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Entertainment

What Profit Participants Need to Know -
Product Placement and Product Integration in Television

By Cesar Rodriguez

The business model for generating income through the distribution of television series has significantly evolved in recent years. For profit participants, understanding this changing face of profit models is critical to their ability to audit and maximize their participation income. Traditionally, producers have generated revenue from license fees paid by networks and syndicators, who in turn sold advertising spots which created awareness and sparked demand for commercial brands. And while traditional advertising remains a significant source of revenue, new methods of promotion, including ***product placement and product integration***, have grown as alternative approaches to creating value for brands and increasing the bottom lines for networks, producers of television series and other interested parties. These new revenue models also create additional opportunities for profit participants who understand them and account for them effectively.

Product placement involves placing a brand prominently into the actual production set where it can be easily viewed by the audience. For example, a production set resembling a computer lab may feature a specific brand of computer; the main characters in a series might continually have the same meal or coffee from a specific franchise; or a home appliance product may routinely appear in a sitcom.

Product integration goes one step further than product placement. With product integration, a brand is integrated into the storyline with specific reference to its value and characteristics. This provides not just brand awareness, but actual promotion within the featured content. It also creates an association between shows, characters and the integrated brands. For example, an action hero might drive a signature car or have a specific drink which he or she consistently mentions, making the brand not just a prop but an active element of the storyline.

In the current market place where viewers easily and frequently switch channels during commercial breaks and/or fast forward through them as they watch their pre-recorded shows, or avoid them altogether depending on the show's original broadcasting format, the use of product placement and product integration creates a substantial financial opportunity for television producers.

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Featuring people, news and business issues for the entertainment and media industry.

In This Issue

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As technologies such as DVRs and new delivery methods such as streaming content work together to modify consumer behavior and potentially devalue traditional commercials, the use of product placement and product integration may create a critical financial opportunity for television producers. In addition to providing a new revenue model and method for brand promotion, product placement and integration may also provide revenue during actual production. Rather than waiting to recoup production costs through arrangements with networks and syndicators, content producers may be able to capitalize sooner and more directly through product placement and integration.

What do product placement and integration mean from a profit participant's perspective? What should you be concerned with as it relates to profit participation payments?

1. THE EXISTENCE OF A BUSINESS ARRANGEMENT FOR PRODUCT PROMOTION.

   Despite enormous evidence of product placement that can be gathered simply by viewing a program, studios still may not account for or disclose all values received from product placement and product integration deals. Whether due to oversight, a contractual interpretation, or a combination thereof, studios sometimes fail to fully and accurately account for product placement revenue in profit participation reports. An audit of participation statements can be a great first step toward uncovering potential business arrangements of this kind.

2. THE ACCOUNTING TREATMENT ON THE PARTICIPATION STATEMENT.

   While some studios recognize the value of product placement and product integration for the profit participant, they may have accounted for the benefits as if they were another revenue stream, and charged a corresponding fee on the total amount received. A more favorable approach would be to account for these benefits as a reduction to production costs. Under this approach, the value received can be treated as a credit to the costs of production of the television series, which has a more favorable effect on the bottom line.

To illustrate this concept, the table to the right compares and illustrates the effect on the bottom line between the different approaches to accounting for product placement and integration.

As seen in the example, accounting for product placement as a reduction to production costs can have a favorable impact on the bottom line and a positive impact on the revenue of profit participants. An audit of the participation statement can reveal and potentially call into question the studio's reporting methodology.

With Hollywood's audience becoming more and more fragmented every day, major brands are willing to spend top dollar on campaigns to achieve market exclusivity and reach targeted audiences. As a result, producers and studios will continue to use innovative alternatives to answer these demands, while subsidizing the costs of production and generating additional revenue streams. In turn, product placement and product integration represent key areas that could bring meaningful value to any profit participant in a television series. &

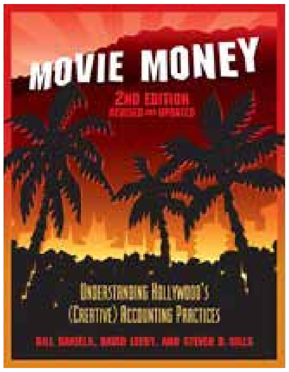
ACCOUNTING FOR PRODUCT PLACEMENT AND PRODUCT INTEGRATION

	Case A*	Case B**
Income		
Network	$ 300	$ 300
Syndication	100	100
Home Video	50	50
Merchandise	70	0
Total Receipts	**520**	**450**
Expenses		
Total Distribution Costs	**150**	**150**
Production Costs	400	400
Product Placement/Integration		-115
Total Production Costs	**400**	**285**
Total Expenses	**550**	**435**
Receipts After Expenses	**$ (30)**	**$ 15**

***Case A**
A $100 product placement deal is reported as merchandise, subject to a 30 percent studio fee.
[$70 = $100 x (1 – 30%)]

****Case B**
A $100 product placement deal is reported as a reduction to production costs, subject to a contractual 15 percent production fee by the studio.
[$115 = $100 + ($100*15%)]

In the News...



MOVIE MONEY BY **STEVEN SILLS**, AUDITING EXPERT

TALENT GETS RAW DEAL AS CONTENT DELIVERY GOES DIGITAL

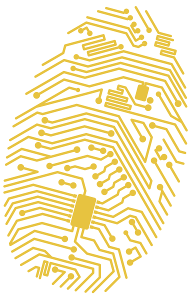
When it comes to divvying up backend homevideo money to profit participants, studios take it from a pot of just 20% of the returns. Why would the studios withhold 80%, and will this ever change? Steven Sills and other experts weigh in.

Click here to read the full article.

CRAFT TRUCK PODCAST WITH STEVEN SILLS

Steven shares some very valuable insights about his work auditing motion picture and television profit participation reports on behalf of talent, producers and investors. Learn about Steven's three tips when entering into a contract and other useful information.

Click here to listen to Jesse Truck's interview with Steven.



Using Digital Audio Recognition to Unlock Revenue Streams

By Peter Klass and Cedar Boschan

Cedar Boschan, principal at Green Hasson Janks, and Peter Klass, manager at Green Hasson Janks, recently attended the Association of Independent Music Publishers' panel discussion on "Digital Audio Recognition: Disruption and New Revenue Opportunities."

A panel of leading music industry experts discussed digital audio recognition technology and the importance of ***digital fingerprinting*** in monetizing content that is frequently infringed upon. Digital fingerprinting summarizes unique identifying characteristics of audio or video material. With sophisticated software, the fingerprints can be used to track copyrighted material on sites like YouTube.

Important highlights from the panel discussion included:

1. METADATA TELLS LICENSEES WHO TO PAY

   From copyright registration to cue sheets, quality metadata is the key to collecting cash. For example, when multiple music publishers submit disagreeing or contradictory rights information to music services, earnings are locked in an escrow account until the parties resolve the discrepancies and tell the music service who to pay.

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LES Women in Licensing Event:

New Licensing Business Models

By Vicky Farrell

The Licensing Executives Society (LES) was happy to present its first ever Women in Licensing Event. Panelists representing the Motion Picture Association of America (MPAA), Southern California Center for Technology and Innovation in Pediatrics (Children's Hospital LA), Intel Corporation, and the California Institute of Technology (CalTech) discussed trends and challenges they face in the licensing realm. The panelists provided diverse perspectives including a corporate viewpoint, as well as one from entertainment and the life sciences. Interesting highlights included:

- Ten new companies emerge out of CalTech each year.
- The Saban Research Institute at Children's Hospital of Los Angeles is aggressively involved in their business development efforts and is also looking at research that can be commercialized.
- The MPAA is trying to build and expand their partnerships outside of the entertainment industry with academia and other industry players.
- Intel is looking at licensing opportunities that are more specific in nature and narrower scope than some of the broader licenses and patents; they are also looking into M&A possibilities.
- Across the board all participants are seeking broader collaboration and expressed a strong desire to stretch their current licensing models. &

2. CHOOSE YOUR TOOLS WISELY

Not all digital audio recognition technology is the same. As Chris Woods, co-founder and COO at TuneSat, explained, Shazam was designed for mobile users to recognize songs in bars, while TuneSat was created to identify production music in TV broadcasts. The basic categories of digital recognition technology include watermarking and fingerprinting technology. Watermarking technology is considered "active" because it requires content owners to encode unique identifiers into masters in order to detect uses, while fingerprinting technology is "passive" because it works by identifying unique characteristics of a file, even if it is an old recording that was released before watermarking existed.

3. HAVE A STRATEGY

Digital rights management is a lot of work for content owners. Jeff Price, CEO and founder of Audiam, recommended sending copies of metadata to all music services so that they are informed about the copyrights and infringements may be deemed willful. Nearly all monetized musical compositions on YouTube are identified based on metadata that links a song to a master, so if a song is linked to a master that has been used thousands of times, one instantly matches such song to thousands of uses.

The Impact of the Los Angeles Business Tax on Entertainment Industry Professionals

By Akash Sehgal

The Los Angeles Business Tax ("Business Tax") has over the years been a contentious privilege tax on businesses that engage in activity within Los Angeles. The Business Tax is generally based on gross receipts generated within Los Angeles and the tax has a number of different classifications that determine the tax rate that will apply to each business. Entertainment industry professionals are generally taxed based on their specific activity, whether the income is earned directly by the individual or through a legal entity in which the individual owns an ownership interest.

Creative artists, which include directors, writers, conductors, actors, actresses and cinematographers, can benefit from the city's "creative artist exemption" which provides an exemption from Business Tax to the extent annual income from creative activities does not exceed $300,000. Once the annual income exceeds $300,000, the creative artist could be taxed on their entire income earned within Los Angeles at the highest Business Tax rate of $5.28 per every $1,000 of gross income generated. For high profile creative artists, this Business Tax can be a significant tax burden when added to California's substantial personal income tax. Over the years, various business and lobbying groups have been successful in getting favorable classification for their respective industries.

The creative artist exemption is a favorable classification that was approved by the city council in 2005 as a result of lobbying efforts. The definition of creative artist activities under the Business Tax code is broad, providing that only

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creative artists' activities include activities primarily for entertainment or aesthetic purposes. The code then lists out a number of professions that would be considered under the exemption. Unfortunately, producers do not currently fall under the definition of a "creative artist".

A producer is defined as any person who is engaged in the business of producing motion pictures, television and radio programs. Production activities include the development of a story, whether based on fact or fiction; the photographing of the story or program, whether by means of photographic film, magnetic tape, or other device; the recording of the program; and the cutting, scoring, editing, and final preparation of the picture, program or commercial for release or viewing.

Producers determine their tax based on a gross receipts and costs measurement that includes the gross cost of production, gross receipts received by the producer in return for lending of services of employees, and gross receipts received by the producer in return for the furnishing of studio facilities. The minimum annual tax to a producer is $145 and the maximum could be as high as $9,245.

As Los Angeles continues to look for ways to increase tax revenue, one area of focus will be entertainment industry professionals. Entertainment industry professionals should consider taking the following course of action in order to better understand their Business Tax compliance responsibilities:

1. Determine whether their activity is subject to the Business Tax and if so speak with a tax advisor about properly registering the business for Business Tax purposes.

2. Take steps to properly document the activity performed on each separate project. For example, clearly distinguish between activity that may fall under the creative artist exemption and activity that falls under the production category, if both activities occur during the same year.

3. To the extent you believe your activity should fall under a more favorable classification, work with a tax advisor familiar with the Business Tax to petition the city for classification under an alternative category such as the creative artist exemption.

The Business Tax is a real tax issue for entertainment industry professionals and the city plans on taking an aggressive and proactive approach to compliance and collection. Entertainment industry professionals should equally be proactive in understanding their Business Tax compliance and reporting obligations and should speak to an experienced tax professional about favorable exemptions that may apply to their activity. &

5 KEY CHALLENGES for the Video Game Industry

By ***Steve Smith*** *(Greenberg Glusker) and Ilan Haimoff*

While the video game industry has experienced significant growth in recent years, it also faces challenges which pose a significant threat to the industry. Ilan Haimoff, CPA, of Green Hasson Janks and Steve Smith, Esq., of Greenberg Glusker collaborated to identify five key challenges confronting the video game industry.

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1. Managing Potential Regulatory Changes

As video games continue to have an increasing impact on society, several questions arise. Will government agencies promulgate more restrictive regulations to minimize the perceived negative impact video games have on children? Will families and educators exert influence which will impact the direction of the industry? For example, like television and television advertising, could family and educational interest groups seek to require a percentage of games to promote education and physical health? With consumers spending as much as $20 billion annually on video games (2013 Sales Demographic and Usage Data Essential Facts published by ESA), will surcharges or other additional taxes be applied in the future? Will new regulations require game companies to make disclosures regarding "free games" that charge for upgrades and other in-app purchases?

2. Adjusting to Technological Changes

Video game distribution has been moving towards digital formats for years, and that movement will likely accelerate over the coming years. That evolution will be challenging from several angles. Game publishers and developers will need to build relationships with companies like Microsoft, Sony, Nintendo, Facebook and others to gain the attention of consumers. Gaming companies will need new ways to maintain financial margins, such as subscription fees or in-app or in-game purchase models, and companies will need to build controls and monitor for piracy in order to protect content and maximize revenue.

3. Connecting with Consumers

Connecting with the consumer in the digital age will present numerous challenges. Game developers will be under continual pressure to provide ever-improving content and graphics. Changing consumer habits and marketing shifts will require inventive ways of reaching target audiences effectively. Game publishers and producers will need to stay connected with consumers to learn about their experience and get continuous feedback, allowing them to adjust and update games as quickly as possible

4. Maintaining Profitability

Consumer demand for higher quality games based on new and expensive technology will cause several financial challenges to emerge. Producers will need to structure deals with publishers and distributors to ensure maximum value, keep development costs in check, and look for as many new revenue streams as possible.

5. Finding the Next Distribution Channel

Although consoles such as Xbox and PlayStation may still be viable and significant in terms of revenue streams, there appears to be a movement towards a limited number of franchise game properties for these consoles, creating a significant barrier of entry. Meanwhile, mobile games are complicated to distribute across multiple mobile communications formats, and social network gaming appears to be trending towards purely casual. Finally, digital free to play games represent a one in a million hit driven business. So what is the next big distribution opportunity? Some believe it may be Valve's new Steam Box console, which allows for inexpensive and rapid downloading of hundreds of games over a platform that is far less expensive than the Xbox One or PS4. &

If you are a producer, recording artist, game developer, or investor who needs assistance with royalty and licensing compliance services, Green Hasson Janks has one of the largest royalty examination teams in the United States. Green Hasson Janks examines third-party records to recover money and other benefits while helping to enhance the relationships with the third party.

To contact our royalty and licensing audit team for additional information please click here for a link to our services.

To submit future topics or provide feedback, please contact Ilan Haimoff at ihaimoff@greenhassonjanks.com

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