STATE AND TERRITORY SCREEN AGENCY FORUM

SUBMISSION TO 2010 REVIEW OF AUSTRALIAN INDEPENDENT SCREEN PRODUCTION SECTOR

Film Victoria
Northern Territory Film Office
Screen ACT
Screen NSW
ScreenWest
Screen Queensland
Screen Tasmania
South Australian Film Corporation

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1 EXECUTIVE SUMMARY

1.1 This submission

This submission is made on behalf of the State and Territory Screen Agency Forum ('The Forum') in response to the 2010 Review of the Australian Independent Screen Production Sector.

The Forum acknowledges the broad focus of the Review. This submission, however, focuses mainly on an assessment of the Australian Screen Production Incentive (ASPI). In particular, this submission is concerned with evaluating the performance of the ASPI with respect to its stated objectives:

- promoting the development of a sustainable independent production sector
- ensuring the creation of a diverse range of quality Australian film and television productions which appeal to audiences, and
- developing and reflecting a sense of Australian identity, character and cultural diversity.

Further, this submission proposes a number of changes to the Producer Offset intended to improve its efficacy, and proposes significant changes to the Location and PDV Offsets to improve the capacity of those measures to deliver the intended benefits.

In this submission we:

- discuss important industry and economic trends and the interdependence of support mechanisms in the Australian film industry
- assess the performance of the ASPI and describe areas requiring fine tuning based on the first three year's operation of the program
- provide detailed discussion of 15 specific issues and make recommendations for each of these.

1.2 The Forum response to the Review

The introduction of the Australian Screen Production Incentive represented a sea-change in film policy thinking. The core intentions of the policy change were to induce producers to be more audience oriented and to increase the sustainability of production businesses. The Producer Offset was intended to make it more likely that producers would build equity in our projects and eventually their businesses by creating a portfolio of rights that generate passive income and would underwrite an ability to invest in new projects.

The task of reviewing the APSI is significantly complicated by the rapid pace of technology driven change in the industry and by the remarkable trajectory of the global economy over the past two years. In brief, the domestic screen industry has to accommodate the effects of rapidly changing business models in content-related industries, global financial downturn, a significantly higher Australian dollar and the emergence of aggressive incentive programs overseas. Isolating and reviewing the performance of the ASPI in the context of this quite confronting set of challenges is not a simple task.

There are, nonetheless, early signs of success. These signs are primarily in the behaviour of some producers who have understood what is possible and are re-structuring their businesses on the basis of the new environment and opportunities created by ASPI. It should be emphasised that shifting the industry to a more long term business-building orientation is clearly an objective that will take some time to realise. Thus, it would be unreasonable to expect conclusive evidence of the success or otherwise of ASPI after only three years of operation.

What can be said is that so far there is no evidence that the fundamental design of the program is unsuccessful. Given the magnitude of the policy change, however, it is inevitable that some unintended consequences should arise and that the need for some fine tuning of policy parameters should become apparent. It is also the case that some policy changes may be necessary to accommodate changes in the relationship between Australia's economy and the global economy. Like the manufacturing industry, the Australian content industry faces a set of difficult consequences arising from the enormous success of the Australian resources sector – all the more so because these changes seem set to continue indefinitely into the future.

Accordingly, our recommendations, summarised below and detailed further in the body of the document, are specific and regard current policy parameter settings rather than advocating any changes to fundamental policy design.

1.3 Summary of Recommendations

Recommendation 1: **Reduce the existing feature film QAPE threshold to $500,000.**

Recommendation 2: **Ensure that the theatrical exhibition test for feature films is flexible and certain and that it be reviewed with the objective of making it more accommodating of innovative distribution arrangements.**

Recommendation 3: **Increase the Producer Offset for documentaries (single episode and series) to 30 per cent.**

Recommendation 4 **Reduce the documentary QAPE threshold to $125,000 per hour.**

Recommendation 5: **Increase the above-the-line cap for single episode documentaries to 30 per cent, or $200,000, whichever is the lesser.**

Recommendation 6: **Introduce a 10 per cent Offset for television episodes 66 to 130.**

Recommendation 7: **Replace the 65 episode limit for children’s programming with a limit of 65 hours of programming.**

Recommendation 8:	**Increase the PDV offset to 30 per cent and reduce the PDV QAPE threshold to $500,000.**
Recommendation 9:	**Increase the Location Offset to 30 per cent and remove the 70 per cent minimum Australian budget expenditure requirement.**
Recommendation 10:	**Include insurance and completion costs in allowable QAPE expenditure.**
Recommendation 11:	**Ensure consistency is a priority in the administration of the ASPI scheme.**
Recommendation 12:	**The industry and screen agencies to develop strategies aimed at supporting producers' interests such as benchmarking deal terms.**
Recommendation 13:	**DEWHA and Screen Australia to use their best endeavours to reduce cost impositions on producers.**
Recommendation 14:	**DEWHA and Screen Australia to explore ways to improve access to information about the outcomes of the ASPI scheme.**
Recommendation 15:	**Establish a joint Industry-Government working party to examine future possible offset treatment for emerging digital media forms.**

2 THE STATE AND TERRITORY AGENCIES: WHO ARE WE, WHAT DO WE DO

2.1 What is the State and Territory Screen Agency Forum?

The State and Territory Screen Agency Forum is an affiliation recently formed to allow the state and territory screen agencies in Australia to present a united submission to the 2010 Federal Review of Independent Screen Production Sector. It has provided a vehicle through which these agencies are able to represent common views to the Federal Government, and it is our hope that it will provide an ability to do so again.

Under this banner, this submission has the signoff of the CEOs of all the state and territory screen agencies that exist in Australia:

- Film Victoria, Sandra Sdraulig
- Northern Territory Film Office, Penelope McDonald
- Screen ACT, Monica Penders
- Screen NSW, Tania Chambers
- Screen Queensland, Maureen Barron
- Screen Tasmania, Karena Slaninka
- ScreenWest, Ian Booth
- South Australian Film Corporation, Richard Harris

2.2 Role of state and territory screen agencies

State and territory screen agencies play an important role in the Australian screen production ecosystem. It is rare for any production or marketing activity to take place without state or territory agency support. Each agency supports the leading practitioners in its state or territory as well as upcoming and emerging practitioners. The agencies see themselves as partners with practitioners and have a very close relationship with the producers and creative teams who have been managing the transition to the new ASPI regime.

The agencies are involved in every aspect of production, from the entry level support of screen resource centres and screen culture activities, through to script and project development and production financing. They support production from drama to kid's television, from documentaries through to animation and newer genres such as digital media and games. All have first-hand experience of grappling with the rapidly transforming media landscape, and working with producers to create projects with cross-platform applications.

We note also that some agencies lend significant amounts of money for cashflow purposes, which has been a crucial element in the success of the ASPI scheme to date. Playing this role has given them insight into the operation of the scheme.

In summary, the state and territory agencies are well placed to comment on the performance of the ASPI to date, and to make recommendations about future policy settings.

2.3 Economic contribution

The direct investment in film support by state and territory screen agencies was approximately $40 million in 2008-09. The total value of production in which state/territory agencies had investment was well over $500 million in that year.

3 STATE OF PLAY

Global media and content markets are in a state of upheaval. Two hundred year old business models are evaporating and new ones appearing with unprecedented rapidity. Google celebrated its 11th birthday last year and Apple is now the biggest music retailer in the world – seven years ago it wasn't even in the business.

In the midst of this change Australian film and television content remain core elements of our cultural identity. Since the 1970s no Australian government has disputed this principle. Nor has any government failed to acknowledge the economic idiosyncrasies of screen content production in a small English-speaking country like Australia that lead to the need for support mechanisms to achieve cultural objectives.

The current dynamism of the media landscape poses immediate and longer-term challenges to policy makers. There is a need to pay attention not just to what is happening in the production sector but to changing patterns of consumer behaviour and emerging new business models. Adapting policy to these changes will be an ongoing challenge across many government portfolios.

This is the context in which the current policy review is occurring – and it is also the context in which the 2011 media industry review will occur. This submission, while focusing on specific issues regarding the Producer Offset and the Location and PDV Offsets, also addresses broader issues of industry dynamics and media policy.

3.1 Local content production depends on matrix of support mechanisms

Notwithstanding general support for the three offsets introduced under the ASPI, the Forum is of the view that there is a need for a number of policy fine-tunings to address emerging gaps between policy intention and outcomes. That there should be such gaps is probably inevitable given the extent of the policy changes introduced three years ago. Our specific recommendations for fine-tuning the ASPI scheme are discussed below.

The ‘three pillars’ of support from governments are:

- **direct support** from the state and territory screen agencies and from the Commonwealth through Screen Australia
- **indirect support** through the Offsets to encourage domestic production and attract offshore activity and through content expenditure of the public broadcasters
- **local content regulation** which supports broadcast of Australian-made content to reflect a sense of Australian identity.

The ASPI scheme therefore belongs to an evolved and interlocking set of policy interventions that includes the Australian content rules for television services and the funding programs of Screen Australia and the state and territory agencies. This set of interventions interacts in complex ways with the operations and output of the screen content production sector. The interconnections of this ‘ecosystem’ should be considered when policy changes are contemplated. In such a complex system, particular attention should be paid to the possibility of unintended consequences of actions. The Forum is of the view there have been some unintended consequences of the ASPI scheme, particularly in its implementation.

For example, the introduction of the Producer Offset was announced at the same time as a reduction in overall direct funding through Screen Australia.

The current reduction in direct support is likely to have a serious impact on the growth of the feature film sector, just as the industry is starting to come to terms with the new scheme. The upper limit for feature film funding (originally $5 million) is mooted to be reduced to $2.5 million. And with total funds available for feature films reportedly falling to $25 million or less, Screen Australia may be unable to arrest what now seems likely to be a very sharp contraction of film production in 2010-11.

3.2 Production sector is an inter-connected ecosystem

The screen production sector is multi-faceted and interconnected. The businesses that comprise it range from individual practitioners running micro-businesses through to vertically-integrated multinational companies. Practitioners increasingly work across multiple genres and platforms, often in combination with partners and co-producers, sometimes across multiple territories. In particular, the growth of the local and international industries have been inextricably linked, particularly over the past 15 years with the development of larger studios on the eastern seaboard, the greater movement of creative personnel between territories and the growth in co-production activity.

It is critical that international production continues to be attracted to Australia. The experience and skills development that it provides and the production infrastructure that it employs are necessary for the maintenance and development of the Australian industry. The attractiveness of Australia as an international production destination is suffering under a perfect storm of factors: a high dollar, disruptive industry change, global financial uncertainty and the growth of incentive programs overseas.

If no, or only low, levels of overseas production occur in Australia then skilled industry participants will leave the industry or will migrate overseas. Such losses of skills and infrastructure are very difficult and costly to reverse. We strongly support arguments for a resetting of ASPI parameters to attract overseas productions.

3.3 Platforms and distribution are fluid, innovation is key

The long anticipated convergence of information technology, communications and media is now upon us. The implications for screen content producers are mixed. Thoughts of democratised distribution and burgeoning niche markets have given way to concerns about shrinking revenues from traditional mass market channels. The search for commercially viable business models to reach paying consumers in the online world remains largely inconclusive. In fact, for Australian content, the success of Apple’s iTunes and Hulu seems to be leading to global mainstream distribution oligopolies that pose even bigger access hurdles than the declining national channels.

Among the challenges for traditional screen content is the ever-expanding universe of games, digital media, social networking and other entertainment/communications hybrids that absorb the time and dollars that consumers might otherwise devote to traditional platforms.

In Australia the Federal Government's decision to undertake the development of the National Broadband Network means that Australia will move to the global forefront of online distribution capacity. This will create opportunities for local content producers and perhaps enable local content entrepreneurs to develop new, viable business models for content production and distribution.

While it is reasonable to assert that narrative-based content forms are still central to cultural expression, it may become necessary to recognise and accommodate new media forms in support mechanisms in order to promote innovation. It is inevitable that existing platform-prescriptive support policies will become anachronistic. Critically, platform prescriptive support mechanisms have the potential to stifle innovation in distribution as well as production leading, ultimately, to a decrease in the relevance and sustainability of Australian content. These are issues which will require continuous, careful monitoring by policy makers.

4 GENERAL PRINCIPLES

The high-level objectives of the ASPI – sustainability, diversity and Australian identity – have been clearly stated many times and are well understood in the industry. To best realise these stated goals and based on the experience of the period of the first three years' operation of the program, we propose a set of lower level guiding principles which we believe should guide efforts to fine-tune program mechanisms:

- encourage greater private sector participation in projects and production companies
- maximise the ability for producers to retain equity
- remove impediments to innovation in production and distribution
- minimise the potential for negative industry distortions caused by policy settings
- maximise certainty for producers and investors
- provide information and data to support decision-making
- minimise administrative and compliance burdens.

5 INTENTIONS AND OUTCOMES

5.1 Positive early signs

The view of the Forum is that the ASPI is a fundamentally good policy innovation that should be continued in its existing conceptual form. There are, however, a number of ways in which the program could be refined to more successfully achieve its goals.

The introduction of the ASPI represented a sea-change in policy thinking with the strongest new policy objective being the business sustainability of screen content producers. One of the core underlying ideas driving this new offset was that it would contribute to greater sustainability by creating an environment where producers could build equity in their projects and eventually own a portfolio of rights that generated passive income and would underwrite an ability to invest in new projects. In a sense the objective was to move the industry from a one-off project 'hit mentality' to a long term business-building orientation. Thus, it would be unreasonable to expect to have conclusive evidence of the success or otherwise of ASPI after only three years of operation.

What can be said is that so far there is no evidence that the fundamental design of the program is unsuccessful. On the contrary, there is some positive evidence, albeit necessarily tentative, that the program is working. Some producers have understood what is possible and are re-structuring their businesses on the basis of the new environment and opportunities created by ASPI.

This fundamental design success of the ASPI to date is all the more remarkable given the timing and circumstances of its launch – just ahead of the Global Financial Crisis and a significant appreciation of the Australian dollar, and at a time when the screen content sector itself is experiencing rapid and disruptive change.

5.2 But a need for fine-tuning

Notwithstanding its general success, the need for a number of policy fine-tunings is now evident, with gaps emerging between policy intention and outcomes. This is probably inevitable given the sheer scale of the policy changes that occurred three years ago.

In contrast to the Producer Offset, the Location Offset and PDV Offset have had more limited impacts on the production industry. The appreciation of the Australian dollar over the past 12 months and the increase in the number of territories offering competitive incentives has in effect wiped out the competitive benefit of these two offsets. The prospect of a more or less permanent elevation of the Australian dollar makes it clear that the Location and PDV Offsets cannot achieve their stated policy objectives at the current 15 per cent rate and the present threshold levels. We return to these points in more detail below. Specifically, the following are areas in which ASPI has performed less well than expected:

1. Low-budget features (and other projects) that previously were eligible for 10BA investment, but that are under QAPE thresholds, are unable to take advantage of the Offset (see Section 6.1);
2. Anecdotal evidence suggests that the theatrical exhibition test is leading to inflexibility in distribution strategies and thereby inhibiting innovation in distribution (see Section 6.2);

3. For a number of reasons, including a higher relative burden of administrative and compliance costs in smaller productions, documentaries appear not to be well served by current Offset parameters (see Section 6.3);
4. Additionally, documentaries may be prejudiced by the existing budget threshold for access to the Offset (see Section 6.4);
5. The above-the-line cap of QAPE is creating a relative disadvantage for documentaries, which have higher above-the-line costs than other forms of production (see Section 6.5);
6. It appears that the 65 episode limit on TV series may be leading to a situation where series do not run past their 65th episode (see Section 6.6);
7. There are indications that children's programming is relatively disadvantaged under the existing episode-oriented caps (see Section 6.7);
8. The PDV Offset is not attracting the targeted type of activity to Australia (see Section 6.8);
9. Similarly, the Location Offset has not succeeded in attracting significant offshore production to Australia (see Section 6.9);
10. Producers believe that that insurance and completion bond costs should be included as legitimate production expenditure under QAPE (see Section 6.10);
11. There are concerns about certainty in the certification process (see Section 6.12);
12. There is concern that Producer Offset benefits are being captured by third parties particularly in the case of the television networks (see Section 6.13);
13. The benefits of the offsets have been limited due to their unanticipated administrative and compliance costs (see Section 6.13);
14. There is a lack of useful statistics on the performance of the Producer Offset reflecting the requirement for tax secrecy (see Section 6.14);
15. The Producer Offset potentially could pose a barrier to the development of new digital media forms and new digital distribution systems (see Section 6.15).

6 SPECIFIC ISSUES AND PROPOSALS FOR THE OFFSETS

A key objective of the Producer Offset is to promote the development of a sustainable independent production sector. Another is to promote diversity of production, with an eye also to audience appeal. The Forum submits that some aspects of the Offset program's design and administration may be working in a way that reduces their effectiveness in delivering these objectives.

6.1 Feature film threshold

The Forum is of the view that the Producer Offset threshold level for feature films, at $1 million, is too high. There are films which are clearly feature films that have cost less than $1 million to produce, for example, among recent films, Kenny, The Jammed and Men's Group. The $1 million threshold works against the sustainability of film production in two ways: firstly by putting upward pressure on budgets (to reach the $1.2 or $1.3 million necessary to achieve a QAPE of $1 million); and secondly by inhibiting innovation in production methods, as explored, for example, in Robert Connolly's paper *Embracing Innovation,* published by the Australian Film Television & Radio School in February 2008.

Connolly's paper presents an alternative, low budget methodology for filmmakers – a methodology that intersects with the direction of technology change, which is putting ever more powerful technologies in filmmakers' hands, at ever lower costs. The $1 million threshold presents a direct obstacle to filmmakers' engagement with the potentials of the technology and the low budget business model. In economic terms, it forms a barrier to entry, disadvantaging young or any filmmakers who lack the track record to attract investment at the $1 million plus level. Significantly, it also closes off the 'family and friends' investment model used by many startup ventures, since few families and friends can afford $1 million plus investments.

CASE STUDY

Issue: Thresholds for low budget feature films

A recently completed feature length film supported by one of the State agencies with a total budgeted cost of $650,000 has achieved a pick up from an Australian based international sales agent and will be marketed with an innovative distribution strategy to reach the target audience devised for the film.

In light of this analysis, the Forum proposes that the threshold be reduced to $500,000, a level that is still consistent with cinema filmmaking. The impact of such a change on ASPI outlays are likely to be low level, and to some extent offset by savings as filmmakers pare budgets below the $1 million plus level demanded by the present threshold. For example, if 10 new films were made at the new threshold, with an average Offset contribution of $200,000, five might be films that would otherwise have been budgeted at the old threshold, with an average Offset contribution of $400,000. In that case, ASPI outlays would be unchanged. While there is likely to be some small impact, we believe this would be easily outweighed by the accruing advantages in innovation and sustainability.

Recommendation 1: Reduce the feature film QAPE threshold to $500,000.

6.2 Theatrical exhibition test for feature films

A similar concern about limiting innovation arises in connection with the theatrical exhibition test for feature films, devised and administered by Screen Australia. The test, which is designed to withhold the 40 per cent Offset from films that are not cinema films, requires that a film be made with the intention of securing a theatrical release. The Film Finance Corporation initially interpreted this to mean a release on at least six cinema screens. Bearing in mind the importance of certainty for lenders and investors, the six-screen test became a defacto standard with which films had to comply at financing stage to achieve all Offset-eligibility.

This test inhibited innovation in film distribution, at a time when the distribution sector has been actively experimenting with new release strategies that downplay the importance of the traditional release windows. What's more, by specifying a six-screen release as the only acceptable evidence of cinematic intent, the test elevated film distributors to the role of gatekeepers, handing them the advantage in the negotiations producers must initiate to gain access to the Offset. Anecdotal reports confirm that the test has undermined the ability of producers to negotiate favourable distribution terms.

The Forum applauds Screen Australia's subsequent decision to overturn this test and assess in a less prescriptive manner the producer's 'bona fide intention' to distribute the film theatrically. The Forum is of the view that maintaining this flexibility remains crucial in order for the industry to remain competitive and responsive to changing conditions in the marketplace, and argues that it should be the subject of ongoing review to ensure that the test remains open to accommodating innovative distribution arrangements.

The other critical issue is certainty, particularly in order to encourage private investment. We advocate investigating a move to a test that provides both flexibility and certainty. The 100 point identity test for opening a bank account provides one possible model for such a test that would achieve both of these objectives.

The Forum envisages that, in time, the theatrical distribution test may need to be replaced with a more flexible concept of a 'commercial distribution' test. The intention of such a test would be to enable innovation in distribution, and move beyond the idea that a theatrical release is essential in all cases. Even for major Hollywood movies, theatrical release has declined in relative importance as revenues from other media windows increases. A new test would better reflect these new marketplace realities.

Recommendation 2:	**Ensure that the theatrical exhibition test for feature films is flexible and certain and that it be reviewed with the objective of making it more accommodating of innovative distribution arrangements.**

6.3 Offset rate for documentary films

The Forum is of the view that the Producer Offset has not worked effectively for documentary productions. The administrative costs associated with accessing the Offset constitute a fixed cost and make up a larger proportion of overall costs for low-budget productions (which includes the vast majority of documentaries) reportedly ranging up to 25 per cent of the value of the Offset. Furthermore the small size of the Offset for most documentary productions puts them below the radar of financiers, leaving many documentary producers in the uncomfortable position of having to mortgage their homes to cashflow offset payments. It amounts to a great deal of effort and risk for very little real benefit.

Documentaries are important to the industry because they are an accessible format for emerging producers. They also have a high social value, often being directly educative and frequently contributing to more transparent and well-informed political processes.

One solution, canvassed by Screen Australia, is to bring low budget documentaries under its wing, in effect removing them from the Offset scheme. While this would free producers from much of the financing and administrative burden described above, it would also increase their dependency on agency funding. This would mean less doors for documentary production finance, and run contrary to the entrepreneurial principles embedded in the ASPI approach.

An alternative approach, which we believe most documentary producers would prefer, would be to increase the Offset for one-off and series documentaries to 30 per cent for documentary series. This would reduce dependency, and rebalance financing and administrative costs at a more acceptable proportion of production costs.

We note that this approach is unlikely to increase overall costs to the Commonwealth. At most increasing the offset to 30 per cent would have a marginal effect. This is because the documentary production sector's capacity to grow is capped by the size of the existing marketplace – primarily Australian broadcasters.

Recommendation 3: **Increase the Producer Offset for documentaries (single episode and series) to 30 per cent.**

6.4 Documentary threshold

Documentary producers find themselves in the same position as feature film producers, facing upward pressure on budgets to meet the $250,000 per hour documentary threshold, and an inhibited capacity to innovate in their production methods. Given the same diagnosis, we prescribe the same remedy: a reduction in the threshold, once again by 50 per cent, to $125,000 per hour.

Recommendation 4: **Reduce the documentary QAPE threshold to $125,000 per hour.**

6.5 Documentary above-the-line cap

The capping of above-the-line costs at 20 per cent of Qualifying Australian Production Expenditure, while appropriate for the higher cost film and television drama categories, is inappropriate for the much lower cost documentary category, in particular, single episode documentaries.

The above-the-line cap was adopted because of concerns about the scale of fees being paid to high-profile actors and other above-the-line elements. But these concerns do not apply to documentary production. In fact, the relatively high proportion of above-the-line costs in documentary budgets is purely an artefact of their relatively low below-the-line costs – that is, their small crew sizes. That documentaries have been caught up in this way would appear to be an unintended consequence of the capping decision.

In short, the cap penalises producers of these documentaries by discounting genuine and reasonable above-the-line costs, apparently for the sake of administrative uniformity. We propose that for single episode documentary productions the cap be set at 30 per cent, or $200,000, whichever is the lesser.

Recommendation 5:	**Increase the above-the-line cap for single episode documentaries to 40 per cent, or $200,000, whichever is the lesser.**

6.6 The 65 episode limit

Under the current arrangements Offset eligibility for TV series expires after 65 episodes. The logic for this appears to be that if a series achieves a run of 65 episodes a threshold will have been crossed that makes further support unnecessary. The series will have built an audience and brand and there will be sufficient content for the series to reach wider markets, including being syndicated.

There is concern that this logic may not be working out as expected. What may not have been taken into account is the way that the Offset itself affects the decisions of a television network (usually the main source of series funding) when a successful series reaches its 65th episode. The network knows that a *new* series will attract a 20 per cent Offset. Even a series that has run successfully for 65 episodes is risky – audiences are fickle and competitors emerge. Thus the introduction of the Offset has made starting a new series relatively less risky than continuing an existing one.

Whether or not this effect outweighs the benefits of continuing an existing series remains to be seen but early indications suggest that networks may be ready to drop series after the support of the Offset expires. If this is the result then the losses imposed by the unintended consequences of the 65 episode limit include: the costs of establishing new series, loss of brand and audience values associated with existing series, and the lost opportunity to build overseas markets for successful series.

We suggest that the current rules run counter to the objectives of sustainability and certainty, in effect penalising success and increasing the risks for producers associated with developing new series.

CASE STUDY

Issue: the 65 episode limit

One successful adult television series is nearing the completion of its 65 episodes and the producers have been informed by the network that further episodes are being developed but only up to the limit of the Offset and that further episodes cannot be made without the Offset.

The reduced Offset will make it more likely that a reasonably successful series will continue beyond 65 episodes, increasing its chances of international sales and building audiences and brand. Cancelling a successful series involves significant costs to producers, networks and investors. However, the reduced Offset recognises that the marketplace will be required to provide more support for additional episodes; but this additional support will not be so significant as to cause the cancellation. This continuity of production will be a significant support to the independent production sector in achieving sustainability.

Recommendation 6:	**Introduce a 10 per cent Offset for television episodes 66 to 130**

6.7 Children's programming

Whereas adult television programs are predominantly one hour in duration, children's programming is predominantly half-hour.

Because the cap on eligibility for the Offset is set at 65 episodes, this means only 32.5 hours of a typical children's series will qualify.

Thus by using episodes as the criterion for the cut-off, children's programming is made less attractive relative to one-hour adult drama.

The solution is to specify the cut-off in terms of hours rather than episodes. A limit of 65 hours would mean 130 episodes in half-hour format, which would brings children's programming to the same cut-off in terms of episodes as one-hour drama.

CASE STUDY

Issue: children's programming

Two series of an internationally successful Australian children's series were to be produced prior to the introduction of the Offset and a third series was produced with the support of the Offset, and with less subsidy given the number of episodes produced. The producer was able in this instance to find the balance of the funds required for the third series but cannot fund any further series without the Offset or the subsidy. This producer is facing similar difficulties with another series which will not have a third series at all even though it has achieved international success and would attract international commissions.

Recommendation 7: Replace the 65 episode limit for children's programming with a limit of 65 hours of programming.

6.8 PDV Offset threshold

The $5 million threshold set three years ago has been overtaken by the movement in the Australian dollar and by changes in the way PDV work is allocated to firms.

Industry practice now is to allocate large jobs between multiple firms in order to better manage the risks of delay and overrun in the completion of complex animation content. In light of this change, we support calls for the threshold to be reduced to $500,000.

In addition, in order to respond to competitive rebates being offered in other jurisdictions and to the appreciation of the Australia dollar, we support calls for the PDV Offset to be increased to 30 per cent.

CASE STUDY

Issue: PDV threshold

A leading Australian business has lost many opportunities to participate in international animation productions because of the high level of the PDV offset threshold. Particularly, the business had an offer from a well known global content producer to provide digital animation services for a production that would have qualified for the PDV offset but for the threshold of $5M and, had the threshold been $500,000, the contract would have been secured

Recommendation 8: Increase the PDV offset to 30 per cent and reduce the PDV threshold to $500,000.

6.9 Location Offset rate

The movement of the Australian dollar against the US dollar has more or less wiped out the competitive advantage conferred by the Location Offset. In the absence of an increased rate, it is difficult to see how Australia can successfully compete for international productions it might otherwise attract. Loss of these productions will have adverse short and long term consequences for the Australian industry and economy. Research undertaken by PricewaterhouseCoopers for Ausfilm suggests an increase in the rate to 30 per cent and the removal the 70 per cent minimum Australian budget expenditure requirement would restore competitiveness. We support this change.

Recommendation 9:	**Increase the Location Offset to 30 per cent and remove the 70 per cent minimum Australian budget expenditure requirement.**

6.10 Inclusions in QAPE

The current qualifying expenditure test includes all production costs associated with a film, but specifically excludes financing costs. While the Forum accepts this approach, it disagrees with the current exclusion of bond and insurance expenditure, which have been deemed ‘financing’ costs. Film production is complex and risky and has always involved insurance and completion guarantees as core budgetary items. Producers have always viewed insurance as production costs, and were bewildered when they were excluded from QAPE in the original ASPI announcement.

The Forum argues that insurance and completion bond costs should be included as legitimate production expenditure under QAPE in a manner that reflects industry realities.

Recommendation 10:	**Include insurance and completion costs in allowable QAPE expenditure.**

6.11 Provisional certification

There has been a reported case of a producer fee being approved at provisional certification stage but disallowed at final certification. Such variations in approvals, where there is no change in the underlying facts, are highly damaging to lender confidence in the ASPI scheme. We would urge Screen Australian to make consistency a priority in its administration of the scheme.

Recommendation 11:	**Ensure that consistency is a priority in the administration of the ASPI offset schemes.**

6.12 Producers’ terms of trade

A recurrent issue for producers, especially television drama producers, is the vulnerability of the Producer Offset to be captured by third parties such as film distributors and television broadcasters, including public broadcasters. It is not that these parties baldly demand that the Offset be paid over to them (although there were early reports of such demands by broadcasters). Rather, it is the capacity of the parties to vary other deal terms, such as license fees or distribution advances, so as to appropriate some part of the value otherwise accruing to producers from the Offset scheme.

This directly threatens one of the fundamental objectives of the Australian Screen Production Incentive – building companies' sustainability over time. The issue of terms of trade is a matter that needs serious addressing across the board, by all government agencies – including state and territory agencies, and public broadcasters – and should also be considered by ACMA (taking a lead from approaches adopted in the UK that have been remarkably successful in helping build the UK television industry over the past 10 years).

CASE STUDY

Issue: certainty of Offset

Producer fees were recently reduced by Screen Australia in a final certificate from the amount included in the application for the provision certificate provided for a project. The reduction was to an artificial level that Screen Australia determined was the arms length proportion of producer fees in relation to the total budget. This had a significant effect on the producer's business and has adverse implications for offset lenders.

We propose that constructive efforts be made to reinforce the capacity of both film and television producers to retain the beneficial ownership conferred on them by the Offset, and to discourage its appropriation, directly or indirectly, by third parties. Other efforts could include, for example, active monitoring and benchmarking of deal terms negotiated by producers with distributors, broadcasters and other third parties. Such benchmarking would draw attention to anomalous terms and at the same time arm producers and investors with more information about the market. A further approach in the case of television production, perhaps beyond the scope of the present review but relevant to the planned 2011 review of local content rules, could be to link the earning of local television content quota points to the value of the fees paid by broadcasters to license qualifying productions. In effect this approach would reward broadcasters for the higher average license fees necessary to trigger local production.

Recommendation 12:	**The industry and screen agencies to develop strategies aimed at supporting producers' interests such as benchmarking deal terms.**

6.13 Administration and compliance costs

There is widespread concern among producers at the burden of costs associated with the ASPI scheme, and the Producer Offset in particular. Some of this burden no doubt reflects the newness of the scheme and the adverse impact of the global financial crisis.

As the market for Offset lending deepens, there may be some reduction in financing charges and transaction costs. Nevertheless, the burden is significant and, as noted above, falls disproportionately on smaller productions. We would urge the Department and Screen Australia to use their best endeavors to streamline processes and reduce cost impositions where possible.

Recommendation 13:	**DEWHA and Screen Australia to use their best endeavours to reduce cost impositions on producers.**

6.14 Tax secrecy

An important issue, largely unforeseen when the ASPI scheme was introduced, is the information consequences of the scheme's location within the tax system. Effectively, for reasons of tax secrecy, the scheme operates within a ‘black box’, impenetrable even to Screen Australia, which administers it. So little information is emitted that exercises like the present review must work with very limited data. This inhibits analysis. While we appreciate the strict confidentiality required for tax matters, we would urge the Department and Screen Australia to explore possible solutions to this problem and work with the industry towards them.

Recommendation 14:	**DEWHA and Screen Australia to explore ways to improve access to information about the outcomes of the ASPI scheme.**

6.15 New media content and digital distribution platforms

The digitisation of traditional media content formats and the emergence of new ones as well as the emergence of new distribution platforms and business models means that support mechanisms that focus on traditional distribution channels may become obsolete. There is significant uncertainty about the extent to which Government should support these new media forms. We believe that it is necessary to evaluate the extent to which rationales for government support of film and television content apply to new media and new distribution platforms. This is an appropriate area of inquiry for Government and industry.

Recommendation 15:	**Establish a joint industry-Government working party to examine future possible offset treatment for emerging digital content and platforms.**