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When the script calls for cash incentives

The lucrative producer offset tax scheme for film and television was supposed to be a shot in the arm for the industry, but the big banks are staying away from the show, writes Alex Boxsell.

Hot from its second screening at the Cannes Film Festival after more than 30 years, the iconic Australian film *Wake In Fright* will play at Sydney's own festival next month, billed as one of the nation's finest films ever made. But while the industry applauds the classic's resurrection, many filmmakers would privately wish more modern productions were gaining the same attention.

Australia's film industry is in the doldrums, but it could have been so different. The federal government's lucrative producer offset – a 40 per cent tax rebate for film and 20 per cent for television – was supposed to be the shot in the arm the industry sorely needed when it premiered amid much fanfare in 2007.

The arrival of the global financial crisis before the offset's first anniversary is obviously cruel timing, rendering producers yet another class of small-business owner unable to breathe life into a recession-plagued industry.

But it is doubtful whether many Australian banks were ever supporters of the offset scheme, despite what many in the industry describe as the most generous film and television government incentive in the world. Many banks, including the Big Four, have merely dabbled in offset loans since the scheme was introduced and few seem to have the appetite for longer-term lending. And it does not help matters that producers at times front up to an interview with a banker in a T-shirt and jeans to put their hands up for million-dollar loans.

The funding situation is somewhat better in television, where recent productions such as Nine Network's *Underbelly* gained substantial audiences at home and sold overseas.

But things are dire in Australian film financing. Less experienced movie producers with low-budget projects (between \$1 million and \$6 million) and no pre-sales to distributors are finding it almost impossible to access the very incentives designed to help them into the industry.

For those who can get loans, Australian banks rarely accept the film as the asset guaranteeing them. Unlike their counterparts overseas, local banks want producers to have “skin in the game”; that is, to provide a personal guarantee or bet the family home.

The problem may be that banks were not properly consulted when the offset was developed between 2005 and 2007. At that time, it was assumed that major European film financiers Bank of Ireland and Royal Bank of Scotland would embrace the Australian offset and expedite many local productions. But both those banks are now at the mercy of government bailouts.

Law firm DLA Phillips Fox has acted for Westpac Banking Group and its offshoot St George Bank in a small number of film and television projects, in which personal guarantees were required for loans. Phillips Fox partner Bill Chapman says the arrival of the financial crisis and its after-effects was “just shocking timing” for the industry, and film financing now ranks “about 1015th in terms of what banks are looking to fund”. The industry spent too much time lobbying the government and not enough time educating the banks about the mechanics of the offset, Chapman says.

Law firm Holding Redlich has acted for several Australian financiers on offset loans, including the feature film *Accidents Happen* (which premieres at the Sydney Film Festival) and television shows *Lockie Leonard* and *Gasp*. Sydney Managing partner Ian Robertson says the risk to the lender can be “extremely low”, especially when a reputable producer has received a provisional certificate from the peak government body, Screen Australia, and insured the film through a completion bond. Although it is difficult and quite expensive for producers to borrow, it is not impossible, says Robertson, who is also deputy chairman of Screen Australia.

The reluctance of Australian banks to lend is so widespread that entrepreneurial Americans have arrived to gain a share of the market.

A small bank by United States standards, National Bank of California (NBCal) has an established history “cash-flowing” film and television around the world. The bank arrived in Sydney in April eager to meet Australian producers and find local banks with which to partner, with a tantalising offer: loans that do not require producers to mortgage their houses.

NBCal has financed two feature films – *Charlie & Boots* and *Beauty and the Beast* – as well as two children’s television shows, all of which qualified for the offset. It is waiting for the first offset cheques to be paid back by the Australian Taxation Office after June 30 before it decides whether to lend in a more substantial way.

NBCal senior vice-president Adrian Ward says the Australian offset is one of the better programs in the world, “both in terms of the way it is administered, plus the fact that it is a 40 per cent gross benefit – that’s pretty substantial”.

“In what other industries are you basically getting a government guarantee against what you are loaning?” Ward asks.

Australian banks are known for their conservatism and he understands their hesitation, Ward says.

“Big banks and a relatively small industry: sometimes that’s not a good combination. But for certain banks there is probably some very good business to be done.”

This is not news to Investec Bank Australia, which has loaned against the offset for one film and one television series, and has more projects in the pipeline. But what sets it apart from the other banks are internal champions of the film industry – both chairman David Gonski and director Geoffrey Levy have previously chaired the Film Finance Corporation.

The head of financial products in the capital markets division, Dean You Lee, says Investec found value in the producer offset by structuring its products to minimise risk, something which suits a specialist, niche lender. Investec will lend as little as \$1 million, and has loaned a total of \$9 million to date. And far from a deterrent, the financial crisis has actually helped to shield Investec from larger Irish and Scottish competitors, You Lee says.

“For the size of the project, you do need some specialist skills in order to get the right structure to manage the risk,” he says. “I would say that the majority of transactions are generally too small for most commercial banks to look at.”

But where they have succeeded, others have failed. Macquarie Group’s Macquarie Film Corporation was liquidated in 2006 after poor takings from films such as *Dirty Deeds*, while Babcock & Brown got involved with April Films in 2004 to make *Jindabyne* before the bank imploded.

Screen Australia has issued 232 projects with provisional certificates under the offset as of May 8: 90 feature films, 97 non-feature documentaries, and 45 other projects (television series, telemovies, direct-to-DVD or online, and short-form animation).

But at March 31, only three final certificates, required before the ATO will provide the rebate, were issued for finished feature films from an overall total of 23. A further 13 certificates were issued for non-feature documentaries and seven for television projects, taking the total amount of qualifying expenditure to \$43.1 million.

Last week’s federal budget explained that a decrease in funding for “government arts expenditure” in the 2010 financial year primarily reflected an “estimated decrease in claims” for the producer offset.

Jane Campion’s film about English poet John Keats’ first love, *Bright Star*, premiered in Cannes on Friday. An Australian/British co-production, the film is believed to have qualified for the producer offset for the Australian portion of the film.

Campion is in the running to win the coveted Palme D’Or for the second time, following her success with *The Piano* in 1993.

Australian outback drama *Samson & Delilah* received a standing ovation at its Cannes screening on the weekend, but producer Kath Shelper says her film did not qualify for the offset because it had federal funding of 75 per cent or more.

The offset scheme is making films more expensive “due to the huge costs that are being charged by those cash-flowing the offset with interest, set-up fees and legal fees”, Shelper says.

“For my next low-budget film it is adding considerable costs to the budget and it is difficult to find cash-flow money for small amounts. The cost of the set-up fees and legals is similar to those seeking large amounts.”

But Shelper says she is confident that the offset scheme's kinks will be ironed out over time and that "cheaper money will become available for cash-flowing".

To understand why producers placed so much hope in the offset, it's necessary to recall how the promising scheme came to be.

The idea for a government incentive struck Holding Redlich's Robertson on a drive back from Canberra after attending a screen industry dinner with former Prime Minister John Howard in 2005.

Robertson was at the time chairman of Ausfilm, which markets Australia as a production destination for foreign films. He says Howard expressed interest in ditching the unpopular investor-focused division 10BA income-tax scheme in favour of something that would assist producers, as small-business owners, but was not open to tax rorting.

Robertson's idea was to create a tax offset for Australian films, similar to the 12.5 per cent (now 15 per cent) location offset that netted *Superman Returns* for Sydney in 2005. It would be available only to projects that had significant Australian content, the same testing used for division 10BA.

The concept was quickly embraced by many in the film and television industry, including director Baz Luhrmann, who told Howard his \$US130 million film, *Australia*, would not be shot in Australia unless something like the offset was introduced. The film is expected to recover about \$US55 million (\$73 million) as a rebate under the offset at the end of June.

By giving producers equity in their projects, it would allow them to roll over any profits into their next production. If this were to happen on a large scale then the industry could thrive.

But not only is it hard to borrow money, the ATO will not allow producers to use a financial year end date other than June 30, meaning filmmakers are faced with the near-impossible task of all trying to finish their projects by June every year or risk higher borrowing costs. Screen Australia says final certificates can take up to 10 weeks to issue.

Despite the difficulties, there are some Australian low-budget films still being made with private finance. Producers Robert Galinsky and Elizabeth Howatt-Jackman raised \$4 million for *Prey*, released this month, as one of the last 10BA films. They plan to fund a \$6 million movie and \$40 million-plus film this year using the offset for the first time.

"I would say, in this climate, it would be almost next to impossible to go to a bank and borrow money on a film, only because there have only been a handful of Australian films that have turned a profit in the last decade," Galinsky says.

Producers are finding some practical flaws with the offset, he says. The 40 per cent rebate ends up really being as low as 30 per cent of the overall budget because it does not cover the major expense of marketing the film, "which is a huge mistake".

But once the industry and banks gain more certainty with the scheme when the ATO cheques roll in after June 30, the situation has the potential to improve.

“It is really going to be fantastic for film here,” Galinsky says. “It will get a lot of films made and I think it will be a return to more commercial films.”

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