VALLEY LAWYER

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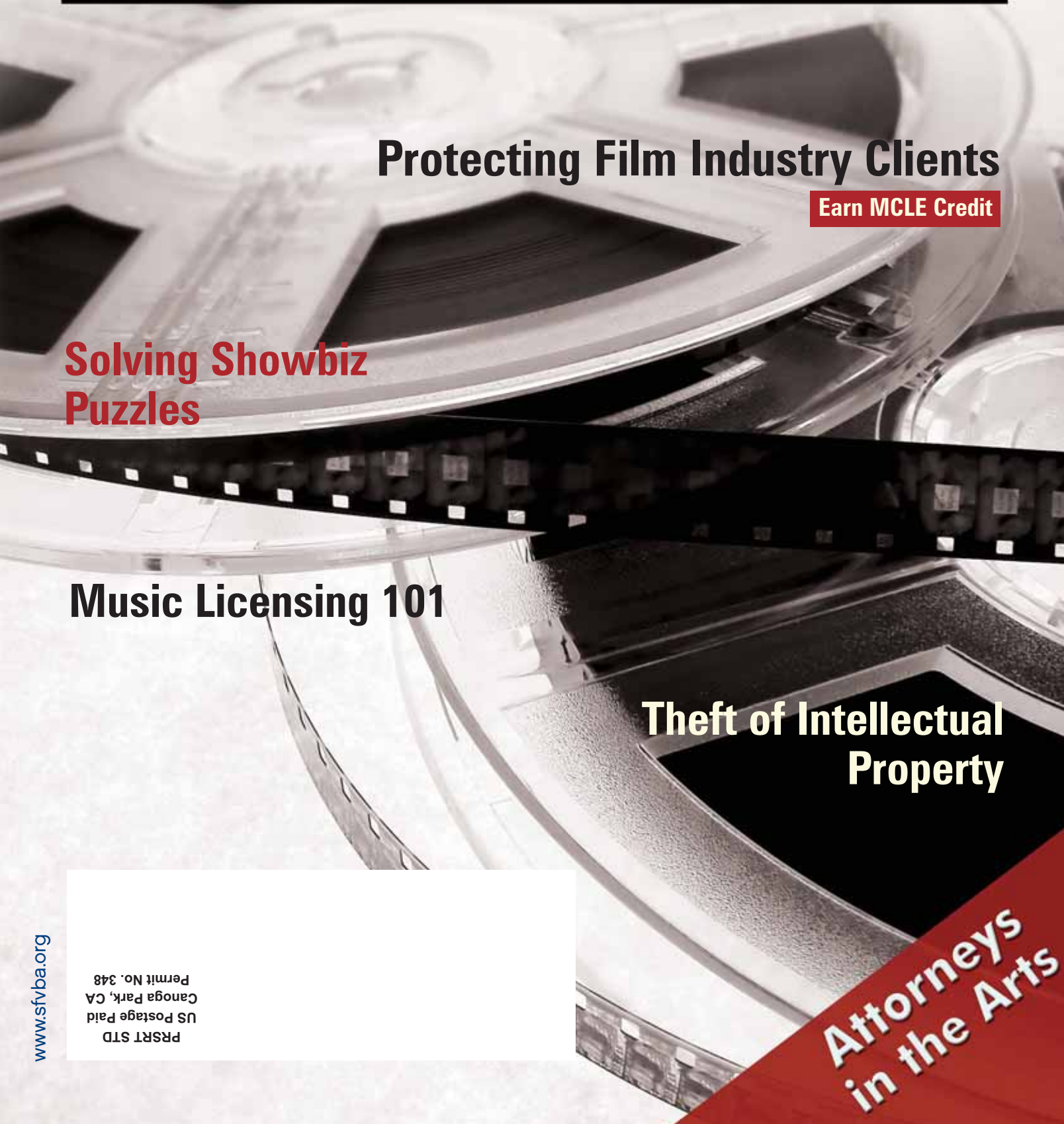
A Publication of the San Fernando Valley Bar Association



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Music Licensing 101

Theft of Intellectual Property

Attorneys in the Arts

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A Call for Volunteers

ROBERT F. FLAGG
SFVBA President

IT HAS NOW BEEN 83 YEARS since the San Fernando Valley Bar Association was founded. Much to my surprise, I find myself President of this 2,000 member organization of Valley lawyers. When I first joined the Bar, I did not set out with this position in mind as a destination. In fact, when years ago one of our members, a colleague whom I have known for more than 20 years, told me I would be President one day, I thought he was kidding. But I know how I got here: someone asked me to help.

Among the eight phrases which compose our mission statement, the last reads: "Preserve and enhance the ideal of the legal profession as a service profession and its dedication to public service." This ideal of the legal profession as a service profession, is a principal theme of my term as President. I became a lawyer to serve. Though the practice of law is many things, including both a learned profession and a business, I firmly believe that it is first and foremost a service profession.

So when I was asked years ago to join the San Fernando Valley Bar Association, its ideal of service fit right into my fundamental philosophy. Later, when I was asked to help revive the moribund Litigation Section, it was a natural thing for me to agree to help. Later, the Section Chair who was moving on to become President asked me if I would mind taking over the duties as Chair of the section. Naturally, I agreed. (I do periodically chastise Past-President Greenberg for leaving me holding the bag.)

And I kept agreeing when asked to help the Bar in various capacities. So here I am, serving as always, this time as President. In turn, I am asking you, our members, our colleagues, our friends and our associates in this service profession: join me in service by choosing one or more of the myriad ways available through the San Fernando Valley Bar Association to support our mission to enhance the ideal of the legal profession as a service profession and its dedication to public service. Among those are:

- **A long-term project to increase diversity in the legal profession:** To further that goal, we are engaged on many levels and through many activities to encourage those of all the multitudinous ethnicities and cultures which are part of our Valley to become members of our profession. Ultimately, this will increase the diversity of judicial officers at all levels in our community and state. Opportunities for involvement range from participating in our elementary school plays for Law Day, to the Bar's sponsorship of a law-related Explorer post to fundraising for scholarships provided, to students through the Valley Community Legal Foundation of the SFVBA.

- **An effort to further support our local courts:** The Bar was initially founded around the goal of bringing a courthouse to the Valley and in recent years, the SFVBA and our Foundation continued that tradition by providing support and funding for construction of a children's waiting room in the Van Nuys courthouse. We have raised additional funds in support of a similar facility for the San Fernando courthouse. We need help to raise additional funds and additional support to make that dream a reality.

These are but two examples of the ongoing efforts now actively being carried out by and through the SFVBA for the benefit of its members and our community. Tell us where your interest lies. Chances are there is a place, a project, a section or a Bar activity where you can help. I'm just asking.

Robert Flagg *can be contacted at robert.flagg@farmersinsurance.com.*

From the Editor

*For question, comments or candid feedback regarding **Valley Lawyer** or **Bar Notes**, please contact Angela at (818) 227-0490, ext. 109 or via email at Angela@sfvba.org.*

ANGELA M. HUTCHINSON
Editor

Dear SFVBA members,

Our Communications Department has had a busy fiscal year. The hard work especially pays off when we receive comments and feedback from our valued members. I encourage you to submit comments to me on articles that you feel were very informative, useful or the opposite. As a non-attorney professional editor and writer for *Valley Lawyer*, I take great pride in implementing feedback received to ensure the magazine's editorial content is relevant to our members.

On that note, I am excited to inform you that I have been selected to receive a scholarship to attend the National Association of Bar Executives Communications Section Workshop in Las Vegas later this month. I look forward to representing the SFVBA and bringing back valuable ideas to help take our Communications Department to the next level.

Inside this issue of *Valley Lawyer*, you'll find substantive articles on entertainment law written by attorneys in the arts. From intellectual property rights to entertainment med-arb to film contracts, you have an opportunity to gain a better understanding and/or further your knowledge about the entertainment industry.

Hollywood's famous "Lights, Camera, Action!" catch phrase is often used in reference to filming a movie. Before a movie is filmed, a script must be written. Before the script is written it, a story must be developed. Before the story is developed, an idea must be conceptualized. Several articles this month focus on intellectual property and the importance of protecting one's ideas through copyright. Whether you have an interest in entertainment or not, I encourage you to learn more about the industry and consider potential partnerships or ways for you to network with fellow SFVBA entertainment attorney members.

If you are not involved in the entertainment industry, maybe you know an actor, writer, producer, director or other creative or business professional who might find the information in this issue helpful as I did from a book author and scriptwriter standpoint.

Entertainment is an intricate part of our Valley community. In my Q&A interview with member David Fleming, an advocate for the arts, he reminded me that although the city of Hollywood is known as the multi-faceted entertainment mecca, the San Fernando Valley is the home to most of the major film studios, production companies, television network, famous actors and industry execs.

With such a thriving Valley community, it's no wonder the SFVBA is committed to serving attorneys from all areas of law practice. So, why do you belong to SFVBA? I hope you enjoy reading the answer to this question from your fellow members who are featured throughout this issue. On behalf of the SFVBA staff, I encourage you to renew your membership today.

Have an entertaining month!

Angela M. Hutchinson

Q&A with Philanthropic Attorney David Fleming

Pledged $1 Million for Performing Arts

By Angela M. Hutchinson

THE SPOTLIGHT IS ON ATTORNEY DAVID W. FLEMING AND HIS wife Jean for their $1M pledge to help build a new performing arts center at California State University, Northridge. Fleming is the vice chair of the $125 million campaign to create the center.

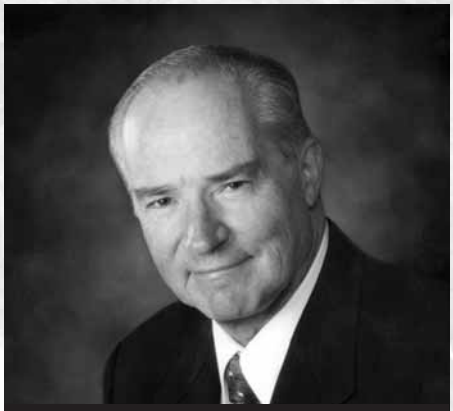
In addition to serving on the board of CSUN's Foundation, Fleming has been the director of the following organizations: The Los Angeles Police Foundation, the Children's Bureau of Los Angeles, the Los Angeles County Children's Planning Council Foundation, the Civic Alliance, the New Majority and the Fernando Award Foundation. He also serves on the board of the Advisors to the Dean of UCLA Law School.

A practicing attorney for fifty years, he is Of Counsel to Latham & Watkins, the third largest law firm in the United States and fifth largest in the world. He is a past recipient of the prestigious Fernando Award, bestowed annually on a San Fernando Valley resident in honor of a lifetime of volunteer service, and the San Fernando Valley Bar Association's Stanley M. Lintz Award, for his contributions to the legal profession and the community.

Born and raised in Davenport, Iowa, he moved to the San Fernando Valley in 1956 and graduated from UCLA Law School in 1959, where he was a member of the Southern California Chapter of Phi Beta Kappa.

David and his wife Jean have two adult sons residing in Southern California. Over the years, the Flemings have personally donated over $5 million to a wide array of charities, including Valley Presbyterian Hospital, CSUN and UCLA Law School.

Inside this issue of *Valley Lawyer's* Attorneys in the Arts, it is an honor to introduce you to fellow SFVBA member, David Fleming, an attorney passionate about performing arts.



Attorney David Fleming

Q: Did you make a plan for what you wanted to achieve in life?

A: My only plan was to be highly successful at whatever I eventually decided to do. Law was an afterthought. I started out as a newspaper reporter and then a broadcaster. I was a staff announcer for CBS in Chicago when one of the network VPs from New York said to me "if I had a kid your age I'd send him to law school and bring him back in the management end of the network". That sounded like a good idea.

My father was retiring and my parents were going to move to either Florida or California. I urged them to settle in Los Angeles where I could go to law school and stay close to CBS. After I got caught up in the law I forgot about broadcasting, and here I am today, 50 years after passing the bar, and still lawyering.

Q: What piqued your initial interest in the arts? And what about law?

A: Having a background in broadcasting, I was drawn to the arts – plays, TV, movies, etc. My wife (who was Miss Illinois in Miss America) became an actress early on in her life. She acted in scores of films, several television series (she was Darrin's secretary in Bewitched), commercials and plays. So we were a part of the arts early on.

Q: Tell us about a compelling aspect to CSUN's "Imagine the Arts" campaign?

A: I have been involved in the Valley's leadership circles for over 40 years. All that time the Valley has needed a venue comparable to LA's music center. Traffic, being what is has become, has made getting downtown during "rush" hours to see plays, concerts, etc. nearly impossible. The new Performing Arts Center will draw people from not just the San Fernando Valley but the surrounding valleys to the north and west – a market of well over 3 million. Our Valley is the largest population center in America without the benefit of a major arts venue.

Q: Has your law career and passion for the arts converged into any unique opportunities?

A: I have represented many great artists over the years, from the American Society of Cinematographers to the Technology Council of the Motion Picture-Television Industry which I helped create and which is now a part of the Academy of Motion Picture Arts & Sciences. I have worked with hundreds of very talented folks in the industry over the years and my wife has become both a screenwriter and a motion picture producer.

Q: Life can be overwhelming at times, how do you maintain a balance?

A: I'd go nuts if I was retired and had nothing to do but play golf. Don't get me wrong. I love golf. But working 10 hours every day – helping non-profits and those in need – has become my joy and fun in life. I have made a very good living. But Jean and I believe in sharing what we have with others. Reminds me

of what my late great attorney friend, John Argue, the guy who brought the Olympics to Los Angeles in 1984, used to say: "My charities are beginning to interfere with my charities."

Q: How do you determine what type of charities you will support?
A: I get asked by so many charities to give and get involved. It's hard to pick and choose – there are so many great causes. But lately I have found I have to ration my time. Age is beginning to catch up with me and Jeanie. I still serve on 13 boards of directors and chair many of them. And I am in the office everyday. I was 75 years old this September, but that's still young.

Q: How did you meet your wife Jean?
A: In 1981, with the prime interest rate reaching 20%, I found myself the owner of two homes with loan payments over $10,000 a month. I decided to sell them but the real estate market was non existent back then. No one could afford to buy. One of my law partners told me to call Jean Blake. I did. We met, fell in love and when she sold both houses and we got married and brought a third one together. She later remarked that I would have done anything to keep from paying a real estate commission – including marriage!

Q: You both cherish the arts, why?
A: Many of our friends and neighbors are, and were, in the industry. We have an academy card and see the latest movies when we have the time. I love all kinds of music, classical particularly. Life is enriched by the arts.

Q: What is one of the most enlightening non-fiction books you've read?
A: I don't get much time to read. But I have found that as I get older history fascinates me – probably because I've live through a lot of it. I was a kid when America was attacked at Pearl Harbor. I grew up during the Second World War and remember what life was like in America back then. We were never more united. I had two older bothers who fought in that war.

Non-fiction books on the war, the founding of America, past presidents (I have met and talked with 10 of them over the years), Churchill (whom I also once met) – all are subjects I love to read about. I recently had lunch with David McCullough, who has written some great historical books. On the National Archives in Washington D.C. are inscribed the words: "What is past is prologue". I believe that.

Q: What is your favorite restaurant in the Valley?
A: If Valley restaurants depended on me for patronage, they'd all be out of business. We don't eat out much. But our tastes are pretty simple. We go to Marie Callender's a lot. Jeanie tells me I'm in a rut when it comes to restaurants – and I am a creature of habit.

Q: Would you prefer to watch the sun rise or set? Why?
A: I love sunsets. From our house just below Mulholland Drive, we can see 30 miles out over the Valley and to the mountain ranges beyond. It is fun at the end of the day to look out as the shadows turn into millions of lights. Very uplifting.

Q: What song title best describes your life.
A: On the Sunny Side of the Street [composed by Jimmy McHugh and lyrics by Dorothy Fields].

Section Profile

Intellectual Property, Entertainment and Internet Law

By John F. Stephens

THE SAN FERNANDO VALLEY BAR ASSOCIATION'S IP, Entertainment & Internet Law Section will be featuring some outstanding CLE's in the upcoming year, including in-house counsel from various studios, technology and internet experts, and cutting edge topics.

Chaired by John Stephens and Co-Chaired by Mishawn Nolan, the purpose of the Section is broad and will provide something for every practitioner. The primary function of the IP, Entertainment & Internet Law Section is to provide a forum for members of the legal community to address intellectual property and entertainment law issues relating to all types of law practices.

The Section will address issues related to copyrights and trademarks, patents, trade secrets, entertainment matters, intellectual property litigation, insurance for intellectual property and intellectual property risk management.

Richard Munisteri of Live Nation will discuss copyright and trademark issues relevant to the entertainment and concert arena at the IP Section's October 23 meeting.

The Section's goal is to provide practical guidance in cutting edge issues dealing with all areas of intellectual property and entertainment, including the cross section between new technology and intellectual property. One example is the new trademark and copyright issues emerging with online games, social websites and ever evolving communi-cation technology.

Each year, the Section holds a year-end roundup where relevant cases of the previous year are discussed and how such cases will impact clients and the practice.

John Stephens *is a partner in the Los Angeles office of Sedgwick Detert Moran & Arnold, specializing in media and entertainment litigation. His clients include entertainment and technology companies, online content and software providers, television and radio stations, and other media entities. He is Co-Chair of the SFVBA's Intellectual Property, Entertainment & Internet Law Section. He can be contacted at john.stephens@sdma.com.*

Theft of Intellectual Property

By Bonnie J. Chermak

ENTERTAINMENT IS MORE THAN just the frivolous diversions that get us through the day. It is also no less than the medium through which the concepts that propel us forward as a civilization are conveyed. The innovation and talent behind an intellectual property is deserving of both respect and protection. For attorneys in Los Angeles, there is a good chance someone has asked at one time or another how they should go about exploiting the screenplay that they have written, or the great idea that they have come up with for a new television series, without getting ripped off. Surprisingly, the answer to this question is fairly simple, despite the fact that the law surrounding this subject is rather complex.

Exploitation of an intellectual property necessarily requires disclosure, or submission of the property, to someone in a position who can make that happen – a producer or a production company, a studio or a network. While it should be presumed that people in such positions are not in the habit of stealing that which they are actually in the business of paying to acquire, the reality is that theft of intellectual property does occur both unintentionally[1] and intentionally.

The first part of the answer to this question therefore is the inevitable caveat: just as nothing can stop a lawsuit from being filed, nothing can prevent the misappropriation of an idea or its embodiment. Theft of this kind, however, can be discouraged, and a remedy can be pursued if protective efforts have been undertaken and certain tests are met. The second part of the answer to this question then, is to advise that the work be registered to establish ownership and date of creation, and that it be submitted under circumstances and in such a manner that makes clear it is being provided with the understanding that its use will be compensated. A better understanding of the state and federal law governing this subject, including what can be protected and how theft is established, will help clarify this answer.

California law concerning the protection of ideas finds it genesis in the *Desny v. Wilder (1956) 46 Cal. 2d 715*, case, which explained that "[g]enerally speaking, ideas are as free as the air * * *[b]ut there can be circumstances when neither air nor ideas may be acquired without cost." *Desny* warns: "[t]he idea man who blurts out his idea without having first made his bargain has no one but himself to blame for the loss of his bargaining power." However, "[t]he person who can and does convey a valuable idea to a producer who commercially solicits the service or who voluntarily accepts it knowing that it is tendered for a price should likewise be entitled to recover." The *Desny* case therefore, utilized the law of implied contracts to protect ideas. This protection is also codified in California in the Civil Code.[2]

Conversely, federal copyright law, found at *17 U.S.C. §102, et. seq.*, expressly excludes the protection of ideas. Instead, copyright law protects "original works of authorship fixed in any tangible medium of expression" which includes literary works. The exclusive rights held by copyright owners include the right to reproduce, adapt, distribute, perform, and display a copyrighted work. Protection of these rights are exclusive to the federal court, as the Copyright Act preempts "all legal or equitable rights that are equivalent to any of the exclusive rights within the general scope of copyright as specified by section 106. . ." [3] "Equivalency" is the critical issue in this inquiry, and to avoid preemption, the state claim must protect rights which are qualitatively different from those protected by copyright law – an 'extra element' which changes the nature of the action."[4]

Historically, this has been a problem for ideas, because while they are expressly precluded from protection under the Copyright Act, they are often so inextricably intertwined with material that is the subject of copyright law as to be deemed preempted.[5] Because copyright law protects against "copying" and idea protection is concerned with unauthorized "use," ideas contained in a writing could be "used" without the substantial "copying" that would invoke the copyright remedy, thereby paradoxically resulting in no remedy at all.

The issue evolved as a discussion of whether an implied contract has the "extra element" that would avoid preemption. While California courts have had no problem asserting its competency to determine contract issues, even if the subject of the contract was copyright,[6] federal courts have not been so quick to relinquish such claims from their preemptive grasp. The greater weight of federal authority has found that contract claims are generally not pre-empted because they contain the extra element of a "promise" that is not involved in copyright protection.[7]

Two Central District decisions, however, have opined otherwise. *Endemol v. Twentieth Television, Inc., 48 USPQ2d 1524, 1528 (C.D. Cal. 1998)*, posited that a contract could conceivably agree to not violate a copyright, and as such would fall under the purview of the copyright laws. *Selby v. New Line Cinema Corp., 96 F. Supp. 2d 1053, 1060 (C.D. Cal. 2000)*, held that because the implied contract in issue addressed nothing beyond the use of the

work, it was equivalent to the rights protected by copyright law. The Ninth Circuit, however, in the *Grosso v. Miramax Film Corp. (9th Cir. 2004) 383 F.3d 965, 968*, case held that the claim in issue there for breach of an implied-in-fact contract was not preempted by the Copyright Act, because it alleged the extra element that transformed the action from one arising under the ambit of the federal statute to one sounding in contract.[8]

One recent case combined the foregoing analyses to hold that a claim for breach of a third party beneficiary contract did *not* have the extra element needed to avoid pre-emption because the claim asserted damage from the defendant's exploitation of the property, but to the extent the complaint could be understood as asserting a claim for use of the idea contained in the copyrighted work, the claim for breach of an implied contract was held to not be pre-empted.[9]

Understanding the elements of proof involved in claims of this kind will further clarify how intellectual properties may be protected. Under California law, an idea that can be the subject matter of a contract need not be novel or concrete, because it could be valuable to the person to whom it is disclosed simply because the disclosure takes place at the right time.[10] Federal law, however, as discussed above, requires the work to be "original."[11] Elements that would be expected to be found in the treatment of a particular subject or genre are considered "*scenes a faire,*" and not "original."[12] Both fields of law require proof of access and substantial similarity. [13]

Under California law, "access" is shown if there is a reasonable possibility that the plaintiff's work has been viewed – not a bare possibility.[14] Under federal law, access is proven when the plaintiff shows that the defendant had an opportunity to view or to copy plaintiffs' work.[15] With respect to substantial similarity, under California law, substantial similarities are determined by a comparison of the two works based on the impression perceived by the average reasonable person.[16]

Under federal law, the Sid & Marty Krofft Television v. McDonald's Corp., (9th Cir. 1977) 562 F.2d 1157, case sets forth a two-part extrinsic/intrinsic test for the evaluation of substantial similarity. The "extrinsic" test is concerned with similarity between the expression of the general ideas of the two works. This expression is found in similarities between the plot, themes, dialogue, mood, setting, pace, characters and sequence of events. The "intrinsic" test asks if an "ordinary reasonable person" would perceive a substantial taking of protected expression based on the total concept and feel of two works. These two tests are alternately considered objective and subjective analyses of expression.[17] As one might expect, these tests are not a solid predictor of how the court will decide the issue. A review of cases discussing the application of these rules is advised before pursuing such claims.

So, now that the issues of what can be protected and how theft can be shown have been discussed, the steps to be taken to protect the property should be clearer. Proving it is the submitter's idea and the date it was created can be aided by its registration with the Writer's Guild. Even a so-called "common law copyright" works for that purpose. Mailing it to one's self through the U.S. mail and not opening it until trial will establish the date the work was created.

As a practical matter, an unopened copy of the exact item being mailed should be maintained. A screenplay should also be registered with the copyright office. An idea should be presented in a manner that indicates the recipient understands and agrees by his acceptance of the idea that if it used, the person tendering the idea will be compensated accordingly. Expressing this "understanding" in a letter that precedes an oral presentation, or accompanies a written submission, will be evidence. A copy of the letter and proof of delivery should be maintained.

Attorneys can also assist with the submission of such materials in this manner. Although many entertainment companies avoid unsolicited submissions, if they come from an agent or an attorney, they will usually accept them. Other circumstances that could support proof of this "understanding" would be if the submission was coordinated through a licensed talent agent, who despite recent reasonable inroads,[18] pursuant to *Cal. Labor Code §1700, et. seq.*, still has the legal monopoly on brokering the employment of writers in this field. While the circumstances of a submission to someone in a position to help exploit the property *in itself* would seem to be enough to establish the "understanding," such should not be taken for granted,[19] and express documentary evidence of intention and understanding should accompany any submission.

Sometimes an entertainment company will insist that a release be executed before the submission will be accepted, whereby the submitter agrees to waive all claims of theft based on a similar idea the company may already have in the works. This is a Hobson's choice best avoided. While it is designed to protect the entertainment company from frivolous claims, it could also be used as a license to steal. It is also wholly unnecessary as the law already protects against theft claims if the defendant proves the idea or work in issue was independently created.[20]

Here in the entertainment capital of the world, Los Angeles attorneys can do their part to protect the process and the creators wherever they may be found, when the inevitable "what should I do?" question arises. Knowing what can be protected, how to prove ownership, and how to preface a submission, is the support needed to keep ideas and their expression flowing.

Bonnie J. Chermak *comes from a family of professional writers and worked in feature and television production before becoming an entertainment attorney. She was with the entertainment litigation firm of Lavely & Singer for four years before opening her own practice focusing on entertainment and business transactions and litigation, in 1995. Ms. Chermak's practice profile and contact information can be found at www.LAEntertainmentCounsel.com.*

[1] See: Bright Tunes Music v. Harrisongs Music 420 F. Supp. 177 (S.D.N.Y. 1976), where it was held that George Harrison's song "My Sweet Lord" unintentionally infringed the copyright in the song "He's So Fine."
[2] Cal Civ Code §980.
[3] 17 U.S.C. §301(a).
[4] Del Madera Properties v. Rhodes and Gardner, Inc., 820 F.2d 973, 977 (9th Cir. 1987).
[5] Selby v. New Line Cinema (C.D. Cal. 2000) 96 F. Supp. 2d 1053, 1058; Musto v. Meyer, 434 F.Supp. 32; 196 USPQ 820 (S.D.N.Y. 1977).
[6] Durgom v. Janowiak (1999) 74 Cal. App. 4th 178, 180, 87 Cal. Rptr. 2d 619.
[7] Lennon v. Seaman, 63 F. Supp. 2d 428, 437 (S.D.N.Y. 1999) reviewing cases from the Fourth, Fifth, Seventh and Eighth Circuits.
[8] Grosso v. Miramax Film Corp. (9th Cir. 2004) 383 F.3d 965, 968.
[9] Morris v. Atchity (C.D. Cal. 2009) 2009 U.S. Dist. LEXIS 14581.
[10] Donahue v. United Artists Corp. (1969, Cal App 2d Dist) 2 Cal App 3d 794.
[11] 17 U.S.C. §102(a).
[12] Baker v. Selden (1897) 101 U.S. 99; Ets-Hokin v. Skyy Spirits Inc., (9th Cir. 2000) 225 F.3d 1068.
[13] Golding v. RKO Pictures, Inc. (1950) 35 Cal. 2d 690, 695; Sid & Marty Krofft Television v. McDonald's Corp., (9th Cir. 1977) 562 F.2d 1157.
[14] Mann v. Columbia Pictures (1982) 128 Cal. App. 3d 628, 651.
[15] Sid & Marty Krofft Television v. McDonald's Corp., supra, 562 F.2d 1157, 1172.
[16] Kovacs v. Mutual Broadcasting System, Inc. (1950, Cal App) 99 Cal App 2d 56.
[17] Apple Computer Inc. v. Microsoft Corp., (9th Cir. 1994) 35 F.3d 1435, 1442-43.
[18] Marathon v. Blasi (2008) 42 Cal. 4th 974.
[19] Grosso v. Miramax, 2007 Cal. App. Unpub. LEXIS 7326.
[20] Hollywood Screentest v. MBC Universal (2007) 151 Cal. App. 4th 631; Granite Music Corp. v. United Artists Corp. (9th Cir.1976) 532 F.2d 718, 721.

MUSIC LICENSING 101

By Dorothy Blake Richardson

MUSIC LICENSING CAN BE a complicated process, even for the entertainment law practitioner. As new and different ways of music are proliferating on the internet and mobile devices, the rules for licensing such uses have been changing rapidly. Following is a brief overview of the most common types of music licenses and a discussion of recent legal changes affecting such licenses.

The first thing to keep in mind when seeking a license to use music is that more than one copyright may be involved. The sound recording is an artist's particular rendition of a song, for example, Michael Jackson's performance of "Thriller." The copyright in the sound recording is owned by the artist who performed on the recording or by the artist's record label. On the other hand, the musical composition, i.e., the sheet music, lyrics and melody, is owned by a music publisher or an individual songwriter. If one is using a sound recording as well as a musical composition, two separate licenses will need to be obtained, one from the record label or artist, and the other from the music publisher or songwriter.

In some instances the sound recording and the musical composition are owned by the same company; this is known as "one-stop shopping." For example, production music libraries control all rights to the recordings in their catalog, and will issue a single license covering both the sound recording and the musical composition.

Synchronization and Master Use Licenses

In order to use a sound recording in a film, television program, commercial or other audiovisual work, a "master use license" will need to be obtained from the record label or recording artist for the right to use a particular master recording. A "synchronization license" is also needed to use the musical composition that is being performed, so-called because the composition is used in synchronization or timed relation with visual images.

Musical compositions often have more than one writer. Sometimes the recording artist will insist on contributing a few bars to the song and will claim a co-writer credit. The more successful the recording artist, the greater the likelihood that the artist will own a portion of the musical composition copyright.

If a song has several different co-writers, the music must be cleared with each of the writers' publishers, who will generally condition their approval on obtaining "most-favored nations" ("MFN") status with all other publishers. This means that regardless of the license fee negotiated with any individual publisher, if any other publisher is granted a more favorable rate, the publisher with the MFN clause will receive the same favorable rate. For example, if one publisher controls 25% of a musical composition copyright, and issues a quote of $5,000 for the use of such publisher's portion of the song in a film, and the other publishers have an MFN clause, it will bring the total synchronization fee for the song to $20,000.

The master use license may also contain an MFN clause requiring the master use fee to be on terms at least as favorable as the synchronization fee. Using the previous example, the total fee for the use of the music in the film would be $40,000, i.e., $20,000 for the synchronization license and $20,000 for the master use license.

Licenses for films and television programs are almost always done on a worldwide basis for a flat fee, for use in all media "now known or hereafter devised." Licenses for the use of sound recordings and musical compositions in DVDs and video games are usually done on a "buyout" basis, meaning that a flat fee is paid for the use in a particular media, worldwide, for the life of the copyright. However, certain music-intensive video games may pay a per unit royalty, especially if the song is a popular one.

Mechanical Licenses

A sound recording is generally owned or controlled by a record company by means of an exclusive recording or license agreement with the artist, which will include the right to make and distribute phonorecords (CDs, vinyl records, cassette tapes, etc.), and to license the rights in the sound recording to third parties. If one wishes to use pre-recorded music on a physical device, a master use license will need to be obtained from the record company. Likewise, whenever a musical composition is embodied in a physical form, such as a compact disc, DVD, video game, toy or greeting card, a "mechanical license" must be obtained from the music publisher.

The fee for the mechanical license is either negotiated between the music publisher and the licensee, or is the subject of a "statutory rate." Statutory rates are determined through lengthy arbitration proceedings before the

Copyright Royalty Board ("CRB"). If a musical composition has been previously published, any person can obtain a "compulsory license" to use it by following the procedures set out in Section 115 of the Copyright Act, which include paying the statutory rate, rendering monthly accountings and obtaining the license before distribution of the record.

In practice, most mechanical licenses are consensual although licensees will generally follow the established statutory rates. Recently, however, certain digital music services that use vast numbers of titles, for example the Slacker personalized Internet radio service, have started issuing notices of compulsory licenses as a means of avoiding the delay of obtaining consensual licenses from a myriad of publishers.

Currently, statutory rates are in effect for the use of musical compositions in phonorecords, digital downloads (digital phonorecord deliveries or "DPD's"), and ringtones. The current statutory rate for the use of a musical composition on a CD is 9.1 cents for works of five minutes or less in duration and 1.75 cents for each minute or fraction thereof over five minutes payable on a per unit basis for each record sold. The statutory rate for DPD's is currently the same as for physical phonorecords. The rate for ringtones was set by the CRB at 24 cents in October of 2008, to the delight of publishers and the consternation of record companies. This rate is currently under appeal by the Recording Industry Association of America ("RIAA").

The CRB also set statutory rates for "interactive streams" and "limited downloads," establishing a complex formula based on the licensee's revenues, other public performance royalties earned and the number of subscribers to the music service. A limited download is a digital music file that is restricted, either by the period of time it resides on the user's computer or by the number of times the song can be played before it times out. Interactive streaming is the transmission of a digital music file to be listened to on demand by the end-user.

In order to request a mechanical license, one must contact the music publisher who controls the song. The Harry Fox Agency ("HFA") issues mechanical licenses on behalf of a large number of publishers including some of the major ones. However, not all publishers are affiliated with HFA, so it may be necessary to contact the publisher directly.

Public Performance Licenses

Playing music on the radio, on television or in any public arena involves the public performance of a musical composition and a sound recording. If a work is publicly performed, one or more licenses may be required depending on the particular use and the media involved. The musical composition component of the performance is licensed from one of three performing rights organizations ("PRO's") for the performance in the United States: American Society of Composers, Authors and Publishers (ASCAP), Broadcast Music, Inc. (BMI) and SESAC. Each of the three PRO's issues public performance licenses and collects license fees on behalf of its membership which consists of music publishers and songwriters.

Royalties generated by public performances outside of the United States are collected by the foreign performing rights organization in the country where the music is performed. Most of these organizations have reciprocal collection agreements with ASCAP, BMI and SESAC. Any radio station that plays music from the ASCAP, BMI and SESAC repertoire must have a public performance license with each of the three PRO's.

Likewise, television stations, concert arenas and other commercial establishments that play music must have public performance licenses unless they fall under an applicable exemption. Radio stations and television networks enter into blanket licenses for public performances of musical compositions with each of the PROs.

The annual fees paid to the PRO's for public performances of music are often the subject of contentious negotiations, although in some cases the license is negotiated on a collective basis. For example, radio station licenses with ASCAP are negotiated by the All Industry Radio Music License Committee.

Other uses of music that are considered to be "public performances" include the streaming of music on the internet, playing of "hold" music on the telephone, and the use of music in Broadway shows and dramatic musical performances. The terms of the ASCAP,

BMI and SESAC licenses only apply to non-dramatic musical performances. The use of music for shows and musicals, known as "grand rights," must be licensed directly from the music publisher. The issue of whether a digital download generates a performance royalty as well as a mechanical royalty is currently the subject of considerable debate, with the PRO's taking the position that a digital download, including a ringtone, is a public performance.

A number of exemptions apply to the requirement to pay public performance royalties. The Fairness in Music Licensing Act of 1998 exempts small commercial establishments such as restaurants from the requirement to pay public performance royalties for musical compositions. In order to qualify for the exemption, a restaurant must have a total of no more than 3,750 gross feet of space (excluding space used for customer parking) and must transmit music that is already covered by a license with ASCAP, BMI and/or SESAC (for example, music from a radio station or commercial music service that has obtained a license).

Other exemptions exist for the performance of music in record stores and other commercial establishments for the purpose of promoting retail sales of records, performances for use in instructional activities in the classroom by non-profit educational institutions, at social functions organized by non-profit fraternal organizations for charitable purposes, and performance of music in movie theaters.

Historically, radio stations in the U.S. have been exempted from paying public performance royalties for sound recordings, the rational being that radio stations help to promote the sale of records. Lately the precipitous decline in sales of CDs has called this exemption into question. The recording industry has been lobbying heavily for the establishment of a public performance royalty for sound recordings on the radio, which is paid in many other countries, although it has met with stiff resistance from the National Association of Broadcasters and other groups.

A limited right to receive royalties for the public performance of sound recordings was established with the passage of the Digital Performance Right in Sound Recordings Act of 1995. The digital performance right applies only to "digital audio transmissions" by webcasters, digital music services such as DMX and Music Choice, and satellite radio services, i.e., Sirius, XM radio. Terrestrial radio and television broadcasters who broadcast over the air (even using digital signals) remain exempt from the requirement to pay public performance royalties for sound recordings, as do companies like Musak that play elevator music and "hold" music.

Digital Royalties for sound recordings are established through rate proceedings before the CRB and are collected through SoundExchange, a non-profit organization previously affiliated with the RIAA. In July of this year, SoundExchange entered into settlement agreements independently of the CRB, establishing rates for four different types of webcasting entities, including non-commercial radio stations.

Statutory rates for the digital performance of sound recordings are only applicable to "non-interactive" webcasts, i.e., they do not include "on-demand" streams of music. The question of what is "interactive" is not an easy one and depends on the specifics of how the music is provided to the end-user. A decision was issued in August of this year by the U.S. Court of Appeals for the 2nd Circuit in the *Launchcast* case. In this case, the court found that because users of the service could build customized radio stations based on their music preferences but could not play individual tracks on demand, the service was not interactive and therefore, the statutory rates applied to the use of the recordings.

Copyright Infringement

With the advent of new and different uses of music, from the garage band selling its music online, to the game show contestant whose performance is played on YouTube, to proliferation of webcasts, podcasts and subscription music services, it is essential to keep abreast of the changing legal terrain. While music is increasingly available and the cost of using it is generally going down, the damages for even a single act of copyright infringement can be substantial.

The damages for infringement of a musical work that is protected by a registered U.S. copyright can include statutory damages of up to $150,000 plus attorney's fees. If ever in need of a music license, it is best to use a reputable music attorney or music clearance company who is familiar with the licensing process and the fees normally charged for different types of uses.

Dorothy Blake Richardson, J.D., M.B.A., *is an experienced entertainment attorney whose practice includes the preparation and negotiation of agreements for the music, film, television and related industries, the counseling of clients to obtain copyright and trademark protection, the licensing of intellectual property content, company formation, due diligence and negotiation of purchase and sale of intellectual property assets. She can be reached at drichardson@dbrlaw.net or (818) 992-2926.*

MCLE ARTICLE AND SELF-ASSESSMENT TEST

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Protecting Film Industry Clients

When the Only Certainty is Uncertainty

By Peter Levitan

THE OFTEN-QUOTED PRONOUNCEMENT BY noted screenwriter William Goldman about Hollywood has never been truer: "Nobody knows anything." This axiom is often taken (erroneously) to mean that Hollywood executives are stupid, but it in fact reflects Goldman's belief and insight that prior to a film's release, the film industry has no real idea how well it will perform.

The perennial key risk in the film industry has long been that even a film that has taken all the conventional steps for success (A-list director and stars, excellent screenplay, timely and engaging subject and genre) can still be a dismal failure. There are also other risks along the way of developing, producing and distributing a film. Just to name a few, the producer, director or star can become incapacitated, severe weather conditions can disrupt filming, or a prolonged labor strike can delay production indefinitely.

To compound such multiple risk factors, the business climate and practices in the film industry are constantly changing, and the balance of power is frequently shifting and audience tastes are constantly fluctuating. As Heraclitus stated, "All is flux; nothing stays still." In the film industry, the only certainty is *uncertainty*. Arthur de Vany, Professor Emeritus of Economics at the University of California, Irvine, who has studied film performance statistics for over twenty years, concluded that the performance predictability of any one film is so low as to be virtually zero.

Risk Management

In formal risk management theory, there are four primary strategies for addressing risk: transferring the risk to another party; reducing the negative effect of the risk (mitigation); avoiding the risk; and accepting the consequences of a particular risk. Since avoiding risk consists of simply not entering into a risky transaction, and accepting a risk consists of simply proceeding with such a transaction, this article describes the primary tools for the more complex strategies of mitigating and transferring risk in motion picture transactions. Furthermore, since some of the tools used to mitigate risk in the film industry are common to all fields (e.g., loan covenants, due diligence, formula for dividing venture profits, and proper valuation of loan collateral), this article only describes risk mitigation and transfer tools as specifically adapted to film production and financing.

Diversification

Diversification, a basic risk mitigation strategy, is used in the film industry in three primary ways. This strategy reduces portfolio risk by combining a variety of investments (e.g., stocks, bonds and real estate) or products (e.g., feature films, TV programming, TV stations, cable TV services, books, newspapers, magazines, music and theme parks) which are unlikely to all move in the same direction at the same time.

The first application of diversification in that film industry is that all of the major studios have become parts of large entertainment conglomerates offering all sorts of leisure and entertainment products, content and services. Since the conglomerates' components move up and down in value at different times and at different rates, they show less volatility than the stand-alone studios did, and more consistent performance under a wide range of economic conditions.

Another form of risk diversification is that a studio or large independent production or distribution company produces and/or distributes up to 20 films each year. Thus, it's relying not on the success of a single film, but a number of films, so its economic well-being is generally not as volatile.

But the primary use of diversification in the film industry is slate financing, third-party financiers financing a number of films (or a studio's "slate") on a pooled basis rather than financing individual films on a project by project basis. Investment risk for such film slate financing is evaluated by a technique called a "Monte Carlo analysis."

The actual historical performance of all of the studio's films over the several most recent years is batched in thousands of possible randomly selected combinations in

which a group of those films could have been released in sequence. From these calculations, the financier can determine the minimum number of films that need to be in a slate in order to minimize volatility and for the slate's results to be within a reasonably predictable range. Some film funds have concluded that the minimum number of films required for a predictable slate is as high as twenty, and some have concluded that it's as low as three.

Although slate financing is a staple of film financing, its results have proven highly erratic and not always satisfactory in recent years. Several hedge funds found that, notwithstanding all the due diligence and analysis they conducted, their slate deals with major studios yielded disappointing results. In several instances, those studios renegotiated their deals with their hedge fund partners, realizing that the hedge funds could become long-term financing partners if treated properly.

Leverage

Another conventional risk mitigation tool taken from general business financing is leverage – the use of debt financing or funding from any other source to minimize the risk and magnify the reward of an investment.

There are two primary sources for additional film funding that can help leverage an investor's, studio's or production company's investment. The first is an advance or "pre-sale" from a distributor who is licensed distribution rights in the film for a particular territory and media before the film commences shooting. Some distribution licenses, but not all, call for the distributor to pay an advance on distribution fees when the film is completed and delivered. Such an advance serves as part of the film's financing package, thereby mitigating the investor's risk and magnifying the potential return.

The second source of funding that can leverage the equity investment in a film is so-called "soft money." This is funding from any of the film incentive programs offered by numerous U.S. states as well as foreign countries to shoot all or a portion of a film in the host jurisdiction.

These incentives take many forms. In descending order of preference, they are: direct subsidies; tax rebates (which are usually the easiest form of tax incentive to administer); transferable tax credits (which are usually based on the amount spent in the host country, but are sometimes based on the film's entire production cost); non-transferable tax credits (which are usually only useful to the local film community in the host jurisdiction, since the production company earning the credit must itself be a taxpayer in the jurisdiction); a flat tax deduction; and lotteries (since only a handful of the numerous applicants are selected to receive lottery funds).

At present, "soft money" film incentive programs are offered by over 40 U.S. states and numerous foreign countries. But individual program guidelines change frequently, so they need to be checked before attempting to access them.

Intellectual Property Rights

The copyright and trademarks associated with a film or television project also figure into a financing transaction. Some financing transactions require the financier to acquire the project's copyright and trademark rights, while others do not.

A lender should be sure to include such intangible intellectual property in the collateral package securing the loan. The legal and economic rights subsumed within a copyright go well beyond the exclusive right to exploit the work itself (to reproduce it, to distribute copies or recordings of it to the public, and to perform or display it publicly[1]), to include the valuable right to authorize derivative works based upon the copyrighted work.

A "derivative work" is defined as a work based on one or more preexisting works, such as a musical arrangement, dramatization or fictionalization.[2] Thus, a copyright owner has the exclusive right to authorize the full panoply of derivative works that could be created based on his or her work: a film, a stage play or musical, a television production, a videogame, a sequel, prequel or remake, and even a theme park ride. All of this makes the copyright itself a potentially lucrative asset that a financier should be sure to capture in its collateral package as a hedge against default by the producer-borrower.

But there are pitfalls in perfecting a security interest in intellectual property. Specifically, copyright is governed by a bifurcated regime. Security interests in the intangible copyright or any of its legal components (e.g., reproduction, distribution or performance rights or proceeds therefrom) are governed by the federal Copyright Act, while all other forms of collateral (e.g., physical items such as sets, props, costumes, physical film elements or copies, DVDs, etc.) are governed by the applicable state's Uniform Commercial Code.

Accordingly, the sole method of perfecting a security interest in a copyright is by filing a document (referred to as a copyright mortgage) with the U.S. Copyright Office.[3] General practitioners unfamiliar with this area occasionally file the customary UCC filings but remain unaware of the need for the critical Copyright Office filing, rendering the client an unsecured creditor with respect to the most valuable of the collateral.

Securities Compliance

When a film is financed through a public offering, the attorney must of course assure that there is full compliance with both federal and state securities laws.[4] Even in a private placement, there must be compliance with such statutes' antifraud provisions.[5] These requirements result in the extensive disclosures, disclaimers and discussion of risk factors seen in prospectuses and private placements.

Nowadays many film and theatrical producers solicit financing on the internet, via an internet forum, chat room or social network such as LinkedIn or FaceBook, but don't register the offering. Any such outright solicitation for investors constitutes a public offering of a security and the advertising of such offer within the meaning of the securities statutes. This poses two problems. First, it violates the requirement of registration of all public offerings. Second, the public advertisement precludes the offeror from qualifying for any of the Regulation D[6] exemptions for private offerings, which ordinarily would be the preferable method of raising financing without having to register the offering.

But the disclosures, disclaimers and risk factor discussions in a prospectus or private placement memorandum do more than just assure compliance with securities statutes. They also offer, to some extent, insulation from lawsuits by litigious investors if and when the film fails to become the next "Titanic" or "Blair Witch Project". For example, the plaintiffs in *Eckstein v. Balcor Film Investors*[7] included not only investors who had read the offering's prospectus, but also investors who had not bothered to read the prospectus.

The theory offered by this second group of investors was fraud on the market: that had the prospectus properly disclosed that offeror's primary distributor – from whom it derived most of its revenue – was disappointed by the poor quality of its earlier films and had already filed suit to withdraw as the offeror's distributor, the offering would not have been successful; and that they purchased their limited partnership units in reliance on this omission of a material fact that enabled the offering to proceed at all. Consequently, offeror's counsel should err on the side of overabundant thoroughness when disclosing every possible risk entailed in a film investment.

Standalone Entity

Another standard film industry practice is to isolate each film project and all assets and contract rights relating to it in a separate single-purpose entity, rather than to leave them commingled with the company's other projects and assets in the entity used for general operations. Leaving a film project commingled with the company's other assets runs the risk that a catastrophic liability occurring in connection with one film (such as a wrongful death award arising from gross negligence) might leave all the company's assets and film projects exposed to satisfy the award.

Thus, prior to commencing any activity on a film project, the film company should create a bankruptcy remote vehicle (BRV), a single-purpose entity to hold all the rights to that film, contract with third parties and produce the film. Once the film has been in distribution for about six months, if no claims of copyright infringement, defamation or invasion of the right of publicity or privacy have been asserted, it's generally considered safe to assign rights in the completed film back to the general operating company.

Completion Guaranty

As in some other industries, a completion guaranty (or completion bond, as it is often called) is a guarantee issued by an insurer (called the completion guarantor or "the bond company") in favor of the lender that is lending the production funds, guaranteeing satisfactory completion and delivery of the film by the agreed upon deadline without requiring the lender to advance any further funds, with the insurer bearing any cost overruns.

The major studios are self-bonding, i.e., they accept the risk of production cost overruns rather than pay a fee to a third-party insurer to bear that risk. But independent production companies typically rely on lenders to furnish funds during the production period, since the payments that will pay off the loan (e.g., advances to be paid by distributors) won't be paid until the film's completion and delivery. Such production lenders require a completion guaranty in order to shift the very substantial risk of cost overruns and even abandonment of the film to a third party.

The completion guarantor's obligations to the production lender under the completion guaranty are that the guarantor will either, at its election, (1) bear the cost of any production cost overruns; (2) take over the production of the film, if required to complete and deliver it to the distributor on time in order to trigger the distributor's obligation to pay the contractual distribution advance to the lender; or (3) abandon the film if cost containment is unlikely and it's early enough during shooting, and reimburse the lender for whatever money it has already advanced to the production company. Given the substantial likelihood of cost overruns being incurred, and the consequences that could result, it is critical that any independent production company or production lender see that a standard completion guaranty is in place, and that it be reviewed and negotiated by counsel experienced in this area.

Other Insurance

As an essential tool for risk transfer, there is a standard production insurance package that producers and financiers alike should assure is in place for any film or television production. Such coverage includes: errors and omissions (E&O) insurance, which covers any copyright infringement, defamation or invasion of rights of privacy or publicity claims; casualty liability; property damage liability; negative (covering the loss, damage or destruction of the completed film master negative); faulty camera (covering any malfunction by camera equipment that impedes shooting); faulty stock (covering faulty film stock); vehicle (covering any vehicles purchased or rented for either on-screen action or for transporting cast and crew); aircraft and/or watercraft, if applicable; props, sets and wardrobe; and the all-important cast insurance.

Cast insurance covers any losses due to a cast member's inability to perform due to accident, illness or death. For an "essential" actor whose appearance in the completed film is required to trigger the distributor's obligation to pay its advance, insurers will require a medical examination before undertaking to insure any costs caused by that actor's non-performance. Individuals known to be serious habitual drug users may be required to take a drug test.

Budgeting – Preparation, Contingency and Final Approvals

A film's production budget also offers opportunities for mitigating risk.

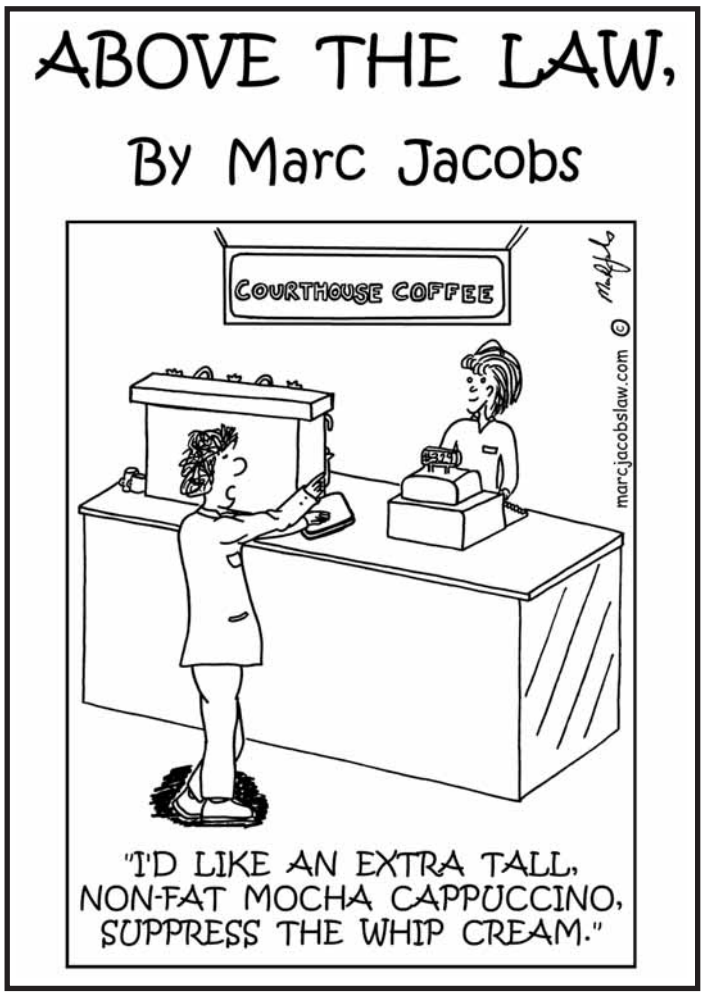
Budget preparation. Preparing a film production budget is complex, highly specialized work. It requires knowledge of many technical variables (e.g., union requirements, rates and fringe costs in the locations where the film will be shot, edited and scored; costs of the myriad supplies and equipment rentals in such locations; applicable office and vehicle rental, insurance and catering costs; etc).

Unless the budget is prepared by an expert who specializes in this work, it could either underestimate or overestimate production costs. Underestimating will likely

result in running out of funding before production is completed. Overestimating will result in a bloated budget that no completion guarantor will bond, since the guarantor would become liable for costs that are not absolutely necessary to complete the film. Therefore, it's critical that the person preparing the budget be experienced and knowledgeable.

Budget contingency. Another risk is that no matter how careful and accurate the production budget, budgeted costs will inevitably fluctuate by the time shooting actually begins. The industry practice is to mitigate this risk by including a contingency line item in the budget equal to ten percent of all the actual direct production expenses. This is not simply a risk mitigation tool; any production lender or completion guarantor will require it to be included in the film's budget.

Final approvals. Another industry practice to address production cost fluctuations as well as assure accountability is to revise the budget immediately prior to commencing shooting. This assures that this "final" budget will reflect the most recent cost information (including any changes in locations, the finally negotiated talent fees, etc.). More important, all relevant parties must sign off on the final budget so that this becomes the budget to which the production will be held (notwithstanding cost overruns or underages arising in the normal course of production).



The parties signing the final approved budget include the production company, the production lender, the completion guarantor and, under certain circumstances, the distributor. Without this mechanism, the parties' respective obligations to each other and the film's cost controls might be compromised.

Cross-Collateralization

Although the term means something different in other fields, as used in entertainment financing "cross-collateralization" means an arrangement by which the costs and revenues of several projects (films, programs or recordings) are pooled together to calculate whether the projects being financed have turned a profit on an aggregate pooled basis, rather than evaluating the profitability of each project separately.

The usual effect of cross-collateralization is that losses on the unsuccessful projects in the pool cancel out would-be profits on any successful project in the pool. Thus cross-collateralization disadvantages those to whom accountings will be due (e.g., investors and profit participants such as producers or actors, etc.) and advantages those who will be rendering accountings to others (such as distributors). In some instances, a party (such as a production company) may play both roles, receiving accountings from one third-party (e.g., the distributor) and rendering accountings to others (e.g., profit participants).

In short, "Risky Business" isn't just the 1983 film that launched Tom Cruise's career. It's the very essence of an industry that attracts many, and requires of attorneys and clients alike astute and judicious risk management if they're to have a fighting chance to obtain the possible rewards that attracted them in the first place.

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[1] 17 U.S.C.A. §106.
[2] 17 U.S.C.A. §101.
[3] In re Peregrine Entertainment, Ltd., 116 B.R. 194; 16 U.S.P.Q.2D (BNA) 1017; Copy. L. Rep. (CCH) ¶26,616; see also In re Avalon Software Inc., 209 B.R. 517 (Bkcy D. Ariz. 1997); but see In re World Auxiliary Power Co. (Bkcy N.D.Cal. 1999) (U.S. Copyright Office filings only apply to registered copyrights and not to unregistered copyrights, which remain subject to the UCC).
[4] E.g., 15 U.S.C.A. §§77a et seq., 78 et seq.
[5] E.g., 15 U.S.C.A. §§77q, 78j; 17 CFR § 240.10b-5 (Rule 10b-5 of the Securities Exchange Act of 1934).
[6] 17 CFR §§ 230.501 et seq.
[7] 8 F.3d 1121, 1993 U.S. App. LEXIS 21534, Fed Sec. L. Rep. (CCH), ¶97,712 (7th Cir. 1993).

MCLE Test No. 15

This self-study activity has been approved for Minimum Continuing Legal Education (MCLE) credit by the San Fernando Valley Bar Association (SFVBA) in the amount of 1 hour. SFVBA certifies that this activity conforms to the standards for approved education activities prescribed by the rules and regulations of the State Bar of California governing minimum continuing legal education.

1. Risk circumvention is one of the four primary strategies of risk management.
True
False

2. Risk mitigation by means of diversification does not exist in the film industry.
True
False

3. Film funds analyze investment risk via an analytical technique called a "Monaco analysis".
True
False

4. Slate financing deals always yield better results than single-picture financings.
True
False

5. In some instances, hedge funds' film deals with film studios have been renegotiated.
True
False

6. Distribution advances are one source for leveraging a film investment.
True
False

7. For soft money financing, non-transferable tax credits are preferable to transferable tax credits.
True
False

8. A financing transaction always requires transferring the film's copyright to the financier.
True
False

9. Perfection of a security interest in film collateral involves a bifurcated statutory regime.
True
False

10. Sequels, remakes, theme park rides and musical arrangements are all examples of derivative works.
True
False

11. Because films are given such wide public exhibition, equity offerings for them must comply with all the securities regulations for public offerings.
True
False

12. With the advent of the internet and social networks such as FaceBook and LinkedIn, they have proven appropriate channels for raising funds for the lowest-budget independent films.
True
False

13. There are distinct advantages in disclosing negative information in insurance questionnaires.
True
False

14. A standard film industry practice is to use bankruptcy remote vehicles.
True
False

15. Both underestimating and overestimating pose problems when preparing a film production budget.
True
False

16. A film's stars must sign its final approved budget to indicate their agreement to be bound by it.
True
False

17. Errors and omissions insurance covers any claims of copyright infringement, defamation or invasion of rights of privacy or publicity against a film.
True
False

18. The First Amendment prohibits producers or lenders from requiring actors suspected of drug abuse to submit to drug testing.
True
False

19. Though highly speculative, film financings can qualify for the exemption offered by Regulation D of the federal Securities Act of 1933 if they meet the stated criteria.
True
False

20. Cross-collateralization favors the party rendering an accounting, not the party receiving it.
True
False

MCLE Answer Sheet No. 15

INSTRUCTIONS:
1. **Accurately complete this form.**
2. **Study the MCLE article in this issue.**
3. **Answer the test questions by marking the appropriate boxes below.**
4. **Mail this form and the $15 testing fee for SFVBA members (or $25 for non-SFVBA members) to:**
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   21250 Califa Street, Suite 113
   Woodland Hills, CA 91367

METHOD OF PAYMENT:
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5. **Make a copy of this completed form for your records.**
6. **Correct answers and a CLE certificate will be mailed to you within 2 weeks. If you have any questions, please contact our office at (818) 227-0490, ext. 105.**

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ANSWERS:
Mark your answers by checking the appropriate box. Each question only has one answer.

1.	❒ **True**	❒ **False**
2.	❒ **True**	❒ **False**
3.	❒ **True**	❒ **False**
4.	❒ **True**	❒ **False**
5.	❒ **True**	❒ **False**
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9.	❒ **True**	❒ **False**
10.	❒ **True**	❒ **False**
11.	❒ **True**	❒ **False**
12.	❒ **True**	❒ **False**
13.	❒ **True**	❒ **False**
14.	❒ **True**	❒ **False**
15.	❒ **True**	❒ **False**
16.	❒ **True**	❒ **False**
17.	❒ **True**	❒ **False**
18.	❒ **True**	❒ **False**
19.	❒ **True**	❒ **False**
20.	❒ **True**	❒ **False**

Solving Showbiz Puzzles

Med-Arb in the Entertainment Industry

By Katherine A. Mills

MUCH HAS BEEN SAID about the dangers of using Mediation-Arbitration ("Med-Arb") as a dispute resolution method. A lack of constitutional due process and fairness, insecurities regarding the fragility of the Med-Arb award, as well as concerns over the potential chilling effect on communications during negotiations, are only some of the criticisms.

However, it has also been suggested that, at least in the entertainment industry, this peculiar ADR hybrid might be more effective in meeting the needs of its participants than other methods. The entertainment industry's unique persona inherently stimulates the exploration of innovative conflict resolution processes, sometimes directed more towards rapid finality, than exacting traditional legal rationale; the Med-Arb hybrid, in combining the process of mediation and arbitration into one coordinated effort, offers the parties a private, inexpensive conclusion to the dispute, allowing them to move on with their business.

The Nature of the Beast

As recognized by many, the entertainment industry (the "industry") is exceptional not only because of its insular culture, but also because of its broad range of legal needs.

Not only does the industry incorporate a variety of substantive legal subject matter into its business operations, but the needs for dispute resolution range from immediate to more protracted forms of relief. Injunctive relief might be critical to moving a project forward or enforcing a cease and desist; while the longer form of litigation might be necessary to reimburse a party for damages sustained, create a deterrent, or establish precedents to determine the course of business operations.

Where the same goals can be achieved through more informal methods of dispute resolution, relationships and projects can be saved, and obstructions to streams of revenue removed. This is why use of ADR has become a well-accepted method of addressing conflict in the industry. ADR's ability to gracefully respond to the broad range of needs of its participants, makes it a perfect fit; and Med-Arb, while pushing the envelope, may be the most adjustable of all of these processes.

Inside Med-Arb

What is it? With the expanding use of ADR, seminal processes, for example mediation and arbitration, have evolved into numerous offshoots and hybrids providing a method to address every possible conflict. One of these hybrid processes is Med-Arb.

By combining mediation with arbitration, the parties first have an opportunity to mediate their conflict and resolve it on their own terms. If the parties are unsuccessful, the mediator changes hats and becomes the arbitrator, rendering a unilateral, final, binding decision. Although some Med-Arb processes require, or provide for, different individuals to perform as mediator and arbitrator, the scheme that appears to be most controversial is the one where the same neutral performs both functions.

Is it just the name? Gerald Phillips ("Phillips") suggests that the problem with Med-Arb may merely be limited to its name. (Phillips is a full-time neutral, and adjunct professor at the Straus Institute for Dispute Resolution, Pepperdine University School of Law.) Phillips is also a staunch advocate for Med-Arb, particularly for use in the industry. Phillips suggests that it may be the term that causes some of the problem, and that the process might be less contentious with a different name; "same-neutral med-arb" and "transitional arbitration" are some of those he suggests (Gerald F. Phillips, "It's More than Just 'Med-Arb': The Case for 'Transitional Arbitration'" CPR, Vol. 23, No. 9 October 2005).

Further, Phillips asserts that mediation purists and cautious litigators might be more apt to accept the Med-Arb if it was marketed under a different name, and categorized as a unique process outside the realm of arbitration and mediation. However, he contends Med-Arb continues to be a popular alternative to the clients he assists in the entertainment industry.

The dangers of using Med-Arb. As the most criticized method of commercial ADR methods, Med-Arb's disapproval rating tends to score highest when considering the behavioral and procedural aspects of the process.

Unease over potential lost opportunities for creative problem-solving in the phase of Med-Arb stems from the idea that there might be a type of chilling effect on communication if participants are aware that their mediator may later become the arbitrator – that they may be less likely to be open and candid, and as a result lose the opportunity for collaborative problem-solving.

Alan L. Limbury, in his paper "Making Med-Arb Work", (presented to the NSW Chapter of The Institute of Arbitrators and Mediators Australia, Sydney, August 3, 2005) cited concerns over the loss of an ability to "walk away" – that Med-Arb participants may be coerced into agreements without having the freedom to bargain freely for the terms. Will participants feel free to accept or reject the mediator's suggestions when they know the same neutral will be the arbitrator? If Med-Arb eliminates the opportunity to "walk-away", can one of the parties now manipulate the process by forcing arbitration if they fail to bargain in good faith? Does Med-Arb provide more opportunity for one of the parties to exploit the other?

Since all negotiations are disclosed in the presence of the same neutral who both mediates and arbitrates the matter, the perception is that there are no "without prejudice" settlement discussions. Therefore, unless the mediation process is confined to only those matters which would be disclosed during the adjudication phase, the neutral's transition from mediator to arbitrator taints the integrity of the process, in that settlement discussions may become evidence considered during arbitration deliberation.

Ex parte communications also raise concerns because unless the parties choose a "non-caucus" approach (which they are free to do), this unsworn evidence, that one of the parties has not had an opportunity to respond to, and may never know about, like the joint settlement discussions, could be used by the neutral in the arbitration deliberation. This factor, in addition to questions of partiality, bias and neutrality, gives rise to allegations that Med-Arb lacks constitutional due process and fairness, leaving the Med-Arb award vulnerable to being set aside. (For more on this, see John T. Blankenship, "Developing your ADR attitude Med-Arb, a Template for Adaptive ADR", Journal TBA Archives 2006 11 ("Blankenship").

Subduing concerns over Med-Arb. Despite concerns over the viability of Med-Arb, there appear to be those who believe the process can be cured. Regarding the chilling effect on communication during Med-Arb, John Blankenship comments that there does not appear to be any empirical research supporting the belief that parties are more reluctant to be open in Med-Arb.

With respect to the opportunity to "walk away" and concerns of coercion, there are those who would argue that the freedom to contract provides parties with an opportunity to enter into these arrangements voluntarily, fully aware of the pros and cons of the process, being completely informed of the repercussions of failing to achieve a settlement before the arbitration phase.

Issues of ex parte communications could be addressed by recognizing that both judges and juries are regularly called upon to ignore information that they hear or see, (when it is ruled inadmissible after disclosure), and in fact jurisprudence has a history of accepting the concept that a trier of fact can ignore improper evidence where necessary to adjudicate a matter (Blankenship).

Blankenship states: "…while denial of due process is always a serious concern, … [it] can be overstated. It is easy to "create" alarm … about violations of confidentiality and due process ... [however,] T[t]he philosophy behind rules of evidence and …procedural safeguards is that these protections will aid in achieving a better result."

Therefore, if the parties who use Med-Arb are satisfied with the result, it could be worth examining whether procedural fairness requirements could be met with disclosure prior to the arbitration phase of Med-Arb through a contract specifying terms, including issues for determination, evidence admissible for deliberation, and defining exactly the jurisdiction within which the arbitrator can act.

Since arbitration legislation addresses issues of due process and fairness and leans towards public policy in favor of enforcement, supporting the public's right to contract out of the judicial system, fully informed contracting parties could sanctify the process by agreeing to the terms of the Med-Arb. A waiver of any matters that might fall outside of more conservative due process and fairness requirements, where parties knowingly forsake due process rights, and with intent, make the decision to enter into a Med-Arb agreement might cure any residual Med-Arb deficiencies.

Commenting with approval on the concept of the Med-Arb procedure, the Appeal Court in *Bowden v. Weickert* (Ohio Court of Appeals No. S-02-017, Trial Court No. 99-CV-395: June 20, 2003) stated that Med-Arb process when properly executed was an innovative and creative way to further the purpose of alternative dispute resolution. Although in that case there was no contract in writing documenting the waiver of certain due process rights, the court did leave open the possibility that a document properly advised upon and executed, could cure any allegations of impropriety in this type of process.

Based on the *Bowden* decision, it appears that such a waiver as discussed above could be found to be enforceable subject only to contract law defenses. While the waiver would need to pass scrutiny in California under CCP 1281 (written agreement to submit a matter to arbitration), and in particular, under

CCP 1281.9 (disclosure of concerns regarding neutrality and impartiality on the part of the neutral), if properly drafted, perhaps concerns regarding the Med-Arb process would be dispelled.

Use of Med-Arb in the Industry

Due to the intimacy and closeness within the industry, like conflicts within a family, many disputes are best addressed by negotiations with some give and take, "we will do it this way this time, but next time …."

Nevertheless, at times there will be a real conflict where the participants simply desire an expedient quiet resolution. The decision may likely then be assessed by doing a cost/benefit analysis; and having a decision, rather than having a particular decision may be more important due to both cost and time concerns.

The goals through mediation and other methods of dispute resolution in this industry may not be the same as others, and depending on the type of conflict, may not even be a good fit for certain matters that arise in industry. For example, employment and Guild matters have their own prescribed patterns for conflict resolution, and certain intellectual property matters may require clarification by the courts. However, in some cases, Med-Arb will afford its participants with ultimate control over the conflict resolution process.

Solutions to the Puzzle

While clearly there are options available to eliminate concerns over the use of Med-Arb as a viable dispute resolution process, the concerns may be less of an issue where the participants are fully informed, have equal bargaining power, and as in the case of the entertainment industry, are part of a discrete niche. (It is notable that Med-Arb is also popular with those in the construction industry.)

Freedom to contract and independence in choosing an appropriate method for conflict resolution are both factors that have been significant in encouraging the advancement of ADR generally; confidence and credibility in the process has been primarily derived from satisfaction with the results.

Therefore, if (as described by Phillips) participants in the entertainment industry continue to choose Med-Arb and they are satisfied with the results, it may not be long before we see Med-Arb as a regular option for dispute resolution in other areas, particularly where the participants are in discrete industries, are well-informed, have access to comprehensive legal advice, and are looking for speedy conclusions to specifically defined conflicts.

Katherine Neff-Mills *practices as an attorney and mediator in Beverly Hills. She has a law degree from the University of Victoria, an LLM in Entertainment & Media Law, and is a candidate for an LLM in Dispute Resolution with the Straus Institute, Pepperdine School of Law. She can be reached at (310) 281-1655 or kmills@beverlyhillsadr.com.*

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Calendar

Probate & Estate Planning Section
Choosing Trustees

OCTOBER 13
12:00 NOON
MONTEREY AT ENCINO RESTAURANT
ENCINO

Diedre Wachbrit Braverman will discuss the short and long-term implications of choosing a trustee.

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Small Firm & Sole Practitioner Section
Strengthen Your Bottom Line through Technology

OCTOBER 14
12:00 NOON
SFVBA CONFERENCE ROOM

William Wais will discuss how to inexpensively add client service capabilities to your small law firm through the use of readily available technology such as SAAS, Cloud Computing and Web 2.0 options. This seminar will help attorneys boost their bottom line without incurring great expense, a must in this current economic climate.

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Workers' Compensation Section
Almarez/Guzman and Ogilvie: Chapter Two

OCTOBER 21
12:00 NOON
MONTEREY AT ENCINO RESTAURANT
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Attorney Saul Allweiss will discuss the latest regarding this critical case.

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Intellectual Property, Entertainment & Internet Law Section
Hot I.P. Issues in Live Entertainment

OCTOBER 23
12:00 NOON
SFVBA CONFERENCE ROOM

Richard Munisteri, Vice President and Associate General Counsel of Live Nation, will discuss copyright and trademark issues relevant to the entertainment and concert arena.

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Family Law Section
Department 2 and Department L Updates

OCTOBER 26
5:30 PM
MONTEREY AT ENCINO RESTAURANT
ENCINO

Judge Marjorie Steinberg, Commissioner Lloyd Loomis and Judge R. Carlton Seaver will update attendees on their departments and discuss important do's and don'ts for their courtroom.

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Business Law, Real Property & Bankruptcy Section
Reviewing the '09 Woodland Hills Bankruptcy Judges' Opinions

OCTOBER 28
12:00 NOON
SFVBA CONFERENCE ROOM

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Litigation Section
Litigating Advertising and Marketing Claims: The "Organic" Movement and More

OCTOBER 29
6:00 PM
SFVBA CONFERENCE ROOM

Attorneys David Gurnick and Steve Holzer will discuss the intricacies of what you can and cannot claim in promoting a company's product and the litigation issues that might ensue.

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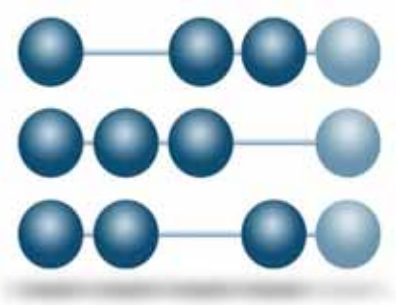

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