

## Changing modes of Film financing in India

### Introduction

The Indian film industry is considered to be the largest in the world in terms of number of films produced in various languages and released annually. In this multi-lingual industry, films are produced in Hindi, Bengali, Tamil, Telugu, and several regional languages. According to a report jointly published by the Federation of Indian Chambers of Commerce and Industry and KPMG, the current value of the Indian film industry is US\$ 2.11 billion and shall grow at 9.1% till 2013.

The two important milestones that have laid the foundation for the process of corporatisation of the Indian film industry are: the Information & Broadcasting Ministry according “*industry*” status to the film industry in May 1998 and the Finance Ministry’s announcement that the entertainment industry would be recognised as an approved activity under “*industrial concerns.*”<sup>1</sup> Since then, the Government of India has taken several initiatives to liberalize the exchange control regulations in film production and financing.

The present bulletin will discuss a short history of the film financing that was prevalent in the Indian film industry and the way it has changed over the years.

### 1.0 Transition from studio system to star system

The film industry was dominated until the 1960s by the film-making companies many of whom also owned studios (known as “*studio system*”).<sup>2</sup> They either employed or contracted with the artistes and technicians on a long-term basis. The film producers would get loans from film distributors against a minimum guarantee that the film was screened in cinemas for a fixed minimum period with no further liability of the producer or even sharing of profit or loss. This system started changing when most performers started going the freelance way since 1960s which resulted in the inception of the “*star system*” and huge escalations in film production costs. In the new changed system, distributors started paying 50% of the film-making cost leaving the rest to the producer who used other sources including conventional moneylenders, corporate resources, and promissory note system or hundi.

The *star system* emerged when the studio system collapsed and freelance performers emerged impacting the financing pattern. In the star system, actors and actresses ceased to have long-term contractual obligations towards any studio or film production firm; rather, they began to operate as freelancers commanding fees in proportion to the box office performance of their recent films.

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<sup>1</sup> Under section 2(c) of the Industrial Development Bank of India Act, 1964.

<sup>2</sup> For details please refer - <http://www.indiaonestop.com/film.htm> - as visited on April 01, 2010.

<sup>3</sup> For details please refer - [http://www.indianetzone.com/35/star\\_system\\_indian\\_cinema.htm](http://www.indianetzone.com/35/star_system_indian_cinema.htm) - as visited on April 01, 2010.

## 2.0 Institutional funding

In 1975, National Film Development Corporation Ltd., (“NFDC”),<sup>4</sup> a Government of India enterprise, was established with a view to promoting and organizing an integrated development of the Indian film industry, to foster excellence in cinema and to encourage the good cinema movement in the country. Over the years NFDC has provided a wide range of services essential to the growth of Indian cinema, and along with its predecessor, the Film Finance Corporation, has so far funded/produced over 300 films.

In December 2000, a Joint Institutional Committee on financing entertainment industry headed by the Department of Banking-Ministry of Finance, with Industrial Finance Corporation of India and Industrial Development Bank of India as its members was created. It submitted an interim report<sup>5</sup> that laid down certain norms for offering financial assistance to the film industry:

1. Institutions should extend finances only to corporate entities.
2. Besides negatives, music rights, satellite TV rights and overseas rights must also be considered as security.
3. Insurance companies must extend insurance cover for films and develop more products for the industry.
4. When financing a single film, the duration of advance may be restricted to -between 6 and 18 months.
5. Banks and FIs should work together with producers to evolve standards for financing and insuring films.
6. Creating a film industry-rating agency by pooling people from banks/FIs, eminent filmmakers and experts in the media sector to judge a filmmaker's credentials.

With the film production companies adopting corporate practices, the transparency grew and led to an environment of trust. This trust enabled the banks/FIs/insurers to deal with the industry like never before. With the growth of industry, film software soon became a \$1 billion industry by 2005, employing around 10 million people. With time, the ancillary industries like dubbing, editing, sound recording, web designing, web-casting, merchandising and promotion also started flourishing. With transparent accounting practices and assured adherence to targets and time-schedules, a buoyant approach of getting films insured, the corporatization of film industry had begun.

## 3.0 Sources of funding films- enhanced scope

The three major sources of funds for the film industry have been the distributors, music companies, and financiers. It was comparatively easier to get finance from the

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<sup>4</sup> National Film Development Corporation of India is the central agency established to encourage the good cinema movement in the country. For details please refer - <http://www.nfdcindia.com/> - as visited on April 01, 2010.

<sup>5</sup>Film Insurance & Financing in India - a case study available at - <http://www.icmrindia.org/casestudies/catalogue/Finance/Finance%20-%20Film%20Insurance%20&%20Financing%20in%20India.htm> - as visited on April 01, 2010.

distributors for producers with a good track record. Now, the producers (proprietorships, partnerships, private & public limited companies) engaged in film production in India rely essentially on self-funding, advances from other distributors against distribution agreements, advances from financiers against financing agreements, sale of negative rights, sale of music rights, bank financing, venture capital investments, equity markets, corporate sponsorships, merchandising, and sometimes also on co-production, if the budget gets inflated due to undue extension of a project.

To lease distribution rights, a producer enters into distribution agreements for a particular territory and/or period with a minimum guaranteed amount, a fixed commission/royalty on gross collections and/or both. With the Indian film industry going global and liberalization in India, foreign participation has increased that has given a fresh lease of life to the industry. Film producers, distributors, and financiers raise finances through equity and preference shares, debentures or bonds, deposits, etc and also execute financing agreements for receipt of royalty, and interests.

The Reserve Bank of India issued broad guidelines to commercial banks regarding bank finance for film production in May 2001.<sup>6</sup> Recently, some film production companies, such as Mukta Arts, have made public share issues (IPO), thus keeping out of the world of gloomy financing. The Film Federation of India is actively seeking to make film financing a viable proposition for banks and films are insured to offset possible losses for banks.

#### 4.0 Foreign participation

Apart from the local options available for film financing, foreign participation has also been encouraged in the recent past. The film production, exhibition, marketing, and distribution related services and products are permitted 100% foreign direct investment under the automatic route.<sup>7</sup> Foreign investors seeking to acquire shares of an existing Indian company engaged in film production, exhibition, or distribution are granted general permission. However, if the foreign investor had or has any existing joint venture or technology transfer/trademark agreement in the same or allied field in India, then prior approval is required from the Foreign Investment Promotion Board. If the foreign shareholder has entered into a JV in the *same field* before then a no-objection certificate of the previous JV partner and approval of the Government is also required.

There is an ever-increasing international presence<sup>8</sup> in the Indian film industry. Reliance ADA Group has entered into a production deal with DreamWorks Studios promoted by Steven Spielberg to produce films with an initial funding of US\$ 825 million for the first three years. Walt Disney has partnered with Yash Raj Films to make animated movies, the Warner Group is funding the Sippys' film projects, Viacom has a joint venture

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<sup>6</sup>For details please refer - <http://rbidocs.rbi.org.in/rbiadmin/Scripts/PublicationsView.aspx?id=2876> - as visited on April 01, 2010.

<sup>7</sup>For details please refer - <http://www.divest.nic.in/manual/chap20.htm> - as visited on April 01, 2010.

<sup>8</sup>For details please refer - <http://www.psalegal.com/pdf/Tax-Affairs-Bulletin-Issue-X12052009122947PM.pdf> - circulated in December 2009 by PSA.

with the TV 18 group to form Viacom-18, and Sony Pictures Entertainment has co-produced with Sanjay Leela Bansali Films.

While the television software, music software & distribution attracted majority of external funding till 2001, the filmed entertainment space (comprising film production, distribution, & exhibition), and niche television channels (news & current affairs) are the current favorites of investors due to favorable industry dynamics & potential growth opportunities.<sup>9</sup>

### Conclusion

Now the film producers have the necessary cover and impetus to invest more in anticipation of greater returns. With increased foreign participation, the shape of film industry is changing rapidly in India. New producers/directors are coming ahead and are exploiting the facilities available while the foreign players are making headways by executing joint venture agreements. All these efforts are ultimately adding to the diversity of the Indian film industry and providing a much-deserved international character. The government is also working with the institutions like NFDC and Film & Television Institute of India towards developing a comprehensive legal structure to get all kinds of movies insured which will definitely give a great boost to the film industry, more importantly to the film finance sector.

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<sup>9</sup>“Financing for Hindi films Shifting industry dynamics” by Sunil Khetrapal as available at <http://www.indiantelevision.com/special/y2k4/filmfinancing.htm> - as visited on April 13, 2010.