MOOCHERS MAKING MOVIES: GOVERNMENT ASSISTANCE TO THE FILM INDUSTRY

Governments should not chase the overseas film production dollar, says **Gene Tunny**

In February 2013, then Arts Minister Simon Crean confirmed that the federal government would offer financial incentives to attract to Australia the filming of Disney's production of *20,000 Leagues Under the Sea: Captain Nemo*, starring Brad Pitt and Angelina Jolie.[1] The minister also called for state government assistance on top of this federal assistance.

Previously, in April 2012, the federal government announced it would give $12 million to attract the filming of *The Wolverine*, starring Hugh Jackman, to Australia.[2] The justification for *The Wolverine* subsidy was that it would increase the existing Location Offset tax incentive, discussed below, to 30% from 16%, a rate considered by the film industry as uncompetitive given the current historically high value of the Australian dollar. No doubt Disney would be making this argument for *20,000 Leagues Under the Sea*, too.

Clearly the film industry, once concentrated in a few centres and Hollywood being the largest and most prominent, has become increasingly internationalised, particularly since the 1970s, and both financing and production are globalised. So productions that might typically have been produced in Hollywood have spread to countries and regions around the world, notably Canada and the United Kingdom. There has been some limited activity in Australia, including the production of movies such as *Scooby-Doo*, the *Matrix* films, and *The Great Gatsby*.

In part, the growing internationalisation in production has been driven by incentives provided by governments to attract films to their countries. Countries around the world, including Canada, the United Kingdom and Germany, and US states are competing for film productions.

Despite the economic activity and attention provided by film productions to Australia, it is doubtful whether Australian governments should subsidise the film industry to the extent federal and state governments do now. As discussed in this article, there is little public policy rationale for these subsidies and no guarantee they will promote a long-term, sustainable film industry locally. Indeed, some other regions around the world, such as the US state of Michigan, have realised that film industry subsidies are highly costly and not justified by the relatively small economic gains.

This article provides an overview of current assistance by Australian governments to the film industry, considers the rationale for such assistance, and provides recommendations for the future.

Industry overview

The Australian film industry is relatively small compared with Hollywood, and typically produces 30–40 feature films every year; the industry spent an average of $240 million per year over the five years to 2011–12. Major locations for feature film production in Australia, particularly big budget features under foreign creative control, are Fox Studios (which recently completed filming *The Great Gatsby*) in Sydney and Village Roadshow Studios on the Gold Coast.

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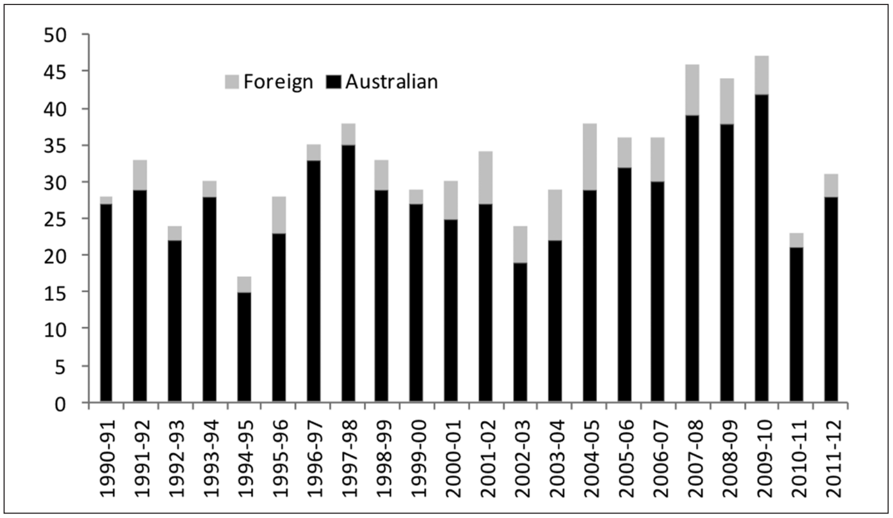
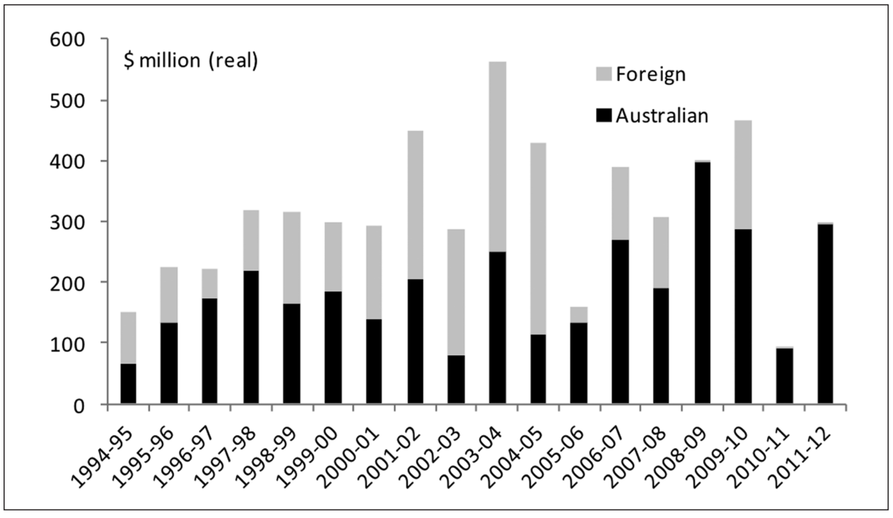
Productions under foreign control have a major impact on the scale of Australia's film industry from year-to-year, and a handful of large foreign productions can almost double total spending associated with the industry, as they did in the early to mid-2000s. So while productions under Australian creative control are numerically dominant, they do not always represent the largest share of total spending by the industry (Figures 1 and 2).

Figure 1: Feature film productions in Australia, by source of creative control



Source: Screen Australia data.

Figure 2: Spending in Australia by film industry



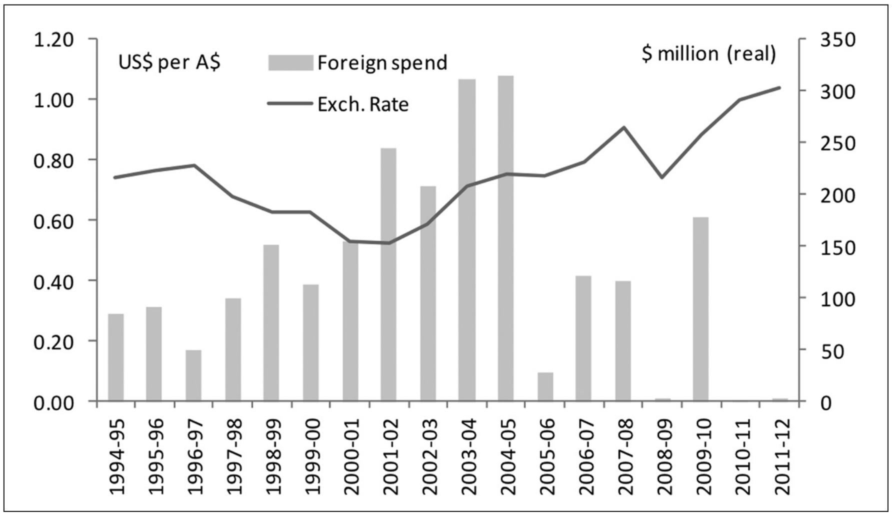
Source: Author's calculations based on Screen Australia and ABS data.

Foreign productions, especially where a large part of the movie is made in Australia, as opposed to a few scenes, have much larger budgets than Australian productions, and hence, can lead to big fluctuations in the industry. While Australian productions have spent between $5 million and $10 million over the last decade and a half, foreign productions have spent between $20 million to $60 million.

So yearly production spending is volatile due to the impact of a number of big budget productions, most recently, *The Great Gatsby*. Given the challenges of financing large budget feature films, it is unsurprising they do not come in predictable numbers every year. Further, the attractiveness of Australia as a destination for foreign productions will depend on the value-for-money of producing in Australia, which depends significantly on the exchange rate.

The initial attraction of Australia to international productions in the early 2000s was the low value of the Australian dollar. Since then, the Australian dollar has increased in value in response to the mining boom, making Australia a less attractive place to make movies, either in whole or in part. As a result, spending by foreign productions in Australia has plunged (Figure 3). As Greg Jericho has observed, the appreciation of the dollar makes the production of *The Wolverine* in Australia 'unusual,' and it could only have occurred with substantial government subsidies.[3]

Figure 3: Foreign productions in Australia



Source: Author's calculations based on Screen Australia, ABS and RBA data.

The exchange rate and the cyclical factors inherent in the sector have increased the volatility in the number of international productions in Australia—and prevented the realisation of a Hollywood on the Gold Coast. As *Local Hollywood* observed, 'The Gold Coast's production history is marked by discontinuity and irregularity as international work is subject to cycles of boom and bust.'[4]

The film industry is not a large employer, and, as would be expected based on the 'discontinuity and irregularity' of the industry, many of the jobs are temporary. Throsby and Zednik (2010) estimate that in Australia, of the 7,000 or so actors and directors who are practising professionals, only 41%, fewer than 3,000, spend at least half their time in industry jobs. Additionally, while we know that 7,350 people are employed in motion picture and video production, the available data do not allow separating motion picture producers from video producers.[5] Post-production service is often identified as an important industry supported by the film production, but it employs fewer than 1,000 people across Australia; moreover, it competes in an international marketplace and attracts overseas productions as well, so co-location is not particularly relevant.[6]

Assistance overview

Assistance to the film industry is provided by both Commonwealth and state governments, though the Commonwealth's Screen Australia is the predominant funder. All the states and territories have their own film industry promotion bodies such as Screen NSW, Film Victoria, Screen Queensland, and Screen WA. Broadly speaking, state film agencies may be viewed as providing topup assistance to that provided by the Commonwealth. The film agencies are not solely confined to feature films but also provide funding for producing and script writing for documentaries and TV programs.

In addition to ongoing support programs, Commonwealth and state governments tend to offer ad hoc assistance designed to attract particular productions, such as *The Wolverine* and potentially *20,000 Leagues Under the Sea*. Indeed, the Commonwealth arts minister recently announced that $20 million is being set aside to attract an international production, most likely *20,000 Leagues Under the Sea*.[7] At a state-level, however, these ad hoc assistance arrangements are often not transparent and the level of assistance is undisclosed, being labeled 'commercial-in-confidence.'

Commonwealth assistance

Assistance by the Commonwealth comprises tax offsets and direct support for a range of activities. The government provides three tax offsets collectively known as the Australian Screen Production Incentive. The tax offsets are the Producer Offset, Location Offset, and the PDV (post, digital and visual effects production) Offset (see Table 1).

Table 1: Tax offsets available for the film industry

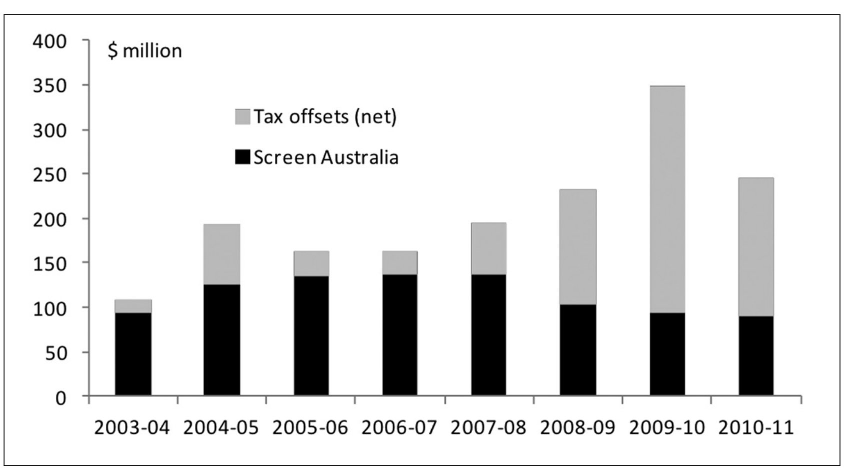
Offset type	Description
Producer Offset	40% rebate on the qualifying spend of qualifying Australian films (and a 20% rebate for other qualifying media)
Location Offset	16.5% rebate on Australian spend of large budget productions that do not meet the significant Australian content test for the Producer Offset
PDV Offset	30% rebate which supports work on post, digital and visual effects production (PDV) in Australia, regardless of where a project is shot

Source: Australian government websites.

The majority of films (representing over 90% of total budget) qualify for the Producer Offset. It appears that the test for significant Australian content under the Producer Offset must be lenient, because *The Great Gatsby* passed the test, based on Australian involvement in the production, including director Baz Luhrmann, even though it is a quintessentially American story.

Total Commonwealth assistance to the film industry amounts to several hundred millions of dollars every year (Figure 4). As the tax incentives are percentages of total spending, the level of Commonwealth assistance fluctuates with spending on production in the industry.

Figure 4: Commonwealth assistance to the film industry, 2003–04 to 2010–11



Source: Productivity Commission, Trade and Assistance Review 2010–11.

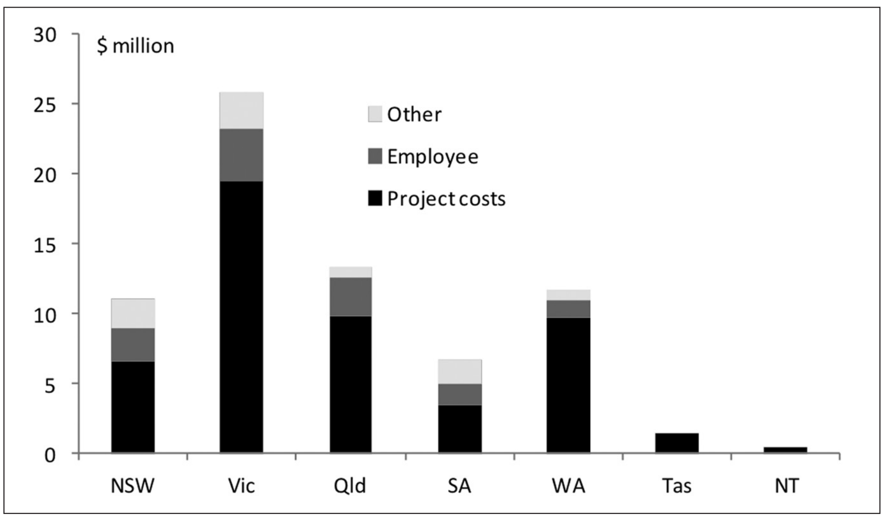
Note: Figure includes assistance to feature films, and TV and documentary productions.

Screen Australia spends money on feature film development support ($2.7 million on 102 feature films in 2011–12) and investments in feature film production ($18.1 million on 16 films in 2011–12).[8] In 2011–12, Screen Australia also invested $21.8 million in television productions and $14.9 million in documentary productions. While Screen Australia invests in the Australian film industry and is entitled to a share of the profits, the profits it receives from film investments appear to be small—an average of around $0.25 million per annum between 2011 and 2012.[9]

State government assistance

The oldest of the state film bodies in Australia is the SA Film Corporation, established by the Dunstan government in 1973. The SA body has funded many well-known Australian films such as *Breaker Morant*, *Picnic at Hanging Rock*, *Storm Boy*, and *Sunday Too Far Away*. Arguably, its most successful films date from the 1970s and early 1980s, and neither it nor other state bodies have funded films with the same cultural impact in recent years. Other states have followed South Australia in establishing their own film agencies, with Victoria's agency now the largest in size (Figure 5).

Figure 5: Expenditure by state film agencies, 2008–09



Source: Productivity Commission, Trade and Assistance Review 2009–10

State film agency assistance also includes funding for the development of screenplays and attendance at international events. Typically, a limited amount of financing for film productions is available through loans from a revolving fund, justified in part as 'cash flowing' the producer offset (where it is not paid until project completion), distribution guarantees, and pre-sales.[10]

State governments also typically provide funds to attract films to their states, such as Queensland's Production Incentive. Assistance is also potentially provided on an ad hoc basis, such as for *The Great Gatsby*, which the NSW government is subsidising by an undisclosed amount. In NSW, film projects can be funded from either Screen NSW funds or from the $120 million State Investment Attraction Scheme.[11]

Assistance in other countries

Film producers have become adept at appealing to governments across the world for tax breaks and production subsidies. Unfortunately, governments are too willing to compete against each other to attract film productions.

New Zealand appears to have offered very large subsidies for the *Lord of the Rings* trilogy, amounting to hundreds of millions of NZ dollars, and was criticised by the OECD for doing so.[12] The OECD would prefer countries reform product and labour markets and invest in education and health for long-term benefits, rather than waste money on film productions that bring temporary production and jobs.

Britain has offered incentives to attract international films since the 1970s. Total film industry incentives have recently come into focus as the UK government aims to trim its budget deficit, and Prime Minister Cameron has announced he would prefer the government funds 'commercially successful pictures' such as *The King's Speech*.[13] This may suggest the government may be willing to divert money from local films to foreign-produced films with a greater chance of international success.

There is also extensive competition for film productions among North American jurisdictions, that is, among Canadian provinces and US states. Canada offers tax relief at the provincial and federal levels, designed to attract US feature films, with British Columbia providing up to $300 million Canadian dollars of tax credits each year.[14] Up to 40 US states have offered tax and financial incentives, but several states have questioned the value of these incentives. Arguments that incentives have cost too much in tax revenue losses have prevailed in Michigan, with a more generous scheme replaced by a smaller, capped tax incentive in 2011.[15] Concerns have been expressed in other US states, too. An economic analysis from the Legislative Fiscal Office of the US state of Louisiana in 2005 found negative fiscal impacts from incentives to attract film production, with the chief economist observing that 'the economic benefits are not sufficient to provide tax receipts approaching a level necessary to offset the costs of the tax credits that stimulated the increased film production expenditures.'[16]

Is there a rationale for public support of the film industry?

Generally, there are two permissible justifications for government intervention in the economy. First, market failure—a very limited set of circumstances where the market fails to provide a socially optimal outcome, such as where there are environmental externalities, or so-called public goods. Second, equity concerns—where the government intervenes to redress some perceived inequity or injustice. It is difficult to see that an equity argument would apply to government support for the film industry, leaving only market failure as a justification for public support.

But is the Australian film industry providing a public good? In economics, a public good is a good or service that is non-rivalous and non-excludable in consumption. Non-rivalous means one person's consumption does not limit another person's consumption in anyway. Non-excludable means people cannot be excluded from consuming it in anyway, so there is no way to collect payment. For a true public good, people can 'free ride' on it and not pay for the benefit they receive. Hence, there is a case for public provision, financed through taxation. National defence is the classic example of a public good.

Even if the cultural protection argument were to justify some public support in the limited number of cases of culturally enriching films, it certainly does not justify public support for Hollywood productions with no discernible Australian content.

Films are clearly not public goods in the strictest sense, as they are neither non-rivalous nor non-excludable. Instead, the film industry tends to rely on arguments around the promotion or protection of Australian culture. Some may argue that films with Australian content enrich our culture by helping tell the Australian story. Films such as *Storm Boy* or *Breaker Morant* may be seen in this regard, and many would argue such films yield benefits across successive generations, so it may be socially optimal to provide public subsidies to assist with production. However, there is no clear case for public support as there is in the case of a pure public good such as national defence.

Even if the cultural protection argument were to justify some public support in the limited number of cases of culturally enriching films, it certainly does not justify public support for Hollywood productions with no discernible Australian content such as *Scooby-Doo* or *20,000 Leagues Under the Sea*. Of course, industry supporters would argue there is Australian content by virtue of Australians working on the production, but this is just an argument for government subsidising jobs. There is, however, no justification for the government supporting jobs in one sector over another, if there is no market failure.

Governments long ago abandoned the notion that they have a major, direct job creation role, and it has been a long time since the government has seen its role as employer of last resort, such as when state railways would employ otherwise unemployable young people as porters. The right policy is for governments to promote job creation with sensible fiscal and monetary policies and framework conditions such as flexible industrial relations and efficient market regulations. Unfortunately, although the lesson that governments should not buy jobs has been mostly learned, governments still succumb to special pleading by politically attractive sectors such as the film and car industries.

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Government officials also hope that film productions will add glamour and attention to a region, creating goodwill and attracting tourists with associated economic impacts. It would be impossible to quantify any benefit to tourism, and hence, this appears a spurious ground for public support. There is also the potential for ill will, where a region is displayed in a negative fashion in a film production. For example, some US states such as Texas do not permit a film receiving public support to show their state displayed in a negative fashion.

Another more subtle argument is that it is necessary to support the film industry through international productions so it has the capacity and scale to produce the limited number of films with genuine Australian content. This appears to be a spurious argument, as there will always be some film production capacity in Australia, and there was indeed this capacity before significant public support commencing in the 1970s—even though it would have been on a much smaller scale. There would be a significant number of people across Australia with the required skills but who may be working in other fields—for example, personal training—as the data on the employment experience of actors referred to above would suggest.

Finally, the policy of specific one-off payments to attract international film productions has even received criticism from Australian film industry participants. Academy Award nominated film producer Grant Hill has described the discretionary payments for *The Wolverine* and potentially for *20,000 Leagues Under the Sea* as 'fluky and flaky.'[17] Of course, the domestic film industry does not oppose assistance, but it appears it may prefer replacing ad hoc assistance to attract international productions with enhanced tax offsets available to all.

From a policy perspective, it is preferable to provide what the Productivity Commission calls generally available measures—assistance promoting some desirable activity not limited to particular firms or industries, avoiding the need to pick winners. Even if ad hoc special assistance to the film industry were ended, film industry assistance would still not qualify as a generally available measure because it specifically targets the film industry. In contrast, the R&D tax credit, at least before the recently announced changes taking it away from our largest companies, is generally available across firms and industries and is designed to ameliorate a market failure: the public spillover benefits of innovation that are not captured by private investors. It is unclear what market failures are incentives to the film industry designed to address.

Conclusions

There is no rationale for the ad hoc payments to attract international productions to Australia, and hence, governments should discontinue them. Other clear areas for reform include:

- cutting the Producer and Location offset and reallocating funds to other government priorities or tax cuts; or, at least

- tightening up the operation of the Significant Australian Content test to ensure only genuinely Australian films (that is, with some cultural value, and certainly not *The Great Gatsby*) qualify.

In terms of industry sustainability, assuming this is a worthwhile goal for the time being, it would be better to focus on the domestic industry instead of foreign productions, which as shown above can introduce a large degree of volatility into the industry, and, hence, the risks of crowding out or having to rely on significant amounts of foreign labour to produce the films.

Ultimately, subsidising any industry means governments have less money to spend on areas of arguably greater public need, such as health and education. Given that government assistance to the film industry does not even appear to guarantee the development of a sustainable film industry in Australia, subsidising the industry, especially through special, undisclosed payments, such as to *The Great Gatsby* production, appears doubly wrong.

Endnotes

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