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SCREEN PRODUCERS ASSOCIATION OF AUSTRALIA SUBMISSION TO THE
FEDERAL DEPARTMENT OF COMMUNICATIONS, INFORMATION
TECHNOLOGY, AND THE ARTS.

REFUNDABLE FILM TAX OFFSET SCHEME
2006 Review of Division 376 of the Income Tax Assessment Act
1997

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1. Executive Summary

SPAA welcomes the opportunity to contribute to the Review. After consultation with the SPAA membership SPAA makes the following recommendations:-

- SPAA members support the Refundable Film Tax Offset Scheme and believe that it has made a positive economic contribution to the industry.
- SPAA members believe that the Offset should be raised to 15% to ensure that Australia remains competitive in a globally competitive environment.
- SPAA members support a re-evaluation of the 70% threshold requirement for budgets between \$15 and \$50 million, particularly in the case of post production work.
- SPAA members support the introduction of post production, digital, and visual effects only Offset to ensure Australia captures a competitive share of the footloose post production digital and visual effects work.
- SPAA has no objection to the introduction of a 'piggy back' incentive where companies that bring in projects worth in excess of \$50 million automatically qualify for the offset on any subsequent projects brought in within an acceptable time frame.
- SPAA requests that the federal government extend the Tax Offset Scheme to include very high budget television commercials with a QAPE in excess of \$1 million to attract footloose productions of this kind to Australia.
- SPAA requests that the federal government consider introducing a provision whereby the international company must attach an Australian producer to the project to ensure that the indigenous industry derives a lasting benefit from the international subsidy.
- SPAA believes the global marketplace for incentives has never been more competitive or fast moving and that the government needs to develop a mechanism for regular revision of schemes to ensure that we remain competitive and don't get left behind.

2.1 Statutory Requirements of the Review

In May 2006, the Federal Department Of Communications, Information Technology, And The Arts (DOCITA) called for submissions to address the following in line with section 376-110 of the *Income Tax Assessment Act 1997*:

1. the success of the tax offset as an incentive for attracting high quality, high budget film production to Australia, taking into account the net cost of the offset; and
2. the impact of the tax offset on the Australian film production industry (including an assessment of the opportunities it generates for employment and skills transfer).

2.2 Specific Issues Raised by DOCITA

DOCITA requested comments on the following aspects of the operation and impact of the offset.

1. Operation and administration of the offset

The Department of Communications, Information Technology and the Arts (DCITA) is responsible for administering the application and certification process of the refundable film tax offset, while the Australian Taxation Office (ATO) is responsible for determining the amount of offset benefit and administering the refund.

Comment is sought both on the operation and administration of the offset incentive. Areas of interest may include compliance costs, efficiency and effectiveness of administration, and satisfaction with Australian Government departmental advice and assistance through the application process.

2. Success of the offset as an incentive and its impact on industry

The offset was designed to attract large budget film productions to Australia in order to develop Australia's film industry.

Comment is sought on whether the offset incentive has attracted high quality, high budget film production that would not otherwise have been made in Australia and whether the offset is an appropriate means by which to achieve this.

Responses are also sought on the effect of the offset incentive on the Australian film production industry. Areas of interest may include whether the offset has helped to generate opportunities for employment, investment in infrastructure, skills development and the showcasing of Australian talent and businesses internationally.

3.1 SPAA Response

SPAA recognises and appreciates the value of imported production to the Australian industry. While the direct benefit to our members is limited, there are many indirect benefits to servicing international productions, to the Australian economy and also to Australian film and television businesses and practitioners. The additional income provided by offshore work contributes to a more stable infrastructure in studio, crew, and post production services. Australian crews and practitioners benefit from the exposure to international practices and technology. The quality of our service work bolsters our reputation as an industry overseas which can do no harm to Australian producers in the international marketplace. International service work is complementary to the Australian production industry in the short term. In this context, SPAA supports the Film Tax Offset Scheme.

3.2 Raising The Level Of Offset To 15%

As mentioned elsewhere in this paper, there is currently fierce competition globally for runaway and footloose film and television production. The environment changes rapidly as new players introduce incentives, currency fluctuations affect American value for money, and the American states become more competitive in offering footloose productions incentives to stay on shore.

While SPAA recognises that the decision to bring production to Australia will always be a sophisticated mixture of talent and pricing elements, SPAA members have observed that Australia's tax offset benefit has slipped behind some of our competitors, most noticeably Great Britain. Currency fluctuations and higher incentives offered by other countries have eroded the competitive position of Australia since the introduction of the Offset. It is our view that the federal government needs to raise the offset to 15% to remain competitive and continue to attract high budget work into Australia.

3.3 Re-evaluation of the 70% eligibility provision for budgets between 15 and 50 million.

SPAA suggests that the 70% eligibility provision for budgets between 15 and 50 million be reviewed to make absolutely certain that it provides more economic impact than if that condition were removed from projects in that budget range. While it may encourage some producers to bring more of their projects work into Australia, it also excludes some projects from qualifying for the Offset.

Based on confidential figures supplied to SPAA by one of its members, the following scenario illustrates the potential economic benefit of a project in the 15 to 50 million budget range: -

On a QAPE of \$25 M on an international project, our members labour costs approximate \$15 M. Federal employment tax revenue from this project would approximate \$4.5 M. The 12.5% Tax Offset would rebate \$3.125 M to the project. Without considering the economic impact and flow on effects through the use of multipliers, or the potential income tax revenue from the project's host company, the federal government is \$1.375 M ahead on the above project.

The economic benefit to the Australian economy from the importation of this 25 million dollar production is estimated in the table below.¹ If the \$25 million expenditure falls short of 70% of the total budget the Offset wouldn't apply and Australia could potentially lose the following economic impact.

Economic Impact of a \$25 million dollar spend in Australia

Industry Sector	Output multiplier	Output	Gross Value added multiplier	Value added	FTE Employment multiplier (FTE's per \$M)	FTE Employment multiplier (FTE's per \$M)
Film and video production and distribution	3.05	\$76,250,000	1.8	\$45,000,000	37	1665
Motion picture, radio, and television services	2.82	\$70,500,000	1.44	\$36,000,000	21	756
Cultural and recreational services (Aggregation of all cultural sectors)	2.81	\$70,250,000	1.45	\$36,250,000	22.6	818.12

Some SPAA members have reported the loss of potential projects due to this provision of the Offset. It is to be anticipated that DCITA will collect information from all companies who have experienced positive and negative effects

¹ Australian Culture and Leisure Classifications (ABS Cat. No. 4902.0).

of the 70% provision as part of this review. SPAA recommends that DCITA model the benefits of the perceived extra work to ensure that the economic impact benefits are superior to the potential benefits of the extra work that would flow from the removal of the provision.

In the case of post production visual effects work, some footloose productions have budgets in this area of \$15 M or more but because the live action shooting components have been done elsewhere they often do not qualify. See 3.5 for further detail on this.

3.4 A Regular Mechanism For Monitoring Effectiveness And Competitiveness Of Incentives

The global media environment is experiencing the most profound changes ever with the transition from analogue broadcasting and exhibition platforms to digital transmission via multiple platforms including the internet. The communication revolution has ushered in footloose productions and in recent years competition for this work between nations has increased markedly.

Additionally currency fluctuations impact on the effectiveness of percentage based subsidies. For example, the exchange rate against the US dollar was 53 cents when Peter Pan began shooting at the Warner Roadshow Studios on the Gold Coast. By the completion of the film the exchange rate had risen 15% to 68 cents. In this rapidly evolving and competitive global environment, Australia needs to keep a permanent watch on developments to ensure we do not get left behind. SPAA recommends that DCITA introduce a regular mechanism to review the effectiveness and competitiveness of incentives.

3.5 Introduction Of A Separate Offset For Post Production, Digital, And Visual Effects Work.

With the market for runaway production shooting as fiercely competitive as ever, the area of post production, digital, and visual effects is one in which Australia can compete. Australia has the expertise in this area as the performance of companies like Animal Logic, Frame Set and Match, Rising Sun Pictures, Photon VFX, Cutting Edge and others have shown.

Increasingly large budget international productions are seeking to outsource computer generated image (CGI) components to take advantage of the best deals and expertise producers can manage. This work is 'up for grabs' on an international scale. Often CGI work is split between several sub contractors so that the work can be completed sooner. Australia currently has few incentives to target this work.

The Tax provisions of 10B and 10BA do not apply to the digital production packages of these projects.

Often the value of the post production visual effects packages on large budget runaway productions is somewhere within the 15 to 50 million range. Rarely would the post production packages approximate 70% of the films budget. This means that Australia does not possess an effective incentive mechanism to attract this kind of work when many of our competitors do. If the federal government were to introduce a post production visual and digital effects QAPE separate to a film's total production budget than it would be in a position to attract some of this lucrative work. SPAA supports the position taken by Ausfilm that \$5M would be an acceptable threshold as post production budgets for CGI component films are often around one third of the budget. \$5 M is one third of the current Offset threshold of \$15 M.

For this proposal to work it follows that the government would have to remove the 70% requirement currently in place.

This would be consistent with the government's policy objectives to "maximise benefits for the Australian film industry including the development of Australian projects with 'high end' production values" and "to ensure Australia remains competitive in attracting high budget film productions and is aimed at providing increased opportunities for Australian casts, crew, post production companies and other services to participate in these productions".²

Additionally, extending the Offset in this way would also be consistent with the recommendation of the government's Digital Industry Action Agenda.

3.6 Introduction Of An Offset To Attract Very High Budget Television Commercials

Along with television drama series, television commercial production is one of the motors of the film and television industry. Television and feature film are linked to the commercials sector as they often share personnel as freelancers move between productions. Studios, equipment hire firms, and post production companies depend on work from commercials and drama production. The health of one sector has an impact on the other.

Since the regulation preventing foreign produced commercials on Australian television was relaxed there has been a

² Australian Government, Refundable Film Tax Offset Scheme fact Sheet 2001.

gradual contraction in the commercials production sector. Previously multi national companies were forced to use local production companies and personnel to make very high budget commercials. In 1999/2000 41 commercials with budgets in excess of \$1 million and 148 with budgets in excess of \$500,000 were made in Australia. In 2003/04 only 26 commercials with budgets in excess of \$1 million and 67 with budgets in excess of \$500,000 were made in Australia.³ In the same period there has been a massive shift to low budget commercials in Australia. 77 per cent of commercials produced in 2003/04 were worth \$50,000 or less compared with 35 per cent in 1999/00.⁴

The introduction of an Offset to attract back the very high budget commercials to Australia would have beneficial effects across the industry. As these commercials are often made for huge multi nationals it would also enhance Australia's reputation internationally. The screening of commercials showing any part of Australia overseas is of course hugely beneficial to Australia's international profile.

SPAA suggests that the government introduce a Refundable Tax Offset of 15% for commercials where the QAPE is in excess of \$1 million Australian dollars. The production cost per second for a 30 second commercial with a \$1 million budget is \$16,666 per second. This compares more than favourably with the production cost of a 90 minute feature film able to access the Offset with a budget of \$15 million which amounts to a production cost per second of \$2,777.

Very high budget commercial production in Australia would have much the same economic benefit as high end drama production and the two sectors complement each other well.

3.7 Introduction Of A 'Piggy Back' Incentive Clause

SPAA has no objection to the introduction of a 'piggy back' incentive clause in the Refundable Tax Offset regulations. It has been suggested by some industry bodies that once a Studio or foreign independent producer has spent A\$50m on a project here, they should be eligible to receive the Offset for all and any further work above A\$1m for the next 2 years or whatever time frame DOCITA regards as reasonable.

This would work as a further incentive for major producers or studios to develop a long term relationship with Australia and thereby ensure a greater continuity of work. It also makes sense to protect the investment the taxpayer has effectively already made in the foreign company and

³ Australian Film Commission, Get the Picture 2004/05.

⁴ Australian Film Commission, Get the Picture 2004/05.

ensures longevity of return to the economy. Such an incentive might assist to smooth out the volatile peaks and troughs that so often characterise the servicing of offshore production.

3.8 Introduction Of A Mandatory Requirement To Hire An Australian Independent Producer

SPAA submits that that the federal government consider introducing an eligibility provision whereby the international company must attach an Australian independent producer to the project to qualify for the Offset. This would ensure that the indigenous industry derives a lasting benefit from the international subsidy.

Some countries have introduced similar measures. Foreign producers wishing to shoot in Ireland and take advantage of the incentives offered by the Irish government must have an Irish co-producer make the application as a requirement of the Irish Film Board's Irish Tax Incentive Section 481.⁵

SPAA suggests that the attachment of an Australian independent producer would have considerable benefits to the development of the local industry. In addition to the development of international standard skills, it would allow local producers modest infrastructure support enabling them to keep developing Australian projects. It would also strengthen the relationship between Australian producers and Australian crews. SPAA would have no objection to the Australian producer being subordinate in this case to the foreign producers, nor would it expect Australian producers to hold copyright.

SPAA would recommend that only independent producers who have produced at least one Australian feature film be eligible and that they must have at least one Australian feature film under current legal option.

⁵ <http://www.filmboard.ie/template.php?id=9>