BRITISH SCREEN FORUM

FRAME THE DEBATE

CONSULTATION SUBMISSION

To HM Treasury

Audio-visual tax reliefs

February 2023

FRAME THE DEBATE

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Introduction

- The audiovisual tax reliefs are a hugely important and successful public policy intervention in the film, TV and video games sectors in terms of support for these sectors, attracting production activity to the UK and driving economic growth

- The reliefs create a virtuous cycle, by boosting production activity in audiovisual sectors, which in turn drives demand for skilled labour and infrastructure, driving further investment in talent and facilities, which reinforces the UK's reputation for quality and acts as a catalyst for further production activity

- Alongside their direct economic benefits, the tax reliefs also help to bring in substantial levels of capital investment (for example, in Leavesden, Pinewood and numerous other studios across the UK) and support the production of culturally valuable British content that otherwise would not be made at all

Historical context

- The audiovisual tax reliefs were designed as catalysts for investment in the relevant sectors. They were designed carefully and rigorously tested with industry before implementation to minimise the risk of unintended consequences

- The tax reliefs have been extremely successful in driving the UK's international competitiveness. Much audiovisual production activity is highly mobile; the question is not so much **whether** it will be made, but **where** it will be made. The tax reliefs have attracted production activity that genuinely would not happen in the UK otherwise, supporting growth, jobs and innovation

- The reliefs have delivered huge returns not only for the Screen Sectors but also for the overall UK economy in terms of Gross Value Added. According to the most recent Screen Business report published by the BFI, they delivered returns on investment for each £1 of tax relief of £8.30 (film), £6.44 (High-End TV), £4.53 (animation), £3.20 (children's content) and £1.72 (video games)

- Looking to the future, it is vitally important for the UK to maintain its international competitiveness in the context of increasing competition from other countries. We need to continue to have a competitive tax incentive that sits alongside our high levels of market investment in skills and infrastructure, which together comprise the ecosystem that makes the UK an attractive prospect for productions

"First do no harm"

- We acknowledge the rationale to ensure the tax reliefs are future-proofed in the context of the OECD Pillar Two model rules, and can see potential merit in appropriate reforms to simplify or "tidy up" the current regime. But we must state from the outset that, while in principle we support the proposed change to expenditure credits (subject to important conditions being met), the future-proofing objectives do not justify proposals to increase the HETV expenditure threshold or to reduce the rate of the tax relief to 'fund' a removal of the 80% cap

- If the full set of proposals in the consultation document were implemented, they would be the most fundamental changes to the UK's creative industry tax reliefs since the Film Tax Relief was introduced in January 2007

- Given the huge amount that is at stake, we have major concerns with the proposals presented:
    i. It appears that some crucially important details remain to be worked out, and there is considerable scope for unintended consequences that could damage the UK's international competitiveness over the long term
    ii. A compelling case for many of the changes has not yet been made, and detailed evidence would need to be presented before the proposals can be fully assessed. We would urge HMT to work up its arguments in greater detail for review by the industry and other stakeholders
    iii. The impact on investor confidence needs to be considered during the consultation and implementation process, as the stability of the regime is critical to its continued success. Inward investment companies looking to begin productions soon may opt to locate elsewhere if there is a risk that the UK's reliefs are going to be changed in negative ways or if there is uncertainty as to their operation

- With a possible EC review of the definition of European Works this year that could potentially result in changes which would act as a drag on commercial incentives to produce in the UK, it is more important than ever that nothing is done to make the UK audiovisual tax reliefs less advantageous to investors

- So, whilst acknowledging the rationale to review the reliefs and potentially introduce expenditure credits – and recognising that it could be damaging to wait too long before making necessary changes – we are greatly concerned about the substantial risks associated with being too hasty and rushing through changes that have not been fully worked-through before they are needed. In particular, we are very concerned that the risks associated with the disruption, uncertainty and potential unintended consequences, could result in the UK losing large volumes of business given the portable nature of many productions

- Before being able to offer support for the new tax reliefs, we would need to see more evidence that they are designed in such a way as to maintain the UK's international competitiveness at the macro level, while at the micro level ensuring that the implementation is done in a manner which at least maintains the current value of the incentive in practice (taking account of any increase in tax liability that results from the expenditure credit being treated as revenue)

- We would also wish to see greater clarity in the plans to recognise in the implementation that film, HETV, animation and children's programmes each has its own unique characteristics, and a new combined scheme should have sufficient flexibility to allow for adjustments in relation to each element individually in the event of changes in future circumstances

- We urge HM Treasury to proceed with great caution and engage on the detail with industry, both to ensure an optimal outcome that maintains the UK's international competitiveness and to manage the process so that overseas production companies are not dissuaded from investing in the UK in the coming months. This is especially important given that we can expect to face more challenging market conditions in the short-term, with instances of projects being cancelled as TV studios and streamers look to reduce their costs in response to global economic pressures, along with other countries competing more intensively to attract inward investment

- HM Treasury should be commended for starting the process in good time, but having done so it is important to take the time to get every aspect of the new approach right before making any changes. There is no need to rush and substantial downside risks of moving forward too hastily

- For this reason, we would urge HM Treasury to revise its timetable and make clear that no changes will be made until the new approach has been fully developed and consulted on with industry. The one downside of extending the timetable between now and the implementation of the new reliefs is that it risks creating prolonged uncertainty for potential investors. To alleviate this uncertainty, during this interim period, guarantees should be given as a matter of urgency to mitigate against the effects of the uncertainty that may arise while options are being considered. In particular, confirmation should be provided that any project that has already begun on the basis of the current reliefs will be able to continue using this system, regardless of the duration of the project (following the precedent set when the sale and leaseback reliefs were replaced). We also see merit in confirming an option for producers to elect to switch to the new rules if they wish to do so.

RESPONSES TO CONSULTATION QUESTIONS (SEE SECTION C)

- Given the lack of detail presented, we can only comment at a high level and would need to see more information before we could assess the proposals more closely
- We encourage HMT to engage fully with industry bodies such as British Screen Forum on the details of the new scheme, as it did when designing the original tax relief schemes

Modernising the film and TV sector reliefs

HMT Proposal	British Screen Forum response
Merging film and TV sector into a single scheme	We recognise that – while the most substantive change in the consultation document relates to moving to expenditure credits – there are some potential benefits that could arise just from merging the four tax reliefs for film and TV (film, HETV, children's and animation) into a single scheme. Even this would be a substantial and disruptive proposed change, and it is important to carefully consider any downside risks, including potential unintended consequences. A persuasive case has not been made in the consultation document, and without seeing further detail it is impossible to judge whether any potential benefits would be realised or disbenefits inadvertently introduced. In particular, any support would be subject to the important caveat that the merged relief should retain the same degree of flexibility as now to change the qualifying criteria or headline rate for any one of the sub-sectors as circumstances demand (perhaps in relation to independent UK film, children's programmes or VFX) without affecting the other sub-sectors.

HMT Proposal	British Screen Forum response
Minimum expenditure threshold (HETV tax relief)	We believe it would be highly counterproductive to increase the minimum expenditure threshold, notwithstanding the inflationary pressures, given the substantial return on investment of projects that access the tax credits. Increasing the threshold would see programmes that cost close to the current £1 million per hour threshold being shot in other territories rather than the UK, or not made at all, reducing production activity in the UK. This would particularly impact high-quality UK dramas made primarily for domestic audiences, making it harder for the PSBs and other broadcasters to invest in this kind of distinctively British content. It would also reduce the potential for the skills development that accompanies the making of such programmes – this has wider knock-on effects, as most of the best-regarded UK talent involved in prestigious high-end projects benefit earlier in their careers from the training they received whilst working on domestic dramas in the £1 million per hour budget range. As such, these programmes form a vital step in the talent ladder for writers, directors and other key roles. If HM Treasury's key concern is around certain genres, such as soaps, accessing this relief, then our suggestion would be to formally add these genres to the exclusion list (as with the legal definition of documentary, we would urge consultation with industry to develop appropriate criteria).
Minimum slot length (HETV tax relief)	We recognise the concerns set out in the consultation document and agree with the thrust of the proposals to address them. Given the importance to us of maintaining the minimum expenditure threshold, we encourage HM Treasury to consider additional rules that would explicitly prevent the likes of soaps from being bundled together to access the HETV relief, rather than increasing the expenditure threshold as the means to exclude these genres. This could be achieved, for example, as part of the proposed option (a) in para 3.12 of the consultation document, according to which the legislation would be amended to apply on an "episode by episode basis" and the minimum slot length reduced to 20 minutes. The lack of detail in the consultation document prevents us from making a full assessment of the two proposed options with any confidence.

HMT Proposal	British Screen Forum response
Legal definition of documentary (HETV tax relief)	We agree that a workable definition would provide greater clarity and certainty, to the benefit of industry and the Government alike. Further consultation is needed with the relevant stakeholders in that part of the sector, to make sure the definition is fit-for-purpose. Key stakeholders to consult with are those who best understand factual commissions and evolving practices in the production of documentaries, such as the main broadcasters and streamers. A fit-for-purpose definition would provide clarity without being too narrow and thereby excluding content that ought to be eligible.

Modernising Video Games Tax relief

HMT Proposal	British Screen Forum response
Video game tax relief (VGTR) qualifying expenditure	There is unlikely to be a benefit to the UK games industry overall if EEA expenditure were no longer eligible, given the current skills shortages. We would expect such a change to negatively affect video game companies and that it would encourage them to move expenditure outside the UK (to lower cost territories or to territories which allowed claims across multiple jurisdictions) rather than attract more expenditure to the UK. The net effect of the proposed changes would be to reduce UK activity and diminish the beneficial impacts of the VGTR. Increasing or removing the subcontracting cap might bring small benefits to small companies but these would be more than offset by the increased costs associated with the removal of eligibility of EEA expenditure.

Reforming audiovisual tax reliefs to expenditure credits

HMT Proposal	British Screen Forum response
Basic structure of the proposed expenditure credit	We recognise the need to future-proof the tax reliefs in the context of the OECD Pillar Two model rules, and in principle we support the proposed change to expenditure credits, subject to a number of important conditions being met: i. As per our overarching concerns, crucially important details of the proposed new credit remain to be worked out, and there is considerable scope for unintended consequences that could damage the UK's international competitiveness. We would need to see more information before we can make an informed assessment ii. The changes to a new system of tax reliefs should be done in a manner which at least maintains the current value of the incentive in practice (taking account of any increase in tax liability that results from the expenditure credit being treated as revenue) iii. The UK regime must remain competitive with other international schemes. This means maintaining the speed, simplicity and certainty that are positive attributes of the current UK regime iv. Any new expenditure credit framework must allow sufficient differentiation to remain to reflect the particular characteristics of the current five audiovisual tax reliefs and to respond to the specific circumstances in each sub-sector with flexibility
Removing the 80% cap on qualifying expenditure	We agree that, other things being equal, removing the 80% cap has the potential to encourage more spend to take place in the UK rather than overseas, which could help the VFX and animation sectors in particular. The benefits could be increased, and the direct cost to the Exchequer minimised, through a more targeted approach that limits the removal of the cap to certain productions that include a certain amount of spend on VFX or animation but then boosted the credit rate for this spend (as the UK Screen Alliance has proposed). However, we would not support any proposal to remove the cap if it were accompanied by a reduction in the overall credit rate, as suggested in the consultation document. The market is highly sensitive to the credit rate, and a reduction would carry a huge risk of a negative impact – in terms of lost inward investment business to other countries – that could greatly exceed the benefit of removing the cap. If the Government remains of the view that there must be some form of trade-off, then our position would be to keep the 80% cap as is and not reduce the overall rate.

HMT Proposal	British Screen Forum response
Replacement of current schemes with expenditure credit scheme for audiovisual tax reliefs	Should new expenditure credits be introduced, we agree that these should fully replace their existing counterparts (with the caveat that they are well-designed and fit-for-purpose). It is vital that assurances are given as soon as possible that transitional arrangements will be put in place to ensure that no-one will be disadvantaged as a result of beginning production in advance of the start of any new scheme. Otherwise, there is a significant risk that the UK will lose highly mobile production projects to other territories during the transition process – which effectively begins immediately with this consultation. We suggest as a key transition principle that any project that has already begun on the basis of the current reliefs will be able to continue using this system, along with an option for producers to elect to switch to the new rules if desired.

A. INTRODUCTION

ABOUT BRITISH SCREEN FORUM

British Screen Forum is a membership organisation through which many of the best informed and most influential people in the UK Screen Sectors convene to interrogate issues of importance and influence policy and the thinking around policy. We provide a unique and trusted space for key players from the Screen Sectors to come together to debate the implications of the evolving landscape and the policy and regulatory environment, and to gain unrivalled insight into emerging themes and innovative technologies.

Members are senior figures drawn from a wide range of businesses and organisations operating in the film, TV, video game and/or online sectors. We aim to cover the whole value chain as well as the full range of means of distribution, so include members who can speak for writers, technicians, independent producers, directors, studio operators, distributors, exhibitors, broadcasters, games publishers, games developers, pay TV platforms and online platforms. It is a unique cross-sectoral mix, with a balance of creative, policy and business specialists. Further details are available on our website.[1]

Including under our former name – British Screen Advisory Council – we have played an important role over many decades in helping to ensure that the public policy framework enables the Screen Sectors to deliver the strong growth in GVA, jobs and exports it has achieved over recent years. Of particular relevance to this consultation, our contribution has included convening the industry working group which worked closely over an extended period of time with HM Treasury in developing the Film Tax Relief (FTR).

ABOUT THIS REPORT

This paper responds to HM Treasury's consultation on the "Audio-visual tax reliefs." Section B provides historical context and emphasises the importance of the tax reliefs as a form of investment in the sector and a means of ensuring the UK is internationally competitive. It goes on to highlight our overarching points relating to the consultation – in particular, the importance of "doing no harm" to a system that is currently working very well. Section C goes on to respond to the consultation questions, organised around the chapters in the consultation document.

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[1] https://britishscreenforum.co.uk/

B. OVERARCHING ISSUES

The audiovisual tax reliefs are a hugely important and successful public policy intervention in the Screen Sectors in terms of attracting production activity to the UK and driving economic growth.

The tax reliefs have been a huge success as a public investment that has delivered substantial returns not only for the Screen Sectors[2] but also for the overall UK economy. As then Chancellor, Rishi Sunak noted in his introduction to the Screen Business report in 2021 *"These reliefs have […] helped to spur a new wave of private investment to develop major production hubs and centre points for high quality crew and studio space all over the UK, from Belfast to Buckinghamshire, supporting tens of thousands of jobs."*[3]

Films, TV programmes and video games made in the UK are the envy of the world, making the UK an attractive location for production. But world-class infrastructure and talent are not by themselves sufficient to attract inward investment: pricing also matters in highly competitive international markets for audiovisual production, and it is thanks in large part to the tax reliefs that the UK is able to attract as much business as it does. This creates a virtuous cycle: they incentivise increased production activity and scale in the film, TV and video games sectors, which in turn drives demand for skilled labour and infrastructure in the UK, driving further investment in talent and facilities to meet this demand, which reinforces the UK's reputation for quality and acts as a catalyst for further production activity.

Alongside the direct economic value and investment that the tax reliefs drive, the tax reliefs also bring a number of other benefits, helping to bring in substantial levels of capital investment and supporting the production of culturally valuable British content:

- It is thanks to the tax reliefs – and the longevity and stability of the current regime – that Warner Bros has invested so much in Leavesden, which is the only studio they own anywhere in the world outside of the US. They have made a significant multi-million-pound investment in renovating and expanding the studio and are seeking to expand it further.

[2] Note: for the purposes of this response, there is no difference in meaning between references to "audiovisual" sectors (as used by HM Treasury in the consultation document) and the "Screen Sectors" (British Screen Forum's usual terminology for the sectors that it covers)
[3] Source: Screen Business: how screen sector tax reliefs power economic growth across the UK, Olsberg•SPI & Nordicity for the BFI, 2021, p9

- The impact of the reliefs in supporting capital investment extends much more broadly: there are similar stories of investment from overseas at Pinewood, Titanic (Belfast) and Wolf (Cardiff) Studios. Such investments (including Leavesden) have resulted in disused industrial facilities – an engine factory, shipyard and cathode ray tube factory – being brought back to life by the film and TV industry.

- The tax reliefs also play an important role in supporting the production of culturally and socially valuable content for UK audiences, especially through their support of independent film and public service genres of television.

- In particular, they support the creation of content in particular public service genres, such as children's programmes, where commercial incentives are weaker and they are able to boost supply from a relatively low base.

In terms of the attractiveness of the UK to investors in content, we cannot be complacent. Every time a new project begins, its producers examine afresh the best place to base their film, TV programme or video game, and so this virtuous cycle continues only so long as the UK remains competitive. The highly mobile nature of much screen sector activity and the international competition to host it is recognised in the report published by the Lords Communication and Digital Committee on 17 January 2023 which concluded that the tax reliefs *"have played an important role in supporting innovation, growth and international competitiveness in the creative industries. We welcome the Government's commitment to continuing such support. But other countries are increasingly adopting similarly competitive tax relief systems. The UK is falling behind. The Government's consultation on creative industry tax reliefs must benchmark UK incentives against those in other countries to ensure the UK remains competitive."*[4] It is in this context that we respond to the consultation on updating the audiovisual tax reliefs.

In this section, we begin by revisiting the careful development and original purposes of the various existing tax reliefs, before going on to present the most recent data on their success in terms of returns on investment and ensuring international competitiveness. We then turn to our overarching comments on the proposed changes in the consultation document.

[4] Source: At risk: our creative future, Lords Communication and Digital Committee, January 2023, page 28, para 80

a) Historical context

- The audiovisual tax reliefs were designed as catalysts for investment in the relevant sectors.
- They have been extremely successful in driving the UK's international competitiveness – alongside our world-class talent and production facilities – and generating substantial returns on the investment.
- Looking to the future, it is vitally important for the UK to maintain its international competitiveness in the context of increasing competition from other countries.

It is important to note that the tax reliefs introduced for high-end television (HETV), children's TV, animation and video games between 2013 and 2015 were built on the proven success and tested design of the film tax relief (FTR) that has been operating successfully since January 2007. FTR was itself developed in very close consultation with industry over a period of many years as a means of replacing the earlier Section 48 and Section 42 tax incentives for film. Following the announcement in the March 2004 budget of the policy intention to introduce FTR, the close engagement with industry continued while the details were worked out, including though the Tax Strategy Working Group chaired by the Minister for the Arts, and through the Inland Revenue Expert Group. British Screen Forum[5] served on both groups along with other key sector bodies and helped to convene wider stakeholder input. Consequently, when policy decisions were subsequently taken to further incentivise the production in the UK of HETV, children's TV, animation and video games, the FTR provided a stable and reliable model for the intervention.

The point here is that the details of the FTR scheme introduced in 2007 – on which the other four audiovisual reliefs are all based – were fully and extensively tested in advance with industry practitioners in order to ensure that FTR would deliver the desired outcome of driving up film production activity in the UK and that unintended consequences would be minimised. The changes now proposed are structurally more significant than anything since 2007. Any change to a new scheme based on expenditure credits requires similarly in-depth industry engagement at a level which goes far beyond that which can be achieved on the basis of the scant detail set out in the consultation.

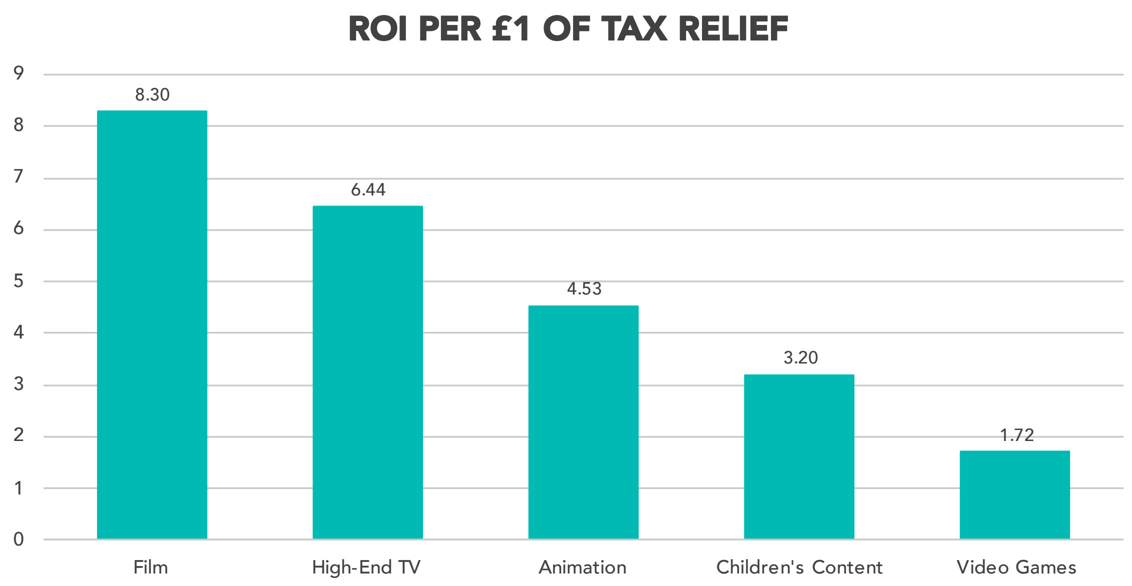
It is crucial to recognise that an overarching key purpose of the tax reliefs is to ensure the UK can remain competitive internationally. Much of the audiovisual production activity in the markets in which global tax reliefs are available is highly mobile; the question for producers, therefore, is not so much **whether** these projects will be made, but **where** they will be made. So, when assessing the impact of the tax reliefs, the relevant counterfactual for mobile productions is not that the projects would not otherwise be made, but rather that they would be made elsewhere – for example in Hungary or California or any other country with good skills and infrastructure and generous tax reliefs. In this context, the tax reliefs are generating production activity in the UK – supporting growth, jobs and innovation – that genuinely would not happen here otherwise. The incentives offered by a selection of the UK's major competitors are summarised in the Annex.

[5] Under its former name, British Screen Advisory Council (BSAC)

It should be clear from this that the reliefs should not be viewed simply just as "subsidies," a corollary of which would be that they ought to be kept as low as possible to minimise the burden on taxpayers. Nor do they represent a "deadweight loss" to the economy, by substituting for private funds in projects that would have been made in the UK anyway.

On the contrary, by acting as a driver of production activity that would not otherwise take place in the UK (or at all, for some smaller indigenous productions), the audiovisual tax reliefs are a huge and enduring success for the sector and for the overall UK economy – both directly and indirectly through capital investment in studios (as detailed above). They have generated a positive return on investment in terms of UK Gross Value Added: according to the most recent Screen Business report published by the BFI, the audiovisual Tax Reliefs delivered returns on investment (ROI) for each £1 of tax relief of £8.30 (film), £6.44 (High-End TV), £4.53 (animation), £3.20 (children's content) and £1.72 (video games).[6] This analysis indicates that the audiovisual tax reliefs all generate positive returns on investment, and that those returns are particularly large for films and HETV. Over and above these headline figures, by stimulating activity around the nations and regions, the Tax Reliefs make a valuable contribution to the Government's "levelling-up" agenda.

The Creative Sector Tax Reliefs deliver high returns on investment



Data source: Olsberg•SPI / Nordicity

Looking to the future, it is vitally important for the UK to maintain its international competitiveness in the context of increasing competition from other countries. A number of other territories have seen the success of the UK and are seeking to emulate it by gaining a larger share of the growing audiovisual production pie. For example, Spain have launched their 'Spain, audiovisual hub of Europe' plan which includes a one-stop shop offering help

[6] Source: Screen Business: how screen sector tax reliefs power economic growth across the UK, Olsberg•SPI & Nordicity for the BFI, 2021

with financial incentives, locations, crew, work visas, etc. Backed by more than €1.6 billion of investment and with enhanced tax incentives as part of its offer, the plan aims to increase audiovisual production in Spain by 30% by 2025.[7]

In addition to the incentives offered in major production centres, several smaller or emerging markets have introduced highly competitive incentives. Research conducted by Olsberg•SPI for British Screen Forum identifies a considerable number of announcements made in the last 12 months alone:

- **Austria** launched an expanded cash rebate incentive in January 2023, worth 35% of eligible costs with no annual budget cap
- **Arizona** legislated a 15% – 20% tax credit incentive, to be launched in 2023
- **Iceland** launched a higher incentive rate of 35% for high-value projects
- **India** launched a 30% cash rebate incentive with a 5% uplift for projects which have a 15% Indian-resident crew
- **Israel** launched a 30% cash rebate incentive in 2022
- **Mongolia** launched a 40% cash rebate
- **New Jersey** launched a "studio partner" system providing additional incentives and exemptions to studios which invest in infrastructure in the state
- **Saudi Arabia** launched a 40% cash rebate, while two regions, **AlUla** and **NEOM** will offer additional incentives
- **Sweden** launched a 25% cash rebate

To be clear, we are not advocating for a 'bidding war' that would lead to a global escalation in tax-relief levels. Rather, we need to retain a competitive tax incentive that sits alongside our high levels of market investment in skills and infrastructure, that together comprise the ecosystem that makes the UK an attractive prospect for productions. The UK needs to maintain its current competitive advantage across all the areas that contribute to its appeal: a high-quality skills base, world-class infrastructure at scale and a competitive tax relief regime. Any changes that would weaken any of these elements, including the tax reliefs, would reduce the UK's attractiveness compared to the alternatives.

With the HETV relief especially, the current regime has proven to be highly responsive to the most significant global structural changes in the sector: as the market for high-quality dramas and other content for streaming services has proliferated, we have secured a significant share of the market both for projects that originated in the UK and for inward investment projects that could have been made anywhere. With the industry continuing to

[7] See https://spainaudiovisualhub.mineco.gob.es/en/home

face significant disruptions – for example, through innovative changes in workflow and production methods such as new uses for VFX and other virtual technologies – it is also important that the UK can continue to be able to compete within these fast-changing currents.

A good example of the success of the current model is Amazon's *The Lord Of The Rings: The Rings of Power* TV production, the first series of which premiered in Autumn 2022. A year earlier, in August 2021, Amazon announced its decision to move filming from New Zealand to the UK for the second series. This relocation marks the first time any of the modern *The Lord of The Rings* live-action projects have been produced outside of New Zealand (including the film trilogy of *The Hobbit*). The relocation is expected to bring several hundreds of millions of dollars of production activity to the UK in the coming years – most, if not all, of which will be additional investment in the UK that would not have happened here otherwise.

Our understanding is that Amazon's decision to choose the UK over other countries was driven by the fact that the UK ticks all the boxes referred to above – world-class talent and production facilities, a supportive policy framework (competitive tax reliefs), as well as the scale to handle large productions. Such is the competitive nature of the location decision for mobile productions such as this, it seems likely that at a higher price (if the tax reliefs were less generous), there is a good chance an alternative location for the production would have been found, notwithstanding the UK's scale and the excellence of its infrastructure and talent base. There are several global hubs with the talent pool, locations, incentives and production infrastructure necessary to attract such a production of this scale. Among the factors that producers consider when selecting a location, particularly for large mobile productions, is the tax credit system, and this cannot be overstated.

b) "First do no harm"

- We acknowledge the rationale to ensure the tax reliefs are future-proofed in the context of the OECD Pillar Two model rules, and can see potential merit in appropriate reforms to simplify or "tidy up" the current regime. In principle, we support the proposed expenditure credits (subject to important conditions being met), But this does not justify proposals to increase the HETV expenditure threshold or reduce the rate of the tax relief to 'fund' a removal of the 80% cap.
- Given the fundamental nature of the proposed changes, there is a huge amount at stake, and we have major concerns with the proposals presented:
    - First, it appears that some crucially important details remain to be worked out, and there is considerable scope for unintended consequences that could damage the UK's international competitiveness.
    - Second, a compelling case for many of the changes has not yet been made, and detailed evidence would need to be presented before stakeholders can fully assess the proposals.
    - And third, the impact on investor confidence needs to be considered during the consultation and implementation process, as the stability of the regime is critical to its continued success.
- Especially regarding expenditure credits, there are substantial risks associated with being too hasty and rushing through changes that have not been fully worked-through, and this could result in the UK losing large volumes of business.
- We therefore urge HM Treasury to proceed with great caution, both to ensure an optimal outcome that maintains the UK's international competitiveness and to manage the process so that overseas production companies are not dissuaded from investing in the UK in the coming months.
- We urge HM Treasury to revise its timetable and make clear that no changes will be made until the new approach has been fully developed and consulted on. And to alleviate the uncertainty during the interim period, guarantees should be given as a matter of urgency to mitigate against the effects of the uncertainty that may arise while options are being considered.

There is some ambiguity in the proposals in the consultation document, which was to some degree cleared up during the stakeholder meeting held by HM Treasury and DCMS representatives just before Christmas. It is worth, therefore, explicitly setting out our interpretation of the proposals set out in the consultation document, which is that, at a high level, taken together they imply the following three steps:

i. **Combine the four tax reliefs relating to film and TV into a single relief, whilst maintaining their specific qualifying criteria**, e.g. the qualification criteria for animation in terms of where it is set would remain different to those in live action

ii. **Refocus the basis on which the Video Games Tax Relief applies to UK expenditure**, whilst keeping the Video Games Tax Relief separate (as specificities relating to video games mean the relief cannot immediately be merged into the combined film/TV relief in its current form)

iii. **Convert the two audiovisual reliefs (i.e. the two reliefs being the 4-in-1 relief for film and TV, and the separate Video Games Tax Relief) into a new form of expenditure credits**. While the consultation document states (para 4.5) that the "*government will consider bringing the VGTR into the scope of the single tax credit*," our understanding is that this is not in fact a current part of the plan – and believe that it would be essential for the Government to consult further with the industry should they wish to make any such change in the future.

If implemented in full, these would be the most fundamental changes to the UK's creative industry tax reliefs since the Film Tax Relief replaced the previous sale-and-leaseback models in January 2007.

We acknowledge the rationale to ensure that the tax reliefs are fit-for-purpose in the future, as the OECD Pillar Two model rules that are being introduced globally mean that there is a need to review how the reliefs work. There is also merit in the desire to simplify and "tidy up" the reliefs where appropriate – both as a general principle and to address sectoral changes such as the blurring between film and TV whereby projects may start as a film and end up as TV or vice versa.

But we must state from the outset that, while in principle we support the proposed change to expenditure credits (subject to important conditions being met), the future-proofing objectives do not justify proposals to increase the HETV expenditure threshold or to reduce the rate of the tax relief to 'fund' a removal of the 80% cap.

Given how much is at stake, we have some significant overarching concerns with the proposals presented in the consultation document:

1. **It appears that some crucially important details remain to be worked out.** Depending on how they are resolved, there is considerable scope for unintended consequences that could cause substantial damage to the UK's international competitiveness over the long-term once the new regime is in place. This could result in the UK permanently losing large volumes of business to other countries that it would have won under the current regime.
   It is worth noting that the original Film Tax Relief was test-driven to destruction through a series of working parties on which industry sat – including those led by the relevant Minister and by Inland Revenue over a period of many months. There is no doubt that this intensive review process contributed to its success from the outset and succeeded in minimising the risk of unintended consequences.

2. **A compelling case for many of the changes has not yet been made.** Given (a) how significant the ramifications of the proposals are, (b) the amount of disruption that may be caused, and (c) the potential for substantial loss of business if anything goes wrong, we do not believe that a compelling case for such a radical set of changes has yet been made, and we would urge HMT to work up its arguments in greater detail for review by the industry and other stakeholders.
   In particular, so we can assess the proposals as carefully as is necessary, we would like to see a presentation detailing the evidence of the expected benefits of merging the film

and TV schemes into a single scheme, and analysis of all the potential implications – positive and negative – of a move to expenditure credits.

3. **Stability of the tax relief is critical to its continued success, and the impact on investor confidence needs to be considered**. A key attraction of the UK regime is its stability and the confidence this gives to potential investors, who know exactly what they are getting when they base their productions in the UK. Any change, however well intentioned, disrupts this stability.
   While obviously not its intention, the consultation and subsequent implementation process itself runs the risk of reducing investment during this period, as inward investment companies looking to begin productions soon may opt to locate elsewhere if there is a risk that the UK's reliefs are going to be changed in negative ways. Even small changes to the tax incentives risk sowing seeds of doubt with global content producers that the UK system is not stable or reliable.
   Such is the competitive nature of the global market for major productions, these changes could have a bigger cost that the direct impact of those changes – which could mean that the overall effect of changes whose direct impact may be marginal may end up being materially negative.
   As a matter of urgency, guarantees should therefore be given to mitigate against the effects of the uncertainty that may arise while options are being considered.

It seems increasingly possible that the European Commission will review the definition of European Works in the coming year, and a plausible outcome of such a review could be that UK content would no longer as count as European for the purposes of meeting the European content quotas in the AVMS Directive. Were this to come to pass, such a change would negatively impact the incentive to produce in the UK. In this context, it is more important than ever that nothing is done to make the UK audiovisual tax reliefs less advantageous to investors than they currently are.

For these reasons, whilst acknowledging the rationale to review the reliefs and potentially introduce expenditure credits – and recognising that it could be damaging to wait too long before making necessary changes – we are greatly concerned about the substantial risks associated with being too hasty and rushing through changes that have not been fully worked-through before they are needed. We are very concerned about the risks associated with the disruption and potential unintended consequences, both of which could result in the UK losing large volumes of business, given the portable nature of many productions. The consultation document does not identify – and to date we have not found – any other countries with significant audiovisual sectors who have already introduced comparable expenditure credit schemes for audiovisual content. While HM Treasury should be commended for being proactive and for starting the process in good time, it is important to appreciate that this is, to a significant extent, a step in the dark and the new plans need to be developed with great care.

Before being able to offer support for the new tax reliefs, we would need to see more evidence that the reliefs will fully meet three vital objectives: firstly, that they conform to the new OECD framework (the main driver of the changes); secondly, that they are designed in such a way as to maintain the UK's international competitiveness at the macro level; and thirdly, ensuring that at the micro level the implementation is done in a manner which at least maintains the current value of the incentive in practice (taking account of any increase in tax liability that results from the expenditure credit being treated as revenue). We would also wish to see greater clarity in the plans to recognise in the implementation that each of the elements in the merged film and TV relief has its own unique characteristics, and a new combined scheme should have sufficient flexibility to allow for adjustments in relation to each element individually in the event of changes in future circumstances.

In particular, we would need to ensure that the new merged relief has the flexibility to allow changes to be made to the headline rate and/or qualification criteria for one element (e.g. film or even a particular subset of films) without changing it for all TV and films covered by the merged relief. In this context, while not the subject of this consultation, we would add that the proposals under consideration should not preclude an ongoing review of particular sub-sectors that would benefit from enhanced incentives in light of ongoing market failures. There are two notable examples of this: the first being independent UK films within a particular budget range, where there are specific issues and whose role in relation to developing skills and talent is critical to the broader sector, in addition to its unique cultural contribution.[8] And second, there have been active policy discussions around a higher credit rate for children's content (including animation) to stimulate the production of high-quality UK programming in this genre, the volume of which has collapsed in recent years.

This month, Sean Clarke the managing director of Aardman, one of the world's leading animation studios, and producers of British hits such as *Wallace and Gromit* and *Shaun The Sheep*, pointed out in a Guardian interview the challenges facing the UK sector as its tax relief becomes less competitive relative to other territories, with Ireland, France, Canada and Spain's Canary Islands now offering headline rates of relief ranging between 37% and 50%:

> *"I have the Spanish calling me all the time, saying: 'Why don't you come to the Canaries, where it's up to 50%?' We have to consider it. […] It's a constant battle of how you raise money. It's amplified at the moment because a lot of countries are more competitive with tax credits and they're building infrastructure, both in terms of studios and training."*[9]

Given the lack of detail in the current proposals, we can only comment at a high level and would need to see more information before we could assess the individual proposals more closely. This caveat applies to all of the specific responses in the next section.

Meanwhile, we would urge HM Treasury to proceed with great caution and engage on the detail with industry: not only to ensure the optimal outcome from the consultation but also to manage the process so that overseas production companies looking to invest in the UK over the coming months are not dissuaded from doing so as a direct result of this consultation. The stakeholder meeting held before Christmas and the more recent

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[8] See British Screen Forum's "Prospectus for Growth in an Age of Change" (July 2022, here) and the "Economic Review of UK Independent Film" commissioned by the BFI from Alma Economics (July 2022, full report and BFI response here)

[9] Source: https://www.theguardian.com/culture/2023/feb/06/aardman-uk-animators-may-have-to-move-abroad

roundtables were a positive sign that HMT and DCMS are willing to listen to industry regarding their concerns, but the risk of lost business in the short term remains high.

The need for careful management of the process is especially important given that we can expect to face more challenging market conditions in the short-term, with instances of projects being cancelled as TV studios and streamers look to reduce their costs in response to global economic pressures. We are also seeing other countries competing more intensively to attract inward investment.

Turning to the next steps, it is important for HM Treasury to take the time to get every aspect of the new approach right before making any changes. There is no need to rush and there are substantial downside risks of moving forward too hastily. We therefore urge HM Treasury to revise its timetable and make clear that no changes will be made until the new approach has been fully developed and consulted on with industry. An updated timetable should be published as a matter of urgency, to address industry concerns.

The one downside of extending the timetable between now and the implementation of the new reliefs is that it risks creating prolonged uncertainty for potential investors. To alleviate this uncertainty, during this interim period, guarantees should be given as a matter of urgency to mitigate against the effects of the uncertainty that may arise while options are being considered. In particular, confirmation should be provided that any project that has already begun on the basis of the current reliefs will be able to continue using this system, regardless of the duration of the project (following the precedent set when the sale and leaseback reliefs were replaced). We also see merit in confirming an option for producers to elect to switch to the new rules if they wish to do so (as we argue in the next chapter in our response to the question on the transition process).

C. RESPONSES TO CONSULTATION QUESTIONS

In this section, we respond to the issues raised in the consultation document, following the consultation document's chapter headings.

We observe that some of the key proposals do not have a corresponding consultation question (minimum expenditure threshold for HETV relief, removal of 80% cap on qualifying expenditure, merging of video games tax relief into a single relief with the proposed combined film and TV relief), while for other proposals there is a series of closely related questions. For this reason, we have organised our response around the key proposals in the consultation document rather than the individual questions.

As we emphasised in the previous section, all of our responses below must be caveated with the fact that we can only comment at a high level on the individual proposals given the lack of detail presented in the consultation document. We would need to see more information before we could assess the individual proposals more closely and encourage HM Treasury to engage fully with industry bodies such as British Screen Forum on the design and details of the new scheme (including elements such as the Guidance notes and the specifics of the financial/accounting details), as it did when designing the original tax relief schemes.

MODERNISING THE FILM AND TV SECTOR RELIEFS

a) Merging film and TV sector into a single scheme (Question 1)

There is some ambiguity in the consultation document. Our interpretation is that the proposal is to combine the four existing tax reliefs relating to film and TV – i.e. film, HETV, children's and animation – into a single relief, whilst maintaining their specific qualifying criteria. Elsewhere in the document, in para 4.5, it states that the *"government will consider bringing the VGTR into the scope of the single tax credit,"* but our understanding is that this is not in fact a current part of the plan and for the purposes of the consultation it should be assumed that video games will remain separate. Were the Government to consider also bringing video games into the merged tax credit in the future, this would be a substantial additional step and, as we state above, it would be essential for the Government to consult further with the industry should they wish to make any such change.

We also interpret the consultation to imply that the merging of the four reliefs into one could happen regardless of whether the relief(s) then get converted to expenditure credit(s). So the proposal to merge the reliefs should be considered separately on its own merits.

- We recognise that – while the most substantive change in the consultation document relates to moving to expenditure credits – there are some potential benefits that could arise just from merging the four tax reliefs for film and TV (film, HETV, children's and animation) into a single scheme.
- Even this would be a substantial and disruptive proposed change, and it is important to carefully consider any downside risks, including potential unintended consequences. A persuasive case has not been made in the consultation document, and without seeing further detail it is impossible to judge whether any potential benefits would be realised or disbenefits inadvertently introduced.
- In particular, any support would be subject to the important caveat that the merged relief should retain the same degree of flexibility as now to change the qualifying criteria or headline rate for any one of the sub-sectors as circumstances demand (perhaps in relation to independent UK film, children's programmes or VFX) without affecting the other sub-sectors.

A tangible potential benefit to industry of this proposal is that it could provide useful flexibility for projects whose business model changes from film to TV or vice versa mid-way through the production.

We also recognise that there may be, in theory at least, some benefits from simplifying the tax reliefs regime – with the key caveat that the merged relief would need to be designed in such a way as to recognise that there are, and will remain, differences between the sub-sectors. Notwithstanding the blurring of boundaries, they still have different business models, production processes and outputs, and this motivates the differences between the current frameworks. A "one size fits all" approach that limits the flexibility needed could be very damaging to some categories of film or TV.

We therefore welcome the fact that in the stakeholder meeting held before Christmas, HM Treasury clarified that the proposal explicitly involves maintaining the specific qualifying criteria. This would seem to mean, for example, that the qualification criteria for animation, in terms of where it is set, would remain different to those in live action. Our assumption is that this also means that other separate criteria would remain in place, so for example the HETV threshold would not apply to all other sectors in the merged relief.

This flexibility also needs to extend to the headline rate of the reliefs. This would reflect the objective of future proofing the tax reliefs regime: external circumstances may change in respect to one sector or sub-sector (whether an existing category such as animation, or a sub-category such as independent film), and we would need to be able to make changes to the rules for that category without disrupting everything else. We would encourage HM Treasury to provide further details of their proposals.

b) Minimum expenditure threshold (HETV tax relief) (no consultation question)

The proposed increase to the minimum expenditure threshold is a highly significant issue – by some distance, the most important single issue raised for some of our Members – and it is concerning that HM Treasury has chosen not to consult on this. Notwithstanding the absence of a specific consultation question on the subject, we set out the issues here.

- We believe it would be highly counterproductive to increase the minimum expenditure threshold, notwithstanding the inflationary pressures, given the substantial return on investment of projects that access the tax credits.
- Increasing the threshold would see programmes that cost close to the current £1 million per hour threshold being shot in other territories rather than the UK, or not made at all, reducing production activity in the UK.
- This would particularly impact high-quality UK dramas made primarily for domestic audiences, making it harder for the PSBs and other broadcasters to invest in this kind of distinctively British content. It would also reduce the potential for the skills development that accompanies the making of such programmes – this has wider knock-on effects, as most of the best-regarded UK talent involved in prestigious high-end projects benefit earlier in their careers from the training they received whilst working on domestic dramas in the £1 million per hour budget range. As such, these programmes form a vital step in the talent ladder for writers, directors and other key roles.
- If HM Treasury's key concern is around certain genres, such as soaps, accessing this relief, then our suggestion would be to formally add these genres to the exclusion list (as with the legal definition of documentary, we would urge consultation with industry to develop appropriate criteria).

The HETV tax relief has played a vital role as a catalyst for production activity that would not otherwise take place in the UK. Most significantly, it has helped to ensure that high-end TV programmes that could be filmed in a variety of international locations are made in the UK.

The economics of high-end TV production are challenging: it is increasingly rare for the PSBs to fully fund HETV programmes and the commissioning broadcasters or producers are required to achieve their budgets through a combination of co-productions, pre-sales (e.g. to international broadcasters or streamers) and the tax relief. In this respect, the economic model for HETV has become very similar to the longstanding model for independent film, and is similarly reliant on the tax relief as part of the funding mix.

The relief has also boosted the volume of domestic content in some public service genres that are especially cost-sensitive, such as comedy, drama and regional production. Given the high costs involved and relatively low ratings that mean that they typically do not "pay their way," in the absence of the reliefs fewer programmes in these genres would be made.

And the HETV relief brings wider benefits for the sector and the overall UK economy, including in relation to workforce development and skills. One of the foundations on which the UK's international competitiveness rests (alongside the value of the tax reliefs) is its world-class skills base. It is important to support production at current or greater volumes in order to maintain a sufficient pipeline of talent and skills, and productions at or just above the current threshold play a disproportionately important role in developing talent. This pipeline ensures we have an effective and thriving skills base that includes high-calibre crew capable of making the highest-budget productions. This is especially important at a time when we are facing significant tech-driven changes in production techniques, for example in relation to 'virtual production,' that requires new skills to be taken on board.

Far from representing a "cost to taxpayers" that needs to be minimised, as seems to be implicit in the thrust of the argument in the consultation document, this relief delivers a substantial positive economic impact, bringing production activity to the UK that would not otherwise take place here. As the chart on p10 shows, it has delivered returns on investment for each £1 of tax relief of £6.44, a substantial ROI in itself and one of the highest rates of any of the audiovisual tax reliefs. In our view, there is no problem to be fixed with regard to the threshold level.

Especially given the massive boom in demand for scripted content in recent years from the likes of the global streamers, we should be doing all we can to make the HETV relief as effective as possible, to maximise the resulting returns to the UK economy.

Although the current HETV threshold is £1 million per hour, in practice a lot of quality prime-time dramas which most viewers and commentators would regard as being 'high end' in nature actually cost a little under £1 million per hour and therefore do not currently qualify for HETV Tax Relief. Such content is nevertheless very cost sensitive and there are already many examples – some of which may be detailed in individual submissions to this consultation from British Screen Forum Members – of quality drama, set in the UK and telling UK-specific stories, and costing less than £1 million per hour being made in Ireland, Budapest and other competitor territories largely as a result of the tax incentives accessible for those productions in those countries. We would therefore take issue with the proposition that there is a significant 'deadweight' burden under the current threshold.

In addition, many high-quality UK dramas – especially those made for the PSBs – have budgets which are at or only marginally above the current threshold. Any increase in that threshold would reduce the incentive to produce that distinctively UK content in the UK rather than in competitor countries. To the extent that this causes programmes to move abroad, this would have the additional negative effect of removing the ability to proactively support skills development amongst UK crew for these shows lost to the UK. Alternatively, some productions with budgets of around £1 million per hour might increase their prices to meet the new threshold – while this would keep those productions in the UK, it would give rise to an unintended inflationary effect.

The main argument for the proposed change in the consultation document relates to inflation in production budgets. We recognise that budgets have of course risen over time, and that it is a delicate balance to get the threshold level right. But the example referred to above of UK-commissioned shows just below the current threshold being filmed overseas suggest that the current threshold is not, in fact, too high.

The consultation document states (para 3.8): "*Rising production costs have meant that several productions which the government expects would have been commissioned regardless of existence of HETV tax relief have become eligible.*" We have seen no evidence of this taking place in practice and none is presented in the consultation document. With this in mind, it is important not to throw the baby out with the bath water and exclude valuable productions that otherwise would not be made in the UK and which also play an important role in skills development.

Our understanding is that HM Treasury's concerns relate to programmes such as soap operas seeking to access reliefs now or at some point in the future as a result of ongoing inflationary pressures. While we recognise that the HETV relief was not designed for programmes such as these, it is important to emphasise that their budgets still fall very far below the current threshold and so there is no real risk of them becoming eligible for the HETV relief even with inflation now or in the coming years. Even so, we appreciate that HM Treasury may wish to put measures in place to guarantee that soaps cannot access the relief, and we would propose that this be addressed in the most direct manner. A pragmatic, targeted and future-proof approach would simply be to formally add these genres to the exclusion list. If this approach is adopted, it will be important to define the genre carefully to ensure that appropriate content is not inadvertently excluded; to this end, as with the legal definition of documentary (see below), we would urge consultation with industry to develop appropriate criteria. Given the likely need to maintain appropriate flexibility to make adjustments over time, there may be merit in incorporating any such definition in Guidance Notes rather than legislation.

As a final point, it is worth noting that while prospects for long-term growth are very good, there is evidence that the recent sharp rise in production spend (which has driven up costs) is reverting to a shallower trajectory. For example, Ampere Analysis predicted at the start of 2023 that worldwide spend on TV content would increase by just 2% this year.[10] As a result, inflation rates might be expected to fall soon, and this may even start to drive some deflation in the coming years. Such developments would mitigate HM Treasury's concerns relating to ongoing budget inflation.

c) Minimum slot length (HETV tax relief) (Questions 2-4)

The issue of the bundling together of short episodes to qualify for the HETV tax relief is not a significant issue for our Members, and we do not have particular views on the specific consultation questions.

Our greater concern, as stated above, is around maintaining the minimum expenditure threshold, and this motivates our response here.

[10] See https://deadline.com/2023/01/tv-spending-spree-over-analyst-predicts-ampere-analysis-1235210222/

- We recognise the concerns set out in the consultation document and agree with the thrust of the proposals to address them.
- Given the importance to us of maintaining the minimum expenditure threshold, we encourage HM Treasury to consider additional rules that would explicitly prevent the likes of soaps from being bundled together to access the HETV relief, rather than increasing the expenditure threshold as the means to exclude these genres.
- This could be achieved, for example, as part of the proposed option (a) in para 3.12 of the consultation document, according to which the legislation would be amended to apply on an "episode by episode basis" and the minimum slot length reduced to 20 minutes. However, the lack of detail in the consultation document prevents us from making a full assessment of the two proposed options with any confidence.

As we note in the previous section, any concerns around soaps can also be addressed – in a more direct way – by simply adding the genre to the list of excluded programmes.

For our members, the most common legitimate usage of the rule allowing multiple episodes to be combined is for two 30-minute episodes of a series in genres such as scripted comedy or dramedies to be grouped together when they have a combined budget across the full hour of more than £1 million. The tax relief is vitally important to support production in these genres, which make an important contribution to the mix of culturally British content aimed primarily at domestic audiences but which by their nature can be difficult to finance and for which international sales are far from guaranteed. For the avoidance of doubt, we would welcome confirmation that the eligibility of such shows is not at risk under the proposed changes.

d) Legal definition of documentary (HETV tax relief) (Questions 5-6)

We recognise that there is a gap in legislation regarding the definition of a "documentary," as the consultation document notes. A consequence of this is that rules are currently inconsistently applied and are subject to individual people's judgement.

The definition in the consultation document, following BFI guidance, provides a useful starting point for discussion (para 3.16): "*a factual or realistic programme based on real events, places or circumstances and intended to record or inform.*"

- We agree that a workable definition would provide greater clarity and certainty, to the benefit of industry and the Government alike.
- Further consultation is needed with the relevant stakeholders in that part of the sector, to make sure the definition is fit-for-purpose. Key stakeholders to consult with are those who best understand factual commissions and evolving practices in the production of documentaries, such as the main broadcasters and streamers.
- A fit-for-purpose definition would provide clarity without being too narrow and thereby excluding content that ought to be eligible.

Further clarity and certainty regarding which types of "documentary" qualify for relief would be very helpful in order for shows to be properly planned and budgeted at each stage of development and production.

It is important to get the definition right, to avoid instances of both false positives and false negatives, i.e. to ensure all types of programmes are excluded that are intended to be excluded, whilst not excluding any types of content that the relief is intended to support. While not pre-judging the industry consultation that is needed, we expect that a broad definition (such as the current BFI definition), but with clearly defined specific categories of content that are excluded, would facilitate consistent interpretation.

An important challenge is not to exclude types of content that ought to be eligible. In the past, UK commissions in the genre were mostly made by the PSBs and independent filmmakers, with Sky making an increasingly important contribution over the last decade. More recently, the streamers have put increased resources into documentary content, and they are among the most popular titles on the global streaming services, with broad appeal across geographies and demographics. As a result, the types of documentaries that are commissioned has evolved considerably over time, in terms of their style, approach, subject matter and target audiences. This has been accompanied by innovations in the kinds of documentaries that are made. All this should be welcomed as contributing to a rich ecosystem of UK-produced documentary content, and it is important that the new definition does not inadvertently make some kinds of content ineligible for the relief that ought to be supported. It is also important not to discourage innovation in new kinds of documentaries through disproportionate measures to avoid "boundary pushing."

This is particularly the case given that there is some evidence of a shift at a global level in content commissioning from scripted to unscripted productions in 2023 (partly to broaden the content mix offered by the streamers, partly because high-quality non-scripted content can be produced at lower price points than the highest-cost scripted shows). As the HETV content mix evolves, it is important that the UK's tax relief regime remains as attractive as it is now for the full range of programming that global players wish to make, to avoid the risk of a diminution on the volume of production that comes to the UK.

MODERNISING VIDEO GAMES TAX RELIEF

e) Video game tax relief qualifying expenditure (Questions 7-11)

The Video Games Tax Relief (VGTR) differs from the other audiovisual reliefs in an important respect, in that European (previously, EEA) expenditure is currently eligible for the relief. The consultation document proposes bringing the VGTR in line with the other reliefs by refocusing it on UK expenditure through a requirement for expenditure to be 'used or consumed' in the UK. The VGTR currently has a subcontracting cap of £1 million per game, and the consultation also proposes to either raise or remove this cap whilst only permitting subcontracting within the UK.

- **There is unlikely to be a benefit to UK the games industry overall if EEA expenditure were no longer eligible, given the current skills shortages. We would expect such a change to negatively affect video game companies and that it would encourage them to move expenditure outside the UK (to lower cost territories or to territories which allowed claims across multiple jurisdictions) rather than attract more expenditure to the UK. The net effect of the proposed changes would be to reduce UK activity and diminish the beneficial impacts of the VGTR.**
- **Increasing or removing the subcontracting cap might bring small benefits to small companies but these would be more than offset by the increased costs associated with the removal of eligibility of EEA expenditure.**

Our position is motivated by the significant importance of EEA labour and spend to UK video games. The UK video games sector is facing a shortage of skilled labour, and the skills gaps are exacerbated as it seeks to grow its workforce to keep up with global demand for its high-quality productions. The skills shortages are especially acute for companies in a range of areas including Art, Animation, IT/Infrastructure, Quality Assurance and Audio/Sound Design.

There is a long-term ambition to increase the amount of skilled labour in the UK, but this will require considerable investment in education and skills, along with a strategic review of talent pathways, and it will take many years for new talent to come through. In the meantime, there is no straightforward way to plug the skills gaps other than enabling companies to hire talent with the necessary skills from overseas. The BFI's analysis of all Video Games Tax Relief Applications since 2014 shows EEA spend is included in 31% of the total (1,045 out of 3,332 applications).

Changing the rules relating to the EEA without making it easier for UK games companies to hire talent in the UK from other countries would be counterproductive: if UK firms cannot bring skilled talent into the UK and cannot benefit when accessing it abroad, all the options for them to scale up in the short term are effectively closed off. Ukie's survey of its members shows that the majority believe the removal of EEA expenditure from qualifying expenditure in VGTR claims would have a negative impact on UK games companies, materially increasing their costs. Around two-thirds of respondents said they would consider reducing the scope of projects currently being developed in the UK, with projects being moved out of the UK either in part or in their entirety.

There was a strong consensus that increasing the subcontracting cap – as proposed in the consultation document – would not bring significant benefits as it is already expensive to hire British-based talent and there is not enough unused capacity in the UK to take advantage of an increased limit. Any benefits that did accrue would be more than offset by the increased costs associated with the removal of eligibility of EEA expenditure.

REFORMING AUDIOVISUAL TAX RELIEFS TO EXPENDITURE CREDITS

f) Basic structure of the proposed expenditure credit (Questions 12-17; 19-22)

The proposals in the consultation are motivated in large part by reforms to the international tax framework, and in particular the OECD Pillar Two model rules. The consultation document argues (para 5.6) that "*reforming the reliefs into refundable expenditure credits*" will "*put the question of whether the audio-visual tax reliefs qualify as income beyond doubt.*" It also argues that this will provide:

- *"Greater clarity for businesses about the amount of credit they can expect to receive;*
- *"Increased attractiveness to inward investors, as refundable credits are recorded as income included in profit;*
- *"Greater flexibility over production decisions, as claimants will no longer need to be loss-making to maximise the benefit of the credit."*

The stated aim for the proposed expenditure credit is (para 5.7) to: "*increase investment in the audio-visual sectors in the UK and stimulate the production of culturally British content. The government wants an expenditure credit that is suitable for the majority of businesses producing film, TV or video games in the UK.*"

Regarding the headline rate, the consultation document stats (para 5.10) that: "*We expect the rate for the expenditure credit to be in line with the generosity of the existing regime. The final rate for the credit will be decided following consultation.*" At the industry stakeholder event held before Christmas, officials clarified that, as we understand it, "generosity" would not be defined in such a way as to penalise industry growth.

We recognise the need to future-proof the tax reliefs in the context of the OECD Pillar Two model rules, and in principle we support the proposed change to expenditure credits, subject to a number of important conditions being met:

i. As per our overarching concerns set out in Section B, crucially important details of the proposed new credit remain to be worked out, and there is considerable scope for unintended consequences that could damage the UK's international competitiveness. We would need to see more information before we can make an informed assessment
ii. The changes to a new system of tax reliefs should be done in a manner which at least maintains the current value of the incentive in practice (taking account of any increase in tax liability that results from the expenditure credit being treated as revenue)
iii. The UK regime must remain competitive with other international schemes. This means maintaining the speed, simplicity and certainty that are positive attributes of the current UK regime
iv. Any new expenditure credit framework must allow sufficient differentiation to remain to reflect the particular characteristics of the current five audiovisual tax reliefs and to respond to the specific circumstances in each sub-sector with flexibility

We recognise the need to ensure that the tax reliefs are fit-for-purpose in the future, and that the OECD Pillar Two model rules that are being introduced globally mean that now is an appropriate time to review how the reliefs work. As we state in our overarching comments, if implemented these would be the most fundamental changes to the UK's creative industry tax reliefs since the Film Tax Relief was introduced in January 2007. We have set out our concerns that some crucially important details remain to be worked out; that a compelling case for many of the changes has not yet been made; and that the impact on investor confidence needs to be considered during the consultation and implementation process, as the stability of the regime is critical to its continued success.

It is for these reasons that at this stage our position can only be to cautiously welcome some elements of the proposals, whilst highlighting our concerns about other elements, including the risks associated with the disruption and potential unintended consequences, both of which could result in the UK losing large volumes of business.

Our position on the final rate of the scheme is that it must at least maintain the current value of the incentive in practice (taking account of any increase in tax liability that results from the expenditure credit being treated as revenue). We recognise that at the level of individual films, under an entirely new model, it is not possible to guarantee that every single project would benefit in exactly the same way under the two schemes. So maintaining the current value of the incentive in practice should mean that for the same level of total production activity in the industry, the overall absolute value of the relief should be no worse than under the current regime. This is important as we believe there may be some hidden costs in the implementation of the new scheme that would need to be worked through carefully. It will also be important to make sure that individual categories of content (smaller independent films or video games, for example) are also no worse off under the new scheme. And finally, we would welcome formal confirmation that the audiovisual sector would not be penalised for its success, i.e. that if overall production activity grows, as we hope will be the case, then the Government understands that the direct costs of the tax relief will grow accordingly – but will be more than compensated by the corresponding growth in the economic benefits that are generated.

Over and above the main rate, it is important the new reliefs are designed and implemented in such a way as to ensure the UK regime remains competitive with other international schemes. This means ensuring that the speed, simplicity and certainty that are currently positive attributes of the current UK regime are carried over to the new expenditure credits. As part of this, it is critical that HMRC retains relevant specialists for each area of production (so for example, film claims continue to be reviewed by film specialists, etc.) in order for it to continue to address applications in a consistent and timely manner.

Analogous to our comment on the main rate about not harming particular categories of content, it will also be important to ensure that particular types of companies are not systematically harmed by the new model. For example, Ukie's preliminary consultation with its members suggests that larger video games companies would welcome the changes, and that it would be beneficial to them to move the relief "above the line" given that it will be treated as income (and provided that the rate of relief remains as generous as the current system, as argued above). They also suggest that other countries where it is largely above the line are increasingly perceived to be more competitive for a given credit rate, and this would make the VGTR look more competitive. This would provide economic benefits by, for example, allowing them to hire more staff in a competitive environment. Conversely, smaller companies are concerned that the change could effectively close off financing options to them as they often borrow against the cash they would receive on the product based on surrendered losses. It is important not to disrupt these existing financing routes through changes to the system.

We also note the expectation that the proposed expenditure credit for the audio-visual reliefs will broadly align with the steps embedded in the Research and Development Expenditure Credit (RDEC) model. If such an alignment included Step 3, which states that *"the credit must not be higher than your company's total expenditure on your workers' PAYE and NICs for the accounting period,"* this would pose serious problems for many audio-visual companies. This is because the accepted list of self-employment grades for film and TV means that the PAYE liability on many projects is minimal for independent producers.

With reference to the combined proposals to (a) move to a new system of expenditure credits and (b) merge the existing film and TV reliefs into a single relief, there is a balance to be struck between, on the one hand, maintaining sufficient flexibility to be able to address current differences between the sub-sectors and future changes to individual sub-sectors; and on the other hand, delivering the benefits in terms of simplicity and "tidying up" to both the Government and to the sectors themselves. As we have stated above, given the differences between the sub-sectors, it is important that any new framework based on expenditure credits allows sufficient differentiation to remain to reflect the particular characteristics of the current five audiovisual tax reliefs and to respond to the specific circumstances in each sub-sector with flexibility.

g) Removing the 80% cap on qualifying expenditure (no consultation question)

The consultation document refers to a perception that the 80% cap on qualifying expenditure encourages the more portable aspects of production, such as visual effects (VFX), to move abroad. It proposes removing the cap but adds (para 5.13) that "*this may necessitate a lower overall credit rate to avoid a substantial additional cost to the taxpayer.*"

It is important to note that the 80% cap on qualifying expenditure was set in order to comply with EU state aid rules. Given the substantial returns on investment from the relief (detailed in Section B), this cap has acted in practice as a limitation on how much value the tax relief could generate – it is not, as has sometimes been portrayed, a measure that was intended to reduce harm to the Exchequer, but rather the opposite in that it acted as a constraint on the scale of positive returns. We are now in a position where the cap is a choice.

- We agree that, other things being equal, removing the 80% cap has the potential to encourage more spend to take place in the UK rather than overseas, which could help the VFX and animation sectors in particular.
- The benefits could be increased, and the direct cost to the Exchequer minimised, through a more targeted approach that limits the removal of the cap to certain productions that include a certain amount of spend on VFX or animation but then boosted the credit rate for this spend (as the UK Screen Alliance has proposed).
- However, <u>we would not support any proposal to remove the cap if it were accompanied by a reduction in the overall credit rate</u>, as suggested in the consultation document. The market is highly sensitive to the credit rate, and a reduction would carry a huge risk of a negative impact – in terms of lost inward investment business to other countries – that could greatly exceed the benefit of removing the cap. If the Government remains of the view that there must be some form of trade-off, then our position would be to keep the 80% cap as is and not reduce the overall rate.

The removal of the cap would be subject to compliance with the Subsidy Control Act 2022. These rules are designed to give more flexibility to intervene with targeted interventions to boost the UK economy. As such, the proposal to remove the cap – by itself – could in theory be a good example of supporting the industry and increasing the overall benefits to the sector and the UK economy.

The proposal is of particular relevance to the VFX and animation sectors, within which growth has lagged other territories, with UK-founded companies prioritising investment overseas rather than investing in the UK. According to the UK Screen Alliance, analysis of UK production between 2017 and 2019 reveals that £1 billion of VFX expenditure on UK-qualifying projects was carried out overseas, equivalent to around 50% of all VFX work carried out on UK-qualified productions in that time period. This overseas investment is due to an unintended consequence of the 80% cap: as VFX and animation work is not tied to where filming takes place, it is the most "mobile" part of the budget and can easily be moved outside of the UK to other jurisdictions that make tax reliefs available for this expenditure.

Analysis by the UK Screen Alliance suggests that removing the 80% cap may not achieve much by itself, given the competitiveness of tax reliefs for VFX and animation work globally. Its proposal comprises a targeted model that limits the removal of the cap to productions whose spend in the UK on VFX or animation work constitutes 5% or more of total spend, but then boosts the rate of the incentive as it applies to VFX and animation work, with an additional boost to support VFX and animation work that occurs outside London and the South East (supporting the Government's levelling-up agenda).

Our view is that the principles behind this proposal – targeted interventions that minimise the potential for any deadweight cost to the Exchequer whilst maximising the potential increase in GVA for the UK economy through the additional VFX and animation work carried out in the UK – have merit and are worthy of consideration as part of the proposed changes to the tax reliefs. It is worth noting that there are also industry proposals for higher rates for independent UK films within a given budget range, as another example of a proposed amendment that takes the form of a highly targeted intervention.[11]

Having set out the potential benefits that might result from removing the 80% cap, we must turn to a major concern that we have with the Government's proposals, one that represents a potential "deal breaker." Whether the Government just removes the 80% cap as per the consultation document, or if it considers more nuanced targeted proposals along the lines outlined above, we believe that any such benefits would be more than offset by losses from reduced inward investment if the overall credit rate were then to be reduced.

As the tax relief generates significantly positive returns on investment, the wording in para 5.13 of the consultation document is an example of the relief being misleadingly portrayed as a "cost to the taxpayer" when the overall benefits to the UK of the additional economic activity are positive: taxpayers, as UK citizens, would ultimately be better off. We therefore believe that the proposal to lower the overall credit rate alongside the removal of the 80% cap is predicated on a false trade-off.

Reducing the credit rate would be a huge concern to us, as the current level of the relief is already at the minimum level to be competitive: headline rates of relief in some other countries (such as Canada) are more generous, and the competitiveness of the UK comes from a combination of the rate of relief, the specific design of the scheme (including the ease of accessing the UK reliefs), and the high quality of our talent base and facilities. Reducing the rate of the credit would almost certainly have unintended consequences by making the UK less competitive than at present, and our expectation is that the combination of removing the cap and lowering the overall rate would lead to a net reduction rather than an increase in inward investment.

Therefore, if the Government remains of the view that there must be some form of trade-off, then our position would be to retain the status quo, i.e. to keep the 80% cap and not reduce the overall rate.

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[11] See British Screen Forum's "Prospectus for Growth in an Age of Change" (July 2022, here) and the "Economic Review of UK Independent Film" commissioned by the BFI from Alma Economics (July 2022, full report and BFI response here)

h) Replacement of current schemes with expenditure credit scheme for audiovisual tax reliefs (Question 18)

The proposal in the consultation is to fully replace the existing five audiovisual tax reliefs with new expenditure credits. It requests views on how best to help manage the transition from the existing reliefs to expenditure credits.

- Should new expenditure credits be introduced, we agree that these should fully replace their existing counterparts (with the caveat that they are well-designed and fit-for-purpose).
- It is vital that assurances are given as soon as possible that transitional arrangements will be put in place to ensure that no-one will be disadvantaged as a result of beginning production in advance of the start of any new scheme. Otherwise, there is a significant risk that the UK will lose highly mobile production projects to other territories during the transition process – which effectively begins immediately with this consultation.
- We suggest as a key transition principle that any project that has already begun on the basis of the current reliefs will be able to continue using this system, along with an option for producers to elect to switch to the new rules if desired.

Our key concern regarding the transition relates to the disruption that this may cause. One of the overarching concerns we raised in Section B is that the impact on investor confidence needs to be considered during the consultation and implementation process, as the stability of the regime is critical to its continued success. This is a pressing issue as inward investment companies looking to begin productions soon may opt to locate elsewhere if there is a risk that the UK's reliefs are going to be changed in negative ways.

Projects looking for a green light now need certainty about what relief they will get – this is especially the case for animation, video games and other projects with longer time horizons. Lead times for games projects in particular can be much longer than for film and TV: some projects can spend 5 – 6 years in development and production before their first release. There is an urgent need for the Government to set out its transitional rules, and to provide reassurances to potential investors, including making sure the timescales give all parties sufficient time to plan for these changes. As we argue above, this is likely to mean delaying the transition point beyond Spring 2024 (while signalling this clearly as soon as possible).

In the first instance, we believe it would make sense for the Government to confirm – and communicate to industry – the overarching principles for the transition. A key principle should be to agree that any project that has already begun on the basis of the current reliefs will be able to continue using this system, regardless of the duration of the project (following the precedent set when the sale and leaseback reliefs were replaced). This principle could easily be expanded to include any future productions that begin (and/or have been issued an interim certificate by the BFI) before a certain date. Similarly for video games, we would need some kind of assurance that anything that formally started significant development before the agreed future transition point would be treated under the old regime, given that projects that are currently in development or are about to begin development may not complete for several years, owing to the varied timelines associated with game development.

We also see merit in providing an option for producers to elect to switch to the new rules if they wish to do so: this can only be to the benefit of all parties as it guarantees that producers of content during the transition process do not lose out either way while boosting the number of projects that use HM Treasury's new regime in its early years. Such voluntary "early adopters" will play a vital role in demonstrating to global producers that the new system works as well as the current one and ensuring a smooth transition from the current regime to the new one.

As a final point, in moving from tax reliefs to expenditure credits, no new limitations on qualifying expenditure should be introduced as this would seriously undermine the efficacy of the scheme.

ANNEX

The audiovisual tax reliefs form a major part of the UK's competitive offer for production investment, alongside creative talent, skilled crew, and high-specification production infrastructure. As the economic and strategic value of production investment has been further evidenced in recent years, many other jurisdictions have introduced or expanded incentives to attract this investment, and the UK's tax reliefs should be seen in the context of this competitive incentive landscape.

High-level information on incentives offered in a selection of the UK's major competitors is provided in the table below, including details of any recent changes or expansions.

INCENTIVES OFFERED BY A SELECTION OF THE UK'S MAJOR COMPETITORS

TERRITORY	SUMMARY OF INCENTIVES
Australia	• Offers a range of incentives aimed at different parts of the film and TV sector • International productions can access the Location Offset and Location Incentive, which offer a combined 30% incentive • The Offset is uncapped, while the Location Incentive draws from a top-up fund, which since launching in 2019 has received AU$540 million from government • For Post, Digital and VFX ("PDV") productions, there is a separate 30% tax credit available • In addition, Australia's states and territories offer incentives which can be combined with the federal system
British Columbia	• Offers a mix of incentives, which can be combined with Canada's federal tax credit (worth 16% of Canadian labour costs) • International productions in British Columbia are eligible for the Production Services Tax Credit (PSTC) worth 28% of resident labour expenditure • Several uplifts are available including 16% for regional filming and 16% for eligible digital animation, visual effects, and postproduction expenditure

TERRITORY	SUMMARY OF INCENTIVES
California	• Has a system of incentives aimed at projects ranging from indie films to major studio productions • Independent films and relocating TV series are eligible for a 25% tax credit, as well as an of uplift of 5% for regional crew hires • Studio features and series are eligible for a 20% tax credit, as well as a range of uplifts for regional filming and expenditure on visual effects work in the state (5%) and for regional crew hires (10%) • Since 2022, California has offered a separate Soundstage Tax Credit for productions utilising newly constructed or renovated soundstages
France	• Offers a range of incentives for domestic and international productions, including the 30% Tax Rebate for International Production (TRIP) • In 2020, this incentive was expanded to provide a 10% bonus (i.e. a 40% incentive rate overall) for productions which spend over €2 million on French VFX
Georgia (US state)	• Offers a 20% tax credit, with a 10% bonus for projects which include a promotional logo in the credits for the finished film or series • The commitment from the state to maintaining the effectiveness of the incentive has been instrumental in its transformation into one of the world's major production hubs • In FY2022, Georgia saw $4.4 billion of expenditure
Ireland	• Offers a 32% tax credit applicable to both local and international productions • The incentive offers a regional uplift worth 2% of qualifying expenditure to productions made outside of Dublin, Wicklow, or Cork • The incentive is available to film and TV productions in Ireland, and as a result of recent changes, has also been expanded to cover video games
Spain	• Offers a tax credit worth 30% on the first €1 million in qualifying expenditure, and 25% thereafter • At the end of 2022, the Spanish government approved major expansions to the incentive, including raising the per-project incentive cap for films to €20 million, and for series to €10 million per episode. The cap on individual salaries was also removed • Certain regions of Spain have opted to offer higher incentives: the Canary Islands offers a 50% incentive, while Bizkaia recently announced it would offer incentives worth up to 70% of eligible costs

Source: Olsberg•SPI research compiled for British Screen Forum

FRAME THE DEBATE

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