

Film Inquiry Submission No. 85

FILM VICTORIA

**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 ELECTRONICS GAMES INDUSTRIES**

JUNE 2003

This submission has been prepared by Film Victoria in response to the invitation by the House of Representatives Standing Committee on Communications, Information Technology and the Arts to contribute to its Inquiry into The Future Opportunities for Australia's Film, Animation, Special Effects and Electronic Games Industries.

The submission should be read in the context of "Growing Victoria Together", Victoria's vision for the future, and "Creative Capacity + ", Victoria's Arts policy.

Film Victoria acknowledges the Inquiry's Terms of Reference. This submission addresses itself to all Terms of Reference, except points (e) and (f).

The four Government bodies with responsibility for aspects of the film, television and multimedia industries in Victoria are as follows:

Film Victoria is the Victorian Government's film body providing strategic leadership and assistance to the film, television and multimedia industry of Victoria.

Film Victoria encourages innovation and the creation of projects of high quality that are of economic and/or cultural benefit to Victoria. Film Victoria, through the Melbourne Film Office, offers incentives to encourage interstate and international producers to locate film and television projects in Victoria.

Australian Centre for the Moving Image (ACMI) is the Victorian Government film agency chartered with promoting the moving image in all its forms. ACMI's facilities at Federation Square in Melbourne include integrated studios, galleries and cinemas that sit on a single delivery broadband network.

ACMI is a continuous research platform that engages general audiences and special interest groups through exhibitions, screenings, education, production, events, lending services and other activities. It is Australia's first Centre dedicated to experiencing, enjoying and exploring the moving image in all its forms.

Multimedia Victoria is the Victorian Government film agency responsible for implementing the Government's information and communications technology policy. Multimedia Victoria has secured Victoria as the game capital of Australia. Its priorities are to improve infrastructure required by the game industry, grow local businesses and develop skills.

Arts Victoria delivers services and programs to enhance the contribution of the creative industries within the Victorian community. A Division of the Department of Premier and Cabinet, Arts Victoria provides high quality advice and leadership in the implementation of the Government's arts policy.

Film Victoria looks forward to working with the Commonwealth of Australia to address and resolve the issues canvassed in this submission.

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EXECUTIVE SUMMARY

Film, Television and Multimedia

Until the 1960's there were few Australian voices heard telling Australian stories on our screens. As a result of Commonwealth support our stories have been heard, in our own voice, in our cinemas and our homes. Internationally our stories have brought an increased understanding of Australia and Australian culture in its many aspects to a wider audience.

Australians are proud of the achievements of their film and television industry and the international recognition it has won. That would not have happened without the support successive Commonwealth Governments have extended this industry.

The Vic Govt

Film Victoria is committed to a vibrant film, television and multimedia industry. It is an integral part of the State's economy and Victoria's social fabric. Ideas converted into the moving image are consumed by nearly 100% of the Australian population. The influence of these creative industries is far reaching and long lasting.

Economically these labour intensive industries can only continue to grow if given the assistance, infrastructure and regulatory environment they deserve. Culturally they are critical to the development and expression of Australian identity.

Film Victoria's recommendations are as follows:

- **Maintain protection for Australian cultural industries under FTA and GATS.** Film Victoria recommends the Commonwealth ensure that any agreements entered into following negotiations for the General Agreement on Trade In Services (GATS) with the World Trade Organisation and the proposed Free Trade Agreement (FTA) with the United States of America not compromise or curtail support mechanisms and regulations that may exist presently for the Australian audiovisual sector, or that any Australian government might wish to implement in the future. (page 9).
- **Revise the 12.5% tax offset to television production.** Film Victoria recommends the Commonwealth revise the 12.5% refundable tax offset measures to include episodic television and telemovie and straight to video film packages where the total value of production exceeds \$15 million. (page 7).
- **Expand the FLIC scheme.** Film Victoria recommends the Commonwealth should review and expand the Film Licensed Investment Company scheme with a view to issuing licenses to a wider range of companies. Criteria for the revised scheme would encourage diversity among applicants, thus ensuring a range of options for filmmakers. A tax offset should be considered to encourage investors. (page 6).
- **Require Australian television networks to commission children's animation.** Film Victoria recommends the Commonwealth revise its Australian Content regulations for children's television to require television networks to commission an amount of Australian children's animation programs annually. This amount would be in addition to the "C" classified material presently required of networks. (page 10).
- **Improve broadband access for film, television and multimedia production.** Film Victoria recommends the Commonwealth implement the recommendations of its Broadband Advisory Group without delay with particular reference to the needs of this sector. (page 5).

The Computer Game Industry and Digital Data

Henry Jenkins, Professor of Comparative Media Studies at Massachusetts Institute of Technology, argues that computer games will become the most significant art form of this century.

If distinctly Australian games are to be part of the international computer game landscape this country has to move to secure its fledgling game industry. In the early days of silent films Australia had a thriving industry. It lost its way, and it took a half a century for the industry to be reclaimed. The same thing cannot be allowed to happen with the game industry.

It is impossible to predict where the computer game industry will go, or what form its content will take. The medium is in its infancy and content of most computer games is simple although the games are increasingly multilayered and offer complex scenarios and choices. The technology will allow ever more choices and convincing virtual worlds and modes of interactivity.

Games will become increasingly important to filmmakers to exploit the intellectual copyright they have created in their films. Conversely films will be made of Australian game content.

If this country's children had no exposure to Australian content on television, in film, on video, in theatre or in books, their concept of their place in the world would be quite different. Australia's game industry must be secured and developed if there is to be Australian content for Australian players.

Victoria has embraced and encouraged all new forms of media - celebrated at the Australian Centre for the Moving Image. Victoria has been foremost among the states in fostering its game industry and is working in partnership with the industry to consolidate the State's position as the computer game capital of Australia.

Film Victoria's recommendations are as follows:

- **Establish a Game Finance Corporation.** Film Victoria recommends that the Commonwealth consider the establishment of a body similar to the Film Finance Corporation to support Australia's game industry. (page 17)
- **Extend 10BA to the game industry.** Film Victoria recommends that the Commonwealth consider the extension to the game industry of the taxation benefits associated with Division 10BA of the Income Tax Assessment Act 1936. (page 18)
- **Extend the 12.5% tax offset to the game industry.** Film Victoria recommends the Commonwealth extend the 12.5% refundable tax offset measures applying to the film industry to the development of electronic games. (page 18)
- **Review and enhance programs to promote Australia's game industry internationally at the major markets.** (page 18)
- **Modify Australian Bureau of Statistics surveys to provide data on creative digital content and its providers.** (page 19)

1 FILM, TELEVISION AND MULTIMEDIA IN VICTORIA

1.1 Film and Television in Victoria

The cornerstone of Victoria's drama production industry has always been television, reflecting the legacy of Crawford Productions from the 1960s.

Television production has some economic advantages over feature films. Production periods are longer. Series like *Blue Heelers*, *Neighbours* and *The Secret Life of Us* can be in production for a number of years. Long term employment is generated in an industry where personnel sometimes have to cope with bursts of activity interspersed with periods of unemployment or underemployment. However both feature film and television are needed to sustain a healthy industry in the long term.

In the four years from 1998/99 to 2001/02 Victoria accounted for 34% of national television drama expenditure. Victorian feature film constituted 12% of national expenditure. The disparity is accounted for by the high dollar value of "foreign" films shot at the Fox studios in Sydney, such as the *Star Wars* prequels and *The Matrix* series. With the completion of the Docklands Studios in Melbourne and increased feature film development funding, Victoria's share of feature film production is expected to increase.

1.2 Multimedia in Victoria

Victoria leads Australia in the development of computer games. In the early 1980's Alfred Milgrom's company, Beam Software, developed *The Hobbit*. Beam Software had a similar effect to that of Crawford Productions a decade or two earlier, with ex-Beam personnel establishing their own companies. Now half of the country's game developers and the largest publishers are based in Melbourne, as is the Game Developers Association of Australia.

As Australia's first centre dedicated to experiencing, exploring and enjoying the moving image in all its forms, ACMI, will place special emphasis on game content – celebrating the computer game industry's achievements and highlighting the cultural significance of the medium.

1.3 Victorian Government Support For Film, Television and Multimedia

In 2000 the incoming Victorian Government, responding to industry concerns, established a Film Industry Task Force chaired by Sigrid Thornton. The Victorian Government, which committed itself to revitalising the industry, accepted the Task Force's recommendations.

The Government nominated the film and television production industry as a Strategic Industry Sector. \$31 million was allocated for industry development and investment in film, television and multimedia production. \$40 million was committed to the construction of a studio complex at Docklands. Film Victoria and ACMI were established as statutory agencies on January 1, 2002.

The Government, through ACMI, supports the collection, interpretation, creation and exhibition of the moving image. ACMI believes that the moving image is an active language that engages with the community. It contends that the socially and culturally aware community that also uses and engages in the creation of the moving image will bring

lasting economic benefits to that community and, in turn, further creativity, quality of life and new and alternative means of expression for many of its citizens.

The Government, through Multimedia Victoria, has been quick to recognise the potential of the game industry and has undertaken several initiatives to ensure the State's pre-eminence in the industry.

1.4 Opportunities in the Film and Television Industry in Victoria

Central City Studios at Docklands will have a major impact on film and television production in Victoria and on the post production sector. The first five sound stages will be commissioned by early 2004. A sixth sound stage and a commercial industry cluster will be progressively developed over the next few years.

The Victorian Government's key performance indicators include a requirement that the studios generate an extra \$100 million of production annually by 2005, \$25 million of which has to be additional local production. The Studio's operating policy is non-exclusive and allows for open access as one of the Government's conditions of operation.

Film Victoria, through the Melbourne Film Office, is active in attracting overseas producers to work in Victoria. It has promoted Victoria as a production destination in the USA, Japan, Hong Kong and China. The direct economic benefit to the State of the "footloose" productions it attracted in 2002/03 is estimated to be \$21 million.

The post production sector - editors, sound mixing facilities, film laboratories, special effects personnel - relies heavily on overseas companies. Without foreign production the local post production sector would not be able to afford the technology that is essential in contemporary film production, nor make it available to local producers at a reasonable cost. In effect overseas productions subsidise use by local producers of post production services.

The substantial increase in funding for Film Victoria, allocated in the Victorian State budget of May 2001, has been effective in stimulating the Victorian industry. In 2000/01 Victorian companies accounted for 21% of national drama production (feature films and television). In 2001/02 that figure had increased to 32%.

Production in Victoria in 2002/03 has an estimated value of \$150 million. The goal of the Victorian Government is to increase the level of production in Victoria to approximately \$250 million annually.

The Victorian Government has identified three major barriers to the growth of the industry in Victoria. In bringing these to the attention of the Inquiry, Film Victoria hopes that they can be addressed and resolved for the benefit of the industry nationally.

1.5 Barriers to Increased Film, Television and Multimedia Production

1.5.1 Bandwidth Access

The tyranny of distance shaped Australia's past and will continue to shape its future.

Affordable bandwidth access is essential to those companies earning export income in a knowledge economy in the twenty first century.

Securing access for post production companies to high speed bandwidth at affordable prices is essential to the growth of the post production sector, in order that the post production companies can send film and television rushes, special effects etc for approval to producers offshore or interstate. Game developers and the animation industry have the same requirement for sending components of work being developed here off shore.

The Commonwealth Government's Broadband Advisory Group (BAG) reported on 22 January 2003. The report recommended that the Commonwealth Government should give high priority to stimulating digital content industries in Australia to improve the take up of broadband. The BAG report also recommended improving access to international distribution channels for the output of Australia's digital content industries.

A key issue is the high costs that Australian creative content producers pay for their international connectivity and access to affordable domestic broadband connections. Content producers, particularly in the film and television post-production sector and the game industry, often have atypical requirements for broadband (eg 'bursty' requirements for transfer of large data files rather than continuous use of high bandwidth connections). These producers rely on tailored product offerings from broadband suppliers to meet their sector specific patterns of use in a cost-effective manner.

Unfortunately, the supply side of the broadband market is not as responsive to sectoral needs as it could be, largely due to a lack of competitive tension. The broadband telecommunications market is characterised by the dominance of the incumbent carrier, Telstra, and a handful of major suppliers. There is little competitive pressure to encourage these suppliers to invest in meeting the needs of a relatively small segment of their total customer base. The problems posed by a lack of competition in the broadband market are more acute in locations outside capital city CBDs.

The Commonwealth Government has constitutional responsibility for telecommunications services, and the major levers, both regulatory and financial, that can be used to meet these challenges. A positive response by the Commonwealth Government to the recommendations of the BAG report would strengthen Australia's digital content industries and, in turn, improve Australia's broadband take up. The Commonwealth has responded to some of the BAG recommendations, mainly in relation to regional broadband issues, but it is yet to indicate when or how it plans to address the recommendations dealing with the strategic role of the digital content sector within a National Broadband Strategy.

Recommendation 1:

Improve broadband access for film, television and multimedia production

Post production film and television companies, animation houses and game developers must have access to high speed bandwidth at affordable prices. Film Victoria recommends the Commonwealth implement the recommendations of its Broadband Advisory Group without delay with particular reference to the needs of this sector.

1.5.2 Current Limitations of Investment Funding

Film Victoria notes that the Inquiry is not seeking submissions that raise issues relating to the Commonwealth's taxation treatment, or funding, of the film industry.

However any examination of the industry has to take into account taxation and funding issues. Without Commonwealth taxation measures and subventions the Australian film and television industry as we know it today would not exist. The reality is that Commonwealth support is integral to the industry.

Film Victoria notes in particular the substantive Commonwealth funding given the film industry through the Film Finance Corporation. Film Victoria has worked extensively with the FFC to finance Australian productions. However the FFC cannot meet the demands being placed on it by the industry. There are more film and television projects with sales/distribution deals in place that satisfy FFC criteria than the FFC can accommodate.

Film Victoria believes the Commonwealth should review the Film Licensed Investment Company (FLIC) scheme introduced in 1998, following recommendations from the Gonski Review into Commonwealth funding for film and television in 1997.

The scheme has been a qualified success. While sums invested attracted a 100% tax concession under Division 10BA of the Income Tax Assessment Act 1936, no tax offset was incorporated in the scheme thus limiting its appeal to investors. Two companies were granted FLIC licenses in 1999. Between them they were licensed to raise \$40 million over two years. They raised \$22.4 million in total.

Film Victoria endorses the proposal from the Screen Producers Association of Australia to the Commonwealth that:

- The FLIC scheme be expanded with licenses being issued to a wider range of companies. A diversity of companies would be desirable, providing choice and promoting competition.
- A tax offset be allowed to make FLIC investment more attractive. SPAA has suggested no tax be paid on up to 50% of returns derived from overseas revenue.

Film Victoria believes the cost of the revised FLIC scheme would be modest. The Commonwealth could control the amount of investment funds to be raised by limiting the number of FLIC licenses and the amounts they are allowed to raise. The tax offset, capped at 50%, would be applied only against revenue derived from foreign sources.

Recommendation 2:

FLIC scheme should be expanded

Film Victoria recommends the Commonwealth should review and expand the Film Licensed Investment Company (FLIC) scheme with a view to issuing licenses to a wider range of companies. Criteria for the revised scheme would encourage diversity among applicants, thus ensuring a range of options for filmmakers. A tax offset should be considered to encourage investors.

1.5.3 Taxation Treatment

In 2002 the Commonwealth introduced a 12.5% refundable tax offset for feature films, telemovies and mini series with a minimum Australian expenditure of \$15 million. This initiative has proved a significant boost to the production of foreign feature films in Australia. However this 12.5% refundable tax offset does not apply to television series of thirteen or twenty-six episodes even though the total budget may exceed \$15 million. The offset also is unavailable to producers of smaller budget telemovies and straight to video films, as they are not able to "bundle" two or more projects to meet the minimum figure of \$15 million.

In March 2003 AusFilm presented a report to the Commonwealth arguing the case for an extension of the rebate. The report included a detailed economic analysis by The Allen Consulting Group which estimated the extension of the offset would result in expenditure in Australia of \$180 - \$295 million, adding \$139 - \$228 million to annual Australian GDP and \$25 - \$41 million to Commonwealth revenue.

The exclusion of episodic television and telemovies has serious economic implications for Victoria, as Victoria's expertise in television production has always been one of its competitive strengths.

When Victoria loses a television production such as a mini series or telemovie to another location, it also loses the work that the production would have meant for the local post production sector. Foreign television producers tend to undertake post production work in Australia using the local post production houses. (Feature film producers tend to repatriate post production work, usually to Los Angeles.)

Competition to attract television production is global. In February this year the Melbourne Film Office lost two television productions it had been working to secure for Victoria. They went to Canada where there is a 16% rebate on overall expenditure, in addition to the attractive rebates offered by the state film commissions.

Recommendation 3:

Revise the 12.5% tax offset as applied to television production

Film Victoria recommends the Commonwealth revise the 12.5% refundable tax offset measures to include episodic television and telemovie and straight to video film packages in instances where the total value of production exceeds \$15 million.

1.6 Commonwealth Support for Film and Television

As noted earlier the Inquiry is not seeking submissions that raise issues relating to the Commonwealth's taxation treatment, or funding, of the film industry. However Film Victoria believes that the Commonwealth's support should be acknowledged.

- The Commonwealth directly supports two national television networks; no other country in the world does this. Its national film school, The Australian Film Television and Radio School, and its archival collection, ScreenSound Australia - The National Screen and Sound Archive, are of international standard. Film Australia exists specifically to record and interpret the life of this nation. The Australian Film Commission provides screen cultural and industry support. The Film Finance Corporation is the Commonwealth's primary agency for funding screen production.
- The Commonwealth provides taxation incentives to private investors through Division 10B and 10BA of the Income Tax Assessment Act 1936 and through the Film Licensed Investment Companies. It also provides for a refundable tax offset for film production to attract large budget foreign productions. Commonwealth taxation measures fostered the growth of this country's film industry. The establishment in 1988 of the Film Finance Corporation stabilised it.
- The Australian Content Standard for commercial free-to-air television stations sets an overall minimum level of Australian programming at 55 percent between 6 am and midnight. There are also specific annual quotas for drama, documentary and children's programs. Pay television licensees and channel providers who provide a subscription TV drama service must spend 10 percent of their total program expenditure on new Australian content and make up any shortfalls in the next financial year

Until the 1960's there were few Australian voices heard telling Australian stories on our screens. As a result of Commonwealth support our stories have been heard, in our own voice, in our cinemas and our homes. And internationally our stories have brought an increased understanding of Australia and Australian culture in its many aspects to a wider audience.

Australians are proud of the achievements of their film and television industry and the international recognition it has won. That would not have happened without the support successive Commonwealth Governments have extended this industry.

1.6.1 Australia/USA Free Trade Agreement and GATS

Australia is presently negotiating the General Agreement on Trade In Services (GATS) with the World Trade Organisation, and a Free Trade Agreement (FTA) with the United States of America. The FTA will precede GATS and therefore could set precedents which might be used in GATS negotiations.

Any agreements reached as a result of these negotiations must not erode that essential support which the Commonwealth has given the film industry.

Film Victoria believes:

- A legitimate distinction can be made between a nation's cultural products and the other goods and services it produces and trades. A country's culture is unique and should be accorded special treatment in trade negotiations.
- A commitment to free trade and a commitment to supporting a nation's cultural policies can co-exist. The regulations and funding assistance given Australia's audiovisual sector by the Commonwealth have not hindered the ability of the USA to penetrate this country's audiovisual sector. In 1999/2000 the USA accounted for 65% of our audiovisual import trade and 83% of the Australian gross box office.
- Australia must be free to pursue its cultural policies, and it must have the flexibility to adopt new measures in the future if they are required.

Film Victoria agrees with the position of the Australian Film Commission as contained in the AFC's Submission of January 2003 to the Department of Foreign Affairs and Trade (Proposed Free Trade Agreement between The United States of America and Australia) and the Submission of May 2003 to the Senate Foreign Affairs, Defence and Trade Committee Inquiry (The General Agreement on Trade In Services and the US Free Trade Agreement). Those submissions include the following:

- The AFC strenuously supports Australia continuing to retain its flexibility to maintain existing measures or adopt new measures designed to support cultural policy objectives.
- Where barriers to trade exist they are for clearly stated cultural objectives and are transparent in their effect.
- The AFC supports Australia maintaining the position of technological neutrality and maintains that Australia should resist the arguments of the US that liberalisation of barriers to e-commerce is linked to the liberalisation of audiovisual. The measures, which Australia presently has in place to support its cultural policy for the audiovisual sector, do not represent any barriers to the development of e-commerce.
- The AFC also argues that Australia should resist the arguments of the US to liberalise in the area of advertising services where Australian content rules apply to television advertisements and to make any changes to the Migration Regulations as they relate to the entry of entertainment personnel.

Recommendation 4:

Maintain Australia's freedom to support our cultural industries

Film Victoria recommends the Commonwealth ensure that any agreements entered into following negotiations for the General Agreement on Trade In Services (GATS) with the World Trade Organisation and the proposed Free Trade Agreement (FTA) with the United States of America not compromise or curtail support mechanisms and regulations that may exist presently for the Australian audiovisual sector, or that any Australian government might wish to implement in the future.

1.7 The Animation Industry in Victoria

Most of the output of the Victorian animation industry has been in children's television. The industry contends that Australian television networks are reluctant to commission animation series. Traditional animation is time and labour intensive. A series of 26 programs usually takes two years to produce.

The Australian Broadcasting Authority's content regulations require television stations to broadcast 96 hours of "C" classified material annually, including 25 hours of first release children's drama. Film Victoria contends that the Commonwealth should rework these regulations to encourage television networks to commission Australian produced children's animation programs. The points system should be reworked so that animated children's drama attracts more points than live action children's drama.

In Film Victoria's view enhanced support for this important sector of the Australian production industry is vital. Animation spans traditional and new media. Animation is used in electronic games to provide the story line and characters. There are also cross overs between stop motion animation, computer generated animation, graphics, post production, visual effects and computer games.

Victoria is renowned for its animation and visual FX. Production houses such as Animation World, Act 3 Animation, C4 and Mickey Duck are internationally recognised. So too are visual FX studios such as Phenomena at AAV, The Swish Group and Complete Post. Victorian animation company, Act 3 Animation, recently completed the animated introduction for Blue Tongue's interactive video game *Jurassic Park*. In 2001 the bulk of Act 3 Animation's work was for the domestic television advertising industry. Now the bulk of its work comes from overseas game companies.

New media has triggered growth in the animation industry. Through its multimedia accords with both the ABC and the SBS, new media animation production has grown and over \$830,000 has been invested in animation-based projects over the last two years. The animation from some of these projects (*Game On Initiative*, *Planet Slayer*, *Strange Attractors* and *Animaterratica*) has won international awards.

Film Victoria recently appointed a dedicated animation officer, the first in Australia, to assist in the development and growth of this sector.

Recommendation 5:

Commonwealth television content regulations should require animated children's production.

Film Victoria recommends the Commonwealth revise its Australian Content regulations for children's television to require television networks to commission an amount of Australian children's animation programs annually. This amount would be in addition to the "C" classified material presently required of networks.

2 COMPUTER GAME INDUSTRY IN VICTORIA

Internationally the computer game industry generates revenue of US\$30 billion exceeding the revenues from the global film industry. Australia's computer game development industry (the game industry) is currently estimated to generate \$100 million in export income.

Income generated by the Australian game industry is predominantly from fee for service development work. Non-Australian publishers who sell internationally the games developed here retain the intellectual property.

In addition to the fee for service sector, structures need to be developed that will enable game development companies to retain the intellectual property in games they create, thus building a strong Australian electronic game industry.

More than half of Australia's game development industry is in Victoria. Australian owned companies such as Bullant Studios, Blue Tongue Software, IR Gurus, Tantalus Interactive and Torus Games have established an international reputation for Melbourne.

Of the top 20 Interactive Entertainment Software Publishers, five (Infogrames Entertainment, Acclaim Entertainment, THQ, Nintendo and Electronic Arts) have either set up their Asian regional headquarters for development, publishing and distribution or have set up a sales and distribution operation in Victoria.

They include Atari Melbourne House which is owned by Infogrames Entertainment: a French public company which is the world's fourth largest independent publisher of interactive entertainment software in the U.S.A. and Europe. Atari Melbourne House is one of Infogrames three international centres for game development. It developed one of the company's most popular international titles, *Le Mans 24 Hours*.

Over 200 titles developed in Victoria by Australian companies have been distributed globally. These include *Jurassic Park: Project Genesis*, *Men In Black 2: Alien Escape*, and *South Park Rally*.

2.1 Victorian Government Support

Victoria has been foremost among the states in fostering its game industry and is working in partnership with the industry to consolidate the State's position as the computer game capital of Australia.

The Victorian Government:

- Is working in conjunction with the Commonwealth and the game industry to ensure the industry has access to bandwidth it needs at commercially viable cost.
- Is working with the Commonwealth and other states towards a consistent classification system for film, game and audio content.

The Victorian Government, through Multimedia Victoria:

- Put in place a policy framework to develop Victoria's game industry. *Game Plan: A Blueprint for Growing the Victorian Computer Game Industry* defined the parameters for Victorian Government initiatives to establish Victoria as the computer game capital of Australia. The *Game Plan* model has been recognised as an industry blueprint by government policy advisers from Lyon, Montreal, Glasgow and Dublin.
- Spent \$150,000 to ensure that the Game Developers' Association of Victoria was established in Melbourne.
- Secured for Melbourne the Australian Game Developers' Conference from 2000 to 2005.
- Provided \$250,000 so Victorian companies could utilise Sony PlayStation 2 Developer Kits for six months to develop prototypes of games to market to publishers. PlayStation 2 dominates the console platform market internationally.
- Commissioned a business plan to establish a Cocoon Game Development Studio. This would provide fledgling game developers with management, legal, accounting and other professional support and facilities, such as sound editing suites and graphics studios.
- Has examined the feasibility of a motion capture facility in Victoria to enable developers to digitise human movement.
- Is investigating the establishment of an Australian Games Innovation Centre in Melbourne. The centre would be home to the Cocoon Game Development Studio, the Game Developers Association of Australia, the Interactive Entertainment Association of Australia and leading Victorian game companies.

The Victorian Government support has fostered the growth of the industry. For example in 1997 IR Gurus received investment support from the Multimedia21 Fund (now the Digital Media Fund) to develop *Riding Star*. The \$100,000 investment returned 110% and directly assisted the business growth of IR Gurus. The company now employs 15 full time and up to 5 part time employees.

By developing a niche in the market for building equestrian game titles, IR Gurus has built an international reputation. Sales figures for 2001 showed that *Riding Star* has sold 300,000 plus units worldwide. The game is published in seven different languages and has been developed for PC, PlayStation One and Gameboy. In addition to *Riding Star*, IR Gurus have produced *Mary Kings Riding Star*, *Equestriad 2001*, *Willow Brook Stables* and *Saddle Club* with Melbourne-based television production company, Crawfords. In conjunction with Acclaim Entertainment IR Gurus developed all PC, PS 2 and X-Box titles for the AFL.

2.2 Cross Content Creation

Film Victoria has identified the growth potential of cross content creation as a priority. It is actively encouraging practitioners from traditional and new media to engage with each other. Film Victoria encourages film and television makers to look at what they are doing afresh, to challenge them to explore new ways to exploit the content they are creating.

Multimedia Victoria has enabled Film Victoria's Digital Media Fund to allocate \$2.5 million to six new programs and industry research, to encourage convergence at the earliest stages of content development. Among these six programs:

- Game Content Development Program will enable independent Victorian game developers to produce market driven game titles in which they own the Intellectual Property (or a percentage thereof) for consideration by publishers.
- Animation Concept Development Program provides seed funding to develop commercially viable animation concepts across a range of platforms including digital television and broadband and delivery.
- Innovative Digital Content Program helps producers develop content for delivery on new digital platforms. It aims to encourage new ideas and new talent.

The game industry is beginning to use film industry personnel and facilities. The benefits of this will be enhanced work opportunities for Victorian actors, post production personnel, and post production facilities.

Victorian company Blue Tongue, for example, used actor Bud Tingwell and an original score performed by the Melbourne Symphony for the game *Jurassic Park: Operation Genesis*, published by Vivendi Universal Games.

2.3 Film Financing Techniques

In order to be able to retain an interest in their intellectual property, game development companies need ways of financing game prototypes and development of the finished product. Australian game companies have just begun to apply film financing techniques to their industry. This will accelerate. The two industries have many similarities and the game industry can benefit from practices that have been refined over several decades by independent filmmakers.

Completion bonds are common in filmmaking and have been used already by Australian game companies. An investment bank or private investor would be more likely to invest if a completion bond were in place to ensure a game will be completed. The publishers would have reduced risk; that is they would not be carrying the entire financing of the game's development, leaving room for the developer to retain copyright in the game.

Developers would then be able to secure better deals from publishers, particularly in regard to the royalty percentage to which they are entitled and the structure of the deal under which they participate in revenue streams.

Gap financing is common in feature films; funds are sourced to cover the difference between the distribution guarantee and the production cost. These are usually secured against rights that have not been covered by the initial distribution agreement, such as some withheld international territories, or merchandising and licensing rights which have been reserved.

If financing techniques, which are common in independent filmmaking, establish themselves in the game industry they will provide financing flexibility for independent developers and increase returns from the games they create.

Australia's electronic game industry will be able to benefit from employing some of the practices and techniques independent filmmakers have developed. Growth could also be accelerated if some of the structures and programs, which have been used by the Commonwealth to develop Australia's film industry over the past three decades, were adapted to the game industry.

2.4 Barriers to Entry to the Computer Game Industry

Ten years ago barriers to entry to the game industry were low. Two or three people could put together a low cost concept which would be sufficient to gauge a publisher's interest. If the publisher were interested then it would commission a fully developed game.

It is still possible for a small team to establish itself. Mobile phone and web game applications pose low barriers to entry, and game boy advance applications are relatively accessible. Film Victoria has programs in place to assist emerging game developers at this level including the Innovative Digital Content Program.

However, development of console games such as Sony PlayStation, Microsoft Xbox and Nintendo Gamecube is well beyond emerging developers. It is these platforms that are the major revenue producers globally.

Before committing to the funding of the development of a game, publishers want a fully developed concept to consider. The cost of producing a prototype is currently around \$250,000. This cost is usually met by the developer and is becoming a considerable barrier to development of games originated by Australian companies.

Ten years ago game consumers would accept relatively low production standards. Now they want games that are not far removed from the standards of feature film production. Production standards on display at the E3 convention in Los Angeles in May 2003 were very high. Victorian developers are aware that they will have to match these if they are to stay relevant in the international market. Cost of development obviously will go higher.

The majority of income earned by game developers in Australia is fee for service whereby international publishers commission Australian companies to develop a game based on a license held by the publisher. While this is crucial to the survival of those companies that have established themselves over the past decade, Film Victoria's aim is to encourage Victorian developers to initiate their own concepts which can be exploited internationally, thus ensuring increased export income and an expanded and stabilised local industry. Film Victoria's Game Content Development Program supports established game developers to produce a playable prototype based on their original idea.

Only established companies are in a position to develop concepts for console games. As noted above it costs approximately \$250,000 to develop a concept to the point where a publisher is prepared to commit the \$4-\$5 million typically needed to bring a game to the international market. Only publishers such as Infogrames have the necessary resources. There is no existing Australian owned game publisher.

This means that, while Australian companies profit from the commissions they receive from international publishers to develop games on a fee for service, they have only a modest participation in profits those games might generate, as they do not control the intellectual property.

If a publisher commissions a developer to produce a game (which the publisher originates), the developer will be entitled to a royalty percentage, usually 15%. But the deal will typically be structured so that the production cost comes out of the developer's royalty fee; the effect of this is that a game has to be wildly successful for the developer to participate in profits. Normally developers build in a production fee at the time the game is being developed.

However if the developer were able to fund the cost of a game they had originated themselves, they could negotiate a better deal as a result of owning the copyright; they may keep 40% of returns.

As well as getting a higher percentage the developer may be able to negotiate a more favourable deal regarding the point at which they share in returns. If the developer were in a stronger position they may be able to insist on development costs being recouped first, prior to returns being shared. This way both the developer and publisher would be paying for the game's cost, and the developer would have a far greater chance of actually sharing in profits.

As with feature films not all games recoup their budgets. Approximately eighty percent recoup only part of their production costs. As with the film industry the profits come from the remainder, some of which are spectacularly profitable. While half a million copies would be a target for a successful game, sales for the top ten best selling electronic games range from eight million to 40 million copies.

Australia's game industry has the potential to generate considerable export income for Australia. The risks are substantial. To be viable an Australian publisher would need capital of \$50 – 150 million. Several successful Australian developers are understood to be considering a public offering to raise funds to establish themselves as Australian publishers.

2.5 The Future

What we see in computer games now is like the stuttering images of early cinema, and their future development will come to dominate the culture in ways that we can hardly anticipate,

Julian Stallabrass, Courtauld Institute of Art. *Australian Financial Review* May 30 2003.

Henry Jenkins, Professor of Comparative Media Studies at Massachusetts Institute of Technology, argues that computer games will become the most significant art form of this century.

If distinctly Australian games are to be part of the international computer game landscape this country has to move to secure its fledgling game industry. In the early days of silent films Australia had a thriving industry. It lost its way, and it took a half a century for the industry to be reclaimed. The same thing cannot be allowed to happen with the game industry.

It is impossible to predict where the computer game industry will go, or what form its content will take. The medium is in its infancy and content of most computer games is simple although the games are increasingly multilayered and offer complex scenarios and choices. The technology will allow ever more choices and convincing virtual worlds and modes of interactivity.

Games will become increasingly important to filmmakers to exploit the intellectual copyright they have created in their films. Conversely films will be made of Australian game content.

If this country's children had no exposure to Australian content on television, in film, on video, in theatre or in books, their concept of their place in the world would be quite different. Australia's game industry must be secured and developed if there is to be Australian content for Australian players.

Funding provided by the Commonwealth through the Australian Film Commission and the Film Finance Corporation has been the principal catalyst for the growth of the Australian film industry these past two decades. That growth has in turn helped a number of Australian owned production/distribution/sales companies establish themselves; three of these are publicly listed.

The Australian game industry is at a crucial point. It is highly regarded internationally. But in the global context it is a niche player existing principally on fee for service contracts from overseas companies. The number of major international publishers is shrinking as consolidation occurs. The development budgets paid to fee for service providers are growing, but the number of games commissioned is diminishing. It will become harder for the Australian industry to survive using the business model it has employed the past decade.

The growth potential for the international industry is enormous; it has enjoyed double-digit growth for the past decade. For Australia to be a viable player it has to generate more intellectual property, and retain control of it. At the same time it needs to grow the fee for service sector of the industry. Income from this work provides training and the opportunity to develop skills. It also provides profits which enable companies to generate original ideas and bear some of the early cost of developing their intellectual property.

The Australian game industry needs the type of support that the Commonwealth has given the film industry.

Recommendations to target the accelerated development of the computer game industry are detailed below. If the Commonwealth were to implement these measures, they should be reviewed after an appropriate period, say ten years, to assess whether they have achieved their goals. At that time a decision could be made as to whether they should be extended, modified or terminated.

Film Victoria endorses the proposals for the game industry by the Game Developers' Association of Australia (GDAA) that the Commonwealth establish an Equity Investment Vehicle similar to the Film Finance Corporation and extend the provisions of Division 10BA of the Income Tax Assessment Act 1936.

Film Victoria is aware the Commonwealth established the Australian Multimedia Enterprise Limited (AME) in 1995 to invest in multimedia projects and concept development. The Commonwealth sold AME to private interests in 1998.

In Film Victoria's view AME was established too early to be able to play an effective role. The industry it was intended to foster was too small at the time. In the eight years since then the international electronic game industry has boomed, and Australia's game industry has established an international reputation.

It is now timely and appropriate for the Commonwealth to establish a funding body to assist the development of Australia's electronic game industry.

Recommendation 6:

Commonwealth to establish Game Finance Corporation

Film Victoria recommends that the Commonwealth considers the establishment of a body similar to the Film Finance Corporation to support Australia's game industry. This body would have a commercial focus, investing in prototypes and game development, providing services such as marketing loans and a cash flow facility, and marketing the Australian game industry internationally. Investments in development would require marketplace attachments, such as distribution guarantees from publishers, as is the case with the FFC. Head office should be in Melbourne where the Game Developer's Association of Australia is located, together with half of Australia's game companies and the major publishers. The Victorian Government is foremost among the states in its support of the game industry, and Film Victoria and Multimedia Victoria lead Australia in the field.

Recommendation 7:**Extension of 10BA to game industry**

Film Victoria recommends that the Commonwealth consider the extension to the game industry of the taxation benefits associated with Division 10BA of the Income Tax Assessment Act of 1936. This will be essential to provide the industry with private investment capital. A system similar to that which certifies films as eligible for Division 10BA taxation concessions would have to be put in place for game industry investments.

2.6 Branding and Promotion

Just as the Cannes Film Festival and the American Film Market set the agenda for deal making in the film industry, two conferences set the deal making agenda for the international game industry: the Game Developers Conference (GDC) held in San Jose every March and the Electronic Entertainment Expo (E3) in Los Angeles every May.

Compared to what has been done to promote Australia's film industry, the Australian game industry has been poorly promoted. In May this year Australia had a stand at E3 for the first time. It was a valuable resource for attendees, but a modest national presence compared to some others. The U.K. stand is reported to have cost one million pounds. Australia's stand cost \$128,000. The Victorian Government contributed \$40,000, the Queensland Government and the Brisbane City Council \$25,000, the Commonwealth contribution was \$23,000.

Recommendation 8:**The Commonwealth should review and enhance programs to promote Australia's game industry internationally.**

Similar resources to those it has employed to promote Australia's film industry at international markets should be applied to the Australian game industry.

2.7 Tax Offset

Australian game developers are competing with developers in Los Angeles, Vancouver and London for commission work. The Commonwealth could offer a 12.5% refundable tax offset to overseas publishers to undertake development work here. As the average development cost of a game is \$5 million the scheme should have a \$10 million dollar threshold and apply to a bundle of games, as long as the package contains no more than three.

Extrapolating from the economic modelling done by The Allen Consulting Group regarding an extension of the scheme to episodic television and bundling of telemovies, the economic benefit of applying this scheme to the Australian game industry could be substantial. It would also have the benefit of stabilising the domestic game industry as it moves into a turbulent period because of the consolidation of publishers internationally: a trend which will reduce the amount of fee for service work available internationally.

Recommendation 9:**Extension of 12.5% tax offset to the game industry**

Film Victoria recommends the Commonwealth allow a 12.5% refundable tax offset to development of electronic games commissioned by non-Australian publishers, where the value of the game exceeds \$10 million or the total value of a number of games – up to three games - exceeds \$10 million.

2.8 Collection of creative industries data and digital content by the ABS

There is no specific classification for creative digital content or creative digital content providers in the collection of data by the Australian Bureau of Statistics (ABS). Therefore when ABS surveys are undertaken they do not yield information specific to this sector.

Industrial Classifications include “film and video production” and “creative arts”. However digital content spans more than one industry.

Product Classifications include classifications such as “books, magazines, newspapers and other printed matter”. Not all products will, or can be, delivered digitally.

Occupation Classifications include “culture and leisure”; this is too general to be useful.

Detailed statistical information regarding digital content and providers is essential if the Commonwealth and State Governments are to formulate policy to assist the growth of industry sectors such as post production and the electronic game industry. Classifications should be made more specific to capture digital content and digital content providers. This information is vital if Australia is to develop its knowledge economy.

Film Victoria recommends that the Commonwealth modify several existing ABS surveys. The recommended changes would not be extensive but they would provide valuable information. Some surveys should also be more frequent; ideally they should be conducted annually. Film Victoria recommends the modification of the following existing surveys:

- The annual Economic Activity Survey could indicate the number of firms providing digital content and the extent of their digital content activity. This information could then be cross-referenced against other information such as income, labour costs, and capital expenditure. This would demonstrate the contribution firms involved in creative digital content are making to overall economic activity.
- Film and Video Production Survey and Film and Video Distribution Survey could provide more detailed specific information. Presently digital content is not recorded as a separate data item. These surveys are not conducted annually; more like every three years.
- The Business Use of Information Technology Survey and Household Use of Information Technology Survey (both presently conducted annually) measure the extent to which Australian businesses and households are using information technology. With suitable amendments they could both provide information on where digital products are going and who is using them. For example, ACMI has indicated its interest in comparative data from the consumer electronics market that measures the increase in the sales of digital video cameras and an increase in the sale and use of desktop computer video editing software, and where and by whom these technologies are being purchased.

Recommendation 10:

Modification of Australian Bureau of Statistics surveys

Film Victoria recommends the Commonwealth amend existing surveys carried out by the Australian Bureau of Statistics to provide statistical information on creative digital content and its providers. If necessary surveys should be conducted annually.

CONCLUSION

A vibrant film, television and multimedia industry is an integral part of the Victorian economy. Victoria has embraced and encouraged all new forms of media - celebrated at the Australian Centre for the Moving Image.

Victoria's game industry is leading Australia in exploiting the skills, talents and vision of the multimedia pioneers and making Victoria part of the global industry.

Economically these labour intensive industries can only continue to grow if given the infrastructure and regulatory environment they deserve. Culturally they are critical to the development and expression of Australian identity.

Film Victoria notes the valuable opportunity this Inquiry has provided to discuss issues of concern to the film television and multimedia industries.

If the Inquiry felt it would assist its deliberations to have direct discussions with industry representatives in Victoria, Film Victoria would be pleased to facilitate appropriate meetings. The State agencies involved in the industry would also welcome the opportunity to make direct representation to the Inquiry.

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