90% of their budget is covered from those sources. What happens to that 10%? How does that get covered?

**Jim Russell 04:20**

So if you, the easiest way to do it would be to include some kind of producer investment or deferral or I guess deferral. We don't like to use that word so much, so let's use the word hold back instead. So as I mentioned, a portion of each budget is payable to the producer in terms of producer fees, and corporate overhead recoveries. So if you're 10% shy on your financing sources, it's a fairly straightforward process for the producer or people related to the producer to defer it or hold back that payment. So another way that this comes up obviously, is if you go to a lender, like a bank or some other kind of lender, they will most likely only give you some margin rate on your tax credit. So let's say 90%, 95%. So you're going to have a built-in shortfall in any event, and the way that those shortfalls are covered off is the same way - you would just have a hold back or reinvestment of producer fees and corporate overhead. Now, people call that PFCO. So if I use that term, don't hit me over the head with a baseball bat. It's just kind of a shorthand for reinvestments or deferrals of your producer fees and corporate overhead recoveries.

**David Steinberg 05:36**

PFCO, you called that?. There's no reason to swear. But okay, PFCO it is. So one, one question that I have is when a producer comes with their sources of financing. And they're--, they're approaching a bank. And explaining to the bank, here's our budget, here's how much we have covered. I'm assuming that the bank would want to look very closely at those sources to determine their legitimacy. For instance, if I were a producer, and I came to you with a distribution advance from a

major distributor, a license fee from a large broadcaster, I had my tax credits all lined up and estimated properly, and we'll throw in something else, maybe telefilm investment, I'm assuming a bank would look at that and feel pretty good about the financial wherewithal of those various sources to come through and cause the-- the payments to come in. But if I'm coming to you with less than the best in the business, if I've got a letter from Uncle Joe's Distribution Inc., things like that, how does the bank look at that? What-- what's their process for analyzing?

**Jim Russell 07:05**

So every bank and every other type of lender will have their own particular approach to determining the quality or the word they often use is "credit worthiness" of these financing sources. So depending on sort of how they manage their own risks internally, they may require financial statements from the financing source, they may do their own sort of background diligence. To find out if the-- if the company has a history of making payments when they say they will, they often use this term called "investment grade", which-- which gets thrown around. And every-- every lender and financial institution has their own view of what investment grade is. But basically, if your distributor or your broadcaster is a big public company, and if they can get access to financial information about them online, you know, through their securities filings or whatever, then they'll say, 'Okay, well, we know this company, and we're willing to bank it'. Just because your financing sources are not sort of these like tier one sources, that doesn't mean the bank or the lender won't interim finance them. But for example, if the-- if the credit worthiness is not super strong, the lender may say, 'Well, I'm only going to, I'm only going to advance a percentage against the contract'. So maybe that's as high as 90,95, maybe it's as low as 50 to 75%. It would really depend on the financing source. If you're dealing with a more conservative lender, they may say, 'Well, that's great that you've got this-- there, this other financing source, but we want to see all of their money in before we start advancing'. And that can be at times a challenging discussion. But you know, it's it's sometimes the only way to proceed if the bank says, 'I'm not going to interim finance that that particular party'. Another alternative that we've seen is when you have financing sources like that, if the producer could go to a second interim financier. So, for example, all of the all of the easier financing sources would be financed by your main lender, but you could have a second lender that would sort of advance funds against these other sources. And they would sort of sit behind the first lender in terms of recovery.

**David Steinberg 09:32**

So if you're in a situation like that, and I want to-- I want to come back on a couple of those points, but you're talking about a second lender. So now we've got two banks involved, and presumably two sets of bank lawyers. And that-- that's inherently going to complicate things a little bit, but yes, I understand that some sources of financing may be better are handled by one bank, and the other sources by another and it's just the way it is, we might have to face a situation where we have the two lenders. And they of course work out things like security as between the two of them in things like priorities agreements. So I get that. Do you think that some banks are more conservative than others when they're looking at the sources of financing and analyzing whether they're, as you say, credit worthy or not? Are some banks easier than others on that issue? Or are they all about the same?

**Jim Russell 10:38**

I think that I think that a lot of the banks are fairly similar. But there are definitely there are definitely banks that have, there are definitely banks that have more, let's call it aggressive or openness towards certain types of financing sources, it really depends on the history of the bank and the history of the lender. So for example, and this--, this is a very broad generalization and I don't--, I don't mean to offend anybody, but it's like, if you have banks that have historically banked a lot of foreign sales contracts, and those would, for example, they tend to be banks, based outside of Canada. But if you-- if your bank has sort of seen a lot of different foreign sales, then they they will know how to do a little bit more diligence on these third party sources. If your bank is sort of a more traditional Canadian television financing thing, they-- they may have less of an openness to that. But it really depends. And I will also say that what goes into the mix is also the producer's experience. So when-- when a bank or a lender is looking at interim financing a project, they're not just looking at the the interim finding-- the financing sources, they're also looking at the producer's experience. So if the producer has been able to sort of execute and deliver to these other sort of third party sources that are not coming up as often, but the producer knows how to get things done, then the bank may have sort of more confidence that this is going to pay out in the end.

**David Steinberg** 12:20

Oh, I see. So one of the things that that I-- I've noticed, over --over all these decades of doing this stuff, is that there's really two levels of analysis in terms of what makes something you know, quote, bankable, unquote. And that is the the credit worthiness as you've described, but also the paperwork that's required, the documents that are required in order to bank one of those sources. And I think you and I have seen over the years, a vast number of changes in terms of that type of documentation. Let's just call it 'assignment documentation' for ease of reference. And we've seen different approaches taken to it and also different reactions to that bank documentation from the buyers, from those distributors and licensees. Can you talk a little bit about that, like, I'm assuming if I come to you with a major studio, buying something or a major streamer, that the credit worthiness issue is probably going to be fine. But how much do-- does the bank look at the documents side of things? And how do they get enough comfort on that?

**Jim Russell** 13:44

So it would really depend, I think, on-- on the bank's approach, because most banks and other lenders too, they would rely more on their counsel to navigate the documents. The-- it's only rarely that we'll see a banker or a lender kind of reach into the assignment document. They'll-- they'll all expect, as I think most of the producers expect, they'll all expect that there's sort of a precedent out there that everyone will follow. So for example, if you're looking at sort of an ordinary course, Canadian sources, so the broadcaster's Telefilm, CMF, Ontario Creates, and other government agencies and private funds in Canada, they have done this trip with interim financing so many times that their assignment documents are sort of locked and loaded. So when they come up in a bank loan, or interim financing, you just take the agreed form, you know, add in the information for your particular project, and you're good to go. And you don't you don't really get into a lot of gnashing of teeth over that kind of document. But, if you're going to be dealing with someone outside of Canada, like if you're-- if you're negotiating something with a large US studio, or even in a mini major, if you're trying to negotiate something with the US broadcaster, that can be quite challenging. If you're trying to negotiate a notice of assignment with a foreign sales agent, for example, these can all be very challenging documents. And the reason

for that is that in the Canadian marketplace, at least, this is my view of it, in the Canadian marketplace, all of the participants know that they have to sort of play this interim financing game with the producers and with the lenders. And they know that their license fees and financial contributions are all going to be paid at the end. And they know that the interim financing with the bank is all part of what needs to be done. In the US experience. It's they they know what they don't know, right? So if a large broadcaster in the US is trying to buy a project, they're not going to be too happy about signing a notice of assignment that has them give up any kind of rights at all. And that's that's the challenge with these assignment documents is there's a perception that, from the studio or broadcaster perspective, their perception is, 'Well, I've already made my contract with the producer and that contract is my contract'. And they'll take the position that, 'Hey, listen, if the producer wants me to tell me to pay the amounts under the contract to some lender, I'm happy to do it. But I'm not going to waive any of my rights, I'm not going to agree to pay 100% on delivery, I'm going to stand by the terms of my contract'. So you're often in this little bit of a conundrum, because the bank wants absolute certainty about how much is payable and when it is payable. And the broadcaster in the studio is saying, 'Well, I'll pay when I'm satisfied that delivery has occurred and fall'. And so because those two points, there may be some gap between them the notice of assignment is used to kind of close that uncertainty off. And that's where you see people getting into, I won't say fights, but let's say challenging discussions with studios and broadcasters outside of Canada.

**David Steinberg** 17:11

Okay, so let's-- let's just talk about that for a second and make sure that everyone is clear on it. What will happen is a producer will negotiate a contract with a buyer, with a-- with a distributor, let's say. And it--, it may have been a very detailed negotiation, it's resulted in an agreement where everybody's happy and ready to move forward. And when the producer needs to get their interim financing together to go to a bank, unfortunately, some of what's in that contract may not work for the bank part of the deal. And the bank or lender may come and say, 'Hey, listen, we need to know how we're going to get paid, when we're going to get paid. And we have to make sure that there aren't too many loopholes, you know, that that distributor has so we're going to close those loopholes that may exist in the distribution agreement with our assignment documentation, be it a notice of assignment, sign of direction, inter party agreement, or whatever you want to call these things'. And that distributor may dig in their heels and say, 'We're not changing anything for anybody'. And if they do that, it creates a big tension there in terms of the producer saying, 'Okay, well, how are we going to get this thing made if you're not cash flowing us, and we have to interim finance your money, we can't get the-- get the film done, or the television series or whatever it is'. That's that's basically what you're saying, right? Yeah, that's right. Okay. And if again, if we look over the recent history or the ancient history as to how distributors and buyers will pay, we were, I'm going to say in the old days used to some money being paid upfront, perhaps a deposit of some sort. So somebody who was paying you a million dollar advance might be paying \$100,000, upfront, and then \$900,000 on delivery. Let's just use that as an example. But then we started seeing payment schedules really stretched out. And can you-- can you describe what the net impact is of that happening, the stretched out payments, and how long you've seen them stretched out?

**Jim Russell** 19:47

So what we've started to see and this, as you said, is going back quite a few number of years. But what we started to see or what it was in the case of broadcasters, they would want us to stretch out their license fee payment over the period of their broadcast term. So for example, if a broadcaster picked up the rights for a seven-year term, I've actually seen a contract where they said, well, we'll pay a little bit up front, and then we'll pay one seven of the remaining amount on the eighth on each anniversary of our term, right? So you go to-- you go to a bank, and the bank says 'We're not giving you seven year debt', right? Like we've these production loans are basically they're, they're there to live out through your production period, and maybe six to 18 months on the back end to cover tax credits, they're not there to interim finance you for seven years. So people would certainly producers would have to go back and talk to their broadcasters and broadcasters would dig in. And at the end of the day, like, the producer would just say, 'Well, I'll only interim finance, you know, the first couple of payments,' and they would, they would kind of putting hold backs and deferrals. For the rest of it, what you're seeing these days is we're not seeing as much of that kind of stretching out over like an insane amount of the term. But with some of the streamers, for example, you'll-- you'll see payments that come, you know, further into their license period. And the banks and other lenders have really just taken a pragmatic approach, which is to say, 'Well, only this percentage of the amount is actually bankable, and the rest of it, it's really the producers risk'. And again, to close the financing plan to be able to get your bank loan close, they-- they will say you'll have to defer the rest. And what that-- what that does, it's partly it's a practical approach. But what it really does, is it puts pressure on the producer to go back to the broadcaster and say, 'I can't interim finance this payment this way. So we're going to have to come to some other arrangement.' And that-- that-- that can create a lot of transaction friction, because you're really kind of breaking up, you're really kind of breaking up the contract that the producer made. And-- and that can lead to some challenging discussions.

**David Steinberg 22:06**

Got it, okay. And of course, it has an impact on interest costs, etc. so all that needs to be taken into account. At the beginning of the process, when we're first approaching a bank, how organized does that producer need to be? Because I used to work with this guy, he might even be on the call right now, who used to have a quote that he used something along the lines of 'Lack of planning on your part does not constitute an emergency on my part', was that you?

**Jim Russell 22:51**

Could have been, could have been. But times have changed. And-- and the customer's always right, David.

**David Steinberg 23:00**

Of course. So when we go in at the beginning, we often have these calls with producers who are obviously borrowers on these bank loans. They're very excited, because a banker, or even a bank lawyer, on occasion, has said, 'Oh, we can close this really quickly. Like we can do this in a week or two weeks or whatever'. And sometimes what gets lost in translation is that, that means that you're fully organized, that you've got everything together, that all your materials are in. How important is it to be well-organized at the beginning, as opposed to, you know, starting conversations with bankers and seeing if they're interested, etc.? What do you think the best approach is for a producer slash borrower?

**Jim Russell 23:53**

Well, given my own tendencies, I would, I would say you want to be as organized and complete as you possibly can be. But in the real world, you know, things are moving pretty quickly. So for example, and I know you've seen this a lot, David, like your--, your producer, in order to get the talent on their project, they have to sort of have a pretty definitive schedule in their mind. So they know when prep needs to start. They know when principal needs to start. Maybe they've even signed pay-or-plays that they need to be ready to go by a particular date. And so the the earlier in advance of that date, that the producer can start dealing with their bank or lender and the earlier they can start getting copies of all the relevant agreements, short form commitments, long form contracts chain of title documents, the sooner they can get all that organized, the better. But, you know, life unfolds the way life unfolds. And sometimes for whatever reason, you just can't get the stuff done. What-- what's happening more and more are sort of larger and larger levels of temporary holdbacks to kind of plug these holes, while people are waiting for long form contracts to get done waiting for the assignment documents to get done. And a lot of the lenders in the space, you know, they're they'll give some kind of early money or interim advance upfront, to kind of helped the producer, you know, get into production while they're moving all this other stuff along. Like aiming for the ideal is-- is obviously the way to go. But, you know, the reality is, we all have to be practical, and we just have to get the deal done as smoothly as we can in whatever amount of time we have.

**David Steinberg 25:37**

Okay, in terms of that organizational question, when is it that you think a producer should ideally have a lawyer lined up and working with them on the deal? Is it necessary to have legal representation early in the process, or could a producer/borrower wait, before they-- they bring in legal expertise?

**Jim Russell 26:05**

I think it really depends on how complex the financing structure is. So if you're-- if you're dealing with, like I said, if you're dealing with kind of the majority of the loans that are out there, it's like a license fee, couple other financing sources and tax credits like that, that you can, you know, you can paper and close that in relatively short order. And on a lot of those transactions, we don't see the producer's counsel come on board until-- until quite late in the process, right. So if you've got a really good business affairs person, working for your producer, or if the producer is really good at business affairs, they can move stuff along on their own. But if you've got some level of complexity, depending on your financing plan, you're probably going to want to get your lawyer involved early, if only quite frankly, if only, to have the producer's lawyer, like really sitting on the shoulder of the of the lender lawyer to kind of make sure that they're that they've got eyes on the deal, and are actually getting the documents done. Like that--, that-- that comes across as as little as a little sort of challenging sometimes, but it's totally the way it goes. Like, you know, in speaking, you know, I do a lot more on the lending side than I do on the producer side. But you know, all of us on the lending side, kind of get it like the producer's counsel there, is there to push, and that's their job.

**David Steinberg 27:25**

Right, exactly. I mean, do you have thoughts about lender counsel? Does-- does a producer/borrower have any say in who the lender or the bank is going to use as their lawyer? Or is that uncommon?

**Jim Russell** 27:44

Well, they do and they don't. Like if-- if you've got a really good working relationship with someone from a previous loan or if you're like, if the producers lawyer likes working with a particular lawyer, then they-- then they should they should raise it. Some-- some lenders, they don't care, like some lenders say, 'I want to use this person', and they'll say, 'Well, that's too bad, we use this other person'. But-- but a lot of the lenders, I mean, the thing for producers to keep in mind is that the the bankers, particularly at the bankers, but also in other lenders, those people are really the sales team for the lending institution, right? So it's, you need to kind of not view them as 'The Bank', right? Like these people they need, they want the loans, they want to do business with people, they want to develop relationships. So it is-- it is about building that relationship. And so if if the producer or the producer's counsel are uncomfortable using a particular lawyer, or if they're concerned that maybe that particular lawyer is-- is good for certain kinds of transactions, but maybe not for this one, you know, then yeah, there's no harm in asking for it. You might not get the answer you want, but you should definitely raise it.

**David Steinberg** 28:57

Okay. And it's interesting what you're saying that, there's, there's sort of a customer service aspect involved, where they do want to make sure that the customer is happy, they want to make sure that the loan goes well, and that the customer will come back again, and do more work with them. And there's a certain amount of competitiveness, I suspect, you know, within the lending community to get the good deals anyway. Nobody wants the legacy ones. But if-- if you're in a situation where you've got different banks talking to you, I guess you're focusing in as a borrower on the terms that are being offered, the interest rates, the setup fees, etc. And you ideally are going to look for the person who is the easiest and best to work with for you. And again, if we-- if we look back on recent and ancient history, there have been some bankers that we've worked with, some of whom you've represented, that have been really quite excellent in the field, and are very pragmatic and do help the producers along. But I think that every producer needs to understand, every borrower needs to understand, that they can only do what they can do, based on what you're bringing to them, how well organized it is. They can't just pull rabbits out of their hat all the time, that's not the way it works. So when we're in those situations where people are begging for support, but they're not properly organized, that there's only so much a banker can do in that circumstance.

**Jim Russell** 30:48

Yeah, I think that-- I think that's right. And I think another important consideration for the producers, is to try and find out if the bankers they're talking to have actually done a deal that looks like the one they've got, right. And that's—that-- that's, you know, it, it's all about communicating with your personal networks, and professional networks, and ask your lawyers and ask your accountants and sort of figure out like, if you've got, you know, if you've got a really basic basic television financing, then you know, there's probably a lot of bankers who could do that. And so it's really a question of, who do you get along with the best, and you know, which bank etc. But if you've got like a challenging like, if you've got a gap financing deal, or if you've got kind of an out of the ordinary kind of private investor or mezzanine lender in your mix, or if you've like, borrowed money from another person that needs to get paid out at closing like it, the more complex your deal is, you're going to want to do a bit of homework in terms of which banker and banks, or which lender and lenders actually have done the stuff you're trying to do.



**David Steinberg** 31:57

Okay, that's great. Well, this has been very, very helpful, Jim, and to our listeners. If you have any questions about any of this, please feel free to contact us. You can find our contact details on this episode's page. And thank you very much for listening in.

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