

Kickstarting Litigation: What is the Future of Crowdfunded Films?

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On April 12, 2013, *The Veronica Mars Movie* project broke fund raising records, with 91,585 backers pledging a total of \$5,702,153. The catch? The film was funded on the crowdfunding website, Kickstarter. *Veronica Mars* became the site's fastest project to reach a million dollars in funding, its highest-funded film project, and its third highest-funded project overall.¹ The return of the cult-television hit made news² and highlighted important legal questions, now that direct public investment and involvement through "crowdfunding" has reached such levels.

The history of arts patronage, at least in the west, goes back to ancient Rome, though it is perhaps best remembered from fabulous examples of Renaissance art. The rise of bourgeois capitalism shifted the patronage system, at least for the arts, towards publicly-supported systems, such as public museums. Patronage on a large scale still exists today, as evidenced by the Disney Concert Halls and American Airlines Theatres of the world, but for the most part, corporate sponsors have replaced private individuals. In the social media age, we now have "micropatronage"³ in the form of crowdfunding artistic works.

¹ Rob Thomas, "The Veronica Mars Movie Project," <https://www.kickstarter.com/projects/559914737/the-veronica-mars-movie-project>.

² See, "Veronica Mars Lives!," *Entertainment Weekly*, Feb. 12, 2014 at 9:00 AM, <http://popwatch.ew.com/2014/02/12/this-weeks-cover-veronica-mars-movie-first-look/> (accessed 2/12/14 9:33 AM); Erin Strecker, 'Veronica Mars' movie is a go! 'My mind is blown' says Rob Thomas -- EXCLUSIVE, *Entertainment Weekly*, Mar 13, 2013 at 8:55PM, <http://insidetv.ew.com/2013/03/13/veronica-mars-movie-is-a-go-kickstarter/> (accessed 2/12/14 9:35 AM).

³ Jenna Wortham, "A Few Dollars at a Time, Patrons Support Artists on the Web," *New York Times* August 24, 2009 (available at http://www.nytimes.com/2009/08/25/technology/start-ups/25kick.html?_r=2&em&) (accessed 2/12/10:50 AM)

So, what is crowdfunding? A prime example is the internet funding platform Kickstarter, which “uses the Web to match aspiring da Vincis and Spielbergs with mini-Medicis who are willing to chip in a few dollars toward their projects.”⁴ As one of its founders explains, “[i]t’s not an investment, lending or a charity. It’s something else in the middle: a sustainable marketplace where people exchange goods for services or some other benefit and receive some value.”⁵ The basic premise is that it provides a meeting place where individuals contribute small amounts, categorized at a certain patronage level, that promise rewards in return—usually insider access or small mementos of emotional more than financial value⁶—to a project that fits into one of Kickstarter’s self-limited thirteen categories.⁷

The results have been remarkable: since 2009 Kickstarter has secured more than one billion dollars for its projects from more than five million backers, of whom more than one million are repeat backers.⁸ Successful projects have debuted at film festivals including Sundance and Tribeca, received nominations from award shows such as the Oscars, and climbed the Billboard charts.⁹ And while it is easy to marvel at these successes, crowdfunded films raise interesting and unresolved legal issues, which this article will briefly examine through the lens of the Kickstarter example.

Intellectual Property: Who Owns What?

The Kickstarter website announces that the designers, filmmaker, producers, and other participants in the projects hosted on the site have “complete control” over the projects, and the platform merely takes a cut (usually 5% for Kickstarter, plus 3 to 5% for Amazon Payments,

⁴ *Id.*

⁵ *Id.*

⁶ *Id.*

⁷ The categories are: Art, Comics, Dance, Design, Fashion, Film, Food, Games, Music, Photography, Publishing, Technology, and Theater. “Guidelines,” https://www.kickstarter.com/help/guidelines?ref=help_nav (accessed 3/4/14, 12:37 PM).

⁸ “Kickstarter Stats,” https://www.kickstarter.com/help/stats?ref=help_nav (accessed 3/4/14, 12:32 PM).

⁹ “Press,” <https://www.kickstarter.com/press> (accessed 3/4/14, 12:22 PM).

which runs the actual pledge processing¹⁰) for hosting and publicizing the project. If the project raises its minimum amount, each backer is charged the amount she promised; and if the minimum is not met, no pledged funds are actually collected.¹¹ Kickstarter is explicit that project creators retain ownership over their work and the backers' funds are mere donations, which are neither refundable nor a true investment with the possibility of a profitable return.¹²

While Kickstarter disavows any liability for contract or license disputes, or the intellectual property of the respective users of the service, it does, interestingly, take a free license for itself to use and exploit any and all submissions to the site, as well as to allow users to “stream, transmit, playback, download, display, feature, distribute, collect, and otherwise use the User Submissions and Trademarks in connection with the Service.”¹³ So while the projects being funded are the property of the creators, the information and media they actually upload to the Kickstarter website, such as the videos explaining the project and requesting funding, are fair game. And while the service promises compliance with the Digital Millennium Copyright Act,¹⁴ this is small comfort to content distributors, whose current encryption systems and legal enforcement of intellectual property claims have had only a modest impact on piracy.¹⁵ In fact, the Better Business Bureau has given Kickstarter an F rating (its lowest) for its failure to address copyright and patent issues.¹⁶

¹⁰ “Fees,” <https://www.kickstarter.com/help/fees> (accessed 3/4/14, 12:05 PM).

¹¹ “FAQ,” https://www.kickstarter.com/help/faq/kickstarter+basics?ref=help_nav (accessed 3/4/14, 12 :02 PM).

¹² “Press,” <https://www.kickstarter.com/press> (accessed 3/4/14, 12:28 PM).

¹³ *Id.* Kickstarter uses the terms “Creators” and “Backers” to reflect the two sides of the equation, and the term “Users” to mean Creators and Backers together.

¹⁴ U.S. Copyright Act, 17 U.S.C. §512.

¹⁵ Jon Garon, “Content, Control, and the Socially Networked Film.” 48 U. Louisville L. Rev. 771, 782 (2010).

¹⁶ BBB Business Review: Kickstarter <http://www.bbb.org/new-york-city/business-reviews/professional-fundraiser/kickstarter-inc-in-new-york-ny-137092>; see also, Charles Luzar, “Kickstarter, Lawsuits, and an F from the BBB,” *Crowdfund Insider* August 22, 2013, 7:23 PM, available at <http://www.crowdfundinsider.com/2013/08/21221-kickstarter-lawsuits-f-bbb-better-business-bureau/>.

And intellectual property issues, there are many. With the collapse of the studio system in the second half of the twentieth century, the film industry lost many of its anti-piracy safeguards,¹⁷ and technological innovation has kept them on edge ever since. *Sony Corp. of America v. Universal City Studios*¹⁸ litigated the issue of personal recording for personal use and its impact on movie-going, in which the studios alleged that such viewing of films crossed copyright boundaries so as to strip the rights holder of her control.¹⁹ *Sony Corp.* demonstrated a “groundbreaking” jurisprudence and recognition that devices that are *capable* of infringing uses are not automatically subject to “secondary copyright liability.”²⁰ This modern fair use jurisprudence has important implications for the future of the entertainment industry as consumers are brought into direct contact with media and as old methods of distribution and advertising are replaced by social media sharing and crowdfunding. As viewers take more control of how they consume media, the lines between owner or licensee and third party become blurred. The threat of unintentional digital piracy, already an issue, could increase as content is shared faster than can be controlled by investors who may believe they have rights to the content. Digital piracy, both intentional and not, is a constant threat and is unlikely to abate anytime soon.²¹

As the pace of innovation increases, the push for “the next big thing” may lead to unfair or corrupt practices. Trade secrets become easy to obtain when numerous “backers” are given

¹⁷ The Motion Picture Production Company, which encompassed all of the major early Hollywood studios and ensured their hegemony through technological patent litigation, was trustbusted in 1915 in *US v. MPPC*, 225 F.800 (D.C. Pa 1915) and the vertically-integrated studio system itself fell apart in the 1970s. See, Jon Garon, “Content, Control, and the Socially Networked Film.” 48 U. Louisville L. Rev. 771, 776 (2010).

¹⁸ 464 U.S. 417 (1984).

¹⁹ Jon Garon, “Content, Control, and the Socially Networked Film.” 48 U. Louisville L. Rev. 771, 778-79 (2010).

²⁰ *Id.* at 780.

²¹ For more information on the issue of digital piracy in the entertainment industry, see, Amy Bunk, *Validity, Construction, and Application of Digital Millennium Copyright Act*, 179 A.L.R. Fed. 319; Jay Dratler, Jr., *Cyberlaw: Intellectual Property in the Digital Millennium*, 2014 ALM Media Properties, LLC.; see, e.g., *Universal City Studios v. Corley*, 273 F.3d 429 (2d Cir. 2001).

sneak peeks or insider information as part of the perks package, which raises the specter of litigation over existing patents or intellectual property that would have been patented. The marketplace technology itself comes with piracy litigation fears: Kickstarter in particular has faced other crowdfunding platforms in court on patent infringement claims for donation models and collection software.²² Kickstarter specializes in creative endeavors, but it lacks external safeguards for the ideas posted to it. The site has already been involved in litigation for patent infringement based on its hosting of a project that may have infringed a third party patent,²³ and has hosted several fraudulent or plagiarized projects.²⁴

With the digitization of media and the rise of personal viewing devices, “the audience has slowly but inexorably gained control over the content it consumes.”²⁵ Crowdfunding is a step along the path of direct-to-consumer developments in an age of increasing audience participation on all fronts. Audience hunger for active participation is age-old, and has spawned derivative works,²⁶ the ownership of which is often called into question.²⁷ Further, audience involvement with content in the planning stage calls into question the very artistic ownership of new works. This situation already came to fruition in 2003 in a case with a Baltimore Ravens fan’s copyright claims regarding the team’s use of a logo similar to one he created.²⁸ The fan, unsolicited, sent a sketch of a logo for the new team as they left Cleveland for Baltimore, asking only that the

²² See *Kickstarter, Inc. v. Artistshare, Inc.*, 2012 U.S. Dist. LEXIS 50444 (S.D.N.Y. Apr. 10, 2012); *Kickstarter, Inc. v. Fan Funded, LLC*, 2013 U.S. Dist. LEXIS 8112 (S.D.N.Y. Jan. 16, 2013).

²³ Michael Rundle, “Kickstarter Sued: Formlabs 3D Printer Accused of Patent Breach,” *Huffington Post* 11/22/2012 10:47 GMT; Joseph Flaherty, “3d Systems Sues Formlabs and Kickstarter for Patent Infringement,” *Wired* 11/21/12 12:16 PM; original complaint *3D Systems v. Formlabs et. al.* available at <http://www.scribd.com/doc/113999366/3D-Systems-v-Formlabs-et-al>.

²⁴ Sam Biddle, “NYU Film Student Plagiarizes His Way to Kickstarter Fame,” *Gizmodo* 5/09/11, 2:00 PM, available at <http://gizmodo.com/5800006/nyu-film-student-fraud-plagiarizes-his-way-to-kickstarter-fame>; Joshua Clover, “Amanda Palmer’s Accidental Experiment with Real Communism,” *The New Yorker* 10/2/12, available at <http://www.newyorker.com/online/blogs/culture/2012/10/amanda-palmers-kickstarter-scandal.html>.

²⁵ Jon Garon, “Content, Control, and the Socially Networked Film.” 48 U. Louisville L. Rev. 771, 787 (2010).

²⁶ *Id.* at 796.

²⁷ Especially before the 1976 Copyright Act extended term limits to unpublished work.

²⁸ *Bouchat v. Baltimore Ravens Football Club, Inc.*, 346 F.3d 514 (4th Cir. 2003).

company send him a letter of recognition and a signed helmet if they used the design.²⁹ The original trial found that the team had mistakenly incorporated the design into their official logo without proper accreditation. Although the team eventually escaped liability for actual damages, the case highlights the potential dangers of fan involvement in creative endeavors. Who is the true owner of the final work when hundreds of comments and suggestions pour in for a work in progress? Such liability fears could limit artistic innovation or stifle creators' acceptance of crowd participation in the future.

Contracts: Kickstarting Liability?

Crowdfunding platforms are third-party platforms with little to no responsibility for the actual projects or other follow-through, specifically disavowing any fiduciary duty or special relationship to users.³⁰ Kickstarter does, however, promise backers that the creators supported through the portal are “legally obligated to fulfill the promises of their project[s],” via the site’s terms of service.³¹ What exactly the promise of “legal action on behalf of . . . backers”³² comprises, though, is an issue that has not yet been litigated. In general, crowdfunding seems to be an example of caveat emptor. The uncertainty of donor relationships in the case of a crowdfunded film is exacerbated by the fact that donors do not receive tax exemptions for their gifts. In traditional philanthropic endeavors, including the arts, the permanent severance of a gift was cemented by a tax write-off. Kickstarter straddles the divide between traditional philanthropy and investment, and confusion is bound to occur. Similarly, a project, once accepted on Kickstarter, is not guaranteed continued hosting or provided any specific warranties. The website’s terms of service reserve the right to deny service for any reason: “The Company

²⁹ *Id.* at 516.

³⁰ “Terms of Use,” <https://www.kickstarter.com/terms-of-use?ref=footer> (accessed 3/4/14, 12:49 PM).

³¹ FAQ,” https://www.kickstarter.com/help/faq/kickstarter+basics?ref=help_nav (accessed 3/4/14, 12 :02 PM).

³² See the warning creators see before they create a project: <https://ksr-assets.s3.amazonaws.com/creator-responsibility.png> (accessed 3/25/14, 11:35 PM).

may assign, transfer, or delegate any of its rights and obligations hereunder without consent.”³³

As crowdfunding develops and becomes more common, the responsibility, contractual or not, of the platforms and sites will most likely have to be litigated.

A separate contractual issue for crowdfunding of new media involves not the creation of content, but instead its distribution. Distribution includes advertising, marketing, rental, physical distribution, and payment collection. Today, the studios are still the major players in distribution because they have the necessary infrastructure,³⁴ but direct interaction between creators and audience has recently “allowed content creators to replace supply chains with . . . one-to-one relationships between client suppliers and the consumers.”³⁵ Traditionally, the distributor had a monopoly over the content and the method of distribution.³⁶ However, audience members as taste-shaping connoisseurs and promoters increasingly utilize crowdfunding. The power of social media enables fans to disseminate works or information with stunning speed. This “curatorial” power has the “potential to reshape the marketing and eventually the green-lighting process for new media.”³⁷ Whereas content owners used to rely on physical objects to control supply, the medium matters less and less now, breaking down the traditional contractual relationships between creators and distributors, and between distributors and consumers. But what are the responsibilities of backers to a project? Kickstarter’s terms of use describe that project creators and backers enter into direct contracts:

By creating a fundraising campaign on Kickstarter, you as the Project Creator are offering the public the opportunity to enter into a contract with you. By backing a fundraising campaign on Kickstarter, you as the Backer accept that offer and the contract between Backer and Project Creator is formed. Kickstarter is not a party

³³ “Terms of Use,” <https://www.kickstarter.com/terms-of-use?ref=footer> (accessed 3/5/14, 10:55 PM).

³⁴ See, Interview with Doug E. Doug, Feb. 11, 2014, Bloomberg TV “Taking Stock,” available at <http://www.bloomberg.com/video/how-filmmakers-use-kickstarter-to-distribute-films-rb92K68XT6qA9~gg8p43UA.html>.

³⁵ Jon Garon, “Content, Control, and the Socially Networked Film.” 48 U. Louisville L. Rev. 771, 787 (2010).

³⁶ *Id.* at 788-89.

³⁷ *Id.* at 796.

to that agreement between the Backer and Project Creator. All dealings are solely between Users.³⁸

Is it realistic for an artistic creator to enter into separate contracts with thousands of funders? Is an implied contract created via the click-through process to confirm one's donation? If there are any real terms or restrictions imputed, does this approach raise issues of fraud or contracts of adhesion?

Regulatory Law: Harnessing Crowdfunding

For many years, the SEC was wary of crowdfunding, as there was little government infrastructure to regulate it. This situation changed with the passage of the 2012 Jumpstart Our Business Startups Act.³⁹ Title II of the Act directly addresses crowdfunding, wherein startups can raise “actual investment funds from individuals in exchange for equity or a share of profits.”⁴⁰ The law's goal was to help restart the stalled economy by removing regulatory restrictions to crowdfund-based models of profit-seeking investment, based off the success of donative models like Kickstarter.⁴¹ Until the rules are fully promulgated, it remains unlawful for content creators and marketplace websites to offer true investment opportunities.⁴² However, upon finalization of the SEC draft rules published on October 23, 2013,⁴³ companies will be able to raise up to one million dollars each in investments during a calendar year without registering with the SEC themselves by utilizing SEC-registered online “funding portals.”⁴⁴ The companies will not be soliciting donations, but will be finding “real” investors and selling stock in the company or

³⁸ “Terms of Use,” <https://www.kickstarter.com/terms-of-use?ref=footer> (accessed 3/4/14, 12:40 PM).

³⁹ Pub. L. No. 112-106, 126 Stat. 306 (2012).

⁴⁰ Larry Downes, “Crowdfunding's Big-Bang Moment,” *Harvard Business Review* 10/28/13 9:52 AM (available at <http://blogs.hbr.org/2013/10/crowdfundings-big-bang-moment/>).

⁴¹ JOBS Act, 158 Cong. Rec. H 1586 (March 27, 2012).

⁴² “Information Regarding the Use of the Crowdfunding Exemption in the JOBS Act” 3/5/14 5:00 PM (available at <http://www.sec.gov/spotlight/jobsact/crowdfundingexemption.htm>).

⁴³ “SEC Issues Proposal on Crowdfunding,” Press Release Washington D.C., 10/13/13 (available at www.sec.gov/News/PressRelease/Detail/PressRelease/1370540017677#.UxaRvbRsvdk).

⁴⁴ Larry Downes, “Crowdfunding's Big-Bang Moment,” *Harvard Business Review* 10/28/13 9:52 AM (available at <http://blogs.hbr.org/2013/10/crowdfundings-big-bang-moment/>).

project.⁴⁵ This dramatically improves the crowdfunding model already sweeping the entertainment industry and may influence significant investment in future films or entertainment endeavors. On the other side, there would remain particular risk for “vulnerable investors lacking ‘financial sophistication,’”⁴⁶ the very type of donors crowdfunding frequently attracts, especially considering the minimal safeguards to protect against fraud currently in place on platform sites themselves. Should the SEC be able to protect investors from “bad investments,” though, or even be able to make such a determination? The line in crowdfunding between donative intent and actual investment could be quite thin in practice. Despite such fears to the contrary, though, it seems more likely that based on the characteristics of today’s investors, the JOBS Act’s proposed crowdfunding regulations substantially limiting the amount an individual can invest provide “adequate provisions” such that “concerns about investor protection are unfounded.”⁴⁷

Conclusion

While Kickstarter and crowdfunding offer a tantalizing glimpse into a potential future of entertainment production, that future is by no means settled. Many of the issues described will most likely be resolved through litigation, and before that, we can merely sit back and watch the drama on and off screen.

⁴⁵ Kendall Almerico, “Will Equity Crowdfunding Be the Death of Kickstarter?” *Entrepreneur* 1/29/14 (available at <http://www.entrepreneur.com/article/231085>)

⁴⁶ Karina Sigar, Comment: FRET NO MORE: INAPPLICABILITY OF CROWDFUNDING CONCERNS IN THE INTERNET AGE AND THE JOBS ACT’S SAFEGUARDS, 64 *Admin L. Rev.* 473, 476.

⁴⁷ *Id.* at 478.