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Equity Crowdfunding Won't Be Equitable

Emily Best · Wednesday, April 8th, 2015

Last week, the SEC issued new rules governing equity crowdfunding, that will allow small investors to become profit participants.

Should we in the filmmaking community, especially those of us who are independent, be cheering?

As an industry, we're still reeling from the drop in DVD sales and the rise of cheap production. We haven't adjusted our business models for the low return world. But a lot of really smart people are working on that problem and need a little more time. We're still in the process of a massive re-education and re-set. Independent film does not lack funding. About $4 billion is spent a year on independent film, as much as any of the studios. So, I don't think financing is a big problem to solve (equitable distribution of that financing to diverse voices – that's still a problem to solve.) But only around 2% of those films make their money back. Let me say that in a more meaningful way: 98% of films do not produce a financial return to their investors. Why would you ask people to invest in films when you know – almost for sure – they won't make money? Financing is not what is broken in film, it's the distribution model that does not return whatever money is made back to the investors and creators. Films that make money at the box office don't return to their investors because there are too many people in between taking a cut. Until we can get returns to investors up, we have no business asking people to invest.

Perks based crowdfunding works very well for filmmakers – the "success" their contributors want is the completion and delivery of the film and the incentives they were promised. Right now, the vast majority of films that crowdfund are successful by these standards. If you add to that "success" metric financial return of the film, the vast majority of films will no longer be successful by audience standards. Then crowdfunding becomes just as star-driven as Hollywood, and full of snake oil salesmen. (Who are the only ones, in my opinion, who would offer a 2% chance at return as an exciting opportunity.)

Crowdfunding works because people invest their own social capital into their projects. It's why it's a relatively trustworthy thing to get involved in – their family and friends (or the audience they've been growing over time) contribute first and send the signal to the rest of the crowd it's ok to pile on. The SEC has built 500 pages of rules around the 4 pages of legislation because they, too, think this is an area ripe for snake oil salesmen. That's why the regulatory burdens the new rules place are so absurdly expensive and difficult to comply with. Which means the third party platforms and their legal teams will take a big chunk of the raise, which can't be higher than $1 million (at my last read of the rules). That puts just as many third parties to a film's revenue as before while massively increasing the upfront costs. The current 2% return rate risks burning and entire new class of crowdfunding contributors and future film investors.

Essentially, it's too early for equity crowdfunding. It's a huge distraction from the much bigger problem, but it's sexy and new and upstream from distribution so it's attractive.

I honestly hope I'm proven wrong, that the film industry takes a very responsible approach moving forward, is transparent about their findings, and that the tech and trade media don't pile on and publish a lot of garbage information coming directly from the sites who stand to make a lot of money on the hopes of independent filmmakers without accurately making them aware of the greater risks of promising something you know you cannot deliver.

On the other hand, maybe a responsibility to a wider pool of investors will be the impetus for more filmmakers considering themselves entrepreneurs. That would be an exceptional outcome.

This is an updated version of the author's thoughts that previously appeared in No Film School.

Top image: A still from Charlie Kaufman's Kickstarter video for the film Anomalisa, which raised $406,237 in non-equity money.

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