

Seven Arts Entertainment Inc.  
Form 10-K/A  
November 09, 2012

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UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549

FORM 10-K/A  
Amendment No. 1

☒ ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended June 30, 2012

☐ TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission File Number: 001-34250

SEVEN ARTS ENTERTAINMENT, INC.  
(Formerly Seven Arts Pictures, PLC)  
(Exact name of Registrant as specified in its charter)

Nevada  
(State of Incorporation)

45-3138068  
(I.R.S. Employer Identification No.)

8439 Sunset Blvd., Suite 402  
Los Angeles, California  
(Address of principal executive offices)

90069  
(Zip Code)

Registrant's telephone number: Phone: (323) 372-3080; Fax: (323) 389-0664

Securities registered pursuant to Section 12(b) of the Act:  
None

Securities registered pursuant to Section 12(g) of the Act:

Common Stock; \$0.01 Par Value  
(Title of Class)

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.  
Yes ☐ No ☒

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes ☐ No ☒

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Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes ☒ No ☐

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes ☒ No ☐

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§ 229.405 of this chapter) is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. ☒

Indicate by a check mark whether the Registrant is a large filer, an accredited filer, non-accredited filer, or a smaller reporting company. See the definitions of "large accredited filer", "accredited filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accredited filer ☐

Accredited filer ☐

Non-accredited filer ☐

Smaller reporting  
company ☒

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). Yes ☐ No ☒

The aggregate market value of common stock, par value \$0.01 per share, held by non-affiliates of the registrant, based on the average bid and asked prices of the common stock on June 30, 2012 (the last business day of the registrant's most recently completed fiscal year) was approximately \$3,011,829. For purposes of this computation, all officers, directors and 10% beneficial owners of the registrant are deemed to be affiliates. Such determination should not be deemed an admission that such officers, directors or 10% beneficial owners are, in fact, affiliates of the registrant.

Number of common shares outstanding as of October 8, 2012 was 11,636,677.

DOCUMENTS INCORPORATED BY REFERENCE

Listed below are documents incorporated herein by reference and the part of this Report into which each such document is incorporated:

None

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## FORWARD-LOOKING STATEMENTS

This annual report on Form 10-K includes forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, which we refer to in this annual report as the Securities Act, and Section 21E of the Securities Exchange Act of 1934, as amended, which we refer to in this annual report as the Exchange Act. Forward-looking statements are not statements of historical fact but rather reflect our current expectations, estimates and predictions about future results and events. These statements may use words such as “anticipate,” “believe,” “estimate,” “expect,” “intend,” “predict,” “project” and similar expressions as they relate to us or our management. When we make forward-looking statements, we are basing them on our management’s beliefs and assumptions, using information currently available to us. These forward-looking statements are subject to risks, uncertainties and assumptions, including but not limited to, risks, uncertainties and assumptions discussed in this annual report. Factors that can cause or contribute to these differences include those described under the headings “Risk Factors” and “Management Discussion and Analysis and Plan of Operation.”

If one or more of these or other risks or uncertainties materialize, or if our underlying assumptions prove to be incorrect, actual results may vary materially from what we projected. Any forward-looking statement you read in this annual report reflects our current views with respect to future events and is subject to these and other risks, uncertainties and assumptions relating to our operations, results of operations, growth strategy and liquidity. All subsequent written and oral forward-looking statements attributable to us or individuals acting on our behalf are expressly qualified in their entirety by this paragraph. You are cautioned not to place undue reliance on forward-looking statements, which speak only as of the date of this annual report. The Company expressly disclaims any obligation to release publicly any updates or revisions to these forward-looking statements to reflect any change in its views or expectations. The Company can give no assurances that such forward-looking statements will prove to be correct.

## PART I

### ITEM 1. BUSINESS

#### Corporate History and Current Corporate Structure

We are the continuation of the business and the successor of the NASDAQ listing to PLC whose predecessor Seven Arts Pictures Inc. (“SAP”) was founded in 2002 as an independent motion picture production and distribution company engaged in the development, acquisition, financing, production, and licensing of theatrical motion pictures for exhibition in domestic (i.e., the United States and Canada) and foreign theatrical markets, and for subsequent worldwide release in other forms of media, including home video and pay and free television. The Company currently owns interests in 33 completed motion pictures, subject in certain instances to the prior financial interests of other parties. As discussed herein, in late February 2012, the Company launched Seven Arts Music and acquired 52 completed sound recordings with the rights to additional albums. On June 30, 2012, Seven Arts Filmed Entertainment, LLC (“SAFELA”) was transferred to the Company. SAFELA, which is 60% owned by the Company, has a 30 year lease to operate a film production and post-production facility at 807 Esplanade Avenue in New Orleans, Louisiana. The post-production facility commenced operations on July 1, 2012.

On June 11, 2010, we were formed and became a wholly owned subsidiary of PLC. As of June 11, 2010, we entered into an Asset Transfer Agreement, as amended on January 27, 2011 and again on August 31, 2011, to transfer all of the assets with a cost basis from PLC to us, in exchange for our assumption of certain indebtedness and for one share of common stock of ours for each ordinary share of PLC which have been distributed to shareholders. Additionally, 28,571 shares of our common stock were issued to PLC in order to satisfy any remaining obligations. This transfer was approved by the PLC shareholders at an Extraordinary General Meeting on June 11, 2010. The purpose of this transfer was to eliminate our status as a foreign private issuer and to assume compliance with all obligations of a domestic issuer under all applicable state and Federal securities laws. Our intention in executing this transaction was to redomicile our business with no change in the economic interests of our shareholders.

On August 31, 2011, NASDAQ approved the substitution of one share of our common stock for PLC’s NASDAQ listing, effective at the opening of trading on September 1, 2011. On that date, each of PLC’s ordinary shares was exchanged for one share of our common stock and commenced trading on NASDAQ as the successor to PLC’s NASDAQ listing. This transaction was approved by PLC’s shareholders at its Extraordinary General Meeting on June 11, 2010.

On November 8, 2011, PLC, was placed into involuntary creditors liquidation under English law. Certain indebtedness of PLC remained with PLC and will be subject to administration or payment in those administration proceedings. In accordance with the asset transfer agreement, PLC has been issued 28,571 shares of our common stock in order to satisfy these obligations.

In February 2012, the Company acquired the music assets of Mr. Michery and 100% of the stock of BJ M., As a result, the Company is now also an independent distributor and producer of sound recordings through Seven Arts Music Inc.

The material assets that were acquired comprise 52 completed sound recordings including two completed albums with DMX, up to two additional albums from DMX and up to five albums from Bone Thugs-N-Harmony. The commitments and liabilities assumed were a promissory note dated June 15, 2010 in the amount of \$200,000, and outstanding recording costs of the performances of DMX in amounts to be approved by us but not to exceed \$140,000.

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In connection with the acquisition of the music assets of Mr Michery, the Company issued 50,000 shares of our Series B Preferred to Mr Michery and his assigns and issued an additional 50,000 shares of our Series B Preferred into an escrow in favor of Mr. Michery and his assigns if two DMX albums and two Bone Thugs-N-Harmony albums generate an aggregate of net earnings before interest and taxes of \$5,000,000 during the next five fiscal years. Mr. Michery is the Chief Executive Officer of SAM.

In February of 2012, the Company also acquired Big Jake Music Inc. (“BJM”) and issued 10,000 shares of our Series B Preferred to Jake Shapiro and his assigns and issued an additional 70,000 shares of our Series B Preferred into an escrow in favor of Mr. Shapiro and his assigns if certain specific terms are met: 40,000 shares are subject to proving valuation and usage of certain advertising credits and 30,000 shares are subject to an earn- out over a two-year period.

On June 30, 2012 Seven Arts Filmed Entertainment LLC (“SAFELA”) was transferred to the Group. SAFELA has a 30 year lease to run a production and post-production facility at 807 Esplanade, New Orleans. (“807 Esplanade”) The post production facility began trading on July 1, 2012. Seven Arts Pictures Louisiana LLC, Seven Arts Pictures Louisiana LLC (“SAPLA”) a related party and/or an affiliate of the Company, entered into a Credit Agreement with Advantage Capital Community Development Fund LLC (“Advantage Capital”) dated October 11, 2007, for the acquisition and improvement of the production and post-production facility located at 807 Esplanade Avenue in New Orleans, Louisiana (“807 Esplanade”) for aggregate principal advances of up to \$3,700,000. This agreement was guaranteed by the Company’s predecessor. Approximately \$3,700,000 plus interest has been drawn under the terms of this Credit Agreement, as of June 30, 2012. The Company has now assumed the liability for \$1,000,000 of this amount due to an agreement with the now mortgagor Palm Finance. A further \$750,000 is owed in tax credits earned to Advantage Capital. A construction loan of \$1,850,000 previously guaranteed by the Company has now also been assumed by the Company for the grant of a 30 year lease on the property 807 Esplanade to run a production and post-production facility.

On August 31, 2012, the Company announced a 1-for-70 reverse split of its common stock effective as of 4:01p.m. EDT. The new CUSIP number is 81783N 201. By virtue of the reverse split, every seventy shares of the outstanding common stock were combined and converted into one share of new common stock with resulting fractional shares rounded up to the next whole share. The Company also announced that it will proportionately reduce the number of its authorized shares of common stock.

Seven Arts also announced that, subject to appropriate and required regulatory filings and approvals, it has declared a warrant dividend to those persons beneficially owning its common stock as of the close of the markets on August 31, 2012. For every ten pre-reverse split shares of common stock held as of such date and time, the holders thereof will be entitled to receive one warrant as a dividend. Until its expiry date, each warrant, once distributed following such approvals, will be exercisable for the purchase of one share of the Company's post-reverse split common stock at a price equivalent to today's post-reverse split closing bid price. The warrants will expire on the earlier of (i) the date that the holder disposes of the common stock in respect of which the warrant dividend was declared, if such disposition occurs on or before the close of the markets on October 31, 2012, or (ii) 5:00 p.m., PST, on January 31, 2013. Seven Arts does not expect that a secondary market will develop for such warrants.

On September 14, 2012 the Company’s common stock began trading on the OTC Markets’ OTCQB marketplace. The Company’s common shares trade under the Company’s symbol “SAPX.” The Company is applying to trade on the highest OTC marketplace, OTCQX, but is trading on the OTCQB tier until the Company is eligible to trade on the OTCQX.

Trading of the Company’s common stock on The NASDAQ Capital Market was suspended at the opening of business on September 14, 2012, due to the fact that the Company could not meet the \$1 minimum bid price listing requirement of NASDAQ for ten trading days prior to September 20, 2012, the expiration date on the Company’s six-month extension to meet this listing requirement.

#### Capital Structure

SAE’s authorized capital total 250,000,000 consists of:

35,667,840 shares of common stock, \$.01 par value per share.. As of June 30, 2012, there were 1,739,900 shares of common stock outstanding, all of which are fully paid and non-assessable. (including the 28,571 shares issued to SAP Plc as part of the asset transfer agreement approved by the SEC in January 2011). Each outstanding share of common stock entitles the holder thereof to one vote per share on matters submitted to a vote of stockholders.



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125,125 Series A preferred shares with a \$10.00 par value per share, 125,125 shares were issued to one shareholder in November 2011 for a transaction completed in August 2011. These shares have a conversion price to common stock of \$10.50/share.

200,000 Series B preferred shares \$100.00 par value per share .180,000 shares have been issued to two shareholders in February 2012 and 120,000 of such shares are held in escrow subject to earn out provisions. The per-share conversion price for the Series B Preferred Stock will be confirmed after September 30, 2012, as a function of 110% of the net asset value per share as of September 30, 2011, as then modified for any issuances of shares during the one-year period thereafter if such issuances are at or below 80% or below of \$1.10 per share

214,007,035 shares of unallocated capital stock

SAE is now a United States issuer and commenced regular quarterly reporting from the first quarter ended September 30, 2011.

## Production History

In September 2004, one of our predecessor companies Seven Arts Pictures Limited (“SAPL”) and SAP, companies previously owned by Peter Hoffman, our Chief Executive Officer, transferred all beneficial and legal ownership to PLC of all of their interests in (i) 12 completed films, eight of which were co-produced through a joint venture between SAPL and Fireworks Pictures Inc., and four of which were produced by CineVisions, a predecessor of SAP, and (ii) the rights to certain development projects then owned by SAP, all for our common stock. The four motion pictures produced by CineVisions are now owned by our affiliate SFF except 9 ½ Weeks II for which we have lost all distribution rights. The remaining three films are: Johnny Mnemonic, Never Talk to Strangers, and Shattered Image. One development property transferred by SAP remains under active development by us; the motion picture rights to the published novel Neuromancer and screenplays based on that novel. SAP, its predecessor CineVisions, and SAPL were founded by our Chief Executive Officer and Director, Peter Hoffman, to produce and license for distribution independent motion pictures, as well as to provide consulting and financing services within the motion picture industry. SAP was incorporated on October 1, 2002 and assumed all the assets and liabilities of CineVisions, which had been incorporated in May, 1992.

## Production Activities of Our Predecessors

No production activities were undertaken by us until January 1, 2005 and all the production activities prior to that date were engaged by our predecessors CineVisions, SAPL and SAP. All our production activities after January 1, 2005 were under our direction. All the films discussed below were produced or co-produced by our predecessors and were distributed by our predecessors. The Hustle and A Shot at Glory were only distributed by our predecessors and were not produced by our predecessors.

## Films Produced and Distributed from 1994-1998

Between 1996 and 1998, our predecessor CineVisions produced and licensed the distribution rights for Johnny Mnemonic, Never Talk To Strangers, 9 ½ Weeks II, and Shattered Image, which were assigned to us by SAP. CineVisions assigned all rights to distribute these films to SAP, which in turn all such rights to us. Subsequently, all rights to 9 ½ Weeks II were assigned by court order to a third-party in final judgment. We own the copyright to the other motion pictures either directly or through grants of all rights in perpetuity, through an affiliate.

## Films Produced and Acquired by SAPL and Fireworks

In 1998, SAPL entered into a joint venture agreement for the production and distribution of motion pictures with Fireworks. Fireworks is a subsidiary of CanWest Global Entertainment, Inc., a large diversified Canadian media company. Pursuant to that joint venture, Fireworks and SAPL produced, acquired and distributed 11 motion pictures (the “Fireworks Pictures”), one of which was returned to the owner and two of which are among the motion pictures now owned by us, Shot at Glory and The Hustle. All SAP’s interest in the Fireworks Pictures were assigned to us in 2004 by SAP, which is the subject of the copyright infringement litigation as discussed in Management’s Discussion And Analysis of Financial Condition and Results of Operations – Legal Proceedings.

Through SAPL, Mr. Hoffman produced and acquired Fireworks Rules of Engagement, Onegin, The Believer, Who Is Cletis Tout and American Rhapsody. These motion pictures are the subject of copyright infringement and contract claims that we, together with SAP and SAFE, have brought against Fireworks and Content Film. See Management’s Discussion and Analysis of Financial Condition and Results of Operations – Legal Proceeding. In particular, in these proceedings, we now claim based on assignment from SAP ownership of the following:

- a). All copyright and distribution rights to American Rhapsody and Who Is Cletis Tout.

- b). All international distribution rights to Onegin and The Believer.
- c). All distribution rights outside the United States and Canada to Rules of Engagement.

Films Co-Financed by SAPL

SAPL, co-financed three motion pictures in conjunction with Fireworks and Paramount. Of these motion pictures, we claim that one of them, Rules of Engagement, was transferred to us by SAP in 2004. As set out below, this motion picture is the subject of copyright infringement and contract claims that we, together with SAP and SAFE, have brought against Fireworks and Content Film. See Management's Discussion and Analysis of Financial Condition and Results of Operations – Legal Proceedings.

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We have since January 1, 2005 produced the following motion pictures:

Title	Talent	Delivery Date	1st U.S. Release	Date Distribution Rights Terminate
American Summer aka The Pool Boys (CR) (All Territories)	Director: Cast:	J.B. Rogers Matthew Lillard Effren Ramirez	06/08 9/11	n/a
Autopsy (CR) (All Territories)	Director: Cast:	Adam Gierasch Robert Patrick	06/08 1/09	n/a
Deal (CR) (All Territories)	Writer:  Director: Cast:	Gil Cates, Jr. & Marc Weinstock Gil Cates, Jr. Burt Reynolds Bret Harrison Shannon Elizabeth Jennifer Tilly	03/07 04/08	n/a
Knife Edge  (All Territories)	Director: Cast:	Anthony Hickox Joan Plowright Natalie Press	06/08 03/10	3/23/2031
Night of the Demons (CR) (All Territories)	Director: Cast:	Adam Gierasch Shannon Elizabeth Edward Furlong Diora Baird	06/09 10/10	n/a
Nine Miles Down (CR) (All Territories)	Director: Cast:	Anthony Waller Adrian Paul Kate Nauta	06/09 07/12	n/a
Noise aka The Rectifier (CR) (All Territories)	Writer/Director: Cast:	Henry Bean Tim Robbins William Hurt Bridget Moynahan William Baldwin	03/07 05/08	n/a
Pool Hall Prophets aka Shooting Gallery (CR) (All Territories)	Writer/Director:  Cast:	Keoni Waxman  Freddie Prinze, Jr. Ving Rhames	09/05 12/05	n/a
Schism (CR)	Writer / Director:	Adam Gierasch	09/12 scheduled 10/12	

Cast:	Callum Blue
	Vinnie Jones

(All Territories )  
Films Acquired by Us

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We have acquired certain distribution rights to the following motion pictures since January 1, 2005

Title	Talent	Delivery Date	1st U.S. Release	Date Distribution Rights Terminate
Back In The Day (All International Territories)	Writer: Director:  Cast:	Michael Raffanello James Hunter  Ving Rhames Ja Rule	03/05 05/05	11/11/2019
Boo (1)  (All International Territories)	Writer/Director:  Cast:	Anthony C. Ferrante Trish Cohen  Happy Mahaney	03/05 10/05	5/14/2008
A Broken Life  (All International Territories)	Writers:  Directors: Cast:	Neil Coombs, Anna Lee & Grace Kosaka  Neil Coombs Tom Sizemore Ving Rhames Grace Kosaka Saul Rubinek	06/08 09/08	10/26/2026
Captivity (All International Territories)	Writer: Director:  Cast:	Larry Cohen Roland Joffe  Elisha Cuthbert	03/06 07/07	5/10/2008
Cemetery Gates (1)  (All International Territories)	Writer:  Director:  Cast:	Brian Patrick O'Tolle Roy Knyrim  Reggie Bannister	03/05 05/06	4/4/2020
Drunkboat  (All Territories)	Writer:  Director: Cast:	Bob Meyer & Randy Buescher Bob Meyer John Malkovich John Goodman Dana Delaney	12/08 07/12	4/28/2011
Gettin' It (All Territories)	Writer/Director: Cast:	Nick Gaitatjis Jessica Canseco	12/06 08/07	4/4/2017

Patrick Censoplano  
Cheryl Dent  
Sandra Staggs

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Hades aka The Black Waters of Echo Pond (All International Territories)	Director: Cast:	Gabriel Bologna Robert Patrick  Danielle Harris	5/09	04/10	10/26/2027
Men Don't Lie (All Territories)	Director: Cast:	Jane Spencer Michael Madsen Elle Travis	not yet scheduled	not yet scheduled	
The Mesmerist (All International Territories)	Writers:  Director: Cast:	Ron Marasco & Michael Goorjian Gil Cates, Jr. Neil Patrick Harris Jessica Capshaw	06/02	09/02	n/a
Mirror Wars (All International Territories)	Writers:  Director: Cast:	Alex Kustanovich & Oleg Kapanets  Vasily Chiginsky Armand Assante Malcolm McDowell Rutger Hauer	11/06	07/07	2/3/2011
+ Popstar (All International Territories)	Writer: Director:  Cast:	Timothy Barton Richard Gabai  Aaron Carter Alana Austin	03/05	11/05	10/19/2014
Radio Free Albemuth (International Territories)	Writer/Director: Cast:	John Alan Simon Alanis Morissette	6/10	NA	6/25
+ Red Riding Hood (All International Territories excl Indonesia, Israel, Japan, Latin American Satellite TV, Mexico, Middle East, Pan Asian Satellite TV, Portugal, Russia, Slovenia/Croatia, Thailand, Turkey)	Writer: Director:      Cast:	Timothy Dolan Randall Kleiser      Lainie Kazan Morgan Thompson	03/06	06/06	5/2/2015



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+ Supercross (All International Territories)	Writer:	Ken Solarz	08/05	5/25/2019	
	Director:	Steve Boyum			
	Cast:	Sophia Bush Steve Howey Cameron Richardson			
The Wedding Chest (All International Territories excluding Russia, Germany and France)	Writer:	Ekaterina Tirdatova	3/08	not yet scheduled	10/4/2021
	Director:	Nurbek Egen			
	Cast:	Natasha Regnier Bolot Tentimyshev			

## Our Business Strategy

Our current business strategy is:

To finance, produce and distribute two to four motion pictures in-house per year with budgets of between \$2 million and \$15 million each. As previously stated, certain of these pictures will receive only a limited theatrical release while others will be released more widely.

To acquire and distribute sound recordings throughout the world, both as singles and albums of both established and new recording artists. We expect to release 3 – 4 albums per calendar year, including albums by the established urban artists DMX and Bone Thugs-N-Harmony

To supplement our core strategy by producing an occasional higher cost motion picture (production budgets of \$30 - \$60 million). We will seek to co-produce such projects with a major studio to guarantee a studio-wide release and obtain a commitment to cover a portion or all of P&A Costs.

To opportunistically acquire distribution rights to an additional two to five motion pictures produced by others, each year, for distribution in theatrical, video and television markets, as an agent, for a 15%-20% fee.

To maximize our current use of tax-preferred financing structures around the world to fund our motion picture productions.

To continue to reduce our financial risk on motion pictures we produce in-house by licensing certain rights to distributors prior to and during production, although we recognize that, particularly in the last year, the licensing market has become more difficult to access as a film financing tool.

To increase our share of distribution revenues by entering into partnerships with theatrical and video distributors, to gain more control over the distribution of our motion pictures and to obtain a greater share of the revenues from distribution of our motion pictures.

To scale our business over time by modestly increasing the number of pictures we develop and produce in-house as well as by more aggressively seeking to acquire for distribution motion pictures produced by third parties.

We believe that this is a particularly opportune time to be producing and distributing moderately priced motion pictures as, according to their public announcements, the major studios plan on reducing the number of pictures that they finance and distribute, preferring instead to concentrate resources on a limited number of high-priced, “franchise” productions. In addition, we believe that certain of the most successful independent motion picture companies have either been acquired or are focusing on higher budget films. We believe that these factors will attract exceptional levels of both talent and projects for lower budget motion pictures and independent film companies such as Seven Arts.

We do not yet have firm commitment for the financing and production of the six motion picture projects described on page one of this prospectus. We have no assurance that we will be able to finance production of these motion pictures but expect to do so within the next 18 months. In each case are currently negotiating financing and distribution arrangements but none are complete.

## Our Competitive Strength

Our competitive strengths include:

The experience of our management and our relationships with independent motion picture distributors.

Our relationships with “key talent” and with independent motion picture distributors around the world.

Our expertise in structuring tax-preferred financings.

#### Production

Since 1996, we and our predecessors have developed, financed, produced, and licensed 16 motion pictures, primarily with budgets in range of \$2 million to \$15 million, for domestic and international markets. Most of our pictures have either received only limited theatrical releases or were released directly to post-theatrical markets, primarily DVD. We may produce the occasional higher cost motion picture (production budgets of \$30 - \$60 million), and if we do so, we will most likely choose to co-produce any such project with a major studio if they guarantee a studio-wide release and provide a commitment to cover a portion or all of P&A costs or with one or more other independent production companies. The number of pictures that we are able to produce and the size of the budget of those films depend upon the funds available to us.

We receive between 50 and 100 submissions of potential film projects or completed films every year, which generally include a “package” of a screenplay and certain talent elements (e.g. producer, director and cast). In certain limited cases, we will arrange for the creation of a screenplay and the “packaging” of creative elements. We commission independent production budgets of certain projects to evaluate the project's suitability for production or distribution. The pictures we produce are selected according to several key criteria formulated to maximize the profit potential of our films, including the potential to license the worldwide distribution rights to the film for an amount greater than the projected production budget (e.g. a minimum profit margin of at least 20%), the potential for the film to be widely accepted as a “quality” or “good” film, whether the key creative talent, including directors and two most prominent cast members, are likely to be both responsible and artistically gifted in creating the motion picture. There are no “rules” or specific strategic limitations on our choice of motion pictures to produce. The decision to move forward with a project is our Chief Executive Officer’s decision based on highly subjective factors. However, we believe that the vast experience of our management team is critical to this decision-making process. We will, however, only consider a motion picture with a production cost in excess of \$15,000,000 if we are able to manage the risks of production through “pre-sales” or equity contribution to production of that picture. Over the past five years, Louisiana has become a popular destination for the production of motion pictures due to very favorable tax incentives. Since 2005, we have produced five motion pictures under the Louisiana Motion Picture Incentive Act (the “Louisiana Incentives”), which provides substantial transferable tax credits for film production activities in Louisiana accredited to us whether we produce or acquire a motion picture. The Louisiana Incentives provide generally that the producer will receive both a 25% (now 30%) transferable investment tax credit on all film expenditures on Louisiana vendors and a 10% (now 5%) transferable labor tax credit on all expenditures for labor performed in Louisiana by Louisiana residents. We generally obtain loans during production of a motion picture in Louisiana secured by these tax credits after a “pre-certification” by the Louisiana Film Office that the applicable motion picture qualifies for the Louisiana Incentives. We are then able to transfer these tax credits at a discount to third parties upon completion of the motion picture, audit by independent accountants of the applicable expenditures and “certification” by the Louisiana Film Office of tax credits payable based on the audited expenditures. We use the proceeds from the transfer of the tax credits to third parties to repay the loan secured by the tax credits, at which time the lender releases its security interest in the tax credits.

We are able to obtain similar refundable (but not transferable) tax credits arising from film production expenditures in the United Kingdom, Canada, Ireland, Italy and Hungary which offer refundable tax credits for production expenditures in each of their territories.

#### 807 Esplanade

In 2007, SAPLA, an entity controlled by Mr. Hoffman’s wife, acquired real property in New Orleans, Louisiana for development by us as a production and post- production facility for motion pictures in Louisiana. We have a 30-year lease on this property, which reverts to SAPLA if we elect to cease operation of the property as a production/post-production facility. The post-production facility in Louisiana commenced operations in July 2012. We anticipate that this facility will be leased to our motion picture productions in Louisiana and to other motion picture productions produced by unrelated parties. In accordance with the Intercompany Agreements any and all such engagements with the Company will provide no profit to our affiliates and we will pay only out of pocket costs incurred by our affiliates with no mark-up.

SAPLA secured a credit facility in the aggregate principal amount of \$3,700,000, which has been used to acquire and begin the improvements on the property. This credit facility carries an annual interest rate of 2% plus the Prime Rate as published in The Wall Street Journal. We have guaranteed the amounts that SAPLA borrows under this facility and no additional consideration is provided for this guarantee beyond the existing agreement between SAPLA and us.

We entered into a new financing agreement with Palm Finance (“Palm”) in November, 2010 to refinance the existing indebtedness secured by our production and post- production facility in New Orleans, Louisiana under which Palm

has acquired the existing credit facility of \$3,700,000 plus accrued interest of our affiliate SAPLA for \$1,000,000 (plus a contingent sum of \$750,000 contingent on receipt of the tax credits by SAPLA) and agreed to advance an additional \$1,850,000 to complete renovation and construction of this facility. Palm's advance and interest at the rate of 15% per annum are due and payable within five years and are secured by the property at 807 Esplanade Avenue in New Orleans and Louisiana film infrastructure and historical rehabilitation credits, as well as Federal historical rehabilitation credits associated with the property.

We do not anticipate the use of any material amount of our working capital to complete and operate this facility, and we expect to realize substantial film production, film infrastructure, historic rehabilitation and other state and federal tax credits and other tax incentives from the acquisition, renovation, and operation of this property as a post-production facility.

SAPLA has filed for historical rehabilitation tax credits available from the United States (26%) and Louisiana (25%) on approximately \$9,500,000 of historical rehabilitation expenses paid in connection with the renovation of the building and property at 807 Esplanade Avenue in New Orleans, Louisiana (the “Property”) and reflected in a compilation of expenses by an independent accounting firm. SAPLA has filed the Part I application for historic rehabilitation credits and has received the Part II and Part III approvals from the United States Department of Parks with respect to the Property. SAPLA will allocate the Federal historic rehabilitation credits to investors in its lessee, 807 Esplanade Ave. MT LLC (“MT”), and receive cash or reduction in indebtedness as a result of such allocation. SAPLA will assign the Louisiana historic rehabilitation for cash.

SAPLA has also filed for Louisiana film infrastructure tax credits (40%) on all of its investment of approximately \$11,500,000 in connection with the Property to date, as reflected in an audit report of an independent accounting firm (which also includes audits of all rehabilitation expenses). SAPLA has approval from Louisiana that the Property is a certified state film infrastructure project and SAFELA, as lessee of MT, is now operating a production and post-production facility at the Property.

Louisiana has certified approximately \$6,500,000 of film infrastructure expenditure, the tax credits accruing on which SAPLA will assign for cash, with the remaining expenses remaining under consideration by the Louisiana Department of Economic Development (“LED”). SAPLA has received no objections to any of its film rehabilitation expenses from LED as reflected in the audit report submitted to LEDF on July 2, 2012. Under a published Opinion of the Attorney General of Louisiana, the Louisiana tax credits vest upon certification as a film infrastructure project which occurred in 2008. Revenue is not recognized until the required audit or compilation of the qualified expenditures is available to the submitted to the appropriate agency. The reserve established by the Company against the revenue to be received from SAPLA from disposition of the tax credits reflects potential discounts on the assignment of credits for cash and any potential reduction in the amount of expenses that may be subject to credits by objection of any Federal or Louisiana agency, even though the Company has at present no reason to believe there will be any such reductions

#### Licensing of Distribution Rights

We license distribution rights in our motion pictures in the United States and in most foreign territories prior to and during the production or upon the acquisition of rights to distribute a picture. We share in the commissions generated by the sales of the pictures. Sale of a license to distribute a motion picture prior to its delivery is termed a “pre-sale” and may occur at any time during the development and production process. In a typical license agreement, we license a picture to a distributor before it is produced or completed for an advance from the licensee, which advance is recoverable by the distributor from our share of the revenues generated by the distribution of the picture in the licensee’s territory, after deduction of the distributor’s expenses and distributor fee. The advance usually is in the form of a cash deposit plus a letter of credit or “bank letter” for the balance payable 10-20% on execution (i.e., the cash deposit) and the balance on delivery (i.e., the letter of credit or “bank letter”). The license grants the distributor the right to the post-theatrical release of the picture in all or certain media in their territory for a predetermined time period. After this time, the distribution rights revert back to us and we are then free to re-license the picture. The license specifies that the distributor is entitled to recoup its advance from the revenue generated by the release of the picture in all markets in its territory, as well as its release costs and distribution fees. After the distributor has recouped its advance, costs, and fees, any remaining revenue is shared with us according to a predetermined formula. This is known as an “overage” and can be a significant source of revenue for us from successful films. However, a film’s poor reception in one market does not preclude it from achieving success in another market and generating significant additional revenue for us in the form of an “overage” in that territory. In all of our licensing arrangements, we retain

ownership of our films and maintain our control of each copyright. We intend to continue the practice of retaining underlying rights to our film projects in order to continue to build our motion picture library to license or sell in the future.

#### Finance

We create a separate finance plan for each motion picture we produce. Accordingly, the sources of the funds for production of each motion picture vary according to each finance plan. We utilize financing based on state and foreign country tax credits (e.g., Louisiana, United Kingdom and Hungary) and direct subsidies), “mezzanine” or “gap” funds, which are senior to our equity, and senior secured financing with commercial banks or private lenders, together in certain cases with a limited investment from us, which is customarily less than 10% of the production budget. Since each finance plan is unique to each motion picture, we cannot generalize as to the amount we will utilize any of these sources of funds for a particular motion picture. We generally obtain some advances or guarantees prior to commitment to production of a motion picture project, but those amounts may not be substantial on smaller budgeted motion picture (e.g., under \$10,000,000), and in certain cases we have committed to production with an insubstantial amount of advances and guarantees. Unless we can manage the risks of production through the use of these financing techniques, we will not likely commit to production of larger budget motion pictures (e.g., over \$15,000,000), and we have never in the past committed to such productions, without substantial advances or guarantees from third-party distributors, or the equivalent in “non-recourse” financings.

## Motion Picture Library

In total we and our predecessors have produced or acquired interests in the following motion pictures to date described below in the table. We own (directly or through grants of all rights in perpetuity of at least theatrical, video, and television rights) either (a) the copyright to each picture designated as “CR” in the table below, or (b) distribution rights in the markets in which we operate for territories outside the United States and Canada (i.e., “International Territory”) or for the territories designated in the table, for no less than 15 years. Historically, in any financial period a small number of motion pictures have accounted for the vast majority of our revenues generated from our motion picture library.

We have lost the right to manage twelve motion pictures (designated “+” in the table below) as a result of the exercise by the Arrowhead Target Fund of its rights under the Arrowhead Loan described above at “Risk Factors”. As a result, Arrowhead is collecting all sums receivable with respect to these motion pictures and all interest in and receivables from these motion pictures has been removed from our financial statements effective June 30, 2009, but Arrowhead has not foreclosed on the copyright and distribution rights of our affiliate in these twelve motion pictures.

For purposes of this table, “Delivery Date” refers to the date the applicable motion pictures is completed and available for delivery to distributors. The “1st US release” is the date on which the film is first released in any medium (e.g. theatrical, video, television) in the United States.

Title	Talent		Delivery Date	1st U.S. Release	Date Distribution Rights Terminate
American Summer aka The Pool Boys (CR) (All Territories)	Director: Cast:	J.B. Rogers Matthew Lillard Effren Ramirez	06/08	9/11	n/a
+Asylum (CR) (All Territories)	Writer: Director: Cast:	Patrick Marber David MacKenzie Ian McKellan Natasha Richardson	05/04	08/05	n/a
Autopsy (CR) (All Territories)	Director: Cast:	Adam Gierasch Robert Patrick	06/08	1/09	n/a
Back In The Day (All International Territories)	Writer: Director: Cast:	Michael Raffanello James Hunter Ving Rhames Ja Rule	03/05	05/05	11/11/2019
Boo (1) (All International Territories)	Writer/Director: Cast:	Anthony C. Ferrante Trish Cohen Happy Mahaney	03/05	10/05	5/14/2008
A Broken Life	Writers:		06/08	09/08	10/26/2026



(All International Territories)	Directors:	Neil Coombs, Anna Lee & Grace Kosaka			
	Cast:	Neil Coombs Tom Sizemore Ving Rhames Grace Kosaka Saul Rubinek			
Captivity (All International Territories)	Writer:	Larry Cohen	03/06	07/07	5/10/2008
	Director:	Roland Joffe			
	Cast:	Elisha Cuthbert			

