

ENTERTAINMENT AND MEDIA REPORT

***THE EVOLUTION OF
PROFIT PARTICIPATIONS /
NAVIGATING DISRUPTION IN THE
MOTION PICTURE AND TELEVISION INDUSTRY***



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WELCOME

Profit participations have always been a complex and emotional subject for talent, who wonder “Am I being paid what we agreed to contractually?” For studios, it is about “Am I paying too much, and are my stakeholders leaving money on the table?” Now, with new delivery methods like SVOD, non-traditional studios like Netflix and the proliferation of scripted television series and independent films, we have entered into a new era where profit participations and deal structuring are continually in flux.

In this year's whitepaper, we take a closer look at where we have been, where we are and where we are going with profit participations in a changing movie and television industry. We have assembled a truly knowledgeable group of industry experts to share their views on this important aspect of the business as they consider what future deal structures will entail. This is our 5th annual whitepaper, and I am extremely proud of the information you will find as you read on.

This paper is part of our continuing efforts to provide value to the entertainment community.



Ilan Haimoff
Partner and Entertainment and Media
Practice Leader,
Green Hasson Janks



**WE HAVE ENTERED INTO A NEW ERA
WHERE PROFIT PARTICIPATIONS AND DEAL
STRUCTURING ARE CONTINUALLY IN FLUX.**

Ilan Haimoff
Partner and Entertainment and Media Practice Leader,
Green Hasson Janks

EXECUTIVE SUMMARY

Introduction

There have been rapid changes in our motion picture and television industry, including how content is delivered to audiences through new media platforms and where content is consumed, driven by a huge increase in revenue generated overseas.

Ilan Haimoff, Partner and Entertainment and Media Practice Leader at Green Hasson Janks, translates this industry change into practical advice.

“If I were to hire a company to distribute my film, I would look at studios that have networks overseas,” Haimoff explains. “The multiples you can make with overseas sales through the international market via a major distributor makes it a one-stop shop rather than having to make territory-by-territory deals. Therefore, you just need to incur the expenses once and the revenue will be maximized.”

Of course, Netflix has disrupted the traditional model and has created a revolution. When they turn on the switch it reflects deals they have made all over the world.

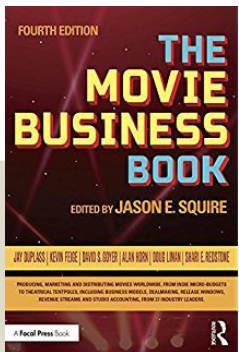
Haimoff expands. “Where you historically had generated income through Netflix, it would be available in the U.S., Canada and the U.K. in the past. Now Netflix, and even Amazon (Prime), have distribution in almost every country in the world. It is global and instantaneous via streaming.” This digital revolution may impact the different windows in the life cycle of motion pictures or television series and may require a response from studios, exhibitors and other stakeholders,” Haimoff added.

On the international front, Haimoff also notes that a title that sells in China could generate significant revenues. “For example, *Furious 7* made more than \$390 million of box office in China alone, which was more than the revenue generated in the U.S. and Canada combined!”

The overseas market goes beyond the movie theaters, as there is a real digital revolution that has occurred and is still occurring. There is a growing customer base overseas whose buying power is increasing. Haimoff alerts content creators to take this into account. “It matters,” Haimoff says. “When you create content, you had better think

about the overseas market. Pick the right distributor to maximize your potential share of the profits. This even applies to what we do at Green Hasson Janks when planning our profit participation audits. We need to make sure we have resources in place around the world through our HLB affiliation, plus we need to gear up for more travel.”

Green Hasson Janks is an independent member of HLB International, a worldwide organization of professional accounting firms and business advisors represented in over 100 countries. This affiliation provides access to the subject matter experts of other member firms in most major cities around the world. “This affiliation provides us and our clients many benefits,” Haimoff explains. “The biggest one for our Entertainment and Media Practice is that we can pursue participation audits almost anywhere.”



THE MOVIE BUSINESS BOOK

Green Hasson Janks Partner Ilan Haimoff authored a chapter on studio accounting and movie and television participation audits for the fourth edition of The Movie Business Book, a definitive sourcebook that covers financing, revenue streams, marketing, globalization and other current topics.

“I am honored to be asked to contribute my experience and knowledge to this book that is comprised of so many talented industry experts,” says Haimoff.

HIGHLIGHTS FROM THE 2017 GREEN HASSON JANKS ENTERTAINMENT SURVEY



63%

Percentage of respondents who think that PVOD will be an option for a mass audience in the next three years



46%

Percentage of respondents who prefer a large upfront payment in lieu of any backend participation in today's entertainment landscape



44%

Percentage of respondents who currently have productions with Chinese investment



58%

Percentage of respondents who think there will be more U.S./China co-productions to bypass the film quota system licensing



70%

Percentage of respondents who think that major studios will experiment with PVOD, but hold off releasing premium blockbuster content on PVOD



84%

Percentage of respondents who think that the likely price point at which a critical mass of viewers would consume PVOD offerings for feature films is less than \$30



49%

Percentage of respondents who say the most attractive M&A targets are those that own an extensive library of film and television products

“**WHEN YOU CREATE CONTENT, YOU HAD BETTER THINK ABOUT THE OVERSEAS MARKET.**”

Ilan Haimoff
Partner and Entertainment and Media Practice Leader,
Green Hasson Janks

**TOP INDUSTRY TRENDS
REPORTED BY OUR SUBJECT MATTER EXPERTS**

This year's subject matter experts weighed in on the trends that will affect the movie and television industry and profit participations in coming days, months and years.

Read on for more in-depth analyses of these and other trends.



TELEVISION

THE NATURE OF STAKEHOLDERS IS EXPANDING.

More content owners, financiers, co-distributors and others are making profit participations more complex.

MORE QUALITY TELEVISION CONTENT WILL BE CREATED.

With so many channels to choose from, audiences will gravitate toward higher quality content, regardless of where it resides.



TELEVISION PRODUCTION IS MORE IMPORTANT THAN EVER.

From a participation audit perspective, more and more Green Hasson Janks clients are involved in television. The number of pay cable channels has expanded enormously, and it appears the reason for this trend is that studios want to take less risk on films, which have higher risk of success.



LITIGATION



PROFIT PARTICIPANTS ARE TURNING TO LITIGATION MORE OFTEN.

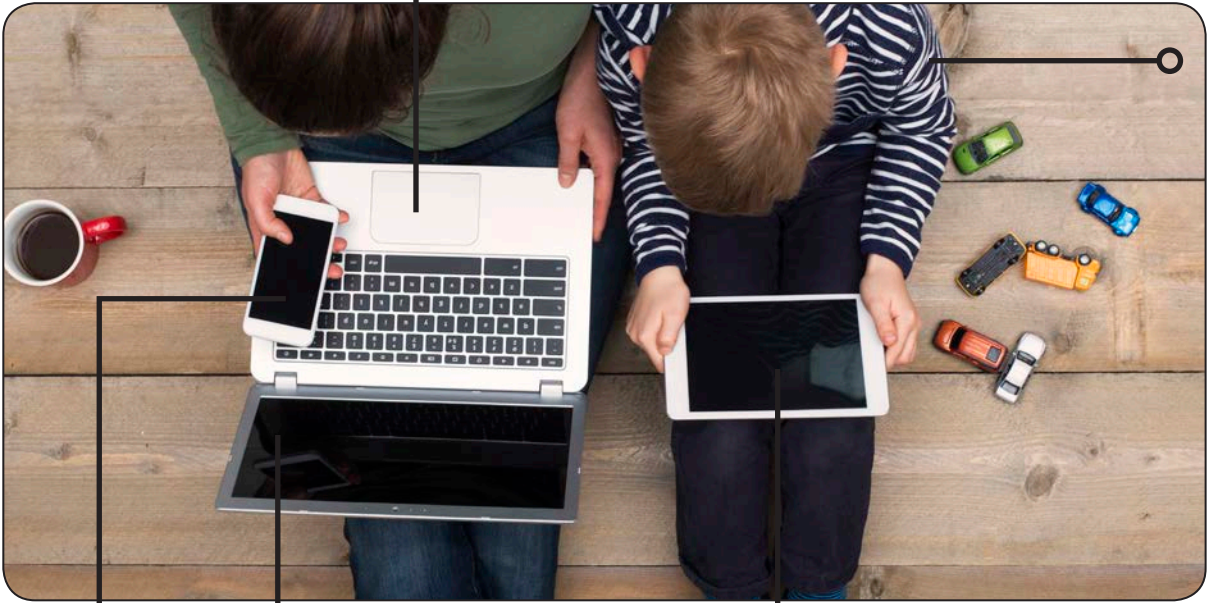
In the past, agencies with package commissions would do participations audits but mostly resolve claims/issues outside of litigation. However, this appears to be changing.



NEW MEDIA

NETFLIX, AMAZON AND APPLE ARE REPLACING TRADITIONAL BUYERS OF CONTENT.

Producers are attracted to the buy-out model with new media buyers, where they are paid their production costs plus a premium, with no backend. While this model has no potential for an upside, it avoids the risk of losing money.



EACH OF THE TRADITIONAL WINDOWS ARE BEING DISRUPTED BY THE LIKES OF NETFLIX.

Is subscription-based video on demand (SVOD) the alternative to, or replacement of, pay television and/or home video? Could SVOD become a single source of consumption for the so-called cord cutters?

THERE IS A SHIFT FROM HOME VIDEO TO SVOD.

The traditional home video business of DVDs and Blu-rays is plummeting. Meanwhile, revenues have dramatically increased for SVOD.

NETFLIX IS A NEW FORCE TO RECKON WITH.

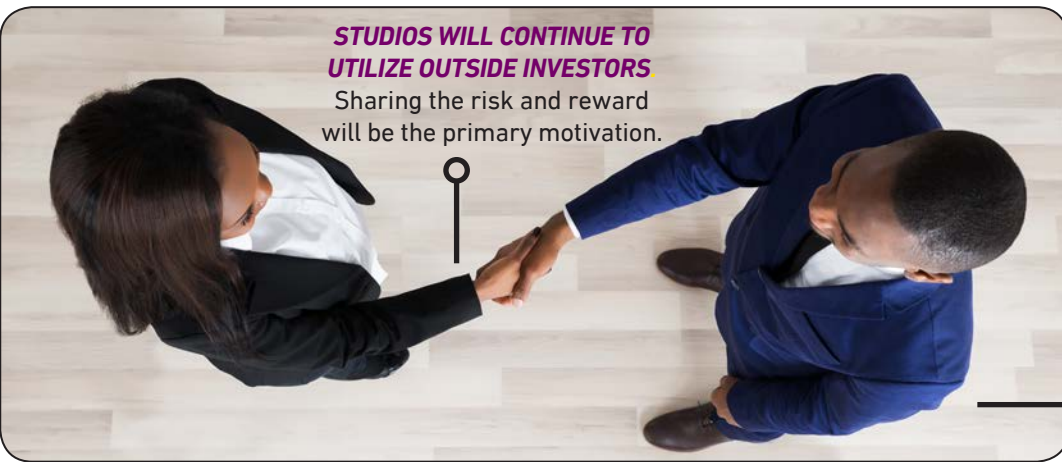
The studios suddenly began to realize that Netflix is a major competitor, which industry leaders have intimated may have been a catalyst for Disney recently announcing that it will be moving its content off of the Netflix platform by 2019 and creating a competing streaming service instead.

PREMIUM VOD (PVOD) IS STILL AN IMPORTANT TOPIC.

In the very near future, we will likely see an increase in PVOD explorations by conventional distributors and premium distributors like Amazon. This new digital platform will allow for early viewing at home, and at price points of up to \$50. A major concern of exhibitors is that PVOD may cannibalize theatrical distribution.



FINANCING



STUDIOS WILL CONTINUE TO UTILIZE OUTSIDE INVESTORS.

Sharing the risk and reward will be the primary motivation.

MERGERS AND ACQUISITIONS MAY ACCELERATE.

Verizon has indicated it has an interest in acquiring a studio or cable company. International buyers, with deep pockets, are also on the lookout. There is even chatter about Netflix being acquired by a major studio. All of these deals reflect the desire to vertically integrate, which is driving much of the M&A activity in Hollywood.

WHITEPAPER EXPERTS

PRINCIPAL CHAPTER AUTHORS

Green Hasson Janks is one of the premier profit participation audit firms in the world. Our professionals have extensive career experience with a wide range of global entertainment and media companies, including every major Hollywood studio and many smaller studios and independent producers. Our dedicated team has extensive participation forensic experience, providing services related to more than 83 of the top 100 domestic grossing live action films of all time through 2014, as well as a long list of top-rated television series.



ANITA WU
Principal,
Green Hasson Janks



ILAN HAIMOFF
Partner,
Green Hasson Janks



STEVE SILLS
Partner,
Green Hasson Janks



PETER KLASS
Senior Manager,
Green Hasson Janks



MICHAEL SIPPEL
Senior Manager,
Green Hasson Janks

WHITEPAPER EXPERTS

INTERNAL SUBJECT MATTER EXPERTS

Green Hasson Janks is an independent member of HLB International, a worldwide organization of professional accounting firms and business advisors represented in over 100 countries. “This affiliation provides us and our clients many benefits,” Haimoff explains. ‘The biggest one for our Entertainment and Media Practice is that we can pursue participation audits almost anywhere.”

BEN SHEPPARD
Principal,
Green Hasson Janks



TRACY LIANG
Supervising Senior,
Green Hasson Janks

EXTERNAL SUBJECT MATTER EXPERTS



CRAIG EMMANUEL
Partner, Vice-Chairman and
Chair of the Talent Practice,
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JOHN BERLINSKI
Partner and Chair of the
Entertainment Group,
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KEN HOLLOWAY
Senior Vice President
Finance and Controller,
Endgame Entertainment



DR. SEAGULL HAIYAN SONG
Senior Advisor, Hogan Lovells
Professor and Director,
Loyola Law School LA



THE HISTORY OF PARTICIPATIONS

PRINCIPAL CHAPTER AUTHOR



STEVE SILLS,
PARTNER,
GREEN HASSON JANKS

Green Hasson Janks Partner Steve Sills, a pioneer in the participations field, shares a story about the origination of participations.

It Started with Jimmy Stewart

Participations are generally thought to have begun with *Winchester '73* starring Jimmy Stewart. The studio could not afford him but paid him a percentage of the profits. The movie was a huge success and made money for Stewart and Universal Studios. Smart performers were getting pieces of their movies long before this, though, as far back as the 1930s and 1940s. Performers that were powerful enough had the leverage to do so.

Profit participation really took off in the 1970s and 1980s, according to Sills.

“Some smaller studios wanted to compete with the big boys and used percentage deals to get the talent on board,” Sills says. “There are some really well-publicized examples like Jack Nicholson on *Batman*, but there are many, many more. The inevitable result was legal challenges, many times centering on the studio’s definition of the ‘net profit’ from which the participations were paid. No matter how much money a film made, it seemed like it just broke even in the end. The irony is that stars still want net deals because it means they are moving up the food chain, even if they do not personally make money — it means they will be able to negotiate for more the next time.”

Key Shifts in the Profit Participation Landscape

Since Jimmy Stewart disrupted the process, there have been seismic shifts in profit participations. The change from digital media to new media is one part, but Steve Sills is more concerned with what has led to that and how studios are reacting.

“It is about vertical integration — studios buying businesses that are ancillary to theatrical distribution and how that affects participations,” Sills says. “For example, we audited a film at a studio and noticed that no sale had been made to Netflix for SVOD rights. The studio had given the rights away as part of a pay television arrangement with an affiliated company. The affiliate retains the Netflix revenue and since the studio receives no share of that revenue, none is reported to the profit participant. The studio still gets the money through the back door — their investment in the pay television entity. My concern is that more of these types of transactions will occur.”

Sills describes another case that changed the profit participation model.

“This case goes back to the 1970s, but it is still resonating today,” Sills explains. “Back then, there was a company called Magnetic Video that negotiated with 20th Century Fox to distribute Betamax tapes of Fox’s films. The cost to produce and market the tapes was approximately 60 percent of the total cost, making the net 40 percent. Of that 40 percent, Fox got 20 percent and Magnetic Video got 20 percent. That became the model, and the standard amount paid to participants became 20 percent. The 60 percent for making the videos eventually was reduced to 25% to 30% as the industry matured. For streaming services, the cost is negligible. So what happened to the 80 percent differential? The studios now just keep it and producers and content creators still get just the 20 percent, even though the costs are reduced or eliminated.”

Sills finds that the issue is with the studios interpreting the contract in their own best interest. His approach is to go in and look at the contract in a different way to claim additional compensation for his clients.

For **Anita Wu, a Principal at Green Hasson Janks** specializing in profit participations, television is a key focus.

“In the composition of our work, we are seeing a shift toward more television profit participations,” Wu explains. “In the past, most of the profit participation audits we performed were focused on the film side of our industry. Now, in the age of ‘Peak TV,’ which reflects the glut of television products out there, a long-running show can easily eclipse the financial success of a blockbuster film, or even a blockbuster film franchise. And talent representatives are fighting hard to secure the backend reward for their clients. Early on, it is difficult to tell how much these television profit participations will ultimately be worth, though. For it to be profitable, a television series

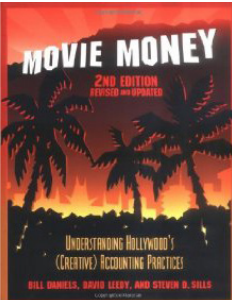
“**IT IS ABOUT VERTICAL INTEGRATION - STUDIOS BUYING BUSINESSES THAT ARE ANCILLARY TO THEATRICAL DISTRIBUTION.**”

Steve Sills
Partner,
Green Hasson Janks

would typically need to be in production for many years. Eighty to one hundred episodes used to be a good mark, but the better marker now is the number of seasons produced, even if a season is only seven episodes.”

Wu also thinks reality television is huge.

“The business model for reality television is very different than for scripted television” Wu expands. “For reality television, there is a level of unpredictability, and perhaps limited potential, for exploitation in the supplemental markets. However, reality television can thrive from other funding sources such as sponsorships, product integrations, format licenses and merchandising.”



**MOVIE MONEY:
UNDERSTANDING
HOLLYWOOD'S (CREATIVE)
ACCOUNTING PRACTICES**

Green Hasson Janks Partner Steve Sills is the co-author of the industry’s most important book on profit participation accounting. The book describes the distribution of a motion picture’s “profits,” which for most filmmakers is a murky, labyrinthine domain ruled by studio/distributor accountants and lawyers.

Movie Money unravels, demystifies and clearly explains the film industry’s unique, arcane and creative accounting practices. It examines a film’s various revenue-consuming components and presents numerous industry definitions of gross and net profits and the many ways in which these figures are calculated. It also provides in-depth discussions of various aspects of profit participation terminology, accounting practices, and deal practices along with chapters on audits, claims and negotiating tips and tricks. A third edition of *Movie Money* is currently in process.

CELEBRATING THE 10TH ANNIVERSARY OF THE PROFIT PARTICIPATION AUDIT DEPARTMENT AT GREEN HASSON JANKS



The first thing one notices about **Green Hasson Janks Partner Steve Sills** when meeting him is his passion for all things entertainment. “I get to work in an industry that I love being involved in,” Sills says. “I love going to the movies and listening to music.” Sills’ involvement with entertainment began at home. He described growing up in a “show business” household.

“My father was a business manager, representing various entertainment clients, like Monty Hall from Let’s Make a Deal fame,” Sills adds. “My mother was an actress and appeared on stage, in film and on television.”

When Sills turned 14, he started singing with a rock n’ roll band, joining various bands several times over the years. Even his military service related to entertainment — he was assigned for a year to a base in Northeast Thailand where he had a radio and television show.

Sills started 40 years ago as a CPA at Laventhol and Horwath. Most of his clients were in the entertainment business because that was his interest. After about five years, Laventhol and Horwath acquired a small entertainment firm that specialized in profit participation audits and asked him to get involved. He did that until Laventhol and Horwath went out of business in 1990. He then started Sills & Adelman.

In 2007, when he was 60 years old, he decided to merge with Green Hasson Janks. He promised the firm that he would stay five years, but it has now been 10, and he is still going strong. He still loves what he does and sees no end in sight.

“Joining Green Hasson Janks has given me the opportunity to expand our practice,” Sills explains. “The entertainment business was transforming into an international market, and I wanted access to more resources to serve my clients.”

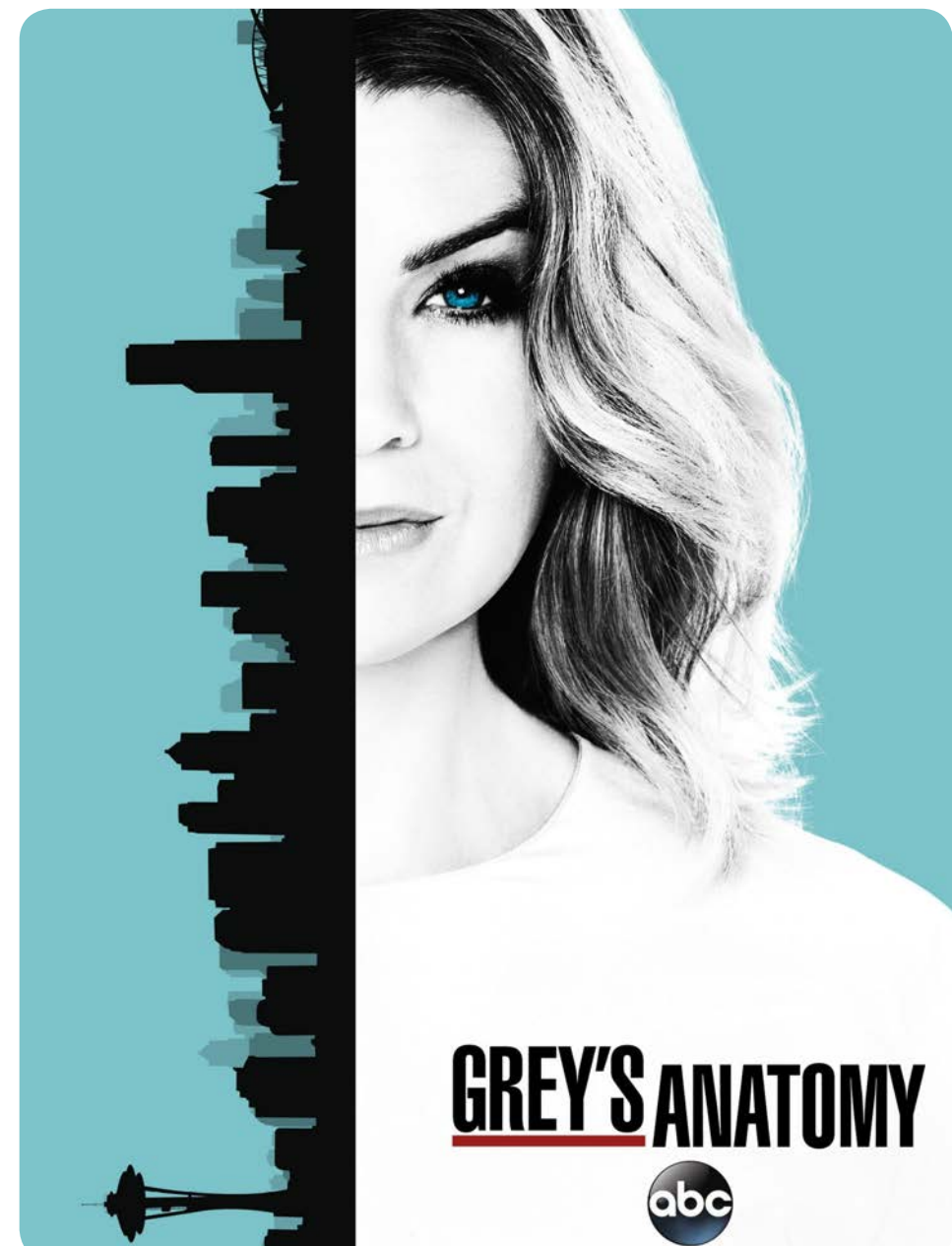
Green Hasson Janks now has 18 people that do profit participation audits, supplemented by the international reach of HLB. Sills feels he could not have grown like that on his own.

Ilan Haimoff, Partner and Entertainment and Media Practice Leader at Green Hasson Janks, applauds Sills.

“Through the merger in 2007, Green Hasson Janks achieved a significant presence in profit participation audits,” Haimoff says. “It also gave us a great presence in the industry beyond participations — it really enhanced our visibility and position. Thanks to Steve, we are the go-to firm for participation audits.”

“**NOW, IN THE AGE OF ‘PEAK TV,’
A LONG-RUNNING SHOW CAN EASILY
ECLIPSE THE FINANCIAL SUCCESS
OF A BLOCKBUSTER FILM, OR EVEN
A BLOCKBUSTER FILM FRANCHISE.**”

Anita Wu
Principal,
Green Hasson Janks





TODAY'S LANDSCAPE: WHO IS GETTING THE \$

PRINCIPAL CHAPTER AUTHOR



ANITA WU,
GREEN HASSON JANKS



Deal Structures are Shifting

In a new world ruled by SVOD, Netflix and a radically altered delivery landscape, it was inevitable that deal structures would change. More content is spread across audiences, films debuting on streaming services and shorter television seasons mean studios want to pay less, while content creators and talent want to be paid at least the same as they have become accustomed to.

Green Hasson Janks Principal Anita Wu sees a definite studio strategy regarding talent.

“For talent, which is largely defined as actors, writers, producers and directors, many studios now set aside a specific percentage for profit participations that is put up for grabs — it is up to the talent and their representatives to divide that percentage among themselves,” Wu explains. “Generally, we are starting to work with a larger number of profit participants on a given project. In a pool deal, presumably, everyone would have the same profit definition. Outside of a pool deal, while there may be some differences in their profit definitions, the interests of the various participants are aligned on most of the issues we come across, and we feel they would get better results if they audited and settled together. They should be allowed to join forces, but some studios balk and instead seem to take a more divide-and-conquer approach to resolving common items of dispute.”

Wu is also seeing the nature of a project’s stakeholders expand to include more content owners, financiers, co-distributors and other roles.

“Definitions tend to lean more favorably to those who

have financial skin in the game,” Wu says. “There may be explicit language in their contracts that addresses at-source reporting, the treatment of ‘soft money,’ limits on the amount, if any, of allowable overhead charges, etc. There also tends to be more visibility to the underlying documents in an audit setting for those who bear some of the financial risk in a project.”

Craig Emanuel, Partner, Vice-Chairman and Chair of the Talent Practice at Loeb & Loeb, also feels there has been a shift in the number and nature of stakeholders.

“Except in limited circumstances you see the concept of first dollar gross participation largely coming to an end and participations, even for major talent who now share in a breakeven ‘pool’ participation (which the studios claim is making them more of a partner in the project ending).” Emanuel says, “The value of the pool is getting reduced, as is the definition of what is being included in the pool, resulting in a shrinking participation. That represents a major shift over the last few years. The only money you can count on is the money that is budgeted into the film. Box office revenue just does not translate the same way anymore, and studios are a lot more savvy in not offering bonuses that would be payable prior to their true breakeven position.”

Emanuel sees a couple of major impacts to talent, producers and stakeholders.

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Craig Emanuel

Partner, Vice-Chairman and Chair of the Talent Practice,
Loeb & Loeb

“There are two aspects to the issue,” Emanuel explains. “Is there a change in the deal structure? Yes. Is there a real change to the economics? Yes again. Netflix is a buyout — are you giving away the upside? But only a small number of movies have an upside anyway. You are giving away your upside and on a highly successful movie you will leave money on the table, but what is the real consequence of that? The Netflix/Amazon/Hulus of the world are changing the nature of our business.”

Emanuel sees differences between companies like Amazon, which has a genuine theatrical release, and Netflix, which does not and where the potential for a backend participation still exists.

“As a consumer, why spend the money on going to the theater if you can see it at home?” Emanuel asks. “The independent film business in many cases is moving away from the theatrical release unless they are the kind of movie that might attract award consideration. For a Fox Searchlight or a Sony Classics, films may get released on 50-75 screens for limited runs but it is hard for them to sustain longer runs unless the film becomes a breakout movie or has attracted attention through festivals or awards.”

Ken Holloway, Senior Vice President Finance and Controller at Endgame Entertainment, a financier and independent film producer, also describes some challenging differences related to producing a feature for Netflix, as compared to the traditional independent model — foreign presales and a studio domestic release.

“Netflix is a great partner, but the tradeoffs are not insignificant,” Holloway explains, “A guaranteed fee comes at a cost of not owning the IP (no library value) and no results-based upside potential. For a content creator, the lack of long-term ownership rights is a material change to their business model.”

Holloway went on to say, “Having said that, the recent trend in independent theatrical release performances has to lead to distributors requiring better terms for the risk of putting up significant P&A — thus lessening a producer’s and talent’s upside, which somewhat levels the field.”

**“THE RECENT TREND IN INDEPENDENT
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Senior Vice President Finance and Controller,
Endgame Entertainment

Craig Emanuel, Partner, Vice-Chairman and Chair of the Talent Practice at Loeb & Loeb, adds some sage advice for the industry.

“We cannot ignore the shift that is taking place in our business,” Emanuel says. “Deals will need to adjust to that model. It is better to get a film made and seen than not. Box office revenue is largely flat, but the younger audiences are moving to Netflix or streaming or not watching movies at all. Many in that generation do not even have a television — they are not going back to the theater unless it is an event movie. There will be exceptions, but that is the changing nature of our business. Exhibitors now have the challenge of getting people to go to the theater — they are updating their venues with features like restaurants, bars, and shopping, and providing more of a cultural experience than just going to the movies.”

Mergers and Acquisitions May Drive Further Industry Disruption

Mergers and acquisitions like Lionsgate’s purchase of STARZ, MGM taking full ownership of EPIX, Hulu’s ownership by Universal, Disney, Fox and Turner, and the pending acquisition of Time Warner by AT&T continue to reshape the entertainment industry and have an effect on participations. Notably, Apple ended 2016 with \$246 billion in cash, enough to buy Netflix and HBO’s parent company, Time Warner, with more than \$100 million left over!

Anita Wu of Green Hasson Janks sees a more complicated participations process as a result.

“We pay close attention to transactions like MGM’s acquisition of EPIX six months ago,” Wu expands. “EPIX is a pay television exhibitor of mostly film. When we audit

profit participations, we look for the money generated in all of the supplemental markets — for example, if a Bond film is shown on EPIX, we want to make sure the transaction was reported at fair market value, and that no other rights were given to EPIX without a proper valuation of such rights. Studios want to extend their reach into all forms of distribution — it is to their advantage to own as many theaters, broadcasters, etc. as possible, and offer their exclusive content to the public, but that also means they can charge their affiliated companies less for access to the content and hold onto more money within their overall corporate structure. From a profit participation perspective, the potential for undervaluing revenues and/or overcharging expenses is real cause for concern. In addition, for services trying to break into the marketplace, there is the intangible value of their exclusive content helping to build their brand. Of course, there also may be benefits from vertical integration — if distributors own several arms throughout the entertainment and media space, their products get out more widely.”

Craig Emanuel, Partner, Vice-Chairman and Chair of the Talent Practice at Loeb & Loeb, also warns about the pitfalls of vertical integration.

“It will have an impact in that you are now faced with an additional level of issues regarding pricing for these different companies,” Emanuel says. “It is always a concern. On one level, having consolidation in certain areas is a good thing because it promotes better commerce between related companies, but we need a greater level of scrutiny to make sure the pricing is fair. Consolidation is inevitable — when studios eliminate the middlemen, the more profitable they become.”

Litigation is Sometimes the Answer

John Berlinski, Partner and Chair of the Entertainment Practice Group at Kasowitz Benson Torres LLP, has a practice that centers on entertainment litigation and involves profit participation disputes and other licensing disputes. He represents both studios and talent.

“There is a general litigation trend,” Berlinski says. “Parties who used to work out differences informally are now resorting to litigation. For example, you did not used to see talent agencies suing buyers, or studios bringing claims against networks, but that is becoming more common because of the focus on the bottom line.”

Berlinski adds, “The way those disputes play out has also changed over the years. More and more disputes are being resolved in arbitration proceedings,” Berlinski explains.

“Arbitration can have the benefit of confidentiality and can offer a more streamlined and cost-effective approach to resolving disputes. The trend towards confidential arbitration has resulted in fewer disputes being made public but no shortage of disputes being litigated.”



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Partner and Chair of the Entertainment Group,
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FIRESIDE CHAT WITH BEN SHEPPARD

GREEN HASSON JANKS LITIGATION SUPPORT AND EXPERT WITNESS PRACTICE LEADER



Jennifer Sullivan, Senior Marketing Manager at Green Hasson Janks, sits down with Ben Sheppard to discuss the role of litigation in today's entertainment landscape.

SULLIVAN: What does the term “expert witness” mean for the entertainment sector?

SHEPPARD: The expert witness concept is about bringing actual industry experience and knowledge to bear on a case to help explain nuances. It is preferable when trying to either support or rebut a damages analysis.

SULLIVAN: In today's landscape, are there some types of cases that come up more than others?

SHEPPARD: Breach of contract cases come up quite often. These can include profit participations when talent, for example, believes a studio is not complying with a contract.

SULLIVAN: In breach of contract cases, are the issues the same as they were five years ago or has it evolved?

SHEPPARD: The types of issues are definitely different from five years ago. One case I recently worked on looked at damages from a SVOD standpoint. I suspect we will see a lot more of that, meaning that as content distribution shifts to new modalities, contractual interpretations are more likely to be questioned.

SULLIVAN: Can you describe “slate financing” and how it differs from profit participation?

SHEPPARD: What changes is who the parties are at the table. Slate financing is where a studio finds an investor to help offset the studio's production risks on a number of films. This has been going on since before I started 20 years ago. The money comes from a variety of sources like bank loans, insurance-backed bank loans, hedge funds and foreign financing — they all have separate revenue participation agreements. It is similar to profit participation, but these investors are typically in a junior position from actors, directors and producers — who will get their money first. As you might suspect, this is an atmosphere that generates disputes.

SULLIVAN: Can you tell us about a specific case you were involved with?

SHEPPARD: Here's an interesting one. I worked on a pre-litigation case for a New Zealand-based feature

film. By “pre-litigation,” I mean there were contractual questions, but no suit had been filed. The bank syndicate that provided the financing had funded a loan with the expectation that they would get their investment back plus a reasonable return.

SULLIVAN: Did they achieve that goal?

SHEPPARD: Partially. After the film's release, they got their money back, but not the return. They were thinking of suing the studio, and they brought me in to look at their greenlight model. I looked at that and their revenue participation agreement to determine if the syndicate's expectations were incorrect. The greenlight model was good, but the assumptions used were not likely to occur.

SULLIVAN: That is interesting. Can you tell us more about the assumptions?

SHEPPARD: It became apparent that they had not thoroughly researched the assumptions they were using to determine the film's revenue. They did not ask the right question — they asked if the assumptions were possible, but not how likely the projections would be achieved.

SULLIVAN: That must have been a long, involved court case.

SHEPPARD: It could have been. The case was in New Zealand, and as part of negotiations, the syndicate's Queen's Counsel asked me if I would have made the deal knowing what I know when the deal was made, and I had to say it was doubtful. I soon heard they had settled.

SULLIVAN: That is not what I expected to hear!

SHEPPARD: We can set reasonable expectations — that is a quality I see lacking from a lot of experts, at least ones I have come up against. I am asked to base an opinion on certain assumptions and I give my opinion, but those assumptions can be wrong.

SULLIVAN: Any final words?

SHEPPARD: In this business, integrity is the only commodity we have. I am not here to find the highest answer or the lowest answer — I am here to find the right answer.



THE IMPACT OF TECHNOLOGY

PRINCIPAL CHAPTER AUTHOR



MICHAEL SIPPEL,
GREEN HASSON JANKS

Technology is driving rapid change in the movie and television industry. Tech experts are working on new and even more disruptive technologies every day. Advances can be in filmmaking, as in the use of drones to film sequences for *Pirates of the Caribbean: Dead Men Tell No Tales*, advances can be in the theatrical experience like 4D or immersive experiences, or they can be game changers like SVOD.

Taking Digital Platforms In-House

There is speculation about the major studios trying to build up their own digital platforms to host their exclusive content. The most obvious player is Disney, which recently announced they were removing their content from Netflix and launching their own streaming service by 2019. According to the *Hollywood Reporter*, Disney will not create the technology, but will acquire a majority of BAMTech, the streaming technology company owned by MLBAM, the internet company owned by Major League Baseball¹.

Green Hasson Janks Senior Manager Michael Sippel sees this as a logical progression.

“The studios are behemoths,” Sippel says. “They have seen how successful Amazon and Netflix are, and they all must be looking at this — I am sure they will all have some form of streaming subscription service within the next three years.”

Acquiring and Investing in Technology Companies

Major studios are spending to quickly ramp up their technology capabilities. Disney again is thinking

strategically with its investment in BAMTech, and others are expected to follow suit.

Sippel sees the reasons for the quick ramp-ups as fairly obvious.

“Technology has already been a huge part of the entertainment industry’s success for at least the past 10 years through Internet, digital and streaming services,” Sippel explains. “It is now a survival strategy to embrace vertical integration and create efficiencies. Studios must focus on the bottom line and show a return on investment for their stakeholders — growth is the name of the game,

even if there are less people going out to the movies.”

Tech Companies Now Producing Original Content

The most prominent examples of tech companies crossing over into content creation are Netflix, Amazon and Hulu, but there are numerous examples.

In these cases, Sippel thinks the word “tech” is ambiguous and misused.

“Anyone in an online digital space could be a tech company,” Sippel explains “Amazon is a tech company and is now a content creator. Apple iTunes and Apple Play are apps you can choose from. Facebook Play is a new one. Google, and many others are in this space. It is logical that the trend will continue. There will be more and more content, and viewers will have endless choices, whether that is good or bad.”

Sippel adds that profit participation and contracts will be affected.

“Generally, participations should remain basically the same, but the deals will be different,” Sippel expands.



“**THE USE AND ADVANCEMENT OF TECHNOLOGY PRESENTS AN EXCITING FUTURE FOR THE WORLD OF ENTERTAINMENT, BOTH WITH CURRENT CONCEPTS SUCH AS VR, 4D AND PVOD, AND WITH UNKNOWN IDEAS YET TO EVEN EXIST.**”

Michael Sippel
Senior Manager,
Green Hasson Janks

“The new players like Netflix and Amazon are looking for structures to get out of traditional backend deals — we are now seeing more buyouts or estimated backend deals. The investors, creators and other talent will still be entitled to profit participations, but the structure and reporting responsibilities might change.”

Cybersecurity and the New Technology

Hacks of companies like Disney, Netflix, Sony, HBO, C-SPAN and many others are a major issue in Hollywood. The issue may stem from the way movies get made — from coming attraction trailers that are designed to draw audiences into cinemas to eye-popping 3-D visual effects that burst off the screen, studios routinely farm out large chunks of work to vendors around the globe who compete to provide lowest-cost solutions².

Sippel sees cybersecurity issues as potentially massive.

“Companies like Sony and Netflix have strong measures in place, but if they can be hacked there is no limit to the hackers’ ability,” Sippel says. “It is an issue. I have seen it in participations, where we are two to five years behind (mostly due to the audit queue). We all saw it become an issue in the home video world (which is now dying anyway), but 5-10 years ago piracy affected the price at which the studio could sell their product due to guys on the street flooding the market with cheap copies. Another concern is release dates. Someone could grab your content and release it ahead of you. I am only slightly joking when I say that studios should seriously consider spending the money to hire a hacker to teach them how to avoid being hacked — maybe they should learn from the best!”



GLOBALIZATION

PRINCIPAL CHAPTER AUTHOR



ILAN HAIMOFF,
GREEN HASSON JANKS



Over the past decade, there has been a continual shift toward international distribution, and the overseas box office can now be as, if not more, important than the U.S. box office. A U.S. flop can be profitable if it makes money overseas — take the recent example of *Transformers: The Last Knight*, which did \$130 million domestically³ and \$475 million overseas. Based on its \$217 million production budget, it would not have been a success if measured by just its domestic revenue performance. All things considered, Paramount recently announced its plans to release another Transformers movie sequel in 2019.

Anita Wu of Green Hasson Janks sees a lot of interest from international investors.

“There are so many investors from countries around the world who want to learn from, and invest in, Hollywood,” Wu says, “Also, with a higher rate of growth in entertainment consumption abroad, domestic entertainment companies are in hot pursuit of forging strategic alliances with international players and expanding their global presence. From a profit participation standpoint, that means we are seeing an increase in our foreign clientele, as well as heightened interest in performing audits internationally.”

Netflix Exclusivity

Netflix is now “the global channel,” with 190 territories and counting. The ambitious channel is also bringing in major names like Adam Sandler and Shonda Rhimes

with big-money contracts to create content. Netflix has original programming, of course, but they also buy the rights to make a television series or motion pictures available to subscribers as a first window in television markets. For example, for a television series on a network, this type of deal says that the next time it shows will be on Netflix rather than cable.

Ilan Haimoff, Partner and Entertainment and Media Practice Leader at Green Hasson Janks, sees confusion in the marketplace as a result.

He sees exclusivity as a way to build the subscriber base for Netflix, regardless of what content is being acquired or created. “It will add to the subscriber base if that is the only place to see the content,” Haimoff explains. “If they generate it, they can control it, but the number of subscribers they can add diminishes vis-a-vis the amount they spend. I hear from bankers that Netflix is borrowing more money to create more content. The goal is to add subscribers, but at some point on the curve it may slow down.”

Haimoff says there are options for staying ahead of the curve. “They can do things like reducing the money spent on new productions, or they can look for new sources of income, such as licensing to television licensees in the U.S. or overseas,” Haimoff says.

Format Licenses

Format sales is a traditional business that has been

around a long time, and was used mostly by game shows and reality shows. In these cases, a show format started in another country and then was sold to other countries. American Idol, Big Brother and Wipeout are examples. Each was customized for a local audience. Homeland is another example — Fox bought the rights based on a show in Israel and made it a huge success after customizing it to an American audience.

Haimoff does not see much correlation to the television market, however.

“On the television side, as much as they try to make the world global, they need to customize a show to reflect local culture, attitudes, humor and much more,” Haimoff says. “Movies have done better, especially where they have broad concepts like science fiction, horror, or action. Again, I would use the Fast and Furious franchise as an example, but there are many others like Star Wars, James Bond or Harry Potter.”











Overall, Haimoff sees this as a growth engine for globalization.

“It is a way to exploit emerging markets for the shorter term,” Haimoff explains. “The rapid growth will subside, but right now it is working. Studios can leverage a franchise or brand and go back for sequels — a great example is Furious 7. The key is to find a way to distribute it to as many territories as possible. It is a form of leverage that generates lots more buyers now, even though this is a traditional concept. By releasing sequels, marketing costs are reduced because people are familiar with the brand.”

“
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Ilan Haimoff
Partner and Entertainment
and Media Practice Leader,
Green Hasson Janks

THE LOS ANGELES TIMES
LIST OF THE TOP 10 GLOBAL FRANCHISES⁴

1		MARVEL CINEMATIC UNIVERSE	\$9.3 BILLION
2		HARRY POTTER	\$7.7 BILLION
3		STAR WARS	\$6.7 BILLION
4		JAMES BOND	\$5.0 BILLION
5		X-MEN	\$3.8 BILLION
6		THE FAST AND THE FURIOUS	\$3.8 BILLION
7		TRANS- FORMERS	\$3.7 BILLION
8		PIRATES OF THE CARIBBEAN	\$3.7 BILLION
9		JURASSIC PARK	\$3.6 BILLION
10		DESPICABLE ME	\$2.7 BILLION

⁴<http://www.latimes.com/entertainment/movies/la-ca-mn-25-most-powerful-franchises-20160524-snap-story.html>

TRENDS IN THE CHINESE FILM INDUSTRY

With China emerging as a significant global player in the film industry, **Chenxi “Tracy” Liang, Supervising Senior at Green Hasson Janks**, sat down with **Seagull Song, a law professor, practicing attorney and published author**, who advises entertainment companies in connection with U.S.-China cross border transactions.

LIANG: What do you think will happen with Chinese investment in the U.S.?

SONG: We have seen a slowdown in terms of China’s direct investment into the U.S. since the beginning of this year due to various reasons. Instead of the “hot/easy money” that flooded from China in the past few years, we will see more “rational money” and more scrutiny in such cross-border transactions moving forward.

LIANG: What about U.S./China co-productions?

SONG: U.S.-China co-productions are still limited in number, and most of them have not been very successful at the box office level, because it is rather difficult to create a movie that is appealing to both Chinese and global/Western audiences due to cultural differences. The new trend now is to produce movies targeting one type of audience (say the Chinese audience only), but then bringing Hollywood “elements/talents” into the film, such as hiring scriptwriters, cast members or even special effects teams to make the film more at an “international standard.” Examples of such include *Monster Hunt* and *Wolf Warriors II*. Both movies were Chinese local productions with Chinese leading actors, distributions and investors; but behind the scenes, Hollywood influences (i.e., creative talents and consultants) were present in both films to give them a “Hollywood feel,” which is more enjoyed by the Chinese moviegoers.

LIANG: What are the opportunities for U.S.-based companies and talent?

SONG: For the major studios, what they are after in China is the market access, meaning 1.4 billion people who are potentially moviegoers and content consumers. For the independents, the Chinese market also means additional distribution channels, meaningful foreign sales revenue and also more financing opportunities. For talent, China provides great opportunities. Given the increasing cooperation between the agencies in Hollywood and Chinese studios and the increasing demand for U.S. talent working on Chinese films, the U.S. talent will see more and more opportunities to work on China-related projects, whether it is related to acting, scriptwriting, composing, consulting or other opportunities.

LIANG: How have the front-end and backend profit participation deals in China evolved over the years?

SONG: Ten years ago, participation deals did not quite exist in China. But thanks to the booming Chinese film industry, participation deals have become much more common these days. Yet, as with the United States and elsewhere, the challenge is how to define the “net profit” in such deals. We have witnessed a number of litigations at Chinese courts as a result of the ambiguity in such definitions during the past two years.

LIANG: Are there any innovative distribution terms utilized by the Chinese players?

SONG: Yes. In addition to the traditional flat-fee and percentage-based distribution arrangements, we also saw the “Box Office Guarantee/Distribution” arrangement. Under such deals, the Chinese distributor will make its own prediction on how well the film will do at the box office level, and then offer a “guaranteed payment” to the film investors. If the film does really well and the box office revenue goes beyond its “guaranteed threshold,” the distributor could enjoy a high percentage (up to 70-80 percent) in the revenue sharing. But on the flip side, if the movie does not sell well and the box office revenue is well below the guaranteed threshold, then the distributor only gets its “distributing fees,” but at the same time needs to pay the “guaranteed share” to the film investors. Under such circumstances, the producer could walk away with a decent package of “guaranteed payment,” despite the failure of the movie at the box office.

LIANG: What changes have you seen in the financing/distribution deals between Chinese investors and Hollywood studios?

SONG: Deals between China and the U.S. have not changed much in the past couple of years. From the Chinese side, even though the Chinese players have become more sophisticated in deal negotiations, most of them still do not have enough bargaining power to get the terms in their favor. From the U.S. side, some of the U.S. players are more interested in working with “highest bidders” rather than “seasoned players” from China because it is “easy money.” But this attitude could lead to potential problems down the road if their Chinese partners are total outsiders and have no clue as to what they are doing. We have seen this happening many times.



U.S.-CHINA CO-PRODUCTIONS ARE STILL LIMITED IN NUMBER, AND MOST OF THEM HAVE NOT BEEN VERY SUCCESSFUL AT THE BOX OFFICE LEVEL, BECAUSE IT IS RATHER DIFFICULT TO CREATIVE A MOVIE THAT IS APPEALING TO BOTH CHINESE AND GLOBAL/WESTERN AUDIENCES DUE TO CULTURAL DIFFERENCES.

Dr. Seagull Haiyan Song
Senior Advisor, Hogan Lovells
Professor and Director, Loyola Law School LA



CRYSTAL BALL: GAME CHANGERS

PRINCIPAL CHAPTER AUTHOR



PETER KLASS,
GREEN HASSON JANKS

So what is next? Not every idea takes flight, but things like SVOD, PVOD and virtual reality/augmented reality may significantly affect how Hollywood does business in the coming years.

Premium Video on Demand

Premium VOD (PVOD) is a term used to describe movies that would be offered to view before being available on streaming services or Home Video (Blu-ray and DVD). Some predict that PVOD may be the next industry disruptor.

Sean Parker's Screening Room Concept

Sean Parker had a 2016 start-up called Screening Room that would give users the ability to watch movies still in theaters from the comfort of their homes for \$50 for a 48-hour rental. Exhibitors were critical of the idea as many theatrical chains oppose any encroachment on the exclusivity of the theatrical window, approximately 60 to 90 days after release, and major studios were concerned with piracy. Screening Room is still in development and currently working on anti-piracy technology.

The Impact of PVOD on Windowing

Because of a concerted effort by the studios to push for shorter windows, in 2017 we witnessed major theater owners reluctantly engage in negotiations to shorten the theatrical window. Theatrical exhibitors do not want movies to be accessible on PVOD during the initial theatrical release, as the first few weeks of a theatrical run are the phase when studios and exhibitors get most of a movie's revenue. Studio heads signal that the PVOD offering will materialize sooner rather than later. Whether PVOD is offered on day 1 or several weeks post release, there is likely to be a contraction of the theatrical window within the next year.

Peter Klass, Senior Manager at Green Hasson Janks, predicts that PVOD will be a major force in the industry.

"In the next year exhibitors will be squeezed to a 30 to 45 days' exclusive theatrical window at most. After that, releases will go directly to streaming and DVD platforms" Klass says.

"The studios and exhibitors have not agreed on a PVOD window, with the sticking point being the revenue share split between studios and exhibitors; until both parties figure out a viable business model to grow the overall pie, a short term alternative will likely be to change the theatrical window. This could be done by shortening the exclusive theatrical window to the first two weeks of a movie's theatrical release and then grant access to PVOD for the rest of the theatrical window," Klass explains.

Ken Holloway of Endgame Entertainment wonders what will happen to theaters when consumers watch movies at home on small screens.

"The theater operators need films to show — what happens when the consumer decides they will not pay to see that type of content on the big screen?" Holloway says. "They will not have enough product to fill their screens. They might supplement with live performance events, but right now that is small, and I am not sure how much bigger it will get."

Peter Klass wonders how this will ultimately affect participations.

"The major impact on the reporting of PVOD for talent and investors on their participation statements is how the studios and distributors will report revenue. Will it be at

100 percent? Or will they try to squeeze the participants by reporting on a royalty basis. Since PVOD is an alternative for the theatrical distribution, it will be interesting to see if studios classify PVOD as theatrical or home entertainment. This should be something to look out for until a new model emerges."

Theatrical Subscription Model — Searching For the Next Netflix

Right now, the great majority of ticket sales are for a specific film, rather than a monthly or weekly subscription, but the subscription model has the industry buzzing. After the tremendous success of SVOD in the home entertainment market, theater owners have begun experimenting with various recurring charges to allow customers to see unlimited movies for a specified time.

Klass thinks this will appeal to the younger generation of viewers, "Millennials like a subscription model like Netflix, but they are not yet the majority of theatergoers." Klass continues, "At this time I don't see this as a replacement option. Right now there is too much risk in upsetting the current business model. You see exhibitors adding bells and whistles to try and keep the theatrical audience and continue to sell popcorn."

Clues from the DEG Year-End 2016 Home Entertainment Report

The annual DEG Report captures the state of the home entertainment market in the U.S. The 2016 report showed that the market has stabilized — SVOD and other digital sales have replaced losses in physical media (DVD & Blu-ray). It is important to note that excluding streaming subscription revenues (SVOD) the market continues to sharply decline. Klass explains, "I believe SVOD is much more analogous to television licensing, and if streaming subscriptions such as Netflix, Amazon and Hulu are not counted then the home entertainment market continues to shrink. The hopeful outlook that new media revenue from EST and VOD would replace the traditional DVD and Blu-ray is all but gone."

"Due to the shrinking home video market, studios are shying away from reporting SVOD similar to TV (at 100%) and leaning to the historical home video royalty model (usually 20% royalty on revenue with no expenses). As there is virtually no cost involved with SVOD distribution—with royalty reporting studios are retaining 80% of the revenue for themselves—profit participants are encouraged to seek advice on the changing film and television landscape."

The Impact of PVOD and SVOD on Release Windows
Industry insiders are contemplating whether SVOD and PVOD will dominate the entertainment scene in coming years. It seems likely that films will have shorter theatrical runs and the ability to see first-run movies in the home will expand. Many insiders also wonder how the emergence of PVOD may impact theatrical admissions and home entertainment spending.

Ken Holloway also sees the generational change affecting home entertainment.

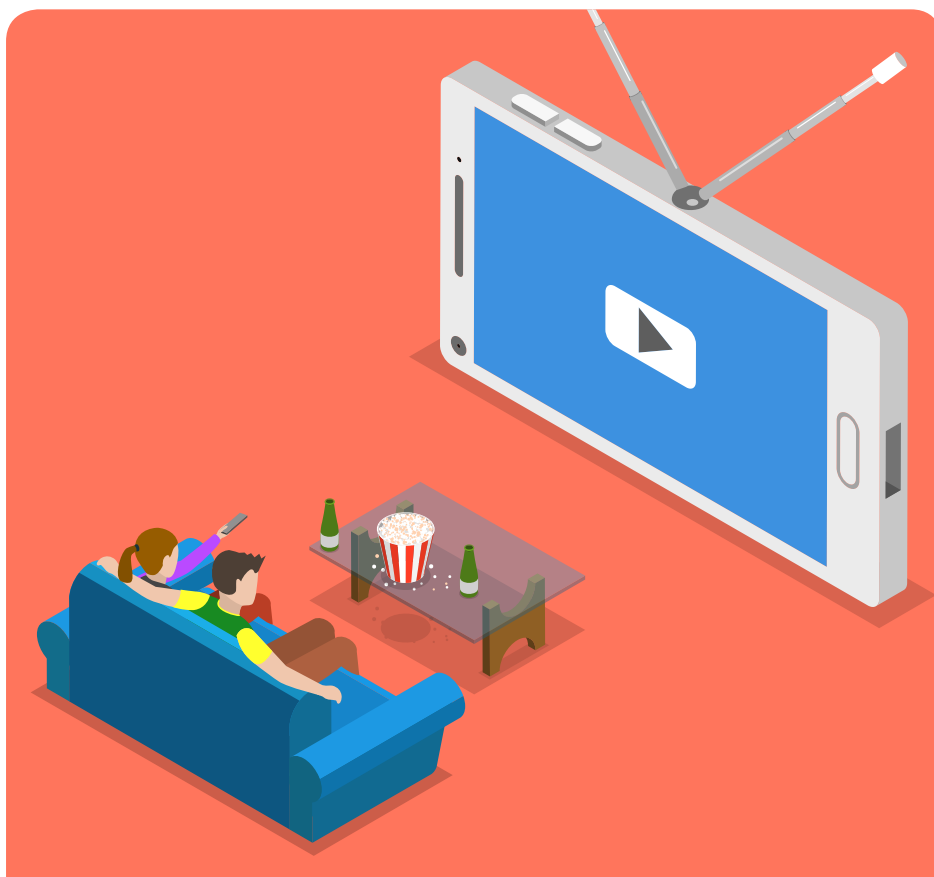
“IN THE NEXT YEAR, EXHIBITORS WILL BE SQUEEZED TO A 30 TO 45 DAYS’ EXCLUSIVE THEATRICAL WINDOW AT MOST.”

Peter Klass
Senior Manager,
Green Hasson Janks

"Millennials have shorter attention spans and demand convenience," Holloway explains. "That may dictate the future of SVOD and PVOD. This generation prizes the social experience of going to a theater for blockbuster events like Star Wars movies and maybe scary movies too, but all in all, they would probably prefer to see a movie at home or on their iPhones."

Holloway also sees the box office as less predictable now.

"In the past, the box office had better predictability," Holloway expands. "Those days are long gone. We don't know what the floor is on box office for a particular film. You might do \$5 million box office on a quality film, with 'A Level' cast off of a \$20+million P&A spend. From a financing perspective, this introduces enormous uncertainty, but our industry will still be willing to finance exciting projects with stars people want to see. *La La Land* and *Girls Trip* were examples of breakouts from that — breakouts will always occur."





DIGITAL ENTERTAINMENT GROUP YEAR END
2016 HOME ENTERTAINMENT REPORT⁵

DEG REPORT: U.S. CONSUMER SPENDING BY FORMAT 2016 YEAR END						
U.S. Consumer Spending (in millions)						
SELL-THRU:	Q4 2015	Q4 2016	YOY	Through Q4 2015	Through Q4 2016	YOY
Sell-Thru Packaged Goods - All	\$2,171.75	\$1,866.43	-14.06%	\$6,070.17	\$5,490.57	-9.55%
Sell-Thru (including EST)	\$2,722.77	\$2,418.89	-11.16%	\$7,976.80	\$7,500.53	-5.97%
RENTAL:						
Brick and Mortar Rental	\$154.84	\$122.32	-21.00%	\$616.27	\$489.56	-20.56%
Subscription (physical only)	\$154.04	\$123.23	-20.00%	\$658.87	\$547.57	-16.89%
Kiosk	\$390.82	\$320.47	-18.00%	\$1,732.24	\$1,434.98	-17.16%
Total Rental (excluding VOD)	\$699.70	\$566.03	-19.10%	\$3,007.39	\$2,472.11	-17.80%
Total Rental (including VOD)	\$1,218.62	\$1,099.39	-9.78%	\$4,975.86	\$4,548.89	-8.58%
DIGITAL:						
Electronic Sell-Thru	\$551.01	\$552.47	0.26%	\$1,906.62	\$2,009.97	5.42%
VOD	\$518.92	\$533.36	2.78%	\$1,968.47	\$2,076.77	5.50%
Subscription Streaming*	\$1,349.72	\$1,705.27	26.34%	\$5,081.88	\$6,230.13	22.60%
Total Digital	\$2,419.65	\$2,791.10	15.35%	\$8,956.97	\$10,316.87	15.18%
TOTAL U.S. HOME ENTERTAINMENT SPENDING:	\$5,291.10	\$5,223.55	-1.28%	\$18,034.53	\$18,279.55	1.36%
Box Office (in billions)	\$3.33	\$3.50	5.02%	\$10.57	\$11.80	11.65%

*Paid subscribers only and does not include SVOD bundled with other

Disclaimer: This report contains information compiled from sources that the DEG believes have accurately reported such information, but which the DEG has not independently checked or verified. As such, the DEG does not warrant its accuracy or reliability. The report is not intended to provide investment or securities advice.

Halloway has some warnings about what comes next.

“The aftermarket inevitably shrinks because the other options are so great now,” Halloway states. “It is more bifurcated every day, and the result is that the cost of the content has to reflect that trend — and you have to be very selective on which films get an initial wide release and which ones are platformed. Also, right now you have Netflix, Amazon and Apple with huge budgets, plus studios and independents. There are a lot of channels who want product and are willing to pay premium pricing for it, but that may well shrink over the next five years or so as winners and losers for the eyeballs are determined. The future will further differentiate between blockbuster and niche product cost structures.”

When asked about his opinion on the impact of PVOD on home entertainment trends, Klass is optimistic.

“PVOD WILL NOT HAVE MUCH OF AN IMPACT ON HOME ENTERTAINMENT. ITS IMPACT WILL BE ON THE THEATRICAL WINDOW - PEOPLE WILL WATCH THEATRICAL AT HOME NOW.”

Peter Klass
Senior Manager,
Green Hasson Janks

“PVOD will not have much of an impact on home entertainment,” Klass says. “Its impact will be on the theatrical window — people will watch new theatrical releases at home now. It does not compete with the Netflix or the TV model or disk purchases. PVOD is for people who do not want or cannot get out to see a movie in a theater; that can be a winning concept if the studios and exhibitors can figure out how to present PVOD as a complimentary offering, not a substitute for the theatrical market.”

Virtual Reality/Augmented Reality
Video games were the first widespread uses for augmented

reality (AR), where the virtual and physical worlds are combined. The last big AR splash was Pokemon Go, which did not need special hardware or software, but Apple and Google are both developing technology to better take advantage of AR. The smartphone industry is now poised to offer apps. In fact, Apple is extending AR to all iPhones and iPads with its iOS 11 — given the size of the market for these devices, the potential is huge.

Virtual reality (VR) actually immerses the viewer in a different world rather than adding to the real world as AR would. For some time, VR has been predicted to be the next major trend, but it has not met those expectations, staying within gaming and industrial parameters for now. It also lacks a social element, since a user puts on their headphones and “tunes out” to be in the virtual world. For VR, the market has been limited to date, but of course all this can change with a disruptive app that changes everything overnight.

Green Hasson Janks Senior Manager Peter Klass does not see VR or AR impacting participations yet.

“It is a complement, a marketing tool — it is not for telling stories yet,” Klass explains. “Because of the limited nature of the stories being told in VR/AR, profit participation has not been much of a factor.”

Ilan Haimoff, Partner and Entertainment and Media Practice Leader at Green Hasson Janks, is unsure of what the future will bring.

“We are watching VR — but we do not know where it will take us,” Haimoff says. “It will continue to impact video games and education but possibly not go mainstream. It is currently an expensive and complex technology which may need to be further tested in the television and motion picture industry, so we will have to see where it goes.”

Defining Success for Industry Gamechangers
Green Hasson Janks Senior Manager Peter Klass thinks that PVOD success will come via critical mass of viewers.

“For PVOD, success will be if more than 20 percent of major studio films are released on PVOD,” Klass says. “If PVOD’s window starts at day 1 of the theatrical window or two weeks into it, that would also be a success because studios will collect their money quicker and a new revenue stream will be created. The bottom line is that as long as the exclusivity window is 30 days or less, it is a major game changer. Studios and producers want it, but exhibitors are holding to the traditional model. PVOD

could grow the market as more people watch at home who otherwise would not make it to the theater, plus it could reduce piracy. Hopefully PVOD will grow the overall revenue pie, as it is in everybody’s best interest to grow the pie.”

Since PVOD and AR/VR are not currently financially relevant to the overall entertainment revenue pie but may likely become game changers in the near future, Klass offers his thoughts on how that can impact profit participants.

“I would advise the talent or their rep to be on the lookout for how future contracts are written and monitor how distributors treat PVOD and AR/VR for reporting to profit participants,” Klass says. “There is the potential to make less money if contracts are written in favor of the distributor over the profit participants”



CONCLUSION

As the motion picture and television industry changes, it is important as a profit participant to stay aware and seek the right advice. As with all contracts, it is especially important to plan for unforeseen changes or advances and to negotiate for meaningful audit rights.

Key Takeaways

In tapping the views of the subject matter experts, certain themes stood out:

- It is now necessary to have a far-reaching overseas distribution network to effectively release most films
- China is the single most important country to keep an eye on for a number of reasons, including its vast movie-going public and its enormous amount of investment money available to Hollywood
- The world is firmly ensconced in a digital revolution where SVOD is entrenched and growing
- Millennials are becoming more and more dominant in the entertainment marketplace, and they are causing shifts away from traditional media and are propelling the shift to SVOD
- Film producers will improve their odds by creating content that will appeal to a global audience
- Television seasons are shorter, which is changing the way profit participations are viewed and calculated
- Television production is increasing due to the proliferation of cable channels and digital services, plus it offers less risk for studios
- Vertical integration will continue to be attractive to entertainment companies
- Mega-mergers and acquisitions may further increase vertical integration and create issues for profit participants

What Does the Future Hold?

Green Hasson Janks Partner Ilan Haimoff sees a bright future for the industry.

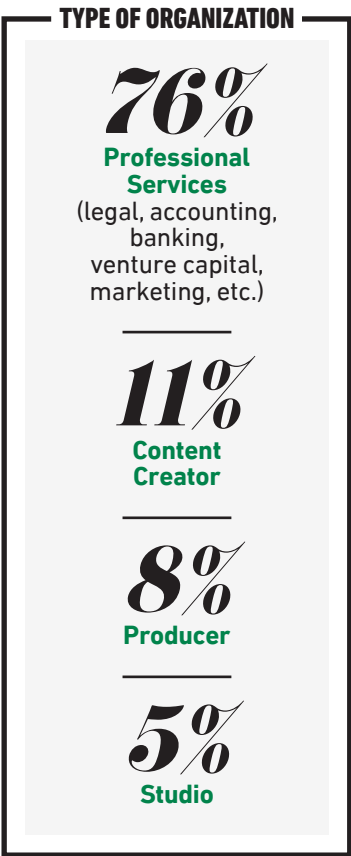
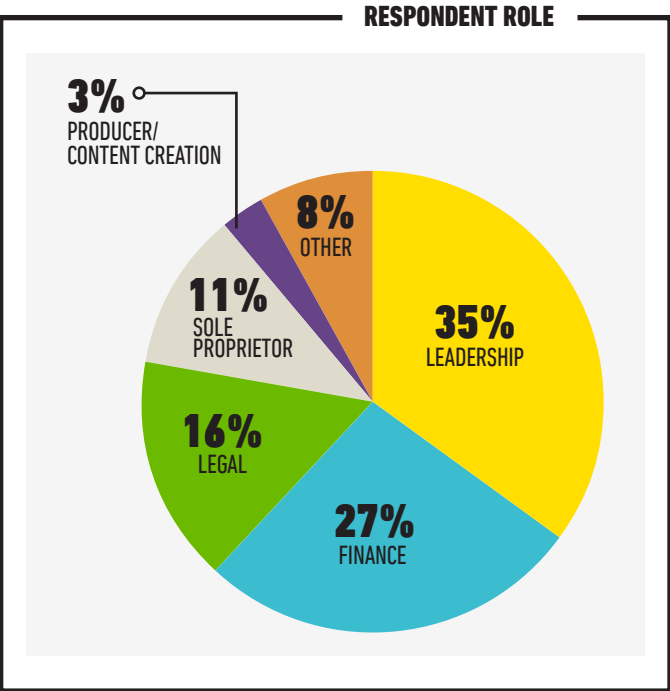
“With continued technology innovations and breakthroughs, you cannot predict the future,” Haimoff states. “During the next five to ten years, we will see the growing impact of new technology. This can mean new ways of consuming content through VR, SVOD, PVOD or anything else that emerges, and at the same time, greater opportunities for producers and distributors to sell quality content. Regardless of what the future brings, there will always be sharing of profits and risk, so participations will thrive for all of us. At Green Hasson Janks, our goal is to make sure everyone is getting their fair share.”



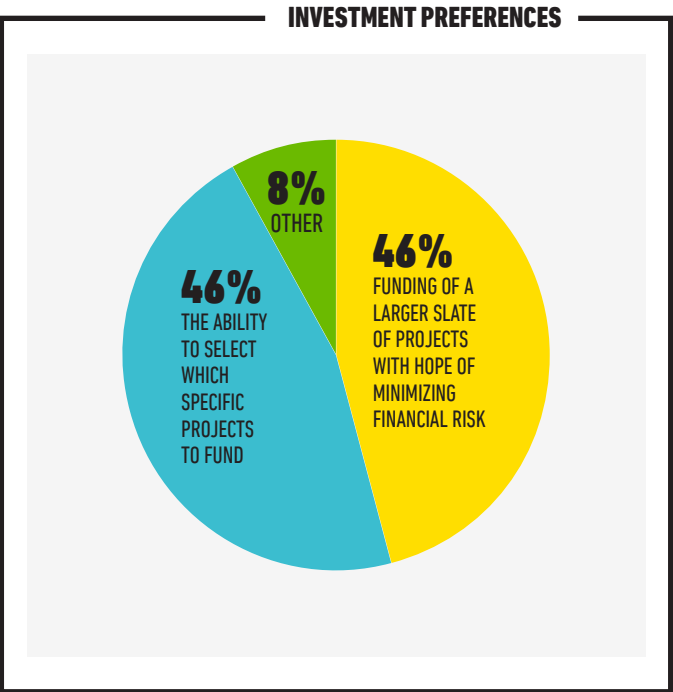
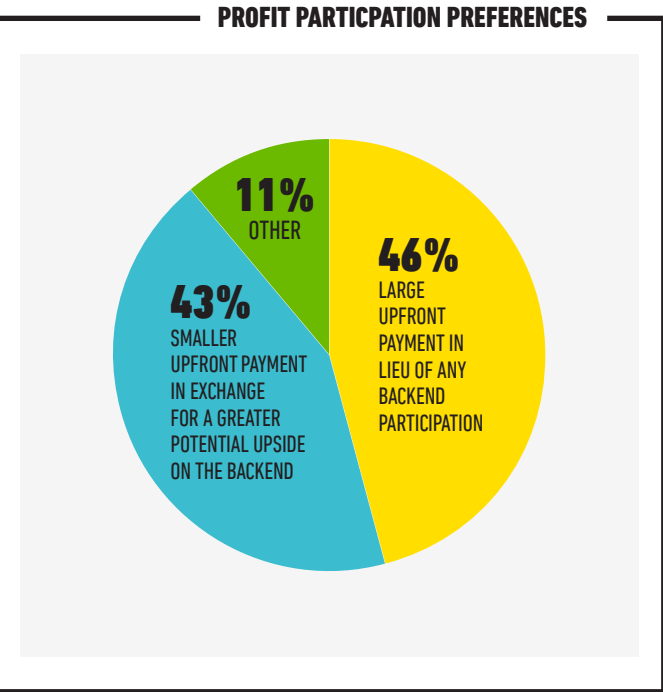
APPENDIX A: KEY TAKEAWAYS FROM THE 2017 GREEN HASSON JANKS ENTERTAINMENT SURVEY

To accompany the subject matter experts' views, Green Hasson Janks conducted a survey of movie and television industry experts.

COMPANY PROFILE

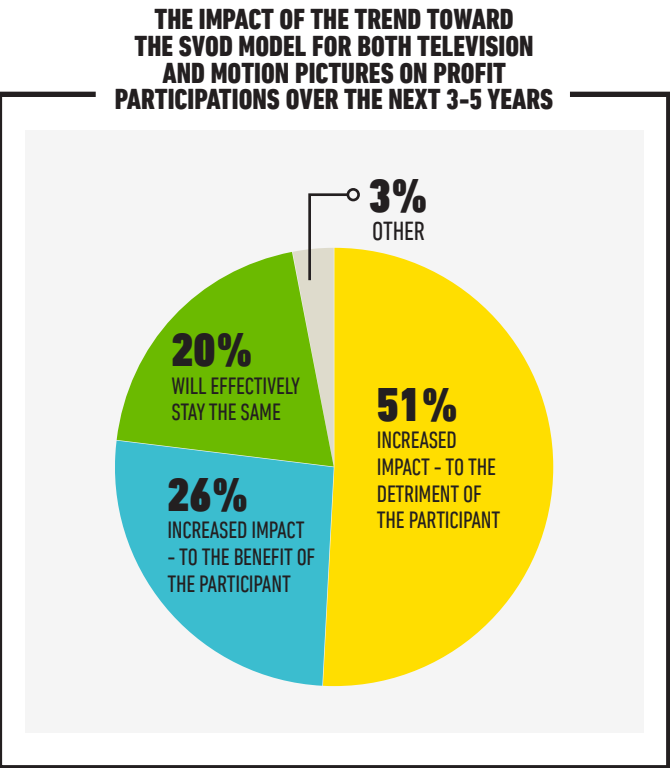
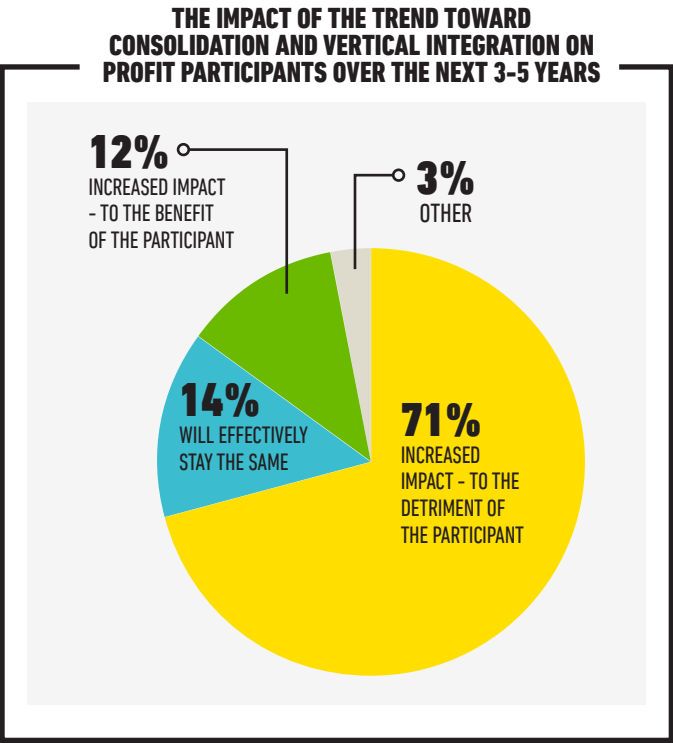
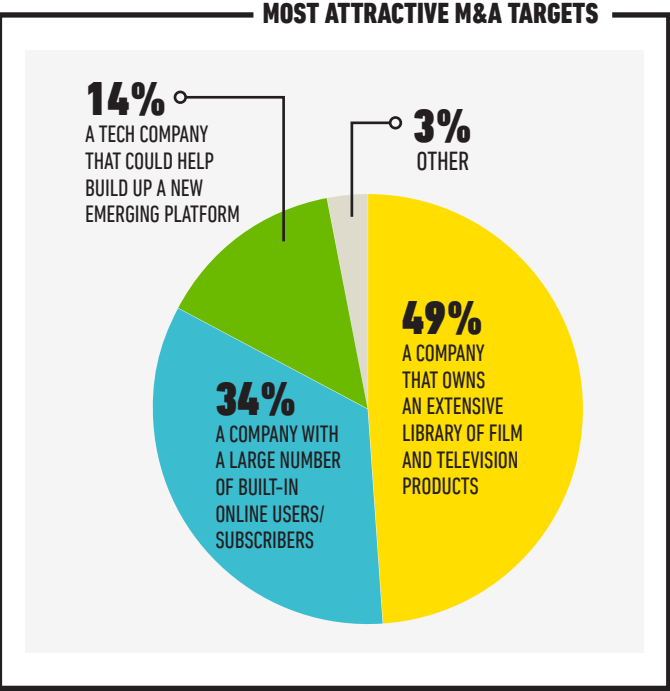


TODAY'S LANDSCAPE

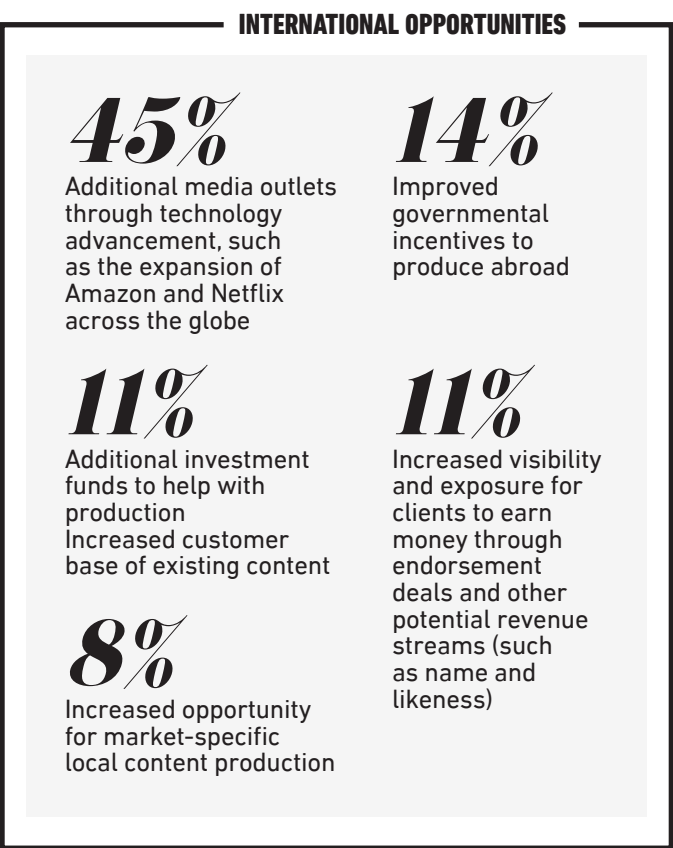


APPENDIX A

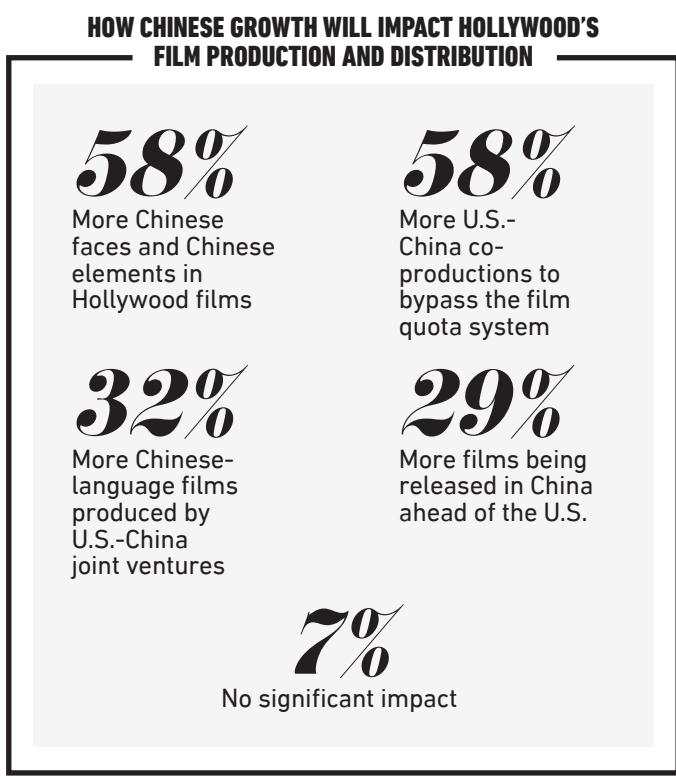
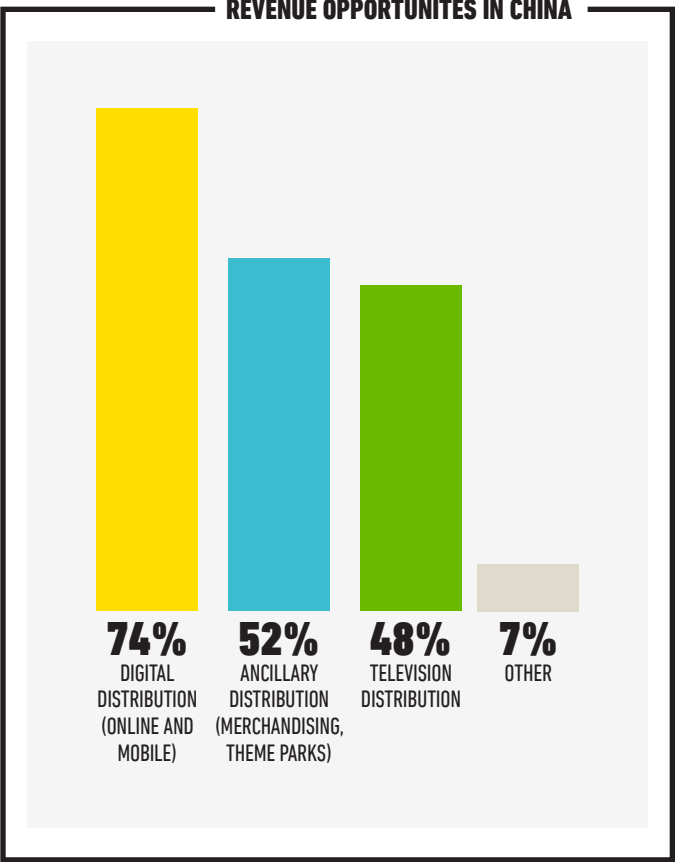
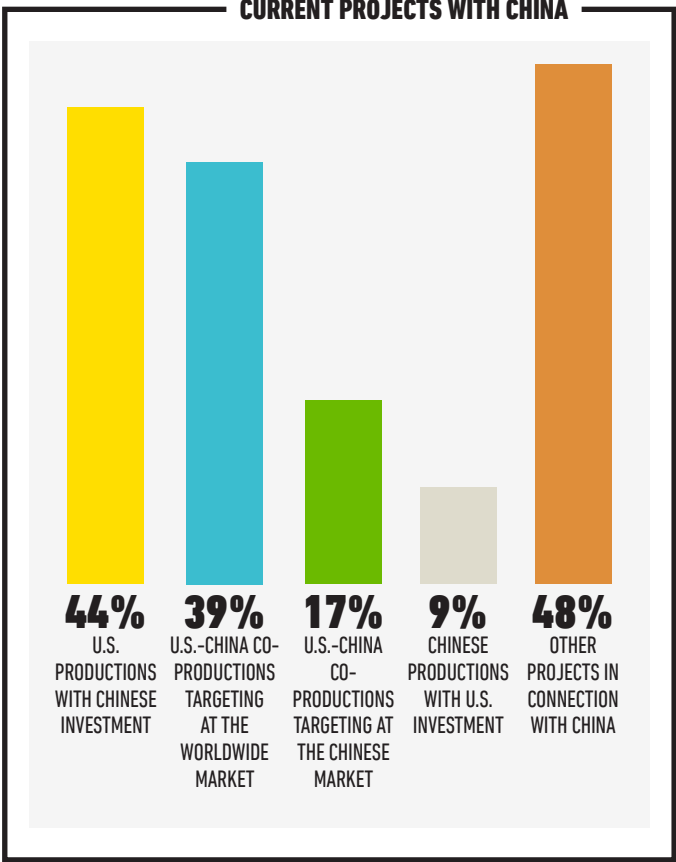
TODAY'S LANDSCAPE



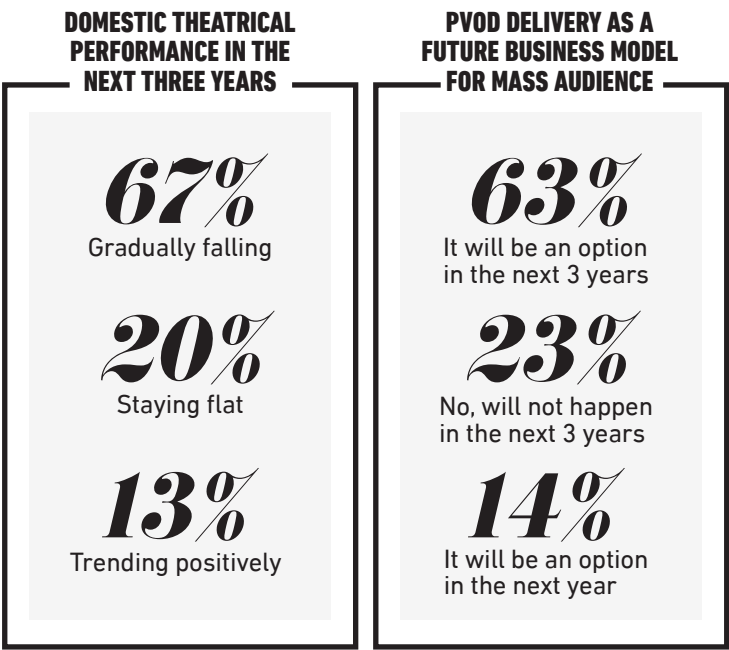
GLOBALIZATION



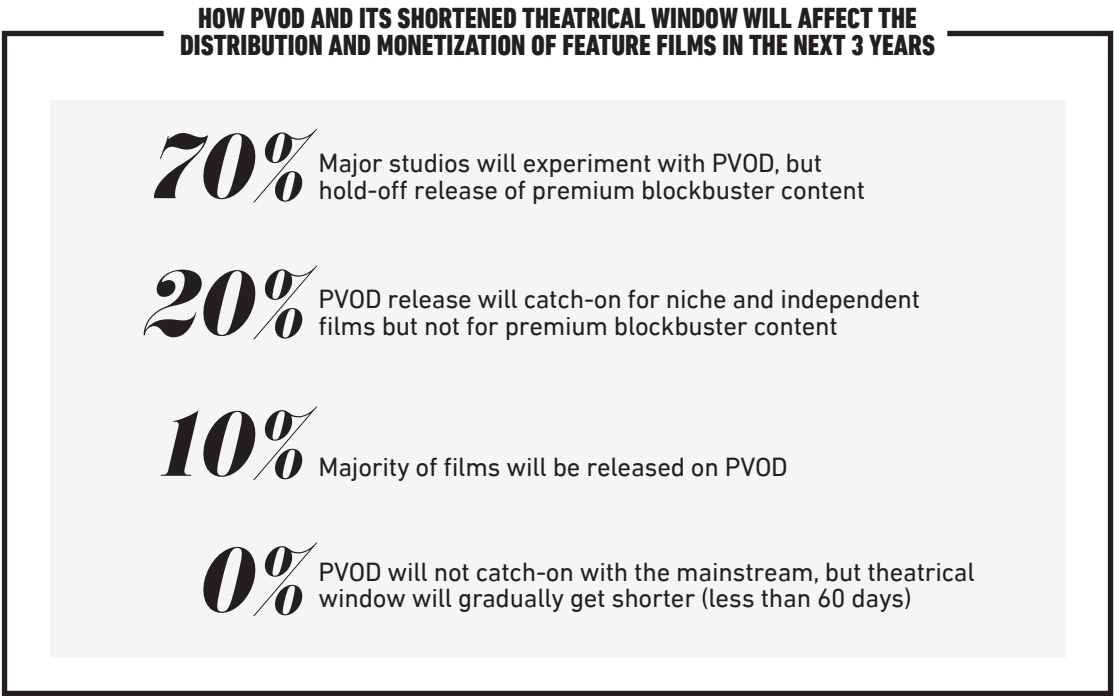
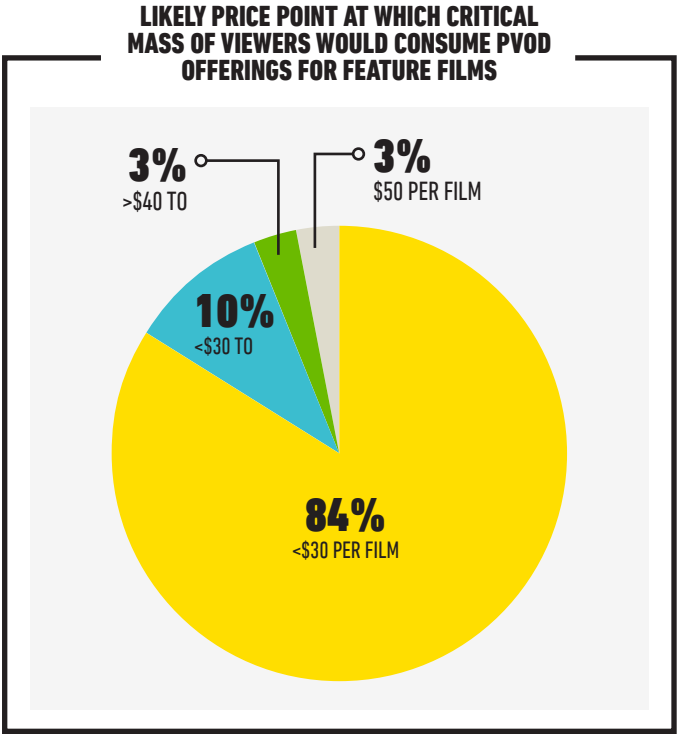
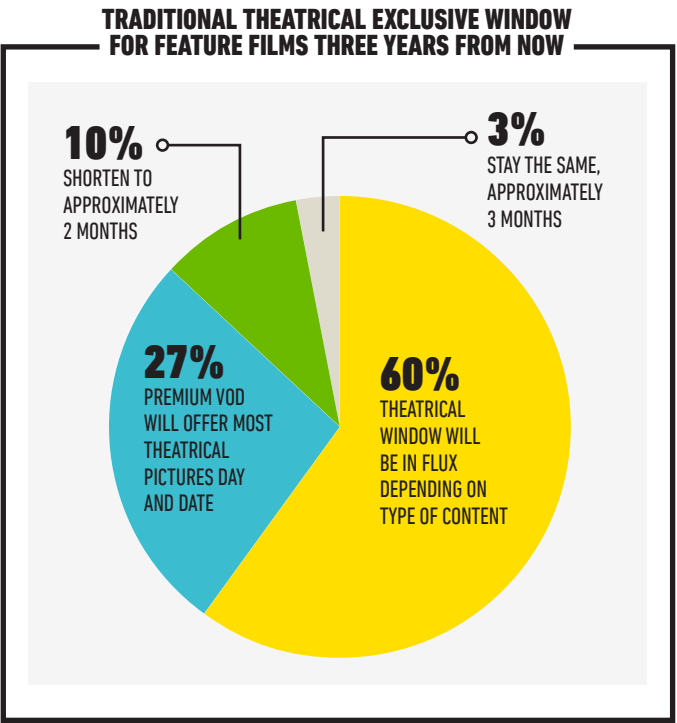
GLOBALIZATION



CRYSTAL BALL PREDICTIONS



CRYSTAL BALL PREDICTIONS





**APPENDIX B: ABOUT THE GREEN HASSON JANKS
PROFIT PARTICIPATIONS PRACTICE**



Green Hasson Janks is one of the premier profit participation audit firms in the world. We perform forensic consulting reviews of motion picture and television producers and distributors to recover money and other valuable benefits while helping enhance relationships with the third party.

We also have a team of professionals available for litigation support and witness testimony, should you require that extra level of support.

Motion Picture and Television Participation experience includes the following areas:

SERVICE OFFERINGS

- | | |
|---|--|
| <ul style="list-style-type: none">• Contract Negotiation• Digital Distributions• Distribution• Entertainment Guild Contracts• Expert Witness and Litigation Support• Joint Venture | <ul style="list-style-type: none">• Most-Favored-Nation• Participation Disputes• Residuals• Royalty/License Agreements• Theatrical Production Audits |
|---|--|

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DEDICATED STAFF FOR
STUDIO TEAM LEADERS

STUDIO	STUDIO FIELD LEADS	PARTNER
CBS	Greg Sills	Steve Sills
DISNEY	Anita Wu/Helen Leu	Steve Sills
FOX	Michael Sippel	Ilan Haimoff
HBO	Peter Klass	Steve Sills
LIONSGATE	Peter Klass	Steve Sills
MGM	Greg Sills	Steve Sills
PARAMOUNT/DREAMWORKS	Peter Klass/Michael Sippel	Ilan Haimoff
SONY	Greg Sills	Ilan Haimoff
THE WEINSTEIN COMPANY	Peter Klass	Ilan Haimoff
UNIVERSAL/NBC/FOCUS FEATURES	Anita Wu/Helen Leu	Ilan Haimoff
WARNER BROS	Sherri Carstens / Michael Sippel	Steve Sills

APPENDIX C: BIOGRAPHIES

PRINCIPAL CHAPTER AUTHORS



ILAN HAIMOFF

Ilan Haimoff leads the Entertainment and Media Practice and the Profit Participation Audit Department. His specialty includes profit participation and forensic accounting on behalf of talent, investors, and co-producers at both the major and mini studios. Ilan has over 24 years of accounting experience in public accounting and private industry serving clients primarily in the entertainment, financial services, and distribution service industries.

Haimoff has written various articles and other publications and has participated in various speaking engagements, focusing on entertainment, profit participation, royalty, internal controls, and anti-fraud.

He is a member of the Motion Picture and Television Fund Professional Advisory Council, the CalCPA Entertainment Conference planning committee (four-time co-chair), the California State University Chancellor’s Advisory Council on the Entertainment Industry, the Institute of Internal Auditors, the Beverly Hills Bar Association, the Association of Certified Fraud Examiners, and the AICPA.

Haimoff is a Certified Public Accountant (CPA), a Certified Internal Auditor (CIA), a Certified Fraud Examiner (CFE) and Certified in Financial Forensics (CFF) by the AICPA. He holds an Accounting bachelor’s degree from California State University, Northridge.



STEVE SILLS

Steve Sills has over 40 years of entertainment accounting experience. His specialty involves audits of production and distribution of motion pictures and television programs on behalf of third-party profit participants. As a consultant, he has given expert testimony in entertainment litigation, been a contract negotiator for profit and royalty participants and participated in settlement negotiations of audit claims. Sills spent 13 years at the CPA firm of Lavenhol & Horwath, before founding Sills & Adelman in 1990. In 2007, Steve Sills joined Green Hasson Janks.

Sills is an attorney, CPA, Certified Fraud Examiner and Certified Financial Forensic. He has been a featured speaker at the California Society of Certified Public Accountants and New York CPA Foundation, as well as the UCLA and USC law schools.

Sills’ publications include: *Profit Participation in the Motion Picture Industry*, Los Angeles Lawyer, April 1989; *Participants in the Motion Picture Industry*, Entertainment, Publishing and the Arts Handbook, 1987; and *Movie Money: Understanding Hollywood’s Creative Accounting Practices*, 1998 (2nd edition published in 2006).



ANITA WU

Anita Wu joined Green Hasson Janks in 2000 and has over 17 years of auditing experience within the entertainment industry. Her specialty includes profit participation audits on behalf of talent, investors and co-producers at both the major and mini studios. She currently manages most of the audits at Walt Disney Pictures and Television and NBC Universal. Anita has also performed audits of merchandise licensing royalties and music royalties.

Wu is a Certified Public Accountant and a Certified Fraud Examiner. She earned her Bachelor of Science Degree with Honors from the Haas School of Business at the University of California at Berkeley, in May 1996. During her years on campus, she actively participated as a member of the International Business Fraternity of Delta Sigma Pi.

She is a member of the Motion Picture & Television Fund Foundation — Professional Advisory Network and CalCPA.



PETER KLASS

Peter Klass has more than 15 years of entertainment accounting experience. He specializes in contractual accounting for movie and television programs with a focus on performing audits of production and distribution on behalf of profit participants. He also has consulted on entertainment litigations, profit sharing arrangements, and settlement negotiations of audit claims.

Klass began his career at Green Hasson Janks in 2009. He currently oversees participation audits and consultations at various studios, including Paramount Pictures, Lionsgate, HBO and The Weinstein Company. Prior to joining Green Hasson Janks, Klass worked at Sony Pictures Entertainment, where he managed issuance of profit participation statements and coordinating worldwide third-party audits.

Klass leads the Filmed Entertainment sub-niche at Green Hasson Janks and is a member of the Motion Picture and Television Fund. He co-authored both the firm’s 2015 whitepaper, *New Media Trends: Consolidating to Meet Consumer Demands* and the 2016 whitepaper, *The Evolution of New Media: Making Money in a World Where Digital Streaming Rules*.

Klass received his degree from the University of California, Los Angeles. He is a Certified Fraud Examiner and is a member of the Association of Certified Fraud Examiners.



MICHAEL SIPPEL

Michael Sippel is a senior manager within our Participations Audit Practice and joined the firm in 2007. He specializes in profit participation audits, contract compliance and forensics. He currently manages many of the audits at Warner Bros, Fox and Paramount/ DreamWorks.

He earned his bachelor’s degree from the University of California, Berkeley in Business and Economics.

Sippel is a CPA, CFE (Certified Fraud Examiner) and ABV (Accredited in Business Valuation). He has written numerous articles, including those related to new media, vertical integration, and “breakeven” deal structures, and has been a featured speaker at the CalCPA, as well as the UCLA and USC film schools.

INTERNAL SUBJECT MATTER EXPERTS



BEN SHEPPARD

Ben Sheppard is a principal leading Green Hasson Janks Expert Witness and Litigation support practice and has nearly 30 years of experience. He has deep expertise in litigation support and expert witness services, as well as forensic investigations and valuations. Sheppard works closely with clients to helping them find answers to situations that may pose a threat to their business.

Starting his public accounting career in Houston, Sheppard previously worked at Deloitte before moving to Los Angeles and accepting a job at Disney. Since then he has also worked for big studios such as MGM and Warner Brothers and as a consultant on litigation, forensic investigation and valuation projects.

Sheppard has offered expert witness opinions in over 35 separate matters, in state courts, federal courts and arbitrations. He has also served as a court appointed neutral expert in a state court matter.

Sheppard is a Certified Public Accountant and Certified Valuation Analyst. He is also a member of the Beverly Hills Bar Association and American Bar Association and is a frequent speaker for a variety of entertainment conferences and for other organizations. He has been published in *Wiley's Litigation Services Handbook*, Sixth Edition and *ABA's Landslide Magazine*.

Sheppard has a BBA in Management Info Systems and MBA in Accounting from the University of Houston.

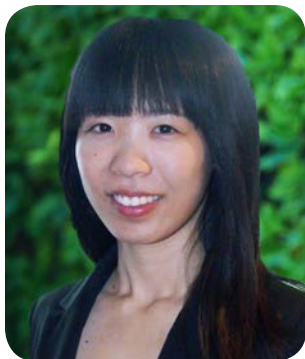


JENNIFER SULLIVAN

Jennifer Sullivan is the senior marketing manager at Green Hasson Janks and has over 15 years of experience in marketing and business development. She has a specialized focus in the areas of accounting, financial services and entertainment. Jennifer is responsible for leading, inspiring and growing the firm's brand internally and externally while advising and collaborating with her team to execute the firm's initiatives in the most efficient and innovative way possible.

Prior to Green Hasson Janks, Jennifer acted as Creative Director for an entertainment firm to rebrand the firm and execute a new marketing and business development plan to increase visibility in the sector. She also held senior positions at two other financial services firms where she opened the west coast office to increase brand eminence and expand client base on the west coast in addition to leading the frontline support team for over 100 clients invested in open end commingled real estate funds.

Jennifer obtained both a Bachelor of Arts degree in Economics and Political Science from the University of Southern California.



TRACY LIANG

Tracy is experienced in entertainment accounting and forensic investigations, specializing in contract compliance and profit participation audits in a variety of industries including film and television, video games and IP licensing.

Tracy is a licensed CPA in the state of California and is a member of the California Society of CPAs. Tracy received her bachelor degree in accounting from Shanghai University of Finance & Economics, and her master degree in accountancy from University of Illinois at Urbana-Champaign.

Tracy is fluent in Mandarin Chinese and has authored several articles on China-US entertainment.

EXTERNAL SUBJECT MATTER EXPERTS



CRAIG EMANUEL

One of the industry's leading entertainment lawyers, Craig Emanuel focuses his practice on the representation of high level writers, directors, actors, producers and production companies in all aspects of motion picture and television transactions at both the studio and independent levels. In 2016, his clients were a part of four of the Best Picture Academy Award nominees.

In addition, he handles the negotiation of strategic distribution and finance-related transactions across all platforms, including the licensing of digital content on behalf of high net worth individuals and production companies. He has also been involved in the creation and launch of a new television network.

Emanuel speaks regularly at venues such as UCLA's Entertainment Symposium, the Women in Film and Television Summit, The Sundance Producer's Lab and at various Film Independent Labs. He was previously appointed as an ambassador of Screen Singapore and has lectured to students of film and television around the world.



JOHN BERLINSKI

John Berlinski's practice focuses on representing television and theatrical talent and studios in their most significant disputes, with an emphasis on providing pre-litigation advice in connection with profit participation audits, negotiating audit settlements and litigating profit participation claims. While most of Berlinski's representations are confidential, certain matters have been the subject of articles in the Hollywood trades and *The Wall Street Journal*.

Prior to joining the firm, Berlinski spent seven years at NBCUniversal, where he was the Senior Vice President and Head of West Coast Television Litigation. At NBCUniversal, he actively participated in and managed the company's entertainment litigation docket, which included disputes involving profit participation, copyright, idea theft, right to privacy, breach of contract, labor and employment and other matters. Berlinski was previously the head lawyer for NBCUniversal's profit participation group, managing a team of attorneys dedicated to providing advice regarding the negotiation of profit participation contracts, the issuance of accounting statements, audits and the resolution of audit claims. Before joining NBCUniversal, Berlinski worked for seven years as a general litigator at a global law firm.



KEN HOLLOWAY

Ken is an accounting/finance executive and has held significant positions in the film and technology industries including Controller/CFO duties, P&L responsibilities, M&A experience and start-up ventures. He has been the SVP of Finance and Controller for the last 11 years at Endgame, with duties in both production and distribution.

Ken is a CPA and received his BSBA in accounting and marketing from the University of Arizona.

EXTERNAL SUBJECT MATTER EXPERTS



DR. SEAGULL HAIYAN SONG

Dr. Song, author of the leading treatise *Entertainment Law* in China, is Senior Advisor at Hogan Lovells and also a visiting professor at Beijing Film Academy and Peking University School of Law. Dr. Song has practiced intellectual property law and entertainment law in mainland China, Hong Kong and the United States for over 20 years. Before joining the academic world in 2012, Dr. Song was Senior Counsel with Disney, overseeing the company's intellectual property division in the Asia Pacific region, a consultant with Arnold & Porter LLP, and a partner with King and Wood Mallesons, heading the intellectual property practice of the firm's Shanghai Office. Dr. Song was acclaimed as an "Asia Law Leading Lawyer" in the field of intellectual property law 2006-2011. Dr. Song is Board Director and Executive Committee member of the Asia Society Southern California Center and also Co-Chair of the US-China Film Summit Committee. Dr. Song also sits on the Advisory Board of the China Intellectual Property Law Society and the Editorial Board of the *Journal of Copyright Society of the U.S.*

Dr. Song has published numerous books and articles in the field of US-China intellectual property law and entertainment law. Her recent books include: *Entertainment Law* (The Commercial Press, 2014); *Selected Chinese Patent Cases*, co-authoring with Chinese Supreme People's Court (Wolters Kluwer, 2014); *New Challenges of Chinese Copyright Law* (Kluwer Law International, 2011) etc.

Dr. Song received her first LL.M degree from Hong Kong University and her second LL.M and J.S.D (Doctorate of the Science of Law) from University of California, Berkeley School of Law. She is admitted to the Bar of People's Republic of China and the California Bar of the United States.

GREEN HASSON JANKS
WOULD LIKE TO ESPECIALLY
THANK THE MOTION
PICTURE TELEVISION FUND
FOR THEIR HELP WITH THIS
YEAR'S SURVEY.

THROUGH THE
MERGER IN 2007
AND CONTINUALLY
INVESTING IN
NEXT GENERATION
LEADERSHIP AND
TOP TALENT,
GREEN HASSON
JANKS IS WELL
POSITIONED TO BE
A LEADER IN PROFIT
PARTICIPATIONS
WELL INTO THE
FUTURE.

Ilan Haimoff
Partner and Entertainment
and Media Practice Leader,
Green Hasson Janks



At Green Hasson Janks, we are passionate about helping our clients and our people #BeMore by focusing on building thriving businesses and creating a better future. The firm works as a business advocate for its clients — providing personalized service and building long-term relationships to help position our clients for the future. Ranked as a top-20 largest accounting firm on the Los Angeles Business Journal's Book of Lists, the firm has 14 partners and approximately 150 staff members that serve over 3,000 clients. The firm is a member of the American Institute of Certified Public Accountants (AICPA), the AICPA Governmental Audit Quality Center (GAQC), the Public Company Accounting Oversight Board (PCAOB), the California Society of CPAs and the California Association of Nonprofits (CAN).

Green Hasson Janks is also an independent member of HLB International, a worldwide organization of professional accounting firms and business advisors represented in over 100 countries. This affiliation provides access to the subject matter experts of other member firms in most major cities around the world. Green Hasson Janks is the exclusive member firm of HLBI in Los Angeles County.

VISION

At Green Hasson Janks, we foster a flexible, entrepreneurial environment so our people achieve their personal and professional goals.

Our success is driven by retaining the best, diverse talent. We invest in our people and technology to deepen firm expertise and fuel sustainable growth. We partner with our clients locally and globally to deliver innovative solutions.

WE TRANSFORM VISION INTO REALITY BY SERVING:

- Media companies that capture our imagination
- Organizations that improve our world
- Food and beverage companies that nourish us
- Businesses that enhance our health and wellness

THE GREEN HASSON JANKS ENTERTAINMENT AND MEDIA PRACTICE

The Entertainment and Media practice focuses on helping forward-thinking, entrepreneurial organizations and individuals within the entertainment and media industry by providing assurance, tax, film and television profit participation, royalty and licensing audit, expert witness and litigation support, and consulting services designed specifically with their needs in mind. Additionally, the firm's dedicated tax team is specifically trained in dealing with complex tax issues for privately held, high-growth entertainment companies. They work with clients to identify tax planning opportunities that may apply to their businesses.

Filmed entertainment is a large section of this industry and includes everyone from production companies to directors and actors. Our Filmed Entertainment Team handles accounting, taxes, profit participation, and other consulting services for growing companies in this industry. We help clients plan for the future through personalized proactive business strategies along with performing general compliance work. We believe in being more than just our clients' accounting firm, we want to be their trusted business advisor.

In our media practice, we work with clients in the areas of advertising, marketing, digital content and new media. We have a dedicated team helping companies involved in media and technology projects gain a competitive advantage and maximize revenues through proactive accounting and strategic planning. Our experience with advertising, digital media and multi-channel networks gives us key insight into understanding issues around revenue recognition, cost allocation, accounting for content production and other complex transactions such as licensing and distribution.

An accounting firm that services tech clients not only needs to have a depth and breadth of technical expertise but also the flexibility and resources to deal with the dynamics of an industry that is constantly changing and innovating — which impact how business is conducted on a daily basis. Green Hasson Janks has the expertise that media and technology companies need to take their business to the next level.

The firm also provides its clients access to resources that highlight emerging trends and inspire thoughtful discussions amongst peers and industry leaders through surveys, industry events, blogs, whitepapers and other publications. The firm is also able to use its breadth of experience to assist clients with best practices and benchmarking to grow your business and plan for the future.