

Film Inquiry
Submission No. 63.....



YORAM GROSS-EM.TV PTY. LTD.

**SUBMISSION TO THE HOUSE OF REPRESENTATIVES
STANDING COMMITTEE ON COMMUNICATIONS,
INFORMATION TECHNOLOGY AND THE ARTS**

*Inquiry into the future opportunities for Australia's Film,
Animation, Special Effects and Electronic Games Industries.*

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An Introduction to Yoram Gross-EM.TV

First established by Yoram and Sandra Gross in 1968, the studio has evolved into a highly respected producer of animation for cinema, television and video, distributed worldwide. Yoram Gross-EM.TV is internationally recognised as Australia's leading producer of quality children's and family entertainment, encompassing both the animation and the interactive technology industry, the latter through Forest Interactive, a division of Yoram Gross-EM.TV.

The last decade has witnessed an even greater international profile for the Yoram Gross studio, whose television series, which include *Blinky Bill*, *Tabaluga*, *Flipper and Lopaka*, *Old Tom*, *Skippy and F.T.P.D.*, have reached a worldwide audience involving an array of international co-producers. Since 1992 the studio's co-production partners have included UK's BBC; Sesame workshop of the USA; ARD and ZDF of Germany; Teleimages S.A. and Millimages of France; EM.TV and VIDEAL GmbH of Germany; and Nelvana Ltd of Canada; as well as Australia's ABC, Network 9 and The Seven Network.

With EM-TV & Merchandising AG acquiring 50% of Yoram Gross in March 1999, Yoram Gross-EM.TV has made the transition from a family business to a strong player on the world stage.

The Seven Network currently programs a dedicated block of television produced by Yoram Gross – a fulfilment of its commitment to screen quality 'C Classified' drama for the children of Australia. Yoram Gross-EM.TV has recently launched *Junior* in Australia, which also holds a dedicated block of programming on the Seven Network plus spot shows on both Nickelodeon and FoxKids.

Wholly-owned subsidiary, Forest Interactive, is a new media producer, specialising in DVD authoring, Internet content and design, CD ROM products, digital style guides, games and game engines. Forest Interactive was established in 1994 in recognition of changes in entertainment media. It has rapidly grown into one of Australia's most creative new media developers producing such titles as *Blinky Bill's Ghost Cave*, which was translated into 11 languages and achieved the 'Number One Children's CD-Rom' place in Germany.

The plan to expand Yoram Gross-EM.TV's position and business both locally and internationally will continue as a core mission.

Due to the breadth of the terms of reference of the Standing Committee's inquiry into Australia's film, animation, special effects and electronic games industries we have chosen to first provide an overview, and then address particular terms of reference in greater detail but primarily by reference to the animation and electronic games industries. This review is very much from our perspective, but we feel our thirty years of experience and broad view of the business can make our contribution significant.

AN OVERVIEW OF ANIMATION PRODUCTION AND THE AUSTRALIAN ANIMATION INDUSTRY

At the time of writing, the latest edition of *Encore Magazine* lists nine animated projects as being currently in production within Australia. Four of these projects are being produced within the Yoram Gross-EM.TV studio.

The life of an animated production can be roughly divided into a number of stages,

- concept acquisition and development
- financing
- production
- exploitation

Concept Acquisition and Development

As an independent producer, YGEM maintains a strong development slate of new projects. These projects may either originate within the studio, be acquired ("optioned") from third party creators, including existing published properties, or may be presented to YGEM by international co-production partners.

Over the past four years YGEM has optioned twenty-eight projects. The key factors in identifying a project to develop are the quality of the idea and its potential appeal to the international market. The reality of animation production is that projects must have strong international appeal in order to be successfully financed, although YGEM has a proud history of developing Australian properties¹,

The projects will then undergo further development within the studio with a view to determining whether the project can proceed to production. The creative side of the development process includes:

- Story ideas and series outline
- Episode synopsis
- character design

¹ Properties produced or in development include *Blinky Bill* (three television series and one feature film), *Dot & the Kangaroo*, *Old Tom* and *Snugglepup & Cuddlepup*.

These elements may then be combined in the preparation of a "bible" for the project (see Annexure "A" by way of example of a bible for a project currently in development at YGEM).

On the business side, the project will be discussed with foreign production houses, investors and distributors or sales agents. The project bible will be instrumental in this process, and will be presented to potential partners at foreign television markets.

Finance

A number of different sources of finance are utilized, both domestically and internationally. These include:

- pre-sales to television networks both in Australia and overseas
- domestic equity investment, including from the Film Finance Corporation Australia ("FFC") and private investors (usually under Division 10B or 10BA of the *Income Tax Assessment Act*)
- international equity investors, including foreign co-producers and media funds
- the provision of pre-sale financial guarantees by distribution companies that may be either cashflowed into production or used to assist in the generation of investment

Given that the Committee's focus is said to not be upon Commonwealth funding issues or taxation treatment, we will not consider the role of either the FFC or the operation of Division 10B or 10BA in detail, but only as these may arise in relation to other issues.

In seeking to raise finance it is critical that an Australian producer be able to bring a significant amount of the budget to the negotiating table in order to reach a competitive deal with foreign investors, co-producers, and distributors. In this context the Australian content standard² plays a pivotal role.

In short, the Content Standard requires that the commercial domestic networks broadcast a minimum of 96 hours of new Australian children's drama ("C" drama) over a three-year period. Most YGEM productions are eligible as "C" drama and accordingly attract a premium license fee from the networks³. This enables YGEM to generate, on average, approximately 15% of the budget for an animated television series from the Australian broadcast sale.

On the other hand, license fees for sales to the local commercial networks of children's animated productions that are not "C" drama tend to be much lower.

² The Australian Content Standard is administered by the Australian Broadcasting Authority and is derived from the *Broadcasting Services Act 1992*

³ Until this year the Australian Content Standard provided protection for the minimum license fee by prescribing a minimum purchase price of AUD\$45,000 per episode. After intensive lobbying from domestic networks the minimum fee has now been removed. The impact of this change remains to be seen.

Such sales (AUD\$2,000 per episode) would amount to less than half of one percent of an average YGEM animated production budget. Given the realities of business, it is reasonable to predict that commercial networks would not purchase "C" drama programming at the current levels without the obligations imposed by the Australian Content Standard. The maintenance of the Standard is therefore KEY to the long-term survival and health of the children's animation industry.

Notwithstanding a high network license fee the majority of the budget for an animated production must be sourced from overseas, hence the necessity for international sales appeal. Australian animation has been remarkably successful in this regard, regularly attracting presales with networks in major European territories that in turn can trigger distributor interest and foreign investment. It is extremely difficult to achieve any level of market penetration, however, in the United States, and in calculating financial returns for a new series it is commonplace to remove a US sale from the equation as the likelihood of a return is relatively remote. It is therefore fascinating that reports of recent trade negotiations have suggested the US be given greater access to the Australian television marketplace, and that local "protections" such as the Content Standard be removed or diluted. Melodrama aside, any such move would be disastrous for the local industry, and the animation industry in particular. In any event, a glance at the daily television guide indicates no apparent shortage of US content on Australian television screens.

Even with overseas presales and a high domestic license fee Australian producers will struggle to fully-finance an animated production without FFC involvement. Accordingly international co-productions are increasingly seen as an important structure for animation producers⁴.

Administered by the Australian Film Commission ("AFC"), the official co-production program allows Australian producers to involve international production partners in the financing and production process whilst maintaining the project's eligibility for Australian funding mechanisms and status as Australian content. However, there are some difficulties with the co-production program that could perhaps be resolved by way of greater attention from Government.⁵

⁴ Of nine animated projects in full production at YGEM since 1998, three have been co-productions produced pursuant to official treaty or Memorandum of Understanding arrangements between Australia and other countries.

⁵ There is particular concern in relation to the arrangements with France, as the "MOU" does not have the status of a treaty, is considered only an administrative arrangement, and is therefore conflicting – to the detriment of Australian producers – with European Union content arrangements. By contrast, the Canadian government has successfully lobbied its French counterpart and achieved more favourable arrangements that are of benefit to Canadian producers. This has led to the facilitation of more co-productions between those two countries.

Production

On average at YGEM a new project is commenced every six months, and the studio has the capacity to maintain four animated projects in production at any one time. Within the studio there are sixty-one full-time employees, whilst a range (between ten and thirty) of freelance independent contractors will be engaged to provide services for any single production. These contractors include scriptwriters, character designers, storyboard artists, layout artists, composers and musicians.

In addition, ancillary service businesses such as audio studios, post-production services and the like are utilised during the production process. It is fair to say that up to 150 Australians are employed across the eighteen-month cycle of each animated series.

The key creative aspects of production take place at the YGEM studio. However, for cost-saving reasons certain repetitive and non-creative aspects of the animation process are sub-contracted to overseas facilities in locations such as China, Hong Kong and the Phillipines. As a matter of simple economics it is not viable for these functions to be carried out in Australia.

Exploitation

Exploitation has been touched upon above in relation to pre-sales and the importance of the Content Standard in maintaining license fees.

One further point is that the advantage of animation over other forms of television is that quality animated productions have a relatively long life in terms of exploitation. Whilst live action productions can quickly date, often becoming merely of novelty value within a year or two, an animated production can maintain its appeal for a much longer period. This is given added significance in relation to the child audience, a section of the viewing community that is constantly renewed.

In addition, foreign-dubbed animation is more readily accepted by foreign audiences than dubbed live action.

THE TERMS OF REFERENCE (TOR) OF THE INQUIRY – ANIMATION FOCUS

(a) The current size and scale of Australia's animation industry.

and

(b) The economic, social and political benefits of the animation industry.

To an extent our comments on TOR (a) and (b) are encompassed in the overview above. Although the Australian animation production industry is relatively small, by necessity or otherwise it has a presence on the world stage. YGEM programs are distributed throughout the world, and new productions regularly attract pre-sales from major overseas networks in territories including Germany, France, Italy, the United Kingdom and Asia. It is noteworthy that animation is the easiest genre to sell internationally.

Economically the benefits of local animation extend beyond the creation of jobs within the production industry itself, and the "animation industry" must be recognised as a component of the wider television/entertainment/media industry. For example, important aspects of the exploitation of a YGEM production typically include:

- product merchandising
- video and DVD releases
- print publishing; and
- live costume character stage shows

One YGEM property generated in excess of AUD\$10m during the period 1992-1999 from merchandising alone.

These "spin-off" benefits are significant contributors to the local economy, and provide a counterpoint to internationally-produced entertainment products. From a cultural viewpoint it is important to ensure that there is an Australian perspective presented both locally and internationally in regards to both kids and family animation.

(c) Future opportunities for further growth of these industries, including through the application of advanced digital technologies, online interactivity and broadband.

and

(d) The current and likely future infrastructure needs of these industries, including access to bandwidth.

There is no reason why Australia cannot be as strong as countries like Canada, France and the Ireland in regards to its contribution and output of quality animation regardless of format (2D, 3D, Flash etc...). The major impediment to our international standing is the commercial and financial reality of our base local market size and our geographical distance from the key world markets and producers/distributors. This can only be addressed with creative Government and industry support.

It is still too early to predict the impact broadband and digital distribution will have on the overall market. There is an unfortunate paradox where as potential channels and means of distribution increase the returns from those channels and means decrease. This makes it very difficult to calculate viable financial models.

During internal discussions at YGEM with production and technical staff in relation to TOR (c) and (d) the following points were raised:

Current infrastructure

- Australia has the infrastructure for Bandwidth access but it is limited.
- Access to Bandwidth is limited due to its prohibitive cost. It is the only product that goes up in price the more you purchase.
- Currently Bandwidth is not efficient due to the limited access, anything over 3MB takes all day. It is faster and more reliable to use Fedex.
- All animation is now digital information, and therefore could benefit enormously from an accessible and cost-effective broadband infrastructure.

Future infrastructure considerations

Communication

- If current bandwidth was more accessible it would be possible to improve communication through such means as Video conferencing. This would be of particular aid in international Co-Productions.
- Real-time transmission and feedback would aid in communication and time management, potentially translating into budgetary improvements.
- Digital Pipeline allows multiple transmissions – could video conference and look at the material sent at the same time, as well as making changes.

Delivery

- Delivery would also be improved if current bandwidth was more accessible. Sending large files to Overseas partners and Co-Producers would improve delivery and aid in the editing process.
- Through a direct pipeline finished materials could be sent to the relevant people. This would aid with revisions and retakes.
- Hi definition TV means much bigger files and infrastructure would have to be able to accommodate this. High Definition requires 4-5 times the bandwidth of Standard Definition.

- It could be possible for someone to be working on material that is in another country = real-time feedback.

Creative Possibilities

- Providing multiple soundtracks and viewing option for television.
- Possible to run our own website and stream our old films without having to be hosted by the ISP.
- Technology is only a tool - you still need to create the story. Education and training in technology needs to be more closely allied with the study of the creative arts.

(e) The skills required to facilitate future growth in these industries and the capacity of the education and training system to meet these demands.

There needs to be a much higher level of dialogue between the training programs and the industry. There is a danger that the private colleges have profit more as a motive than appropriate feeding of the industry at large. It is all too easy to attract young students to the "glamour" of the entertainment business rather than basing enrolment upon the industries needs. Consequently there are many wide-eyed graduates with no appropriate job prospects.

In our view there is a current lack of understanding in new graduates of basic elements of the animation craft such as perspective, colour, storytelling, human movement and writing. Current courses appear to point students in the wrong direction, focussing too much on the technological tools and neglecting the creative side.

In the future additional foundations on the technology side should supplement the basic core skills training on the creative side.

(f) The effectiveness of the existing linkages between these industries and the wider cultural and information technology sectors.

We believe that all current linkages are ad hoc at best. There is definitely a lag and quite possibly a significant lack of new knowledge of the potential of new technologies for the animation business and likewise a misunderstanding by the technologists of the creative core of content creation. This is further compounded by the erratic and often hyperbolic developments and claims of the technology sector. A perfect example was claims that we could watch TV over the Web and when we all tuned in we were greatly disappointed and went back to the lounge room.

(g) How Australia's capabilities in these industries, including in education and training, can best be leveraged to maximise export and investment opportunities.

Please refer back to (e), but also note the following.

Despite the concerns detailed here, Australia has achieved a remarkable degree of respect in the global industry – HOWEVER, so have Canada, New Zealand, Ireland...etc. We need to constantly market our achievements and monitor the activity of our competitor nations so that we can meet their challenges to our continued growth.

(h) Whether any changes should be made to existing government support programs to ensure they are aligned with the future opportunities and trends in these industries.

Much greater fiscal and direct financial flexibility and creativity in how the industry is supported is needed. All too often we are trying to fit a square peg into a round hole to make our business commercially viable.

Australia only has a population of approximately 20 million to support its local industry – the concept of a level playing field between us and a country like the USA, with a base market of 260 million, is absurd in the extreme.

Because we are dealing with content that has to be culturally flexible to compete on the world market, there must also be a significantly more realistic and flexible approach in regards to local content standards. Our business, in particular, without any Government support requires up to 85% of a projects budget to be derived from outside Australia. We not only compete against heavily subsidised countries like Canada, France, Ireland and the UK, but also against relatively closed territories such as the USA, China and Japan.

Due to the hegemony of the USA a free trade agreement will not be free when it comes to entertainment content. We need to both protect our patch of cultural ground as well as encourage flexibility in the content we create, so that our programs will be enjoyed both by ourselves and the international market.

THE TERMS OF REFERENCE OF THE INQUIRY – INTERACTIVE FOCUS

c. future opportunities for further growth of these industries, including through the application of advanced digital technologies, online interactivity and broadband

Forest Interactive, a wholly-owned subsidiary of YGEM, is a producer of children's entertainment and edutainment products. For the first 6 years of Forest's life its core business was CD-Rom production with an attractive low risk/ low development cost model. This business is no longer a viable option due to

- The dilution of the children's market across many new channels of delivery (eg: Pay TV, game platforms, on-line digital TV etc)
- Free content available on the internet
- Massive drops in price point for CD-Roms and a retail market oversaturated with cheap titles
- Retailers reluctant to give shelf space to this low margin low turnover product, giving preference to high margin high turnover console titles.

- Younger and younger kids turning to console games previously only played by late teens
- Kids content available on console and hand held platform

Further growth in the electronic games industry requires moving to new platforms for delivery of the content as well targeting an older audience in the short term to maintain profitability. In the long term it requires a rebuilding of the kids market as children's content must not be sacrificed.

Emerging Markets include: Mobile phone gaming, Broadband, Interactive TV and Interactive DVD

Threats:

- PC games market shrinking while console games is expanding
- Pressures to decrease cost of developments in light of falling sales volumes worldwide
- Falling RRP's and changes in technology – We must find cheaper ways of developing CD ROMs or increase sales locally and internationally
- Greater financial risk when move into 3rd party deals on new development deals – especially across new technology which is highly competitive
- Cost of entry into new markets; development, prototypes, sales, increased overheads, loss in profitability
- Consolidation of games industry worldwide means more developments come from fewer developers and only larger, prominent developers with AAA titles are being encouraged to release new games
- Fast changing market – We must move rapidly to keep ahead of competitors

Current Gaming Platforms

1. Handheld (Gameboy, Gameboy Advance and Sony PSP (to be released 2004).
Handheld is best platform for kids games – espec Gameboy. But Sony PSP most likely will be a platform for all ages gaming.
Development costs: \$100K to \$250K – however must have a License
2. PC
Whilst kid's CD-Rom is a dying channel, reference and utilities (eg language, clip art ect) continue to sell on PC, albeit in limited numbers with the advent of internet competition. However, hardcore, high-end games for PC remains a robust market and still a competitor to console. For this reason many successful titles are released on both PC and console.
Development costs for PC are slightly lower than for console (no licence fees), but net profits are lower on a PC title than for its PlayStation equivalent. So whilst risk is lower for PC development, the potential pay off is higher with console.
Average Development costs: AUD\$900,000 – 2.25 million
3. Console (Xbox, Playstation, PS2, Gamecube)
Violent action games aimed at teens and up dominate the console game market as this is clearly where the biggest money is to be made. Games for

younger children do exist but only based on very strong licences (eg Disney) and backed by companies who can take the risk. Development for console is an extremely expensive and high risk exercise that mirrors the feature film model – to the extent that many games are based on well known licensed characters from film and TV.

Development costs: min AUD\$2.25 million - 3 million

4. Online

A barrier to further development in online interactive content development is the much discussed current problems with rollout and take-up.

Prohibitive costs and lack of availability severely limit the number of Australians on the internet. Without an audience there is no support for content development. The revenue model – or lack thereof also needs to change. The ISPs need to start behaving like content deliverers (eg TV stations) and start paying content providers for the content. Most internet content is expected to be provided free of charge, with the ISPs and Telcos taking all revenue as phone call charges and service provision fees.

The lack of broadband infrastructure and accessibility is also an impediment to developers as upfront costs in obtaining and maintaining broadband connection in order to develop content and keep up with what's happening in the rest of the world, is prohibitive.

The future for broadband online multiplayer gaming is potentially huge, propelled by the advent of new consoles. Xbox and PS2 have internet connectivity. However it is early days with only a few really successful titles. A current trend the licensing of triple A big name products for online games (eg the massively multiplayer online game (MMOG) The Matrix Online). The Online Game Market, the MMOG market is still very much in the "early adoptor" stage. As best shown by tepid sales for The Sims Online, big names and large marketing budgets often do little to drive "early adoptor" sales. Note that online gamers must be connected to a broadband Internet service so again growth is limited by broadband accessibility.

There needs to be an awareness of the potential tempered with an element of caution, a clear strategy for building up the online gaming community, and sensible revenue models. While several online role-playing games for PC currently earn significant subscription revenues, most other attempts at online "pay per play" gaming have failed.

Developing for Australia

Australia is too small a market to develop interactive content in isolation, leaving aside the current barriers to broadband adoption. To date all our CD-Roms have been successful via international sales deals. There needs to be more understanding and support for Australian interactive companies – more opportunities for co-production with overseas partners, support for travel, and worldwide networking opportunities.

Example: AusTrade has offices in the USA and has a presence at E3 – the largest international Electronic Games Industry Expo. The AFC, who have a small fund for interactive development and grants for travel to interactive trade fairs were not only unaware of AusTrade's presence at E3, they were completely unaware of E3 at all.

Most companies represented at the AusTrade stand, and the most successful interactive companies in Australia, are Melbourne based. It appears that the Victorian Government has a better understanding of and offers far greater support to the interactive industry than NSW government. In one sense Forest is penalised for being based in NSW and cannot benefit from any of the opportunities afforded Victorian companies.

d. The current and likely future infrastructure needs of these industries including access to bandwidth

see above

e. the skills required to facilitate future growth in these industries and the capacity of the education and training system to meet these demands

The education and training system is largely inadequate. Arguably it is in a difficult situation, with the electronic gaming business in such a constant state of growth and flux.

Most people in the industry are self taught – and have worked their way up the company.

Some have done crash courses at one of the many private colleges and emerge with the belief that they are experts in the field. Their real learning is in the workplace. As an employer, Forest tends to avoid anyone from these courses, choosing university graduates or personnel with proven experience instead.

Skilled personnel is harder to find in some areas than others. Graphic and web design skills are more common than programming – particularly interactive game programmers and particularly lingo programmers who are most rare of all. There are no known courses for learning lingo properly, although it is touched on to some degree or other in many courses.

The very specialised fields of Electronic Game conceptualisation, production, project management and commercialisation are skills that are not taught anywhere. All practitioners in this field seem to be self taught and to have evolved to these roles from other disciplines. Most challenging of all for an Australian game company is finding adequate funds for each production. These funds can rarely be found within the country and it takes good international contacts, tenacity and who knows what amount of luck to fund a project, then sell it once it is completed.

Overview of some study courses (*graduate comments italicised*)

- COFA/ UNSW: Bachelor of Digital Media

Covers web design, multimedia design, motion graphics, desktop compositing, 3D modelling and animation, video editing, sound design, sound editing, digital composite. Touches on Director lingo and HTML enough to facilitate design in Director and for the web.

- Overall a very good course.
- First year the course ran was in 2000. It was a bit all over the place, but has now settled down. There has been an upgrade of equipment, and there are now more computers. Very high demand course and hard to get into – needed high marks.
- Crosses over with standard graphic design
- Still evolving to strengthen the conceptual side. Didn't feel really taught how to design and conceptualise.
- Should be a 4 year course. Trying to do too much.
- Nice and broad – gives you a taste of all then lets you specialise in years 2 – 3.

UNSW also has computer science courses for intense programming.

- UTS – Bachelor of Design in Visual Communication – more conceptually based.
- Bachelor of Media Arts and Production (used to be called communications) – broad, can major in film or sound or etc. Do not have 3D.

These two courses are comparable with UNSW course above.

- Computer graphics College, East Sydney - Diploma in Multimedia production

Private institution

1.5 years full time (3 days/week)

"Great course – shovelled it in. Tonnes of info. Money well spent. I came out of it being able to handle every situation"

Subjects:– lingo programming, html, javascript, 3D modelling and animation (infinD), digital audio (sound editing, mixing, making techno music using "Rebirth"). Flash, Director, After Effects, video editing, graphics/web graphics (Fireworks, Photoshop, Illustrator, Freehand)

Well equipped with lots of computers.

g. how Australia's capabilities in these industries, including in education and training, can be best leveraged to maximise export and investment opportunities

Australia needs to raise its profile. This is largely a PR exercise. American and Europeans – our greatest potential partners - see the distance a great barrier and traditionally see Australasia's use only as a source of cheap labour. The most successful Australian gaming companies are mostly outposts for the large international publishers providing rendering and modelling farms.

The insular American market is a particularly tough nut to crack and exporting content to this territory is extremely difficult.

Greater support network within the industry would also be a help. Despite the reasonable number of interactive companies in Australia and some apparently successful ones, we feel entirely alone and feel we are working everything out from first principles every time. We see each other as competitors, rather than working together to get out into the rest of the world. Not only within the private sector. Lack of a focussed approach and communication is clearly evident within the government (see note about Victorian support for Interactive *vs* NSW and note about AFC unaware of AusTrade activities). The government should also look at the Canadian Government as a good example. Canada is now well and truly on the world map as a source of great interactive content, film and television content. Various treaties and government cash and tax incentives make it a more attractive location for filming than Australia and a more viable partner for co-production as well.