Australian Government

Department of Communications, Information Technology and the Arts

REVIEW OF AUSTRALIAN GOVERNMENT FILM FUNDING SUPPORT

ISSUES PAPER

JULY 2006

SUBMISSIONS CLOSING DATE: 11 AUGUST 2006

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Purpose

The Australian Government announced in the context of the 2006–07 Budget that it would review the full range of Government support measures being provided to fund film production in Australia. The purpose of the review is to ensure that the current film funding measures, and the structures which underpin them, are appropriate and effective.

The review is broad ranging and all Australian Government programs for funding film are within its scope. This Issues Paper provides only a brief list of the possible key issues.

The purpose of this Issues Paper is to canvas the key issues likely to be considered by the review and to assist stakeholders to provide submissions. Stakeholders are encouraged to respond to the terms of reference, and to comment on any other relevant areas. .

Terms of Reference

The review will outline the Government's policy objectives for the Australian film industry, analyse the current state of the industry, and examine the range of Government support measures for funding films to ensure that the most effective mix of direct and indirect support is achieved and that appropriate structures to facilitate this are in place.

1. The review will consider and make recommendations on the efficiency, effectiveness and appropriateness of Government support measures for funding films in Australia, including the extent to which these measures address Government cultural objectives to promote the development of a sustainable Australian film industry and enable the creation of a diverse range of quality film and television product.

In particular, the review will examine the effectiveness and continued appropriateness of different mechanisms of Government support for the industry, including: investigating whether, and to what extent, tax incentives and other Government support measures are appropriate and effective in attracting private sector investment to the industry; and developing possible options for improving the effectiveness of tax incentives and other government support measures, where necessary.

2. The review will develop options for future funding for the film industry including the most appropriate balance of direct and indirect support mechanisms.

3. The review will assess whether the agencies involved in funding films and their functions should be realigned to ensure the most effective delivery of the Government's objectives.

Reviews of funding for the Film Finance Corporation for 2008–09 and beyond and of Film Australia will form part of this broader review process.

This review will also take account of the findings of the 2005 review of the 10BA and 10B tax incentive schemes, which is examining issues relating to the clarity of the operations of these schemes. The findings of the 2006 statutory review of the Refundable Film Tax Offset scheme will also be taken into account in this review.

The review will be completed by October 2006.

Definitions and scope

The review will examine Australian Government programs that provide financial support for the film industry in Australia.

There is no single definition of 'film' and it can be interpreted in many different ways. Existing direct funding mechanisms and the Division 10BA scheme, which represent the bulk of Australian Government support mechanisms , focus on feature films, documentaries, mini series and telemovies. These categories will therefore be a particular focus of this review.

Nevertheless, subsections 124K(1) and 124ZAA(1) of Australia's *Income Tax Amendment Act 1936* define film as *'an aggregate of images or images and sounds, embodied in any material'*. This definition, which is both platform and format neutral, includes categories which are eligible for funding under Division 10B such as short drama, educational, training and multimedia.

The following programs are also encompassed by the review.

- Programs that provide financial support for marketing Australian films and Australia as a destination for foreign production.
- Public access, industry support, and preservation programs.

Given the review deals with programs of financial support, current Government regulations applying to Australian television content are not within the review's scope.

Global Context

The last decade has been difficult for Australian films.

The competitive environment is increasingly dominated by a handful of global entertainment conglomerates. In recent years, Hollywood studios have been absorbed into global entertainment companies, creating a matrix of ownership and control that extends very broadly and is quite diversified. The strength of the US film sector is evident in many countries around the world. In 2005, US films took 85 percent of Australian box office receipts which is consistent with their market share worldwide.

In some countries, particularly those whose first language is not English, local films maintain a larger share of domestic box office. For example, French films received an average of around 36 percent of domestic box office share over the last five years while Japanese films received around 34 percent of Japan's box office earnings. However, the average number of local titles released in that period in France was 214 (41 percent of total releases) and in Japan it was 270 (42.5 percent of total releases).

In Australia, the average market share of box office for domestic production was 5.2 percent (over the five year period from 2000–04) and the number of local releases was 22 (8.2 percent). For this same period, Canada's average share of box office for domestic production was 3.2 percent and its average number of local releases was 69 (17 percent). Local Canadian films managed an even smaller share of the total Canadian box office than Australian films at the Australian box office, despite the fact that the number of Canadian local releases was almost double the number of Australian local releases. This demonstrates that the problem of competing with significant English language production hubs is not just confined to Australia.

Changes in audience consumption of films are also impacting on revenue sources for film producers. New technologies are being embraced by consumers as a means of accessing audio-visual and other entertainment.

In 2005, the total box office in Australia decreased by 10 percent on the previous year. This downturn was also echoed internationally, with box office receipts in most major overseas territories falling last year. For example, Japan was down eight percent, Germany was down 18 percent and North America was down four percent.

The future success of the Australian film industry is becoming increasingly dependent on its capacity to adapt quickly and appropriately as technology changes, audience preferences vary and sources of commercial revenue adjust.

Australia's film industry

The Australian film industry employs about 50 000 people with over 2000 businesses involved in film and video production. The majority (84 percent) of these businesses are small businesses (employing 0–4 persons). However, over half (52 percent) of people employed in the film and video production sector are employed by large businesses (those with 100 or more employees) which comprise 1.6 percent of the total number of businesses.[1]

Total box office takings in Australia for 2005 were $818.5 million, which as indicated above, was a decrease of 10 percent on the previous year. There were 330 films released in Australia last year, 27 (or eight percent) of which were Australian. Australian films earned $23 million or 2.8 percent of the total Australian box office, up from 1.3 percent in 2004 but below the ten year average of 4.8 percent.

Most of the recoupment on investment in Australian feature films comes from international sales as contributions from the Australian market are usually cashflowed into the production budget in the form of pre-sales and distribution guarantees. Since the late 1990s, there has been a contraction in the number and size of sales of Australian (and other independent) feature films to overseas markets. This has had a negative impact on the profitability of Australian feature films and recoupment levels.

[1] Australian Bureau of Statistics, *'Television, film and video production'*, Survey 8679, (2002-03), p.15

The Australian film production industry is made up mainly of a large number of small firms with low profitability. In contrast, the film distribution and exhibition sectors are more concentrated, more profitable and the major companies involved in these sectors have links to US companies, whether through contracts or ownership.

Australian producers rely on a complex array of financing arrangements in order to get their films made. These can involve equity investment, the provision of presales and distribution guarantees and Government funding assistance. Producers will often negotiate to release their rights in their films to secure private finance. Private investment in feature films is currently very low. This would appear to be a function of an inherently high risk in terms of returns, and the opportunity cost presented by investment options in other industries.

Given that financing from distributors, exhibitors and private investors rarely covers the costs of production, most films rely on Government support in order to fill the financial gap. Of the 22 feature films produced in 2004-05, more than 85 percent utilised Australian Government production investment assistance (that is through 10BA and 10B tax incentive schemes or through the Film Finance Corporation.

Statistics indicate that 10BA tax incentive scheme investment since 1988 (when the Film Finance Corporation was established) has fluctuated but has had a downward trend overall. The value of 10BA investment in Australian film production was at its lowest in 2000–01 ($8.85million) and at its highest in 1990–91 ($34.42million). In 2004–05, the value of 10BA investment was $25.59million, but 10BA investment was only significant for a small number of films.

It should be noted, the value of 10BA investment refers to the portion of 10BA film budgets eligible for a deduction. These figures are compiled by the Department of Communications, Information Technology and the Arts (referred to in this document as DCITA or the Department), and are based on budget figures provided to the Department by the filmmakers. They do not include investment made through the 10B scheme.

Financing for Australian television production differs from the arrangements for film. production revenue is generally earned by increments through the transmission of the product by the broadcaster. The main form of revenue is advertising revenue and this influences a commercial broadcaster's capacity to incur costs in the production or purchasing of programming.

There are different methodologies used to track local television production which, by its nature, involves expenditure on production over more than one year. The Australian Film Commission's National Drama Survey for 2004–05 reports that the annual hours of local television drama broadcasts have fallen from an average of 722 hours in the late 1990s to 575 hours in 2004-05. The survey also indicates that expenditure on television production in Australia has fallen from a peak of $393 million in 2000–01 to $205 million in 2004–05, well below the 10 year average of $297 million.

The Australian Communications and Media Authority (ACMA), in its Broadcasting Financial Results report, records the actual expenditure and actual broadcast hours in a given year by broadcasters. In contrast, the Australian Film Commission (AFC) reports funding commitments based on the total budget of titles attributed at the date of principal photography. While the different methodologies used do not allow for a direct comparison, ACMA statistics indicate that commercial broadcasters' expenditure on drama (adult and children's combined) increased by more than 26 percent in the period from 2000-04.

Australian Government support

The Australian Government is committed to maintaining a strong, active and vibrant Australian film industry for both cultural and economic reasons. In its 2004 Election Policy Statement, the Government committed to *'facilitating greater private investment in the film sector and continuing to encourage a more entrepreneurial approach to secure the long-term viability of our film industry'* [2] This commitment includes promoting Australian and international appreciation and audience reach for Australian film and television productions.

A vigorous film sector enables the development and production of Australian film and television programs which:

- are of interest and relevance to the Australian public;
- have the potential to attract wider exposure in international markets; and
- enable a record of Australian life and culture to be kept for future generations.

To advance the Government's cultural objectives, developing a creative and highly skilled Australian film and television production industry which can successfully compete in a commercial context is also important. To this end, the Government supports the development of a production industry that has a sound commercial base. Such an industry could be characterised by:

- the creation of a rich variety of high quality film, television and other audiovisual productions which have appeal for a range of Australian and international audiences;
- the existence of a number of viable long term businesses of different sizes and structures which are competitive in a commercial environment;
- marketplace confidence in the quality of the product and a clear understanding of investment vehicles;
- a pool of skilled artists, technicians and business people and training and development opportunities for them; and
- the capacity to adapt to change, to meet new and emerging consumer demands and to offer leadership in implementing technological shifts.

[2] See: Strengthening Australian Arts, The Howard Government Election 2004 Policy, p.10-14, Joint Media Release, Senator the Hon Richard Alston and the Hon Peter McGauran MP, Government Delivers Film Industry Package, 4 September 2001

- Australian Government financial support for Australian film and television production is currently provided in the following areas:

- production which is either culturally significant or has commercial potential or both;
- script, professional, industry and audience development;
- preservation of our film and television heritage;
- advanced education and training of industry practitioners;
- encouragement of private investment in production;
- promotion of Australian films and Australia as a location for filming; and
- encouragement for large budget productions to undertake substantial production in Australia.

Direct Government support is currently largely delivered through funding to the following Government agencies and other organisations.

Film Finance Corporation Australia (FFC)
The FFC is the principal agency for funding the production of film and television in Australia. It funds the most expensive program formats that are not always able to attract full financing from the market. These formats include feature films, mini-series, telemovies and documentaries.

Australian Film Commission (AFC)
The AFC is the primary agency for supporting development of film, television and interactive media projects and their creators. The commission focuses on project, audience and market development for the independent production sector. Since 2003, it includes the National Film and Sound Archive (NFSA).

Film Australia Ltd (FAL)
FAL produces and distributes documentary programs under its National Interest Program (NIP) which examines matters of national concern or which illustrate or interpret the lives and activities of Australians. Film Australia maintains its Lindfield site, a library and an archive, which are accessed by the independent documentary sector at reduced rates.

Australian Film Television and Radio School (AFTRS)
AFTRS is the national, advanced level training institution for the film and broadcasting industries.

Australian Children's Television Foundation (ACTF)
ACTF is a national, non-profit organisation. It encourages the development, production and dissemination of television programs, films and other audiovisual media for children.

Ausfilm
Ausfilm is a not-for-profit organisation which markets Australia as a destination for film production and provides advice on all aspects of filming in Australia.

AGENCY/ORGANISATION	FUNDING 2006-07 $m
Film Finance Corporation Australia (FFC)	70.50
Australian Film Commission (AFC)	52.49
Film Australia Ltd (FAL)	13.17
Australian Film, Television and Radio School (AFTRS)	20.12
Australian Children's Television Foundation (ACTF)	2.58
Ausfilm	1.35
TOTAL	**160.21**

The Australian Government also provides indirect funding support through:

- Division 10BA of the *Income Tax Amendment Act 1936* which aims to encourage private investment in culturally relevant, high quality Australian film and television productions. Investors in 10BA certified Australian films are able to claim an immediate deduction for the full amount of their investment in the year the investment is made.
- Division 10B of the *Income Tax Amendment Act 1936* which is a broader-based concession relating to the first ownership of copyright in a production. It allows a 100 percent tax deduction to initial investors over two financial years, starting when the film is first used to derive income.
- The Film Licensed Investment Company (FLIC) Scheme aims to encourage quality Australian film and television production by facilitating greater private investment. The licence allows one licensee, (the FLIC Company), to raise concessional capital of up to $10 million per year in each of 2005–06 and 2006-07 for investment in qualifying Australian films. It provides the potential for an additional $20 million for investment in the local sector while the FLIC investors benefit from a 100 percent upfront tax deduction on shares purchased in the FLIC.
- The Refundable Film Tax Offset (the offset) is an incentive for attracting large budget foreign film productions to Australia with the aim of providing greater employment and skill development. This tax offset reduces tax liability by 12.5 percent of qualifying Australian production expenditure, with any excess refundable to the taxpayer. The offset was recently extended to include high-budget television series as an eligible format. The offset is not available to productions that access the Division 10BA or 10B schemes.

Key Issues

What does the Australian film industry need to do to increase its chances of success and sustainability?

The project-by-project approach which has characterised the Australian film industry to date is coming increasingly into question. It is frequently suggested that the industry needs to make a transition from a cottage industry to one which is based on successful business enterprises, possibly through a restructuring, There is also considerable debate about the degree to which the film industry is genuinely responsive to audience demand. This debates continues even though the relatively small size of the Australian industry, the impact of distributor and exhibitor preferences, and the high risk profile of film production are also generally recognised as being factors that need to be considered when judging success rates.

These observations suggest the need for both Government policy makers and industry stakeholders to reconsider their focus.

The impact of changing communication platforms and the advent of greater interactivity will also continue to profoundly change the engagement that a customer can have with a creative idea or property. The potential for delivering audiovisual content via multiple new platforms suggests that producers need to design projects that encompass a variety of elements beyond the traditional film or program. While multi-platform delivery tends to be discussed in terms of the potential for additional revenue streams, this potential is yet to become a reality in the Australian context.

In assessing how Government should best deliver its film funding support programs, it is important to understand the film industry's capacity to innovate and undergo structural change where this is necessary.

Comment is sought on:

- the key challenges facing the Australian film and television production sector;
- whether there are impediments to investing in Australian film production;
- whether the industry can do more to increase its competitiveness, both in the marketplace and as a vehicle for investment; and
- whether the industry is suitably responsive to audience demand.

How can Government objectives best be met?

As stated above, the Government has made a strong commitment over many years to a healthy local film and television sector. Government support measures have also been directed towards increasing audience awareness, access and participation across the broad range of cultural support programs.

It is important that Australian Government assistance focuses on areas of greatest impact, encourages increasing levels of private investment, and is delivered in the most efficient and effective way.

Support measures should result in additional activity which:

- would not otherwise occur, and is not a replacement for private investment;
- should be transparent, accountable and cost effective; and wherever possible
- should be a catalyst to innovation, export and private investment.

Wherever possible the cost of any support measure should be known in advance.

Comment is sought on:
- whether the current Government objectives for the film sector are appropriate;
- the areas where Government support is most needed or appropriate;
- the appropriateness of the current balance of support between genres and platforms; and
- the best way to maintain overall consistency in Government support programs with the general principles outlined above.

What balance should be struck between direct and indirect funding?

A mix of direct and indirect support has been provided by the Australian Government to the film industry for over 20 years, but direct support is the dominant support measure with an estimated 75 percent of total support having been provided through outlays.

Most other countries have a mix of both measures but the proportion of direct and indirect Government support differs widely from country to country.

A much higher proportion of indirect support is provided in the UK and Germany. While both countries are in the process of introducing new mechanisms, a new UK scheme is based around tax credits. There has been significant discussion in Germany about tax rebate models similar to the UK model.

In contrast, more than 90 percent of French government support is provided through direct financial assistance and Denmark and Norway provide no support through their taxation systems. Canada has a balanced approach with government support almost equally provided between direct and indirect approaches. New Zealand employs a rebate scheme based on criteria very similar to the Australian Refundable Film Tax Offset. Unlike in Australia however, the New Zealand rebate is paid as a grant rather than through the tax system.

Comment is sought on:
- the effectiveness of direct and indirect funding;
- the relative strengths and weaknesses of direct and indirect support mechanisms;
- whether the existing balance between these support mechanisms used by the Australian Government is still appropriate and effective; and
- if not, what a more appropriate balance might be.

What options are there for stimulating growth in private investment?

Tax incentives designed to increase private investment in film tend to fall into two main types:

- tax credits, rebates and refunds to production companies, which operate in a similar manner to the Australian Refundable Film Tax Offset; and
- tax incentives for investors, like Division 10BA, which accelerate deductions.

Where the direct beneficiary of an incentive is a producer, this is classed as a tax incentive for producers. These may be claimable on completion of the film, or a component of the incentive can be provided upfront (eg Division 10BA).

In some countries, like Australia, a tax incentive for producers is offered principally to attract runaway productions where eligibility criteria are expenditure-based. In other countries, a mixture of direct and indirect support is offered for national product. This support is provided either solely on cultural criteria or by using a combination of cultural and expenditure criteria.

Comment is sought on:

- whether tax incentives are still an effective and appropriate mechanism;
- the appropriateness of the current 10BA/10B schemes;
- whether a tax incentive for producers should be considered instead of a tax incentive for investors;
- the criteria which should apply for Australian participation in any incentive scheme; and
- any other models that might be effective in encouraging private investment.

What is the most appropriate model for direct Government support to the film industry? Is the current agency structure a model that is delivering the best possible outcomes?

The industry 'value chain' includes training and development, script development, production, marketing and distribution, exhibition and archival activities. The table below provides an indication of Government agency involvement in these functions.

FUNCTION	AUSTRALIAN GOVERNMENT AGENCIES INVOLVED
Individual professional development	AFTRS, AFC, Film Australia
Production funding for emerging talent	AFC, FFC, Film Australia ACTF – children's TV, Australia Council
Production funding for established talent or where there is major private support	AFC – feature film development, new media, FFC, ACTF, Film Australia
Support through tax incentives	DCITA, ATO
Access and outreach programs	AFC (screen culture programs and NFSA), Film Australia, ACTF
Preservation	AFC (NFSA), Film Australia
Sales and marketing	AFC, FFC, ACTF, Ausfilm, DCITA
Support for business/enterprise development	AFC, AFTRS, Film Australia
Research	AFC, DCITA

The current arrangement of agency functions utilises a 'many doors' approach to Government support. Under this arrangement there are several different avenues that can be used to seek Government funding support for films. This approach has been justified, partly on the basis that the processes of decision-making in this area can be subjective, for instance on issues such as the quality of a project or its projected audience appeal.

This approach of providing access to different forms of Government support, has also been seen as encouraging the widest possible diversity of Australian production, consistent with the Government's cultural objectives.

On the other hand, it has been argued that a consolidation of existing funding avenues could provide a more strategic approach to both the assessment of film projects and to the achievement of other support objectives. Proponents of this view argue that the current distribution of activities among a range of agencies has led to a lack of co-ordination. This is based on a view that because those seeking financial support are able to cherry pick among the various agencies, such support is often less well targeted than it should be.

In recent years, some agencies have taken on new roles or are carrying out their functions in new ways. For instance, the Film Finance Corporation has introduced an 'evaluation' process to complement its previous 'marketplace' process. Under the evaluation process, which is specifically targeted at feature films, the FFC has creative input into the projects which it funds. The FFC uses expert staff to evaluate the quality and audience appeal of potential productions as well as an assessment, where appropriate, of the quality and readiness for production of the scripts of potential projects.

It is also noted that, in terms of Government support for cultural activity, the 'many doors' approach is basically unique to the film and television sector. It is not reflected in funding for arts programs, for example, which at an Australian Government level is offered through the Australia Council and the Department of Communications, Information Technology and the Arts.

One approach could be to re-configure agency responsibilities so that functions such as business development, access and outreach, collections, archiving/preservation and marketing are delivered in a more consolidated way.

Comment is sought on:

- whether current agency functions and structures are appropriate;
- whether the 'many doors' approach is the most effective; whether it should continue to apply, and if so, to what extent;
- ways of making support for script development and production more effective;
- the most appropriate way of treating specific formats such as drama, documentary or children's programming;
- whether different mechanisms are needed for productions supported solely for cultural or national significance reasons, compared to projects with higher commercial potential;
- whether there is an adequate focus on the commercial prospects of projects;
- whether support should be directed or redirected to other areas, to improve effectiveness in, for example, distribution, marketing, new platforms or formats;
- ways of using Government support to leverage greater income from other sources; and
- whether past success should be rated more highly than it now is as a funding eligibility criterion.

SUBMISSIONS

Submission are invited from interested parties on matters covered in this paper. Submissions are also invited to address any other relevant issues not specifically addressed in this paper.

Submissions should be provided by **Friday, 11 August 2006**, and addressed to:

Mr Peter Young
General Manager
Film and Digital Content
Department of Communications, Information Technology and the Arts.

It would be appreciated if submissions could be provided electronically and preferably in a format compatible with Microsoft Word 2003.

They should be emailed to: filmreview2006@dcita.gov.au

or can be mailed to:

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Persons providing a submission should be aware that submissions may be made public and that they should, therefore, clearly indicate whether any aspect of the submission should be kept confidential. Where confidentiality is requested, submitters are encouraged to also provide a public version of submissions.