

CANADA FEATURE FILM FUND DISTRIBUTION TERMS & CONTRACT REQUIREMENTS

Distribution, sales agency, licensing, and sub-distribution agreements (“distribution agreements”) entered by applicants seeking or receiving financial assistance from Telefilm Canada are to be submitted to and approved by Telefilm Canada and contain provisions acceptable to Telefilm Canada. (Telefilm reserves the right to require any modifications at any time to such agreements.)

(The term distribution as used in this document shall mean distribution, subdistribution, sales agency, syndication, licensing, selling, marketing, and exploitation of any kind.)

A: Applications with a Distributor for the Canadian Theatrical Rights

For all productions where Telefilm Canada requires an eligible Canadian distribution company to be attached to the project, such attachment is to be demonstrated with a valid deal memo or agreement between the producer and the eligible Canadian distribution company, negotiated at fair market value, which outlines all rights and/or options being licensed or acquired, the territory, the term, all relevant terms and conditions, including all deductions permitted from revenues and admissible expenses. The commitment letter/agreement must guarantee the film’s theatrical release in at least its original language market in Canada within one year of its delivery.¹ In the case of double shooting or for animated productions, the distributor and producer are to decide whether the primary market is English or French and contact Telefilm Canada for approval.

If a broadcaster is also attached to the project, the broadcaster’s agreement is to provide for a minimum window, to allow for a meaningful Canadian theatrical release prior to the broadcaster rights being exploited.

Please note that Canadian distribution rights can only be held by Canadian companies. Such companies are to remain for the duration of the distribution term a Canadian-controlled corporation under the Investment Canada Act.

(Please see further below for other principles and parameters relating to distribution terms and contracts.)

B: Applications with a Distributor or Sales Agent for International Distribution Rights

- i. When international distribution rights are sold or licensed to an international sales company, Canadian or otherwise, to be considered eligible, the international sales company must:

¹ In cases where there is a distributor or sales agent for territories outside of Canada, any holdback on the release of the film within Canada must still allow for a theatrical Canadian release to occur no later than one year from delivery.

- demonstrate to Telefilm Canada's satisfaction a level of experience and expertise sufficient to arrange for the film's optimal distribution in all territories and media for which the international sales company is proposed to acquire the rights.
 - have a sufficient volume of business and business plans to ensure the company's future financial viability.
 - participate annually as an international sales company in major international markets.
 - have a proven commitment to the international distribution of independent feature films.
 - if affiliated with a Canadian broadcaster, be a separately incorporated entity, distinct from the operations of the broadcaster(s) with which it is affiliated.
 - normally sell its productions directly to foreign distributors/broadcasters without recourse to the services of a foreign sub-agent or sub-distributor.
- ii. Where some or all international rights are retained by the producer at the time of production financing, Telefilm Canada will retain the right to approve all distribution arrangements and agreements for the production, and the production company will be expected to secure the commitment of an appropriately qualified international sales company or agent as soon as possible.

(Please see further below for other principles and parameters relating to distribution terms and contracts.)

C: Applications Without a Distributor

Please refer to the current guidelines as to which projects may apply for production financing without a distributor for the Canadian theatrical rights.

A preliminary market assessment will be required with the application for production financing, which may include promotion and marketing plan and a summary of audience reach and promotional strategy. (Please refer to the current guidelines as to the specific requirements.) All distribution arrangements are subject to the prior written approval by Telefilm Canada.

D: General Principles relating to Canadian and International Distribution Arrangements

- i. Buyouts of distribution rights and/or sub-distribution rights are not generally acceptable. If this is the structure you are contemplating, please contact the business affairs department to discuss.
- ii. Default rights:
To ensure that the films which Telefilm supports have the widest possible availability to the public, distribution agreements are to include default provisions, with such provisions to include the right for the producer to recover the distribution rights in the event of bankruptcy or insolvency of the distributor/sales agent, or any act or petition that seeks creditor protection.
- iii. Preliminary Marketing and Distribution Strategy:
Applications for production financing should be accompanied by a document, agreed to by the production company and the distribution company, which analyzes the project's potential for success in the domestic and, if applicable, international theatrical marketplace. In addition to representing the distribution company's overall enthusiasm for the project, the preliminary marketing and distribution strategy should identify the following:
- a detailed description of how the box-office projections are built up given the demographics of the film,
 - anticipated P&A spend,
 - the proposed release pattern,
 - the performance of comparable films,
 - a description of the key marketable elements of the film, and
 - a description of how the proposed advertising spend drives the box-office projection, including the type of media targeted, the tie-ins, cross-promotions, etc.

iv. Distributors' Reporting Requirements:

All distribution agreements entered into by applicants to Telefilm Canada's programs are to contain provisions specifying the details to be provided by the distributor or sales agents in their reporting to producers and/or to Telefilm Canada. Telefilm Canada requires distribution reports which, at a minimum, provide the following details on a current and cumulative basis:

- 1) gross theatrical box office per territory and language version.
- 2) gross sales per territory and medium.
- 3) gross receipts per territory and medium.
- 4) foreign exchange rates (where applicable).
- 5) distribution and sub-distribution fees per territory and medium.
- 6) detailed expenses per territory and medium (where applicable).
- 7) grants received.

Distribution revenues earned during the relevant reporting period are to be reported on a cash basis.

Distribution expenses must be reported during the period in which the activity was undertaken, whether the activity was paid for during this reporting period or not. Telefilm Canada does not accept the reporting of distribution expenses in a given reporting period for activities that have not yet been undertaken.

When a collection account management agreement is in effect, reporting on the above elements from the distributor may be suspended to the extent that the collection account manager receives and relays the detailed information and underlying documentation. In any event, the distributor is still bound to retain books and records on all the above elements.

v. Audits and Distributors' Books and Records:

Applicants undertake to contractually require distributors and sales agents to maintain complete and accurate books and records of all financial transactions and other activities regarding the project, in accordance with generally accepted accounting principles.

Telefilm Canada requires in its agreements with applicants that it be permitted to audit the books and records of the distributor(s) of any production which benefits from Telefilm Canada's financial support. The applicant shall ensure that the applicant's or the applicant's appointed representative's examination and audit rights in respect of the distribution agreements are not limited to less than one time per year and that distributors and sales agents will not close or lock their books at any time during the term of any distribution agreement or for as long as the distributor/sales agents receive Production Revenues, whichever occurs later.

vi. Cross-Collateralization:

Telefilm has certain restrictions regarding the cross-collateralization of revenues and expenses:

- Cross-collateralization of Canadian and non-Canadian revenues and expenses is not allowed.
- Cross-collateralization of revenues and expenses against other titles carried by the distributor is not allowed.
- Cross-collateralization of revenues and expenses for non-Canadian territories with different recoupment schedules or different expense structures is generally not allowed, except in the instances of multiple territory agreements (excluding Canada) whereby the distributor or international sales agent pays a significant aggregate amount of money for such multiple territories and where there is an acceptable expense cap for all territories.

vii. Minimum guarantees for Canada must be clearly broken out from the minimum guarantee(s) for the US and foreign territories.

viii. If a security interest is taken by the distributor, a step-back letter acceptable to Telefilm will be required, protecting Telefilm's copyright (if applicable) and Telefilm's rights to revenues (if applicable).

E: Distribution and Sales Agency Fees

Proposed distribution fees or commissions (“fees”) are subject to Telefilm Canada’s review and approval. (Telefilm Canada may require as a condition of financial participation that proposed fees be revised or reduced.)

Fees are to be reasonable, consistent with industry standards, and provide a reasonable expectation of recoupment of funds advanced or invested by Telefilm Canada.

Under no circumstances will Telefilm Canada accept the pyramiding of fees – all fees are to be inclusive of fees/commissions payable to sub-distributors and sub-agents. (A sub-distributor/sales agent is a company hired by the distributor to negotiate sales in a territory or group of territories within the overall territory acquired by the distributor. Sub-distributor/sales agency fees are defined as those fees taken by a sub-distributor/sales agent for the business of selling the production in a territory or group of territories within the overall territory acquired by the distributor. However, a “local distributor’s fee” is NOT included. A local distributor: (a) is the company that arranges the exploitation to the end-user (i.e., the theatergoer, video retailer, the broadcaster) in the territory, and (b) usually (but not always) pays a “minimum guarantee” to acquire the exploitation rights to the film in the territory.)

i. Maximum Distribution Fees

<u>Canada</u>	<i>Maximum</i>
Theatrical	35%
Non-theatrical (including in-flight)	50%
PPV, Pay, Network, Cable, and any other TV	30%
SVOD/VOD/EST/Electronic Rental	30%
Video (Blu-ray, DVD, etc.) minimum royalty to producer	20%
Video (Blu-ray, DVD, etc.) non-royalty fee plus maximum expenses of 40% of video gross receipts	25%
Other – not to exceed without approval	25%
Merchandising and Ancillary	Negotiable case-by-case

(A Canadian theatrical distributor acquiring all rights within Canada may charge a flat fee up to 35% on all acquired rights.)

<u>USA</u>	25%*
<u>Rest of World (ROW)</u>	35%

For video sales, reserves should be reasonable and reversed/liquidated within 12 months. In all royalty models, the share retained by the distributor is calculated on gross sales and is inclusive of all fees, commissions, and expenses paid to applicable third parties, including but not limited to distributors, sub-distributors, and sales agents.

Producers will consult with Telefilm Canada if a local distributor uses a different fee structure than outlined above, or if the grant of distribution rights is on an “outright” basis, i.e., without any access to revenues based on local exploitation.

ii. Maximum Sales Agent Fees

	<i>Maximum</i>
<u>USA</u>	25%*
<u>Rest of World (ROW)</u>	35%

iii. Fees for producers and non-eligible arm's length companies

Telefilm will allow for production companies (or their related entities, including non-arms length distribution companies) to receive 15% of minimum guarantees, sales, or license fees for sales they directly complete (except for pre-sales included in the financing of the production, which shall have no sales fee deducted). Such fee shall be inclusive of any sales agent or producer's agent fees. These same provisions also apply to non-eligible distributors who have been approved to represent the film within Canada. Producers and non-eligible distributors may also claim actual, verifiable, reasonable, and customary direct third-party out-of-pocket distribution expenses, to a maximum of 10% of gross receipts.

* A sales agent or a worldwide distributor acquiring the rights for the USA and in conjunction with ROW may charge an aggregate sales fee of up to 35%, exclusive of arms-length local distributors' fees.

F: Distribution and Sales Expenses

Distribution and sales expenses are to be actual, verifiable, reasonable, and customary direct third-party out-of-pocket expenses net of discounts and rebates and similar allowances, and exclusive of salaries and overhead.

i. Expense Caps:

With respect to Canadian non-theatrical and international distribution and sales agency agreements, Telefilm Canada will generally require that such agreements provide for limitations (caps) on allowable expenses. Such expense caps should be negotiated based on reasonable projections for revenues and expenses and should generally include a cap based on either a percentage of gross sales (generally 10%) and/or an absolute dollar amount. (Such caps may be exceeded where the producer has prior written approval with the distributor or sales agent over the additional expenses and has consulted with Telefilm in advance.)

It is expected that in general, the expense cap (together with any market charges, if applicable) will be in the range of 10% of gross receipts.

The above cap is not applicable in Canada for Canadian distributors that have secured a Canadian theatrical release.

Telefilm will also consider uncapped P&A expenses in major territories where the distributor has provided a firm commitment to theatrically release the film within that territory. Such release commitment is to include an acceptable minimum number of screens and markets and should only be reducible upon unfavorable test screening results. A marketing plan would be required in such cases, outlining the anticipated P&A spend, to be at a level commensurate with the planned release.

Other distributions and sales expenses that would be allowed outside of the above cap include:

- royalties/residuals.
- versioning expenses, including all costs related to dubbing and/or sub-titling the production (and trailer into other languages) only if such expenses were not covered in the production budget or final costs as per the Telefilm production funding agreement.
- all costs related to shipping all elements of the production required by the distributor for its exploitation throughout the territory.
- all costs incurred by the distributor in connection with obtaining all clearances necessary in order to exploit the production throughout the territory, including the registration of relevant trademarks on behalf of the producer.
- encoding and conversion costs (NTSC to PAL).
- the duplication of delivery materials required to be delivered to licensees.
- censorship and re-cutting fees.
- reasonable audit and legal fees incurred in connection with collections.

ii. Distribution Expenses

Allowable distribution expenses (net of any non-recoupable financial assistance) may only be deducted by the distribution rights holders, and are costs related to:

- campaign creation,
- publicity,
- material production costs,
- printing,
- dubs (only if such expenses were not covered in the production budget or final costs as per the Telefilm production funding agreement), and
- other related costs, including packing, transportation, insurance, customs tariffs, import taxes, those related to censorship requirements and prestigious festival /market entry costs.)

Access fees and costs relating to attendance at festivals and/or markets by producers and/or distributors are not considered eligible distribution expenses. See further below for access and travel expenses related to sales.)

Non-eligible distribution expenses include, amongst other things, travel, accommodation, and living expenses for producers, distributors, and their respective employees.

iii. Sales Expenses

Allowable sales expenses (net of any non-recoupable financial assistance) may only be deducted by the international sales agent, and are costs related to:

- the reasonable and proper costs of materials delivered to local distributors (e.g., costs of manufacture, storage, vaulting, freight, delivery, and courier costs),
- outside audit fees for audits of distributors (net of any recovery of audit costs),
- advertising,
- publicity (including publicity events such as press conferences and the costs associated with the attendance of key talent, director),
- publicist fees associated with a special promotion (excluding sales agent's employees),
- outside legal expenses (to enforce any sub-distribution or third-party agreements),
- messenger and courier costs directly related to the film
- screening costs
- Attendance at film markets, including travel (except producers), booth costs, the cost of creation of promotional and publicity materials for the markets, and market advertising. * (Costs are to be reasonably allocated amongst all titles represented at the market.)

* Sales Expenses may also include a one-time market charge to be negotiated between the producer and the sales agent (and to be approved by Telefilm) to cover all costs related to cover the sales agent's attendance to film markets. There should be a corresponding commitment from the sales agent to attend to a minimum number of markets to earn the market charge. In such cases, market costs would not be a deductible expense elsewhere.

Non-eligible sales expenses are any costs not specifically listed above (unless approved by Telefilm) and include, amongst other things, travel, accommodation, and living expenses for producers, distributors, and their respective employees.

iv. Other notes applying to Expenses

Distribution expenses must be net of any non-recoupable financial assistance the distributor has received from Telefilm or elsewhere.

Interest (to a maximum of Prime + 2%) is to be included in the expense cap and may only be charged on minimum guarantees (not on P&A expenses) actually paid to producer and not yet recouped.

Interest charged on distribution advances/minimum guarantees prior to the receipt of full payment by

the producer is chargeable by the producer (to the extent that any portion thereof has not yet been paid) and must be included in the production budget. Interest charged after full payment of the distribution advance/minimum guarantee (and/or payment of any portion thereof) until such time as the advance is fully recouped, may be charged by the distributor (subject to the restrictions above) but only to the extent that such interest, together with all other chargeable distribution expenses, does not exceed the expense cap.

Financing costs, set-up fees, finder's fees, and additional material charges are to be covered by the production budget for each film and are not generally acceptable as distribution costs or as other deductions from production revenues. This would include agent's fees for securing a distributor's MG.

Unless agreed to by Telefilm, CAMA fees should represent an average of 1% of gross receipts.

G: Other Distribution Agreement Parameters

In addition to key standard terms, distribution agreements should also include the following clauses. (This is not an exhaustive list, but is intended to provide information on certain clauses that often may be absent from distribution agreements submitted to Telefilm):

- Terms should not exceed 25 years, such terms should only be renewed on mutual approval of producer and distributor/sales agent, and terms of sub-distribution/sub-agency agreements should not exceed 5 years past the expiry of the distribution/sales agency agreement.
- Multiple Territories: If a producer is contemplating the signature of a multiple territory agreement as part of the financing of the production, then such agreement should stipulate: (a) the minimum guarantee for each territory (if the recoupment structures for each territory differ from each other or if the Canadian territory is involved), and (b) the appropriate cross-collateralization wording is included in the contract (see above).
- Package Sales: a production may be sold as part of a package of productions provided that:
 - a) the distributor has made their best effort to maximize revenues for the production by selling the production separately.
 - b) the allocation of revenues and expenses among the productions sold as a package will be fair and reasonable, and
 - c) distribution reports (via notes) disclose any package sales and the allocation of the revenues and expenses to the production.
- Withholding taxes: for agreements involving international rights, withholding taxes are to be included in the distributor's gross receipts for the period in which the taxes were returned to the distributor (i.e., a distributor may only calculate fees/commissions and expenses on Gross Receipts when actually paid to the distributor and not on any amounts withheld by government sources). As such, withholding taxes are not considered to be Distribution Expenses.
- All distribution corridors and recoupment arrangements are to be explicitly confirmed in the distribution agreement.

Telefilm has full discretion in the application and interpretation of the above information to ensure that it meets the spirit and intent of this policy. In all cases Telefilm's interpretation shall prevail.

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