

## Calling All Angels: How Investment Backers Can Finance A Demo Album

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### Introduction

As any unsigned artist almost certainly knows from experience, one of the most difficult and frustrating aspects of starting out in the music industry is producing a high-quality demo tape acceptable by today's standards. The days of sending in a rough cut of yourself singing cover tunes in your basement are over, for better or for worse. In today's market, major labels want to acquire artists, not develop them -- and that means that if your demo does not consist of original material deemed marketable by present standards, and if the demo is not professionally produced, you should probably do yourself a favor and save the postage money.

Of course, this presents an unfortunate problem, because a high-quality finished product does not come free. In fact, for a demo disc of between three and five songs (three would be considered the minimum number of songs on a demo that you intend to shop to labels, and five the maximum), you should expect to spend anywhere from \$10,000 to \$40,000. And that figure doesn't even necessarily include promotional costs, such as website development and showcase expenses. To say the least, doing it right does not come cheap.

For an artist already signed to a major label, \$40,000 or more in costs may not put too much of a dent in the recording budget. But for unsigned artists, or those who don't have the luxury of a big recording budget, there is fortunately another viable option: angel investor financing.

### Angel Investments

In outside or "angel" investor financing deals, the investor will agree to put up a fixed sum of money which is then used by the artist to create a demo album from scratch. In practice this likely means the artist will use the funds to hire an independent producer -- and, if required, a songwriter -- under a separate agreement between the artist and producer to complete the work. The funds are used to cover all of the expenses incurred in creating the album. This would include, but may not be limited to, the following:

- The producer's studio time;
- Retaining a studio engineer; The artist's travel expenses incurred in recording;
- Reproduction of masters;
- And promotional expenses such as website development, press kits, pictures, etc., and the hiring of individuals in connection therewith.

And as noted above, these costs can run anywhere from \$10,000 to \$40,000 to produce a high-quality demo album.

In consideration for providing these up-front costs, the investor typically becomes entitled to a share of the advance the artist will presumably receive upon being signed to a record label, coupled with the rights to "points" -- short for percentage points -- on the first album created and distributed while the artist is under contract with the major label. Points are royalties, and represent a percentage of the suggested retail list price for every album sold. As part of

every record deal, it will be stipulated that the artist will receive a fixed number of points on the sale of each album. The artist may then use any number of those allotted points as contractual consideration in independent agreements. In other words, if you have an investment deal with the artist that calls for the investor to receive 2 points on album sales, that means the investor is getting 2 points for himself out of the number of points received by the artist in his or her deal with the record label (which will be at least 2 points).

To illustrate this concept more clearly, consider the following hypothetical, in which an angel investor agrees to provide \$25,000 of investment backing in exchange for 25% of the artist advance, plus 2 points. Assume that the total cost of producing the demo including promotional and other miscellaneous expenses comes to \$23,500.

As a threshold matter, the angel investor is entitled to \$1,500 back. Subsequently, the demo will be shopped around to labels in an effort to land a record deal. To continue our hypothetical scenario, suppose the artist signs with a major and receives a \$50,000 advance. The investor receives 25 percent of the advance, or \$12,500. The total amount of the investor's capital that has now been returned to him is \$14,000 (\$1,500 of seed money that was never used, plus \$12,500 of the artist's signing bonus). That means the investor is still out of pocket \$11,000. However, as noted above, the investor will also likely be entitled to "points" on the artist's first album created while under contract with the label.

After the record label recoups its own out-of-pockets on the deal -- including the advance paid to the artist (perhaps a topic for another day) -- the artist and investor will start receiving funds from points on album sales when the album is distributed and sold in stores. In this way, based on the investor's entitlement to 2 points, the \$11,000 balance assumed by our hypothetical will be further paid down. Naturally, the goal is for the album to be successful enough to not only pay off the investor's balance, but to also make all parties contractually involved -- including the investor -- extremely wealthy on the deal.

To sweeten the deal, an artist might go further and give the investor a claim on albums subsequent to the first. For example, if the artist is signed to a major label, it is likely the contract will give the label an option -- which the label may or may not choose to exercise at its own discretion -- to create a second, third, or even fourth album with the artist. Thus, the underlying artist agreement with the angel investor can provide that, if subsequent albums are made under the record deal the artist signs with the label, the investor can receive a portion of the advance plus points on any subsequent albums. The artist might consider a regressing scale (in which, for example, the investor gets only points but no portion of the advance, or one less point for each subsequent album, etc.), because if the label ever decides that a third or fourth album is commercially viable, it will only be because the first albums were huge successes. In other words, even if the investor has the rights to 1 point on the fourth album, that 1 point will potentially be worth as much, if not more, as the 2 points on the first album, when the artist's commercial draw was less powerful.

### **Sounds Good, But Now What?**

Perhaps the hardest part about angel investor deals is knowing where to find them. In other words, where exactly can artists search for angel investors who are looking to invest in projects? Not surprisingly, there are no fixed or magic answers to this question. The shortest (and most accurate) answer is that they are potentially everywhere. That is, not only are potential angel investors operating outside of the music business, but your very best bets may be such "non-music" types. Family and friends are obvious examples, but consider also professional venture capitalists or businesspeople looking for a home for some investment capital. An investment deal for a demo album is, in principle, no different from any

speculative business venture. So don't be shy about marching right up to a venture capitalist and giving him solid reasons why an investment in your demo album is a smart business move for that person.

### **Conclusion**

There is room for some outside-the-box thinking on these investor agreements. For example, left unaddressed thus far is how to deal with a situation in which the artist develops a commercially prosperous singing career for reasons wholly unrelated to the demo album that is the subject of the investment agreement. That is, suppose that the artist completes her demo album with the investor funds, but that while the demo is being shopped, the artist competes on *American Idol* and wins first place. Does the investor get a piece of that? Whatever the intent, the contract should be drafted carefully to ensure that situations such as this are accounted for. And whether giving the investor such a large and sweeping entitlement to future artist income makes sense for the artist simply depends on the facts specific to any given case.

In all events, while there is certainly room for creativity and flexible thinking on angel investment deals, this article has illustrated the basic mechanics of how such deals generally work. Because one of the hardest and most frustrating aspects of life as an unsigned artist is simply generating funds sufficient to finance a quality demo in the first place, angel investment deals can be a powerful -- and perhaps underused ---method to get you to your goals more quickly. Calling all angels!

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